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Commission on
International
Trade Law**

YEARBOOK

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NOTE

Symbols of United Nations documents are composed of capital letters combined with figures. Mention of such a symbol indicates a reference to a United Nations document.

The footnote numbering follows that used in the original documents on which this Yearbook is based. Any footnotes added subsequently are indicated by lower-case letters.

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INTRODUCTION

This is the fourteenth volume in the series of Yearbooks of the United Nations Commission on International Trade Law (UNCITRAL).¹

The present volume consists of three parts. Part one contains the Commission's report on the work of its sixteenth session, which was held in Vienna from 24 May to 3 June 1983, and the action thereon by the United Nations Conference on Trade and Development (UNCTAD) and by the General Assembly.

In part two most of the documents considered at the sixteenth session of the Commission are reproduced. These documents include reports of the Commission's Working Groups dealing respectively with international contract practices and the new international economic order, as well as reports and notes by the Secretary-General and the secretariat of UNCITRAL. Also included in this part are selected working papers which were before the Working Groups.

Part three contains selected summary records of Commission meetings, legal texts adopted by the Commission, relevant resolutions of the General Assembly, a bibliography of recent writings related to the work of the Commissions, prepared by the secretariat, and a check list of UNCITRAL documents.

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¹To date the following volumes of the Yearbook of the United Nations Commission on International Trade Law abbreviated herein as Yearbook ... (year)] have been published:

<i>Volume</i>	<i>Years covered</i>	<i>United Nations publication, Sales No.</i>
I	1968-1970	E.71.V.1
II	1971	E.72.V.4
III	1972	E.73.V.6
III Suppl.	1972	E.73.V.9
IV	1973	E.74.V.3
V	1974	E.75.V.2
VI	1975	E.76.V.5
VII	1976	E.77.V.1
VIII	1977	E.78.V.7
IX	1978	E.80.V.8
X	1979	E.81.V.2
XI	1980	E.81.V.8
XII	1981	E.82.V.6
XIII	1982	E.84.V.5
XIV	1983	E.85.V.3

THE SIXTEENTH SESSION (1983)

A. Report of the United Nations Commission on International Trade Law on the work of its sixteenth session (Vienna, 24 May-3 June 1983) (A/38/17)^a

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INTRODUCTION

1. The present report of the United Nations Commission on International Trade Law covers the six-

^aOfficial Records of the General Assembly, Thirty-eighth Session, Supplement No. 17 (A/38/17) (10 August 1983) (hereinafter referred to as "Report"). The Report has also been issued as document A/CN.9/243 (29 June 1983) and is reproduced here.

teenth session of the Commission, held at Vienna, from 24 May to 3 June 1983.

2. Pursuant to General Assembly resolution 2205 (XXI) of 17 December 1966, this report is submitted to the General Assembly and is also submitted for comments to the United Nations Conference on Trade and Development.

CHAPTER I. ORGANIZATION OF THE SESSION

A. Opening

3. The United Nations Commission on International Trade Law (UNCITRAL) commenced its sixteenth session on 24 May 1983. The session was opened on behalf of the Secretary-General by Mr. Carl-August Fleischhauer, the Legal Counsel.

B. Membership and attendance

4. General Assembly resolution 2205 (XXI) established the Commission with a membership of 29 States, elected by the Assembly. By resolution 3108 (XXVIII), the General Assembly increased the membership of the Commission from 29 to 36 States. The present members of the Commission, elected on 9 November 1979 and 15 November 1982, are the following States:¹ Algeria,** Australia,** Austria,** Brazil,** Central African Republic,** China,** Cuba,* Cyprus,* Czechoslovakia,* Egypt,** France,** German Democratic Republic,** Germany, Federal Republic of,* Guatemala,* Hungary,* India,* Iraq,* Italy,* Japan,** Kenya,* Mexico,** Nigeria,** Peru,* Philippines,* Senegal,* Sierra Leone,* Singapore,** Spain,* Sweden,** Trinidad and Tobago,* Uganda,* Union of Soviet Socialist Republics,** United Kingdom of Great Britain and Northern Ireland,** United Republic of Tanzania,** United States of America* and Yugoslavia*.

5. With the exception of Central African Republic, Senegal and United Republic of Tanzania, all members of the Commission were represented at the session.

6. The session was also attended by observers from the following States: Argentina, Bulgaria, Canada, Chile, Democratic People's Republic of Korea, Finland, Greece, Holy See, Jamaica, Lebanon, Libyan Arab Jamahiriya, Morocco, Netherlands, Portugal, Republic of Korea, Switzerland, Thailand, Tunisia, Venezuela and Zaire.

7. The following United Nations organs, specialized agency, intergovernmental organizations and inter-

national non-governmental organization were represented by observers:

- (a) *United Nations organs*
United Nations Industrial Development Organization
- (b) *Specialized agency*
World Bank
- (c) *Intergovernmental organizations*
Asian-African Legal Consultative Committee
Commission of the European Communities
Council for Mutual Economic Assistance
Council of Europe
Hague Conference on Private International Law
International Institute for the Unification of Private Law Organization of American States
- (d) *International non-governmental organization*
International Association of Democratic Lawyers

C. Election of officers

8. The Commission elected the following officers:²

- Chairman: Mr. M. H. Chafik (Egypt)
- Vice-Chairmen: Mrs. J. Vilus (Yugoslavia)
Mr. T. Sawada (Japan)
Mr. M. J. Bonell (Italy)
- Rapporteur: Mr. J. Barrera Graf (Mexico)

D. Agenda

9. The agenda of the session, as adopted by the Commission at its 269th meeting on 24 May 1983, was as follows:

- 1. Opening of the session
- 2. Election of officers
- 3. Adoption of the agenda
- 4. International contract practices
- 5. International payments
- 6. International commercial arbitration
- 7. New international economic order
- 8. Co-ordination of work
- 9. Status of conventions
- 10. Training and assistance
- 11. Relevant General Assembly resolutions
- 12. Future work
- 13. Other business
- 14. Adoption of the report of the Commission

E. Adoption of the report

10. The Commission adopted the present report at its 284th meeting, on 3 June 1983 by consensus.

*Term of office expires on the day before the opening of the regular session of the Commission in 1986.

**Term of office expires on the day before the opening of the regular session of the Commission in 1989.

¹Pursuant to General Assembly resolution 2205 (XXI), the members of the Commission are elected for a term of six years. Of the current membership, 19 were elected by the Assembly at its thirty-fourth session on 9 November 1979 (decision 34/308) and 17 were elected by the General Assembly at its thirty-seventh session on 15 November 1982 (decision 37/308). Pursuant to resolution 31/99 of 15 December 1976 the term of those members elected by the Assembly at its thirty-fourth session will expire on the last day prior to the opening of the nineteenth regular annual session of the Commission in 1986, while the term of those members elected by the General Assembly at its thirty-seventh session will expire on the last day prior to the opening of the twenty-second regular annual session of the Commission in 1989.

²The elections took place at the 269th and 274th meetings, on 24 and 26 May 1983. In accordance with a decision taken by the Commission at its first session, the Commission has three Vice-Chairmen, so that together with the Chairman and Rapporteur, each of the five groups of States listed in General Assembly resolution 2205 (XXI), sect. II, para. 1, will be represented on the bureau of the Commission (see *Official Records of the General Assembly, Twenty-third Session, Supplement No. 16 (A/7216)*, para. 14 (Yearbook ... 1968-1970, part two, I, A).

CHAPTER II. INTERNATIONAL CONTRACT PRACTICES: UNIFORM RULES ON LIQUIDATED DAMAGES AND PENALTY CLAUSES³

Introduction

11. At its twelfth session, the Commission requested its Working Group on International Contract Practices to consider the feasibility of formulating uniform rules on liquidated damages and penalty clauses applicable to a wide range of international trade contracts.⁴ At its fourteenth session, the Commission considered the draft uniform rules prepared by the Working Group and requested the Secretary-General to incorporate in the rules such supplementary provisions as might be required if the rules were to take the form of a convention or a model law, to prepare a commentary on the rules, to prepare a questionnaire addressed to Governments and international organizations seeking to elicit their views on the most appropriate form for the rules and to circulate the rules to all Governments and interested international organizations for their comments, together with the commentary and the questionnaire.⁵

12. At its fifteenth session the Commission had before it the rules with the required supplementary provisions and the commentary (A/CN.9/218),⁶ together with an analysis of the responses of Governments and international organizations to the questionnaire and of their comments on the rules (A/CN.9/219 and Add. 1).⁷ At that session the Commission considered the form that the rules might take, and also considered the substance of article A, paragraph 1, and articles D, E, F and G of the rules. It thereafter referred these articles for consideration to a Drafting Group.⁸ As the Drafting Group was unable to complete its work in the time available, the Commission decided that the secretariat should submit a revised text of the rules for consideration by the Commission at its sixteenth session, taking into account the discussion at the session and within the Drafting Group. It also decided to determine the form of the rules at the sixteenth session.⁹

³Yearbook ... 1982, part two, I, A.

⁴Yearbook ... 1982, part two, I, B.

⁵The Commission considered this subject at its 270th, 271st, 272nd, 273rd, 274th, 275th, 276th, 277th, 278th, 282nd and 283rd meetings on 24, 25, 26, 27, and 30 May and 1 and 2 June 1983. Summary records of the meetings are reproduced in this volume, part three, I, B, 2.

⁶Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 31 (Yearbook ... 1979, part one, II, A).

⁷Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 44. (Yearbook ... 1981, part one, A).

⁸Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17* (A/37/17), para. 18. (Yearbook ... 1982, part one, A).

⁹*Ibid.*, para. 40.

13. At its current session the Commission had before it a revised text of the rules, with explanatory footnotes (A/CN.9/235).^d

Discussion at the session⁸

14. The Commission commenced its deliberations by considering whether the uniform rules should take the form of general conditions, a convention or a model law.

15. There was some support for the view that the uniform rules should take the form of general conditions. In support of this view, it was noted that general conditions could be used by parties as soon as they were finalized by the Commission and would accordingly come into use earlier than if one of the other forms were adopted. Furthermore, parties would have the freedom to adapt the rules to suit the needs of the particular contracts concluded by them. Once the general conditions were widely accepted in international trade, they would influence the drafting of national legislation on liquidated damages and penalty clauses. In opposition to the form of general conditions, it was noted that they would be ineffective where they conflicted with applicable mandatory national laws. The degree of unification achieved by this method would therefore be very limited.

16. There was support for the view that the form of a convention should be adopted. In support of this view, it was noted that a convention would provide the most effective form of unification. Since liquidated damages and penalty clauses were frequently used in international trade contracts, an effective unification of this subject-matter was necessary. The procedure for the adoption of a convention, either through a conference of plenipotentiaries or through the General Assembly, would bring the rules to the attention of States and generate interest in the rules. In opposition to the form of a convention, it was observed that a convention on the subject in question would receive little support by way of adherence to it. In this connection, it was noted that recent experience seemed to indicate that many conventions never received the requisite support for their entry into force. It was also noted that the scope of the subject-matter covered was very limited, and that, accordingly, a convention was inappropriate. The procedure for the adoption of a convention through a conference of plenipotentiaries would also involve considerable expense. Some representatives whose first preference was for the form of a convention indicated, however, that they could accept the form of a model law if a majority supported that form.

17. The majority view supported the form of a model law. It was noted that this form enabled States, at the time the model law was incorporated in their national legislation, to make changes necessary to make the

^dReproduced in this volume, part two, I.

^eFor the summary records of the discussion, see A/CN.9/SR.270-278, 282 and 283.

model law effective in their own legal systems. Furthermore, a model law would, in particular, have influence at a regional level on the drafting or modernization of the laws governing liquidated damages and penalties. It was also noted that a model law could be adopted by the Commission, and therefore involved far less expense than the adoption of a convention. In opposition to the form of a model law, it was noted that the adoption of a model law by the Commission would not create sufficient interest among States in the model law, which would consequently be ineffective as an instrument for unification. Furthermore, since it was open to a State to make changes in the model law, either at the time of incorporation into its legislation or subsequently, the uniformity achieved through the model law might be limited. Some representatives whose first preference was for the form of a model law indicated, however, that they could accept the form of a convention if a majority supported that form.

18. It was observed that the central question to be considered was the extent of commitment to the view that the laws in regard to liquidated damages and penalties needed unification. If there was no real commitment to this view, any uniform rules which might be approved would be ineffective, whatever the form in which they were embodied, that is, if a convention were adopted, it would not enter into force, and if a model law were adopted, it would not be followed by States in their legislation.

19. Attention was directed to the fact that, at its fifteenth session, the Commission had noted that it might be useful to cast the uniform rules in a form which might enable the rules to be used for several purposes.⁹ Following, for example, the form used in the Hague Convention relating to a Uniform Law on the International Sale of Goods of 1 July 1964 (the Hague Convention) to which was annexed the Uniform Law on the International Sale of Goods, a convention might be drafted to which could be annexed uniform rules on liquidated damages and penalty clauses. Contracting States to such a convention would be obligated to adopt these uniform rules. Furthermore, the convention could permit a reservation (as, for example, in article V of the Hague Convention) that the uniform rules were only to apply when the parties to a contract had chosen to apply the uniform rules to their contract. States not adhering to such a convention could regard the uniform rules as a model law which might be used in revising their national legislations.

20. There was considerable support for the adoption of this approach. It was noted that this approach would enable the Commission to proceed to the drafting of the rules, and to decide, after the drafting was completed, whether the rules could appropriately be annexed to a convention or should form a model law. Furthermore, the exact scope of a possible convention and the reservations to be permitted therein could be deter-

mined after the completion of the drafting. The Commission accordingly decided to discuss the revised draft uniform rules submitted to it, on the provisional basis that they might constitute a set of uniform rules to be set forth in an annex to a convention. It also decided that, after discussion by the Commission, the rules should be referred to a drafting group for consideration in the light of the discussion.

Creation of the Drafting Group

21. It was decided that the Drafting Group should consist of France, India, Sierra Leone, Spain, Union of Soviet Socialist Republics and United States of America.

Discussion of specific articles

22. The text of article A, paragraph 1, as considered by the Commission was as follows:

Article A, paragraph 1¹⁰

Revised draft (draft model law)

“(1) This law applies:

“(a) To contracts in which the parties have agreed that, upon a total or partial failure of performance by a party (the obligor), the other party (the obligee) is entitled to [recover or to withhold] an agreed sum of money from the obligor, [where such sum is intended as a pre-estimate of damages, or as a security for performance, or both] [where such sum is intended as a pre-estimate of damages to be paid by the obligor for loss suffered by the obligee as a consequence of that failure, or as a penalty for that failure, or both], and

“(b) Where, at the time of the conclusion of the contract, the parties have their places of business in different States, and the rules of private international law lead to the application of the law of (the State adopting the Model Law).

“(1 bis) Except as expressly provided in this law, it is not concerned with the validity of the contract or of any of its provisions.”

23. The Commission considered subparagraph (a) of this paragraph, and discussed whether the words “recover or to withhold” should be retained. Under one view, they served a useful purpose in clarifying that the rules were not restricted to cases where the agreement between the obligee and obligor contemplated the payment of an agreed sum by the obligor upon failure of performance, but also covered cases where the agreed sum had been paid by the obligor to the obligee before failure of performance and was to be withheld upon failure of performance. It was suggested that the word “retain” should be substituted for the word “withhold”. However, under another view, although the retention of these words did not cause difficulties, they should be deleted since they were superfluous.

⁹Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17 (A/37/17)*, para. 17. (Yearbook ... 1982, part one, A).

¹⁰The text of the specific articles was before the Commission in document A/CN.9/235 (reproduced in this volume, part two, I).

24. It was noted that there was a divergence between the terms "total or partial failure of performance" used in this subparagraph and the terms "non-performance of an obligation, or defective performance other than delay" used in article E. The view was also expressed that the terms "total or partial failure of performance" were unclear and that the terms might be deleted. It was agreed that the Drafting Group should, in any event, provide a uniform terminology.

25. The Commission considered whether the word "agreed" in the phrase "agreed sum of money" was appropriate. It was suggested that this word might be misleading, as parties might not specify a sum in a liquidated damages or penalty clause, but instead specify a method of determining a sum. The prevailing view was that the word "agreed" was sufficient to cover cases where the contract specified a method of determining the sum.

26. The Commission considered the two alternative phrases at the end of the subparagraph defining the nature of the agreed sum. There was general agreement that neither alternative was fully satisfactory. As regards the first alternative, it was noted that the meaning of the term "security" was unclear. As regards the second alternative, it was noted that the reference therein to "loss" suggested that the agreed sum was only payable if the obligee could prove that he had suffered loss. It was also observed that under both alternatives, where the agreed sum was described in its character of a pre-estimate of damages, it was described as "intended" by the parties to constitute such a pre-estimate. It was suggested that such a formulation might require an inquiry by a tribunal into the intention of the parties and that such an inquiry would be difficult and inadvisable.

27. There was some discussion as to the types of clauses which might be covered by the subparagraph, and it was decided that the Drafting Group should take this discussion into account in its examination of the subparagraph.

28. The Commission decided to defer the consideration of paragraph 1 (b) and 1 bis.

29. The text of article D as considered by the Commission was as follows:

Article D

Revised draft

"If a failure of performance in respect of which the parties have agreed that the obligee is entitled to an agreed sum of money occurs, the obligee is entitled to the agreed sum unless the obligor [proves that he] is not liable for the failure of performance."

30. There was general agreement that the previous draft of this article was preferable. This draft was as follows:

"Unless the parties have agreed otherwise, the obligee is not entitled to recover or to forfeit the agreed sum if the obligor is not liable for the failure of performance."

31. It was noted that the previous draft expressed the ideas contained in the revised draft in a more concise form. There was general agreement that the opening words of the previous draft should be deleted, as their function was now served by article X. There was also general agreement that the proposal in the revised draft to place on the obligor the burden of proving that he was not liable for the failure of performance (that is, by the insertion of the words "proves that he") was inadvisable, as the allocation of burden of proof should be left to the applicable law governing the burden of proof. A view was also expressed that the rule might be reformulated in a positive form.

32. The previous draft was referred to the Drafting Group for consideration in the light of the deliberations in the Commission.

33. The text of article E as considered by the Commission was as follows:

Article E

Revised draft

"(1) Where the contract provides that the obligee is entitled to the agreed sum on delay in performance of an obligation, the obligee is entitled both to require performance of the obligation and to the agreed sum.

"(2) Where the contract provides that the obligee is entitled to the agreed sum on non-performance of an obligation, or defective performance other than delay, the obligee is entitled either to require performance, or to the agreed sum. If, however, [the obligee proves that] the agreed sum cannot reasonably be regarded as a substitute for performance, the obligee is entitled both to require performance of the obligation and to the agreed sum."

Paragraph 1

34. The prevailing view was that the revised draft of paragraph 1 was preferable to the previous draft. There was general agreement with the rule set forth in the paragraph. There was also general agreement that the phraseology describing the failure of performance should be in conformity with that to be adopted for article A.

35. A suggestion was made that paragraph 1 should specify that the rule expressed therein under which the obligee was entitled both to performance and the agreed sum should also be extended to the case where the contract provided that the obligee was entitled to an agreed sum upon delivery at a place other than that provided in the contract. This suggestion was not adopted.

36. Under one view, the words "the contract provides that" should be deleted, because the need for a contractual agreement creating a liquidated damages or penalty clause as a pre-condition for the application of the rules had already been set forth in article A.

Furthermore, the inclusion of these words might suggest that article E was not subject to the rule contained in article D. Under another view, however, these words clarified the scope of the paragraph, and in particular, directed attention to the fact that the nature of the contractual agreement determined whether paragraph 1 or paragraph 2 of the article applied. It was further suggested that the words "as specified in the contract" might be added after the words "the obligation" to clarify the rule.

37. The Commission considered whether the retention of the word "require" in the phrase "entitled to require performance" was necessary. The view was expressed that this word was necessary as it clarified the content of the entitlement to performance. The prevailing view, however, was that the rule contained in the paragraph would not lose its substance by the deletion of the word. The view was also expressed that the retention of this word would confer on the obligee a right to specific performance, which was undesirable, as the existence of this right should be determined by the applicable law. It was pointed out that the omission of that word would not necessarily avoid that result in all legal systems. Furthermore, the deletion of this word might enable drafting changes to be effected which might make article Y superfluous.

38. The paragraph was referred to the Drafting Group for consideration in the light of the deliberations in the Commission.

Paragraph 2

39. There was general agreement that the paragraph did not need to describe the types of non-performance other than delay and that the phraseology describing non-performance in this article should be in conformity with the phraseology to be adopted in paragraph 1 of this article and in article A. There was also general agreement that the words "the obligee proves" were unnecessary, and that the allocation of the burden of proof should be left to the applicable law governing the burden of proof. It was also noted that, in conformity with the prevailing view expressed in regard to paragraph 1 of this article, the word "require" should be deleted in the phrase "to require performance".

40. There was considerable discussion as to whether the compromise achieved in this paragraph was satisfactory. In the circumstances described in the first sentence, there was an alternative entitlement to performance or to the agreed sum and, in the circumstances described in the second sentence, a cumulative entitlement. Under one view, retaining only the rule contained in the first sentence would lead to simplicity of result. Furthermore, the cumulation envisaged in the second sentence could sometimes lead to unjust enrichment of the obligee. In opposition to this view, it was observed that the paragraph embodied a delicate compromise between the approaches of the legal systems which conferred an alternative entitlement and those which conferred a cumulative entitlement, and should therefore be maintained. It was suggested that the paragraph

should be redrafted to make the right to alternative or cumulative entitlement depend on the terms of the contract. It was noted, however, that, even under the present drafting, the terms of the contract would prevail over the rules in this article by virtue of article X; what was needed was a rule to determine the issue when it was not resolved in the contract.

41. There was support for the view that the phrase "substitute for performance" was not sufficiently clear, and that an attempt should be made to find an alternative phrase to express the idea to be conveyed.

42. The paragraph was referred to the Drafting Group for consideration in the light of the deliberations in the Commission.

43. The text of article Y as considered by the Commission was as follows:

Article Y

"Where, in accordance with the provisions of this (Convention) (law) the obligee is entitled to require performance of an obligation, a court is not bound to enter a judgment for specific performance unless the court would do so in respect of similar contracts not governed by this (Convention) (law)."

44. There was support for the view that the rules should not deal with the issue as to whether an obligee was or was not entitled to specific performance. This issue should be left for determination to the applicable law. It was therefore suggested that article E, which referred to the right to performance, should be redrafted so as to eliminate the need for article Y. The Commission therefore agreed to postpone the consideration of article Y until it had before it the text of article E as revised by the Drafting Group.

45. The text of article F as considered by the Commission was as follows:

Article F

Revised draft

"Where the obligee is entitled to the agreed sum, he [is not entitled to damages] [may not assert a claim for damages] to the extent of the loss covered by the agreed sum. He [is also not entitled to damages] [may also not assert a claim for damages] to the extent of the loss not covered by the agreed sum, unless he can prove that his loss grossly exceeds the agreed sum."

46. The Commission noted that this article reflected a compromise between two approaches to the relationship between the right of the obligee to the agreed sum and his right to claim damages. Under the first approach, the obligee was only entitled to the agreed sum and could not claim damages, even if his loss resulting from the obligor's non-performance was not fully compensated by the agreed sum. Under the second approach, the obligee was in such circumstances entitled to claim damages in addition to the agreed sum. It was

noted that each of these approaches had advantages and disadvantages and that, in particular, under the second approach the function of the agreed sum in creating certainty as to the compensation recoverable upon failure of performance was diminished. It was suggested, however, that each of these approaches resulted in greater certainty as to the rights and obligations of the parties as to the compensation recoverable than did the compromise approach in this article. Under the compromise approach, it was suggested, there would be frequent disputes as to whether the loss suffered by the obligee grossly exceeded the agreed sum.

47. There was support for the second approach noted above, and greater support for the first approach. There was also considerable support for the view that the article reflected an acceptable compromise that did not create too great a degree of uncertainty.

48. The Commission considered other compromise solutions which might be considered more acceptable than the one contained at present in the article. There was support for the view that different rules might be adopted depending on whether the agreed sum constituted liquidated damages or performed a different function. If it constituted liquidated damages, the obligee should not be entitled to claim damages in addition to the agreed sum, while in other cases the obligee might be permitted to claim damages to the extent of the loss not covered by the agreed sum if the agreed sum could not reasonably be regarded as compensation for that loss. This approach was further elaborated in suggestions that the revised draft of the article might be acceptable if instead of the phrase "unless he can prove that his loss grossly exceeds the agreed sum" at the end of the article, there were substituted either the phrase "unless the agreed sum cannot reasonably be regarded as a substitute for performance" or the phrase "unless the agreed amount cannot reasonably be regarded as liquidated damages". These latter suggestions also attracted considerable support.

49. After extensive deliberation, however, the Commission was of the view that the rule expressed in the article as currently drafted was the most acceptable. There was wide agreement that a more appropriate word should be substituted for the word "grossly". The revised draft was accordingly referred to the Drafting Group for consideration in the light of the deliberations in the Commission.

50. The text of article X as considered by the Commission was as follows:

Article X (new article)

"The parties may by agreement only derogate from or vary the effect of articles D, E and F of this (Convention) (law)."

51. A suggestion was made that parties should not be permitted to derogate from or vary the effect of article D. However, there was wide support for the substance of the

article in its present form. It was noted that there might be advantages in permitting the parties to determine the allocation of the loss caused by the obligor's failure of performance even if he was not liable for that failure. Allocating the loss to the obligor in such circumstances prevented a dispute as to whether or not the obligor was liable for his failure of performance, and was not necessarily unjust to the obligor.

52. It was noted that, under this article, parties were free to vary the effect of articles D, E and F, either expressly or impliedly, and that this should be clarified either by specifying this, or by deleting the words "by agreement" which might suggest the need for express agreement.

53. The article was referred by the Commission to the Drafting Group for consideration in the light of the deliberations in the Commission.

54. The text of article G as considered by the Commission was as follows:

Article G

Revised draft

"(1) The agreed sum shall not be reduced by a court or arbitral tribunal.

"(2) Notwithstanding the provisions of paragraph 1 of this article, the agreed sum may [shall] be reduced [though not below the extent of the loss suffered by the obligee]:

"(a) if the agreed sum is shown to [be grossly disproportionate in relation to] [grossly exceed] the loss that has been suffered by the obligee; or

"(b) (i) if parties have provided that the obligee is entitled to the agreed sum even when the obligor is not liable for the failure of performance, and

"(ii) if the obligee claims the agreed sum when the obligor is not liable for the failure of performance, and

"(iii) if entitlement to the agreed sum would be manifestly unfair in the circumstances."

55. There was considerable discussion as to whether the rules set forth in paragraph 2 (b) of the article were needed. Under one view these rules should be retained, as they were a method of mitigating the possible hardship which might result to the obligor when the parties varied the rule set forth in article D and enabled the obligee to claim the agreed sum even when the obligor was not liable for his failure of performance. It was also observed that it was desirable to retain the term "manifestly unfair", mentioned in paragraph 2 (b), as a criterion for reducing the agreed sum, as there may be cases where the agreement between the parties fixing the agreed sum might not be equitable. It was further observed that manifest unfairness should also be applicable as a criterion for reducing the agreed sum when parties had varied the rules set forth in articles E and F, and such variation resulted in unfairness to the obligor. The prevailing view, however, was that para-

graph 2 (b) should be deleted. It was noted that, if parties had varied the rule set forth in article D, their agreement should not be interfered with under this article. It was further noted that the concept of manifest unfairness was not precise. Furthermore, paragraph 2 (b) as drafted was complicated and difficult to understand, and the reduction of the agreed sum sought to be secured thereunder could in many cases be also secured under paragraph 2 (a).

56. There was general agreement that the principles set forth in paragraphs 1 and 2 (a) should be retained. There was wide support for combining these principles in a single paragraph, as this would lead to simplification. In this connection, there was support for a simpler rule that a court or arbitral tribunal might reduce the agreed sum unless that sum could be regarded as a pre-estimate of damages. The prevailing view, however, was that such a rule would not provide sufficient guidance to a court or arbitral tribunal.

57. The Commission considered whether, if the conditions for reducing the agreed sum were satisfied, the article should oblige the court or arbitral tribunal to reduce the agreed sum (that is, by specifying that the agreed sum shall be reduced) or whether it should give the court or arbitral tribunal a discretion as to reduction (that is, by specifying that the agreed sum may be reduced). The imposition of an obligation on the court or arbitral tribunal was supported on the ground that this would lead to greater certainty in the operation of the article. Furthermore, it was noted that, under article F, if loss grossly in excess of the agreed sum existed, the obligee was entitled to claim damages and thereby obtain increased compensation. Accordingly, article G should set forth a parallel rule under which the obligor was entitled to a decrease in the sum payable by him if the agreed sum grossly exceeded the loss. There was, however, somewhat greater support for the view that the issue should be left to the discretion of the court or arbitral tribunal. It was noted that, if the conditions for reduction were satisfied, a court or arbitral tribunal would, in practice, always reduce the agreed sum.

58. The Commission also considered whether guidelines should be established to assist the court or arbitral tribunal in determining the extent of reduction when the conditions for reduction were satisfied. There was support for retaining the words "though not below the extent of the loss suffered by the obligee", thereby imposing a limit below which a reduction could not be made. There was considerable support, however, for the view that the extent of reduction should be left to the discretion of the court or arbitral tribunal, which could then make an equitable reduction having regard to all the circumstances of the case. It was also noted that it was not easy to formulate a comprehensive set of principles to guide the court or arbitral tribunal which could be incorporated in the article.

59. The Commission referred the article for consideration to the Drafting Group in the light of the deliberations in the Commission.

Proposed structure of the draft uniform rules

60. The Commission considered a proposal of the secretariat for the structure of the uniform rules. This proposal set forth certain articles as forming "Part I: Scope of application and general provisions", and indicated that "Part II: Substantive provisions" might consist of articles D, E, F and G considered by the Commission. The proposal set forth the following articles as forming part I:

Article A

"These Rules apply to international contracts in which the parties have agreed that, upon a failure of performance by one party (the obligor), the other party (the obligee) is entitled to an agreed sum from the obligor, whether as a penalty or as compensation [for that failure]."

Article A bis

"For the purposes of these Rules:

"(a) A contract shall be considered international if, at the time of the conclusion of the contract, the parties have their places of business in different States;

"(b) The fact that the parties have their places of business in different States is to be disregarded whenever this fact does not appear either from the contract or from any dealings between, or from information disclosed by, the parties at any time before or at the conclusion of the contract;

"(c) Neither the nationality of the parties nor the civil or commercial character of the parties or of the contract is to be taken into consideration in determining the application of these Rules."

Article B

"For the purposes of these Rules:

"(a) If a party has more than one place of business, his 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.

"(b) If a party does not have a place of business, reference is to be made to his habitual residence."

Article C

"These Rules do not apply to contracts concerning goods, other property or services which are to be supplied for the personal, family or household purposes of a party, unless the other party, at any time before or at the conclusion of the contract, neither knew nor ought to have known that the contract was concluded for such purposes."

Article X

"The parties may by agreement only derogate from or vary the effect of articles D, E and F of these Rules."

61. The Commission noted that the text of article A, set forth above, which defined the contracts to which the draft rules applied, and the text of article X, had been considered in substance by the Commission and had been remitted by the Commission to the Drafting Group, and would be considered by the Commission at a later stage when the Drafting Group submitted the texts as prepared by it to the Commission.

62. The Commission noted that article A *bis* (a) set forth above, was derived from article 2 (a) of the Convention on the Limitation Period in the International Sale of Goods (New York, 1974),⁶ and that paragraphs (b) and (c) of article A *bis* were identical with paragraphs (2) and (3), respectively, of article 1 of the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980, hereinafter referred to as the Vienna Sales Convention).⁷ The Commission also noted that article B, set forth above, was identical with article 10 of the Vienna Sales Convention, and that article C, set forth above, was derived from article 2 (a) of the Vienna Sales Convention.

63. A view was expressed that paragraph (c) of article A *bis* and article C might be reformulated to provide that the rules only applied to contracts of a commercial character. While there was wide agreement that, in principle, the rules should apply only to commercial contracts and not to consumer transactions, the prevailing view was that there would be great difficulty in defining the term "commercial", as different legal systems approached such a definition in different ways.

64. The Commission accordingly accepted the rules expressed in articles A *bis*, B and C, and these provisions were remitted to the Drafting Group.

Possible reservation clauses in a convention

65. The Commission considered a proposal of the secretariat on possible reservation clauses which might be incorporated in a convention if the uniform rules were to be annexed to a convention. The Commission noted that the substance of these reservation clauses were those mentioned at an earlier stage in the deliberations in the Commission as clauses which might possibly be so incorporated.

66. The clauses considered by the Commission were as follows:

Contracting-in clause

"Any State may declare at the time of signature, ratification, acceptance, approval or accession to this Convention that it will apply the Uniform Rules only to a contract in which the parties to the contract have agreed that the Uniform Rules be applied thereto."

⁶Yearbook ... 1974, part three, I, B (A/CONF.63/15).

⁷Yearbook ... 1980, part three, I, B (A/CONF.97/18, annex 1)

Writing requirement

"A Contracting State whose legislation requires contracts to be concluded in or evidenced by writing may at any time make a declaration that it will apply the Uniform Rules only to a contract concluded in or evidenced by writing where any party has his place of business in that State."

67. The Commission agreed to the substance of these clauses but took no decisions on them because, if the uniform rules were to take the form of a model law, such decisions might not be necessary. With regard to the writing requirement, one delegation stated that to achieve a result similar to that in the Vienna Sales Convention it would also be necessary to use the approach of article 12 of that Convention or to find another appropriate solution.

Proposal of Drafting Group

68. The Commission considered the text of the rules as submitted by the Drafting Group. The Commission noted that there had been agreement within the Drafting Group on the text of all articles, with the exception of article E (2). The provisions submitted by the Drafting Group, except for article E (2), were those now appearing in annex I.

69. Article E (2) as submitted by the Drafting Group was as follows:

"If the contract provides that the obligee is entitled to the agreed sum upon a failure of performance other than delay, he is entitled either to performance or to the agreed sum. If, however, the agreed sum [cannot reasonably be regarded] [was not provided] [as a substitute for performance] [as compensation for that failure of performance], the obligee is entitled to both performance of the obligation and the agreed sum."

70. After deliberation, the Commission agreed that the phrase "cannot reasonably be regarded" was preferable to the phrase "was not provided", and that the phrase "as compensation for that failure of performance" was preferable to the phrase "as a substitute for performance". The Commission adopted the text of article E (2) retaining the preferred phrases noted above.

71. The view was expressed that the rule to determine the place of business of a party contained in article B (1) was unclear, because the place of business was determined by reference to its relationship to both the contract and its performance. It was suggested that the adoption of a single point of reference (for instance the place of performance of the contract) would lead to clarity. The prevailing view, however, was that as the text contained in this article had been adopted in the Vienna Sales Convention, it should also be adopted in this article in the interest of consistency.

72. The Commission noted that the change of the word "grossly" to "substantially" in articles F and G was of a drafting nature, and was not intended to indicate a change of meaning.

73. The Commission was in agreement with the view that paragraph 1 *bis* of article A of the revised draft as set forth in paragraph 22 above was unnecessary. The Commission also agreed that article Y set forth in paragraph 43 above should be incorporated in a convention if the uniform rules were to be annexed to a convention.

74. Several suggestions of a drafting and linguistic character were made with a view to ensuring conformity of the text in all the working languages of the Commission. The secretariat was requested to take note of these suggestions, and to ensure such conformity.

75. The Commission considered whether the title "Uniform rules on liquidated damages and penalty clauses" was appropriate. The view was expressed that the present title was suitable and indicated the two types of clauses dealt with in the rules. The prevailing view, however, was that a change was desirable, because in civil law systems the term "penalty clause" covered both penalty clauses and liquidated damages clauses as understood in the common law. It was suggested that the title should read "Uniform rules on contract clauses for an agreed sum due upon a failure of performance". It was agreed that this title should be provisionally adopted.

Decision of the Commission

76. After deliberation, the Commission completed its work on liquidated damages and penalty clauses by adopting the draft rules on the substance of the subject as set forth in annex I to this report.¹¹

77. The Commission noted that, in the discussions as to the form that the draft rules might take, three possibilities had initially been considered: the form of general conditions, a model law, or a convention following the structure of the Vienna Sales Convention. After observing that the views were divided on the form the draft rules might take, a fourth possibility had also been noted as a compromise solution, that is, to adopt the form of a convention in which the draft rules were set forth in an annex, which could accommodate both the convention and model law approaches. The States which did not wish to adhere to a convention might use the annex as a model law (see paragraphs 14 to 20 of this report). The Commission also took note of a sample draft convention prepared by the secretariat to provide for the event that the fourth possibility would be adopted. This draft convention is set forth in annex II to this report.

¹¹One delegation stated that, notwithstanding the considerable efforts made by the Commission and the spirit of accommodation shown by all delegates in the course of the work, it remained to be convinced that the topic of liquidated damages and penalty clauses was, by virtue of its intrinsic nature, an appropriate subject for unification.

78. Although there appeared to be a greater preference in favour of a model law, there was also considerable support for the approach based on a convention with the rules annexed thereto. However, the Commission could not reach a consensus as to the form which the draft rules should take. In view of the importance of this issue, which was of interest to all States, the Commission considered that any decision on the final form of the draft rules should be one for the Sixth Committee of the General Assembly.¹²

CHAPTER III. INTERNATIONAL PAYMENTS¹³

A. Draft Convention on International Bills of Exchange and International Promissory Notes and draft Convention on International Cheques

79. The Commission, at its fourteenth and fifteenth sessions, considered the possible future courses of action concerning the draft Convention on International Bills of Exchange and International Promissory Notes⁸ and the draft Convention on International Cheques.¹⁴ Divergent views were expressed as to whether these draft texts should be reviewed and revised, in the light of comments from Governments and international organizations, by the Commission itself or first by the Working Group on International Negotiable Instruments. The Commission postponed its final decision on that question to its seventeenth session but placed this item on the agenda for the present session to allow for possible discussion in case pertinent information would be available.

80. At its current session, the Commission considered a suggestion of the secretariat to devote a substantial period of time of the seventeenth session to a substantive discussion of key features and major controversial issues to be identified by the secretariat in an analysis of all comments of Governments and international

⁸Yearbook ... 1982, part two, II, A, 3 (A/CN.9/211).

¹⁴Yearbook ... 1982, part two, II, A, 5 (A/CN.9/212 and Corr.1 (Spanish only)).

¹²One delegation stated that in its view majority support had clearly emerged during the deliberations in favour of a model law. Accordingly, the Commission should adopt the rules in the form of a model law. It was observed by another delegation that it had originated the proposal for adopting a convention with the Rules annexed thereto, and at the time this proposal was made it had appeared to command wide support. At the conclusion of the deliberations, however, it had been uncertain whether this proposal commanded the same support. The more appropriate course for the Commission to adopt in these circumstances was to ascertain the opinion in the meeting and to take a decision as to form accordingly, rather than to leave the decision as to form to the Sixth Committee.

¹³The Commission considered this subject at its 280th meeting on 31 May 1983.

¹⁴Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), paras. 17-21 (Yearbook ... 1981, part one, A); report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17* (A/37/17), paras. 44-50 (Yearbook ... 1982, part one, A).

organizations. This suggestion was made in the light of the first comments received from Governments, and in view of the need to expedite matters and, in particular, to assist in the long-term planning of the work programme of future sessions.

81. The Commission, after deliberation, accepted this suggestion in principle. However, divergent views were expressed as to the appropriate duration of such discussion. While some support was expressed for fixing the duration already at the current session, the prevailing view was that a precise assessment could only be made after the comments on the draft texts had been received by the secretariat.

82. The Commission, after deliberation, authorized the secretariat to determine, in the light of the comments received by 30 September 1983, the appropriate duration of the discussion, but not exceeding two weeks.

B. Electronic funds transfers

83. The Commission at its fifteenth session decided that the secretariat should begin the preparation of a legal guide on electronic funds transfers, in co-operation with the UNCITRAL Study Group on International Payments.¹⁵ It was suggested that the legal guide should be designed to identify the legal issues, describe the various approaches, point out the advantages and disadvantages of each approach and suggest alternative solutions.

84. The Commission at its current session took note of a progress report that the secretariat had begun the work leading to the preparation of the legal guide (A/CN.9/242).¹ The Study Group had met once during the past year and two meetings were tentatively scheduled for the next year. It was expected that several draft chapters of the legal guide would be made available to the seventeenth session of the Commission for general observation.

CHAPTER IV. INTERNATIONAL COMMERCIAL ARBITRATION: MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION¹⁶

85. The Commission, at its fourteenth session, entrusted the Working Group on International Contract Practices with the preparation of a draft model law on international commercial arbitration.¹⁷ The Commission, at its fifteenth session, took note of

the report of that Working Group on the work of its third session (A/CN.9/216)² and requested it to proceed with its work expeditiously.¹⁸

86. The Commission, at its current session, had before it the reports of the Working Group on the work of its fourth session held at Vienna from 4 to 15 October 1982 (A/CN.9/232)³ and of its fifth session held in New York from 22 February to 4 March 1983 (A/CN.9/233).⁴

87. The Commission took note of these reports and expressed its appreciation to the Chairman of the Working Group, Mr. Iván Szasz. It noted that the Working Group had considered draft articles 1 to 36 (A/CN.9/WG.II/WP.37 and 38)⁵ and 37 to 41 (A/CN.9/WG.II/WP.42),⁶ revised draft articles I to XII, XXV and XXVI (A/CN.9/WG.II/WP.40),⁷ and some further issues possibly to be dealt with in the model law (A/CN.9/WG.II/WP.41).⁸

88. The Commission was agreed that the preparation of the model law was of great interest for both developed and developing countries and that it could help to facilitate international commercial arbitration as an appropriate method of settling disputes in international trade transactions. It was suggested, as an additional step towards developing international commercial arbitration, to consider suitable means by which the Commission and its secretariat could assist regional arbitration centres and similar institutions in developing countries. Another suggestion, which should be considered at a later stage, was to include in the model law on arbitration some provisions on conciliation. Yet another suggestion was that the Working Group should carefully study all aspects of the relationship between courts and arbitral tribunals.

89. The Commission requested the Working Group to proceed with its work expeditiously.

CHAPTER V. NEW INTERNATIONAL ECONOMIC ORDER: INDUSTRIAL CONTRACTS¹⁹

90. The Commission had before it the report of the Working Group on the New International Economic Order on the work of its fourth session (A/CN.9/234).⁹ The report set forth the deliberations of the Working Group on the basis of the report of the Secretary-

¹Yearbook ... 1982, part two, III, A.

²Reproduced in this volume, part two, III, A and D, respectively.

³Reproduced in this volume, part two, III, B, 1 and 2, respectively.

⁴Reproduced in this volume, part two, III, D, 3, 1 and 2, respectively.

⁵Reproduced in this volume, part two, IV, A.

⁶Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17 (A/37/17)*, paras. 88 and 89 (Yearbook ... 1982, part one, A).

⁷The Commission considered this subject at its 283rd meeting, on 2 June 1983.

¹⁵Reproduced in this volume, part two, II.

¹⁶Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17 (A/37/17)*, para. 73 (Yearbook ... 1982, part one, A).

¹⁷The Commission considered this subject at its 279th meeting, on 31 May 1983.

¹⁸Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17 (A/36/17)*, para. 70 (Yearbook ... 1981, part one, A).

General entitled "Draft legal guide on drawing up contracts for construction of industrial works: sample chapters" (A/CN.9/WG.V/WP.9 and Add. 1-5).⁶ The report noted that the Working Group had considered the draft outline of the structure of the guide (A/CN.9/WG.V/WP.9/Add.1)⁷ and the draft sample chapters on "Choice of contract types" (A/CN.9/WG.V/WP.9/Add.2),⁸ "Exemptions" (A/CN.9/WG.V/WP.9/Add.3)⁹ and "Hardship clauses" (A/CN.9/WG.V/WP.9/Add.4).¹⁰

91. The report further noted that there was general agreement in the Working Group that the draft outline of the structure was acceptable on the whole. It was generally recognized that, as the work progressed, some rearrangement of chapters might become necessary and the secretariat was given a discretion to do so, if needed, taking into account the views expressed during the deliberations at the Working Group. It was agreed in the Working Group that the guide should be drafted so as to be of practical value for various categories of persons involved in negotiating and drafting international contracts for construction of industrial works, such as administrators and businessmen, as well as for lawyers. The context of the new international economic order was stressed and it was pointed out that the guide would be of particular benefit to purchasers from developing countries.

92. The Commission expressed its appreciation to the Working Group and its chairman for the progress made in this extremely complex field. The importance of the guide for developing countries was stressed and the Commission agreed with the Working Group on the need to prepare the legal guide expeditiously.

93. The view was expressed that other legal aspects of the new international economic order were also important and it was suggested that a long-term programme for the work of the Working Group should be considered. In this connection, it was pointed out that the issues listed in the report of the Working Group on the work of its first session (A/CN.9/176)¹¹ should be taken into consideration in connection with the future work, since they had been included in the work programme of the Commission. It was noted that a duplication, which might result from considering issues dealt with by other international organizations, should be avoided. One delegation stated that the legal issues in the field of deep sea mining should be dealt with by the body especially envisaged under the Law of the Sea Convention (see A/CN.9/234, para. 22).

CHAPTER VI. CO-ORDINATION OF WORK²⁰

A. General co-ordination of activities

94. The Commission had before it a report of the Secretary-General which set forth the main activities of the secretariat for the purpose of co-ordination of work

in the field of international trade law since the fifteenth session (A/CN.9/239).¹² Representatives of a number of international organizations active in the field of international trade law reported to the Commission on the co-operation between their organizations and the Commission.

95. The representative of the Council of Europe indicated that his organization was continuing to co-operate with the Commission in respect of the legal problems arising in international payments. It had been decided to postpone any decision as to whether the revision of the 1930 Geneva Convention providing for a Uniform Law for Bills of Exchange and Promissory Notes was desirable until the Commission had completed its work in respect of negotiable instruments. The Council was also co-operating with the Commission in its work on electronic funds transfers. As to the legal value of computer records, a subject on which the Council of Europe had adopted a recommendation to Governments, the Council would make its experience available to the Commission. The representative of the Council of Europe also reported on the status of its work in preparing draft conventions on reservation of title and on bankruptcy.

96. The representative of the Council for Mutual Economic Assistance (CMEA) reported that a regional seminar had been held in Moscow in April 1983 on the Convention on the Limitation Period in the International Sale of Goods (New York, 1974) and the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980). The seminar, in which the Commission's secretariat participated, was attended by the heads of the legal departments of the Ministries of Foreign Trade of the countries belonging to CMEA.

97. The representative of the Hague Conference on Private International Law reported that the newly elected members of the Commission which were not members of the Hague Conference had been invited to the second session of the special commission created by the Hague Conference to consider the preparatory work for the revision of the 1955 Hague Convention on the Law Applicable to International Sale of Goods. The session would be held in November 1983. At the fourteenth session of the Conference it had been decided to postpone work which might lead to the revision of the 1931 Geneva Convention for the Settlement of Certain Conflicts of Law in connection with Bills of Exchange and Promissory Notes.

98. The representative of the Organization of American States reported that the draft agenda for the Third Inter-American Specialized Conference on Private International Law, which will be held at Washington in the spring of 1984, includes overland transport of passengers and goods as well as maritime transport. In regard to the latter, it was expected that the Conference, rather than preparing a regional convention on the subject, would probably adopt a resolution supporting

⁶Reproduced in this volume, part two, IV, B.

⁷Yearbook ... 1980, part two, V.

²⁰The Commission considered this subject at its 269th, 281st and 282nd meetings, on 24 May and 1 June 1983.

¹²Reproduced in this volume, part two, V, A.

ratification or accession to the Hamburg Rules. The suggestion was made that the Commission and the Organization of American States should co-operate in the promotion of conventions such as the Hamburg Rules which are of universal interest.

99. It was also reported that the Commission's secretariat had participated in the seminar organized last year by the Organization of American States by giving lectures on the Vienna Sales Convention and that similar participation was planned for this year with lectures on industrial contracts and on the Hamburg Rules.⁷

100. The representative of the International Institute for the Unification of Private Law reported that 58 States had participated in the diplomatic conference held at Geneva from 31 January to 18 February 1983 to adopt a Convention on Agency in the International Sale of Goods. The Convention was designed to supplement the Vienna Sales Convention prepared by the Commission. The representative of the Institute also reported that work was progressing satisfactorily on several subjects of interest to the Commission, including leasing contracts, factoring, codification of the law of international trade and uniform rules relating to liability and compensation for damage caused during the carriage over land of hazardous substances.

101. The representative of the Asian-African Legal Consultative Committee (AALCC) spoke of the assistance which the Commission might be able to give in support of the Regional Arbitration Centres established by the AALCC.

102. The representative of the World Bank reported on the close co-operation between his organization and the Commission in respect of the Commission's work on industrial contracts. He mentioned that the World Bank was often involved in this type of contract, particularly in connection with industrial development projects in developing countries. He stated that the Bank was glad to give its support to the Commission and its secretariat in the preparation of the legal guide on industrial contracts, which would be of great value.

Decision of the Commission

103. The Commission expressed its approval of the co-ordination activities of the secretariat. It also welcomed the statements of those representatives of other organizations who had spoken. The secretariat was urged to continue its efforts in this regard. In respect of the organizations mentioned in General Assembly resolution 34/142 on the co-ordinating role of the Commission, attention was drawn to the particular need to strengthen the co-operation with the United Nations Conference on Trade and Development. The secretariat was requested to submit a report to the seventeenth session of the Commission on the actions taken to create closer co-operation between the two

organizations, with a view to implement General Assembly resolution 2205 (XXI), II, paragraph 8 (f) and paragraph 10.

B. Current activities of international organizations related to the harmonization and unification of international trade law

104. The General Assembly, in resolution 34/142, requested the Secretary-General to place before the Commission at each of its sessions a report on the activities of other organizations related to international trade law together with recommendations as to steps to be taken by the Commission.

105. At its fifteenth session, the Commission repeated its desire, expressed at its fourteenth session, that a report should be submitted at regular intervals on all the activities of other organizations active in the field of international trade law. In response to this request the Commission had before it at its current session a report of the Secretary-General entitled "Current activities of international organizations related to the harmonization and unification of international trade law" (A/CN.9/237 and Add.1-3).⁸

106. There was general agreement that the report was informative and useful to government officials and law professors alike and that it also contributed to the co-ordination of activities among international organizations.

107. It was suggested that the work of certain other international non-governmental organizations should be included in future reports.

Decision of the Commission

108. The Commission took note with appreciation of the report on current activities of international organizations related to the harmonization and unification of international trade law.

C. International transport of goods: liability of international terminal operators

109. The Commission had before it a report of the Secretary-General on some recent developments in the field of international transport of goods (A/CN.9/236).⁹ The report described the activities of other organizations in the areas of marine insurance, transport by container and freight forwarding. It also described the work of the International Institute for the Unification of Private Law on the liability of international terminal operators, and discussed the principal legal issues connected with the preliminary draft Convention on Operators of Transport Terminals, which had been prepared by the Institute. The report noted that the

⁷Yearbook ... 1978, part three, I, B (A/CONF.89/13, annex I).

⁸Reproduced in this volume, part two, V, B.

⁹Reproduced in this volume, part two, V, C.

preliminary draft Convention sought to unify the disparate legal rules governing the liability of international terminal operators, so as to fill in the gaps in the liability regime for the international transport of goods which had been left by international transport conventions, such as the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg Rules). The report also noted that the central features of the preliminary draft Convention paralleled those of the Hamburg Rules.

110. The Commission noted with appreciation that the Governing Council of the International Institute for the Unification of Private Law had adopted the preliminary draft Convention at its sixty-second session, held in May 1983. The Commission was informed by the observer from the Institute that, when the Governing Council adopted the text, it expressed its great interest in the possibility of co-operation by the Commission in work on this project. The Governing Council decided that, if the Commission took up the topic the Institute would, upon a request by the Commission, transmit the text to the Commission for its consideration and would forego engaging in further work on the topic.

111. There was general agreement that the work of the Institute on the liability of international terminal operators was of a high quality and of great importance.

112. The view was expressed that co-operation by the Commission with the Institute and undertaking work on the topic of liability of international terminal operators would constitute a concrete example of the fulfilment by the Commission of the co-ordinating role entrusted to it by the General Assembly.

113. It was suggested that work by the Commission on the formulation of uniform rules on this topic should not be limited to storage and safekeeping of goods in international transport, but should also include storage and safekeeping of goods not involved in transport. Moreover, it was suggested that the Commission should not at this stage prejudge the ultimate form which the uniform rules on the topic should take, for example, convention or model law.

114. The Commission noted with appreciation the statement by the Secretary of the Commission that work on this topic, even within a working group, could be absorbed within the existing budget of the Commission, and would entail no additional financial implications. The Commission also noted with appreciation the statement by the Secretary of the Commission that this project would not itself create a need for additional staff in the secretariat although, as noted in the Medium-Term Plan, 1984-1989 (A/CN.9/XIV/R.1, para. 50), which was approved by the Commission at its fourteenth session,²¹ the overall increase in the role and responsibilities of the Commission had created a need for two additional professional staff members in the secretariat.

²¹Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 122 (Yearbook ... 1981, part one, A).

Decision of the Commission

115. The Commission decided to include the topic of liability of international terminal operators in its work programme, to request the International Institute for the Unification of Private Law to transmit its preliminary draft Convention to the Commission for its consideration, and to assign work on the preparation of uniform rules on this topic to a working group. The Commission deferred to its next session the decision on the composition of the Working Group. The secretariat was requested to submit to the Commission at its next session a study of important issues arising from the preliminary draft Convention by the Institute, and to consider in this study the possibility of broadening the scope of uniform rules to cover storage and safekeeping of goods not involved in transport.²²

D. Revision of the Uniform Customs and Practice for Documentary Credits

116. The Commission was informed that the definitive text of the current revision of the 1974 version of the Uniform Customs and Practice for Documentary Credits was expected to be completed by the Commission on Banking Technique and Practice of the International Chamber of Commerce within a short time and to be adopted by the Council of the International Chamber of Commerce during the month of June 1983. It was further expected that the new version of the Uniform Customs and Practice for Documentary Credits would be submitted to the Commission at its seventeenth session with a request for endorsement similar to that given by the Commission in 1975 to the 1974 version of the Uniform Customs and Practice for Documentary Credits.²³

E. Legal aspects of automatic data processing

117. The Commission had before it a note by the secretariat which conveyed in an annex a report on legal aspects of automatic data processing of the Working Party of the Economic Commission for Europe (ECE) and the United Nations Conference on Trade and Development (UNCTAD) on Facilitation of International Trade Procedures (A/CN.9/238).²⁴ The report of the Working Party described legal problems which arose in the teletransmission of trade data and suggested actions which might be undertaken by various international organizations in their respective areas of

²²Reproduced in this volume, part two, V, D.

²³Two representatives reserved their positions on these matters, having preferred these decisions to have been postponed until the next session of the Commission, so that they could consult with relevant circles in their countries. One of them also indicated that the subject of international terminal operators was quite different from the subject of storage and safekeeping of goods not involved in transport. This subject also had no relevance to international trade law.

²⁴Report of the United Nations Commission on International Trade Law on the work of its eighth session, *Official Records of the General Assembly, Thirtieth Session, Supplement No. 17* (A/10017), para. 41 (Yearbook ... 1975, part one, II, A).

competence. The report of the Working Party suggested that, since the problems were essentially those of international trade law, the Commission as the core legal body in the field of international trade law appeared to be the appropriate central forum to undertake and co-ordinate the necessary action.

118. The Commission took note of the intention of the secretariat to submit to the seventeenth session a report on the actions which the Commission might take to co-ordinate activities in this field, keeping in mind the areas of competence of the various international organizations concerned.

CHAPTER VII. STATUS OF CONVENTIONS²⁴

119. The Commission considered the status of conventions that were the outcome of its work, that is, the Convention on the Limitation Period in the International Sale of Goods (New York, 1974);^a the Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980);^b the United Nations Convention on the Carriage of Goods by Sea (1978 Hamburg Rules);^c and the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980).^d The Commission had before it a note by the Secretary-General entitled "Status of Conventions" (A/CN.9/241)^e which set forth the status of signatures, ratifications and accessions to these Conventions.

120. The Secretary of the Commission informed the Commission that the secretariat had intensified its efforts to promote these Conventions, particularly through its co-ordination and training and assistance programmes (see paras. 98, 99, 127 and 128 of this report). As regards the Convention on the Limitation Period in the International Sale of Goods and the United Nations Convention on Contracts for the International Sale of Goods, the Secretary noted that world-wide interest in these Conventions was growing and that, due to this encouraging trend, these Conventions might be expected to enter into force as early as 1984. In this regard, the Secretary of the Commission reported that the Council for Mutual Economic Assistance (CMEA) had organized a seminar on the two Conventions at which general support was expressed for the Conventions. In addition, the Secretary expressed the hope that since the United Nations Convention on Contracts for the International Sale of Goods and INCOTERMS were mutually supplementary, the International Chamber of Commerce might promote the Convention in conjunction with INCOTERMS.

^aYearbook ... 1974, part three, I, B (A/CONF.63/15).

^bYearbook ... 1980, part three, I, C (A/CONF.97/18, annex II).

^cYearbook ... 1978, part three, I, B (A/CONF.89/13, annex I).

^dYearbook ... 1980, part three, I, B (A/CONF.97/18, annex I).

^eReproduced in this volume, part two, VI.

²⁴The Commission considered this subject at its 269th meeting on 24 May 1983.

121. As regards the United Nations Convention on Contracts for the International Sale of Goods, the Commission was informed that steps towards the ratification of this Convention were being taken in several States, and that some of these States anticipated that they would ratify the Convention in 1984.

122. The Secretary of the Commission stated that, once the Convention on the Limitation Period in the International Sale of Goods and the United Nations Convention on Contracts for the International Sale of Goods entered into force, the secretariat could concentrate its efforts on promoting the United Nations Convention on the Carriage of Goods by Sea. As regards this latter Convention, the Secretary of the Commission reported that the UNCTAD was also taking steps to promote this Convention, since the United Nations Convention on International Multimodal Transport of Goods was necessarily linked to the entry into force of the United Nations Convention on the Carriage of Goods by Sea. Moreover, the Secretary noted that, if the Commission undertook work on the topic of international terminal operators, this could help to promote interest in the United Nations Convention on the Carriage of Goods by Sea.

123. Several States indicated that the question of adhering to the United Nations Convention on the Carriage of Goods by Sea was under active consideration, and that the Convention was regarded favourably in various circles.

124. A view was expressed that the process of identifying and discussing problems and issues arising from the Convention should be accelerated. It was suggested that this could perhaps be accomplished through regional consultations among States interested in maritime transport.

CHAPTER VIII. TRAINING AND ASSISTANCE²⁵

Introduction

125. The Commission, at its fourteenth session,²⁶ agreed that it should continue to sponsor symposia and seminars on international trade law. It was considered desirable for these seminars to be organized on a regional basis. In this way, it was felt, a larger number of participants from a region could attend and the seminars would themselves help to promote the adoption of the texts emanating from the work of the Commission. The Commission welcomed the possibility that regional seminars might be sponsored jointly with regional organizations. The secretariat was requested to make such arrangements as it found desirable in this regard.

²⁵This subject was considered by the Commission at its 283rd meeting, on 2 June 1983.

²⁶Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 109 (Yearbook ... 1981, part one, A).

At its fifteenth session,²⁷ the Commission considered the progress made by the secretariat in organizing such symposia and seminars, and agreed that the secretariat should continue to explore various possibilities of collaborating with other organizations and institutions in the organization of such symposia and seminars.

126. By its resolution 37/106 of 16 December 1982, the General Assembly reaffirmed the importance, in particular for the developing countries, of the work of the Commission concerned with training and assistance in the field of international trade law, and welcomed the initiatives being undertaken to sponsor regional symposia and seminars. The Assembly also expressed its appreciation to those States that had made financial contributions to be used towards the financing of symposia and seminars and of other aspects of the training and assistance programme of the Commission, and to those Governments and institutions that were arranging symposia or seminars in the field of international trade law. Furthermore, the Assembly invited Governments, relevant United Nations organs, institutions and individuals to assist the secretariat in financing and organizing symposia and seminars.

127. The Commission had before it a report of the Secretary-General entitled "Training and assistance" (A/CN.9/240).²⁸ This report set out the steps taken by the secretariat to implement the decisions of the Commission and of the General Assembly. The report noted, in particular, the association of the secretariat with several regional seminars in the field of international trade law. The secretariat had co-operated with the Organization of American States (OAS) in a seminar organized by the Inter-American Juridical Committee of the OAS at Rio de Janeiro in August 1982 which considered, *inter alia*, the activities of the Commission and, in particular, the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980). The secretariat had participated in a seminar organized by the Council for Mutual Economic Assistance (Moscow, 14 and 15 April 1983) on the Vienna Sales Convention. The secretariat had also co-operated with the Regional Centre for Arbitration, Kuala Lumpur (established under the auspices of the Asian-African Legal Consultative Committee) in a seminar organized by the Centre (Kuala Lumpur, 2 and 3 November 1982) on aspects of the Commission's work on international commercial arbitration. The report noted that it was planned to collaborate in the holding of other regional seminars. The report also noted that, while the principal limitation on the organization of symposia and seminars was that not enough funds were available for this purpose, the secretariat would continue its efforts to explore all suitable opportunities for training and assistance, and to make the work of the Commission known.

²⁸Reproduced in this volume, part two, VII.

²⁷Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17* (A/37/17), para. 132 (Yearbook ... 1982, part one, A).

128. The Secretary of the Commission made a statement in which he outlined some of the projects planned for the ensuing year. He noted, in particular, that the secretariat of the Inter-American Juridical Committee of the OAS had agreed to incorporate the subject of the Hamburg Rules in the annual international law seminar of OAS at Rio de Janeiro in August 1983. He also noted that it was planned to collaborate with the International Trade Centre (UNCTAD/GATT) in a project to train governmental trade promotion agencies and private-sector organizations in developing countries on how they could advise exporters and importers on legal aspects of foreign trade.

Discussion at the session

129. The view was expressed that future reports on training and assistance should specify more clearly the extent and the manner of the involvement of the secretariat in the projects mentioned therein. It was also suggested that thought might be given to developing teaching material on international trade law which could be used in universities.

Decision of the Commission

130. The Commission expressed its appreciation of the endeavours made by the secretariat in the field of training and assistance, and approved the general approach taken by the secretariat in this area.

CHAPTER IX. RELEVANT GENERAL ASSEMBLY RESOLUTIONS, FUTURE WORK AND OTHER BUSINESS²⁸

A. Relevant General Assembly resolutions

1. General Assembly resolution on the work of the Commission

131. The Commission took note with appreciation of General Assembly resolution 37/106 of 16 December 1982 on the report of the Commission on the work of its fifteenth session.

2. General Assembly resolution on a unit of account and adjustment of limitations of liability

132. The Commission took note with appreciation of General Assembly resolution 37/107 of 16 December 1982 on provisions for a unit of account and adjustment of limitations of liability adopted by the Commission.

3. General Assembly resolution on international economic law

133. The Commission took note of General Assembly resolution 37/103 of 16 December 1982 on progressive development of the principles and norms of inter-

²⁸The Commission considered this subject at its 283rd meeting, on 2 June 1983.

national law relating to the new international economic order. It also took note that the secretariat had conveyed to the United Nations Institute for Training and Research (UNITAR) information on the activities of the Commission relevant to the study being conducted by UNITAR on this issue.

134. A view was expressed that this study was connected with aspects of international trade law and that the Commission should make a more active contribution to it.

B. Newsletter

135. The Commission, at its fifteenth session, requested the secretariat to prepare a note for its sixteenth session which would consider the format a newsletter on the Commission might take, as well as the administrative and financial implications. At its current session, the Commission had before it a note of the secretariat which suggested that, for various financial and administrative reasons, it would be preferable for the secretariat to issue an informal newsletter reporting on matters of relevance to the work of the Commission addressed to participants at Commission and Working Group meetings, and perhaps to selected members of the general public who have consistently expressed interest in the work of the Commission (A/CN.9/XVI/R.1).

136. The view was expressed that an informal newsletter issued once or twice a year would serve to keep persons interested in the work of the Commission, and especially participants at meetings of the Commission and its Working Groups, abreast of new developments.

137. The view was also expressed that some thought should be given to the means by which information regarding court decisions interpreting the conventions prepared by the Commission could be widely disseminated once those conventions came into force, as was expected in the next few years. In this respect attention was drawn to the fact that the International Institute for the Unification of Private Law had for many years given wide coverage in its *Uniform Law Review* to the decisions concerning application and interpretation of the most significant conventions existing in the field of international trade law. It was suggested, therefore, that in view of the expertise acquired by the Institute in this difficult task, which calls for considerable expenditure in money as well as in terms of staff, the Commission should request its secretariat to explore with the Institute the possibility of concerted action in this connection.

138. The Commission requested the secretariat to provide it with more detailed information at its seventeenth session.

C. Other business

139. One delegation was of the view that the Commission should have a well thought out programme of work. A list of possible subjects—short-term and

medium-term—should be prepared and submitted to the States members of the Commission in advance so that the Governments could consult the various concerned ministries and departments and decide on the priority of subjects to be undertaken. *Ad hoc* decisions on one subject should be avoided. Priorities should be given to the subjects which were of a development nature and were directly connected to international trade. In deciding on the priority subjects, the Commission should co-ordinate with UNCTAD and UNIDO. Further, it should avoid duplication of work. The time had come when the Commission should also do some introspection about its objectives and methods and, in particular, on the question of how to achieve uniformity, as the question of "convention" or "model law" would continue to come up until a solution was found. The valuable time of the Commission should not be wasted in endless debate on this question. The secretariat should try to find a compromise solution. Further, this Commission should adhere to its age-old tradition of reaching decisions by consensus.

D. Date and place of the seventeenth session of the Commission

140. It was decided that the seventeenth session of the Commission would commence on 25 June 1984 in New York. The secretariat was requested to decide whether the session should last for two or three weeks once it had received the comments of Governments and interested international organizations on the draft Convention on International Bills of Exchange and International Promissory Notes and the draft Convention on International Cheques.

E. Sessions of the Working Groups

141. It was decided that the Working Group on International Contract Practices would hold its sixth session from 29 August to 9 September 1983 at Vienna and its seventh session from 6 to 17 February 1984 in New York.

142. It was decided that the fifth session of the Working Group on the New International Economic Order would be held from 23 January to 3 February 1984 in New York.

F. Composition of the Working Group on International Contract Practices

143. It was decided that the membership of the Working Group on International Contract Practices should be expanded to include all States members of the Commission.

ANNEX I

Uniform Rules on Contract Clauses for an Agreed Sum Due upon Failure of Performance

[Annex reproduced in part three, II, A, in this volume]

ANNEX II

**Draft United Nations Convention on Contract Clauses
for an Agreed Sum Due upon a Failure of Performance**

[Annex reproduced in part three, II, B, in this volume]

ANNEX III

List of documents before the Commission[Annex not reproduced. See check-list of UNCITRAL
documents at the end of this volume]**B. United Nations Conference on Trade and Development (UNCTAD):
extract from the report of the Trade Development Board on its twenty-seventh
session (Geneva, 3-20 October 1983) (TD/B/973)^a***"B. Progressive development of the law of international trade: sixteenth annual
report of the United Nations Commission on International Trade Law**"(Agenda item 7 (b))*

"499. For the consideration of this item, the Board had before it the report of the United Nations Commission on International Trade Law on the work of its sixteenth session,⁶⁷ distributed under cover of TD/B/968.

"Action by the Board

"500. At its 619th meeting, on 4 October 1983, the Board took note of the report of the United Nations Commission on International Trade Law on its sixteenth session."

⁶⁷Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17 (A/38/17)."
(Reproduced in this volume, part one, A).

⁶⁹December 1983. Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17 (A/38/15) (16 February 1984), vol. II, chapter II, division C: Other decisions; Other action taken by the Board.

C. General Assembly: report of the Sixth Committee (A/38/667)^a

INTRODUCTION

1. At its 3rd plenary meeting, on 23 September 1983, the General Assembly decided to include in the agenda of its thirty-eighth session the item entitled "Report of the United Nations Commission on International Trade Law on the work of its sixteenth session". At its 4th plenary meeting, on the same date, the Assembly decided to allocate it to the Sixth Committee.

2. The Sixth Committee considered this item at its 2nd to 8th meetings, from 28 September to 7 October, and at its 59th meeting, on 30 November 1983. The summary records of those meetings (A/C.6/38/SR.2-8 and 59) contain the views of representatives who spoke during the consideration of this item.

3. At the 2nd meeting, on 28 September, the Chairman of the United Nations Commission on

International Trade Law at its sixteenth session introduced its report on the work of that session.¹

4. In addition to this report, the Committee had before it in connection with the item a note by the Secretary-General (A/C.6/38/L.18) relating to the consideration of the report by the Trade and Development Board of the United Nations Conference on Trade and Development.

CHAPTER I. CONSIDERATION OF PROPOSALS

5. At the 59th meeting, on 30 November, the representative of Austria introduced a draft resolution (A/C.6/38/L.15) sponsored by Argentina, Australia,

¹Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17 (A/38/17) (reproduced in this volume, part one, A). The report was submitted pursuant to a decision by the Sixth Committee at its 1096th meeting, on 13 December 1968 (see Official Records of the General Assembly, Twenty-third Session, Annexes, agenda item 88, document A/7408, para. 3) (Yearbook ... 1968-1970, part two, I, B, 2).

^a8 December 1983, Official Records of the General Assembly, Thirty-eighth session, agenda item 127.

Austria, Brazil, Canada, Chile, Egypt, Finland, France, Germany, Federal Republic of, Greece, Hungary, Italy, Japan, Kenya, the Netherlands, Nigeria, the Philippines, Senegal, Singapore, Sweden, Thailand and Yugoslavia, later joined by Belgium, Cyprus, Jamaica, Morocco, Spain, Trinidad and Tobago and Turkey, as well as a draft resolution (A/C.6/38/L.16) sponsored by Australia, Austria, Chile, Egypt, Finland, Germany, Federal Republic of, Greece, Nigeria, the Philippines, Singapore and Thailand, later joined by Cyprus and Japan.

6. At the same meeting, the Committee adopted draft resolution A/C.6/38/L.15 by consensus (see para. 8, draft resolution I) and draft resolution A/C.6/38/L.16 without a vote (see para. 8, draft resolution II).

7. The representatives of Algeria and Tunisia spoke in explanation of vote before the vote and the represen-

tative of the United Kingdom spoke in explanation of vote after the vote concerning draft resolution A/C.6/38/L.16.

CHAPTER II. RECOMMENDATIONS OF THE SIXTH COMMITTEE

8. The Sixth Committee recommends to the General Assembly the adoption of the following draft resolutions:

[Text not reproduced in this section. The draft resolutions were adopted, with editorial changes, as General Assembly resolutions 38/134 and 38/135. See below, section D.]

D. General Assembly resolutions 38/134 and 38/135 of 19 December 1983^a

38/134. REPORT OF THE UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW^b

The General Assembly,

Having considered the report of the United Nations Commission on International Trade Law on the work of its sixteenth session,¹

Recalling that the object of the United Nations Commission on International Trade Law is the promotion of the progressive harmonization and unification of international trade law,

Recalling in this regard, its resolutions 2205 (XXI) of 17 December 1966, 3108 (XXVIII) of 12 December 1973, 34/142 of 17 December 1979, 36/32 of 13 November 1981, 36/111 of 10 December 1981 and 37/106 of 16 December 1982, as well as its previous resolutions concerning the reports of the United Nations Commission on International Trade Law on the work of its annual sessions,

Recalling also its resolutions 3201 (S-VI) and 3202 (S-VI) of 1 May 1974, 3281 (XXIX) of 12 December 1974 and 3362 (S-VII) of 16 September 1975,

Reaffirming its conviction that the progressive harmonization and unification of international trade law, in reducing or removing legal obstacles to the flow of international trade, especially those affecting the developing countries, would significantly contribute to universal economic co-operation among all States on a basis of equality, equity and common interests and to the elimination of discrimination in international trade and, thereby, to the well-being of all peoples,

Having regard for the need to take into account the different social and legal systems in harmonizing and unifying the rules of international trade law,

Stressing the usefulness and importance of sponsoring symposia and seminars, including those organized on a regional basis, for promoting better knowledge and understanding of international trade law and, especially, for the training of lawyers from developing countries in this field,

1. *Takes note with appreciation* of the report of the United Nations Commission on International Trade Law on the work of its sixteenth session;

2. *Commends* the United Nations Commission on International Trade Law for the progress made in its work and for having reached decisions by consensus;

3. *Calls upon* the United Nations Commission on International Trade Law, in particular its Working Group on the New International Economic Order, to continue to take account of the relevant provisions of the resolutions concerning the new international economic order, as adopted by the General Assembly at its sixth and seventh special sessions;

^aOfficial Records of the General Assembly, Thirty-eighth agenda item 127.

^bA/RES/38/134, 27 January 1984.

¹Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17 (A/38/17) (reproduced in this volume, part one, A).

I. INTERNATIONAL CONTRACT PRACTICES^a

Report of the Secretary-General: revised text of draft uniform rules on liquidated damages and penalty clauses (A/CN.9/235)^b

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INTRODUCTION

1. At its fourteenth session, the Commission considered draft uniform rules on liquidated damages and penalty clauses applicable to a wide range of international trade contracts prepared by its Working Group on International Contract Practices.¹ At that session, the Commission requested the Secretary-General to incorporate in the draft uniform rules such supplementary provisions as might be required if the rules were to take the form of a convention or model law, and to prepare a commentary on the model law. At its fifteenth session the Commission had before it the uniform rules incorporating such supplementary provisions, together with a commentary thereon.²

^aFor consideration by the Commission see Report, chapter II (part one, A).

^b31 March 1983. Referred to in Report, para. 13 (part one, A). See also annexes I and II to the Report (part three, II).

Yearbook references for United Nations conventions mentioned in the notes of this document are as follows: Yearbook ... 1974, part three, I, B (A/CONF.63/15) for the Convention on the Limitation Period in the International Sale of Goods; Yearbook ... 1980, part three, I, B (A/CONF.97/18, annex I) for the Convention on Contracts for the International Sale of Goods.

¹Report of the United Nations Commission on International Trade Law on the work of its fourteenth session (1981), *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), chapter III, A (Yearbook ... 1981, part one, A).

²A/CN.9/218 (Yearbook ... 1982, part two, I, A).

2. At its fifteenth session, the Commission considered whether the uniform rules should be embodied in a convention, in a model law or in general conditions. The Commission decided to defer a decision on this question till its sixteenth session.³

3. The Commission also discussed the substance of articles A, paragraph 1 (the type of clause to be covered in the uniform rules), D, E, F and G on the draft uniform rules.⁴ After its discussion, the Commission referred these articles to a Drafting Group for consideration in the light of the discussion in the Commission. The Drafting Group was of the view that it would be unable to complete its work in preparing a revised text of the draft uniform rules in the time available. Accordingly, the Commission decided that the secretariat should submit a revised text for consideration by the Commission at the sixteenth session, taking into account the discussion at the fifteenth session and within the Drafting Group.⁵

4. The present document has been prepared in response to that decision. It sets out the draft articles considered at the fifteenth session (headed "previous

³Report of the United Nations Commission on International Trade Law on the work of its fifteenth session (1982), *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17* (A/37/17), chapter II, paragraph 17 (Yearbook ... 1982, part one, A).

⁴*Ibid.*, paragraphs 18-39.

⁵*Ibid.*, paragraph 40.

draft"), and sets out thereunder the corresponding revised draft articles (headed "revised draft"). Two draft articles (articles X and Y) are new articles drafted as a result of the discussions. Explanatory footnotes to the draft articles are included. In preparing the revised draft, an attempt has been made to reflect most of the suggestions for modification of the rules which received support during the discussions at the fifteenth session. Alternative suggestions are advanced where there was no prevailing view as to the desired modifications. Some suggestions are also made of a purely drafting nature.

5. For convenience of reference, the articles not considered at the fifteenth session (article A, paragraphs 2 and 3, and articles B and C) are also set out in the present document.

PART I. THE RULES: SCOPE OF APPLICATION AND GENERAL PROVISIONS

Article A, paragraph (1)

Previous draft (draft Convention)

"(1) This Convention applies to contracts in which the parties have agreed [in writing]⁶ that, upon a total or partial failure of performance by a party (the obligor), another party (the obligee) is entitled to recover, or to forfeit⁷ an agreed sum of money when, at the time of the conclusion of the contract, the parties have their places of business in different Contracting States."

Previous draft (draft Model Law)

"(1) This law applies to contracts in which the parties have agreed [in writing]⁶ that, upon a total or partial failure of performance by a party (the obligor), another party (the obligee) is entitled to recover, or to forfeit⁷ an agreed sum of money:

⁶"[in writing]". While there was no consensus during the deliberations as to whether this requirement should be maintained, the prevailing view was that, if the form of a model law were adopted for the uniform rules, the issue of formal requirements for the agreement should be left to be determined by the State adopting the law. If the form of a Convention were adopted, the solution adopted in articles 11, 29 and 96 of the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980) (hereinafter referred to as the "Sales Convention") should be adopted.

⁷"Forfeit". While there was general agreement that the rules should cover forfeiture as delimited in the commentary to the previous draft rules (A/CN.9/218, para. 20) (Yearbook ... 1982, part two, I, A), concern was expressed that the translation of "forfeit" in the various language versions was unclear or inappropriate. In the revised draft rules, alternative solutions are provided. The first (suggested in the Drafting Group established at the fifteenth session of the Commission) is to substitute the phrase "is entitled to an agreed sum of money" for the phrase "is entitled to recover, or to forfeit an agreed sum of money". A commentary would then explain the scope of the phrase "is entitled to". The second is merely to substitute the word "withhold" for the word "forfeit", as the translation of "withhold" does not appear to pose the same difficulties.

"(a) When, at the time of the conclusion of the contract, the parties have their places of business in different States, and

"(b) When the rules of private international law lead to the application of the law of (the State adopting the Model Law)."

Revised draft (draft Convention)

"(1) This Convention applies:

"(a) To contracts in which the parties have agreed that, upon a total or partial failure of performance by a party (the obligor), the other party⁸ (the obligee) is entitled to [recover or to withhold]⁷ an agreed sum of money from the obligor,⁸ [where such sum is intended as a pre-estimate of damages, or as a security for performance, or both] [where such sum is intended as a pre-estimate of damages to be paid by the obligor for loss suffered by the obligee as a consequence of that failure, or as a penalty for that failure, or both]⁹, and

"(b) Where, at the time of the conclusion of the contract, the parties have their places of business in different Contracting States, [or where the parties have their places of business in different States and the rules of private international law lead to the application of the law of a Contracting State¹⁰].

⁸*Exclusion of guarantees.* There was general agreement that the rules should not apply when parties had provided that the sum agreed as liquidated damages or a penalty could be claimed under a guarantee (i.e. it is agreed between the parties that the obligor is to arrange for a guarantee to be opened by a financial institution in favour of the obligee, and that under this guarantee the obligee can claim from the financial institution the agreed sum if it falls due). To exclude such cases, the words "the other party (the obligee)" have been substituted for the words "another party (the obligee)", and the words "from the obligor" have been added.

⁹*Types of agreements covered by the rules.* It was noted that while the rules were only intended to cover agreements for liquidated damages and penalties, the wording of the previous draft rules might cover other types of agreements (e.g. parties had provided that an agreed sum was to be the payment for proper performance, but was to be withheld if performance was defective; parties had provided that an advance payment made by one party was recoverable by him if performance by the other party was defective; parties had provided that one party could make payment by instalments, but on default in the payment of any one instalment all outstanding instalments became immediately payable). In the revised draft rules, alternative solutions are provided. The first (suggested in the Drafting Group established at the fifteenth session of the Commission) is to add after the words "agreed sum of money from the obligor," the following words: "where such sum is intended as a pre-estimate of damages, or as a security for performance, or both". Because of the ambiguity of the word "security" in this solution, an alternative solution is to embody the same idea in more explicit terms by adding the following words: "where such sum is intended as a pre-estimate of damages to be paid by the obligor for loss suffered by the obligee as a consequence of that failure, or as a penalty for that failure, or both". The use of both the terms "pre-estimate of damages" and "penalty" in the latter wording would also clarify to those accustomed to common law concepts that the rules covered both liquidated damages and penalties as understood in the common law.

¹⁰If the uniform rules were to take the form of a Convention, it was suggested that the conditions under which the Convention would apply should be aligned with the conditions under which the Sales Convention applied. Accordingly, the article has been modified to bring about such alignment.

"(1 *bis*) Except as expressly provided in this Convention, it is not concerned with the validity of the contract or of any of its provisions."¹¹

Revised draft (draft Model Law)

"(1) This law applies:

"(a) To contracts in which the parties have agreed that, upon a total or partial failure of performance by a party (the obligor), the other party⁸ (the obligee) is entitled to [recover or to withhold]⁷ an agreed sum of money from the obligor,⁸ [where such sum is intended as a pre-estimate of damages, or as a security for performance, or both] [where such sum is intended as a pre-estimate of damages to be paid by the obligor for loss suffered by the obligee as a consequence of that failure, or as a penalty for that failure, or both]⁹, and

"(b) Where, at the time of the conclusion of the contract, the parties have their places of business in different States, and the rules of private international law lead to the application of the law of (the State adopting the Model Law).

"(1 *bis*) Except as expressly provided in this law, it is not concerned with the validity of the contract or of any of its provisions."¹¹

Article A, paragraphs (2) and (3)¹²

"(2) The fact that the parties have their places of business in different States is to be disregarded whenever this fact does not appear either from the contract or from any dealings between, or from information disclosed by, the parties at any time before or at the conclusion of the contract.

"(3) Neither the nationality of the parties nor the civil or commercial character of the parties or of the contract is to be taken into consideration in determining the application of this (Convention) (law)."

Article B¹³

"For the purposes of this (Convention) (law):

"(1) 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.

"(2) If a party does not have a place of business, reference is to be made to his habitual residence."

Article C¹⁴

"This (Convention) (law) does not apply to contracts concerning goods, other property or services which are to be supplied for the personal, family or household purposes of a party, unless the other party, at any time before or at the conclusion of the contract, neither knew nor ought to have known that the contract was concluded for such a purpose."

Article X (new article)¹⁵

"The parties may by agreement only derogate from or vary the effect of articles D, E and F of this (Convention) (law)."

Article Y (new article)¹⁶

"Where, in accordance with the provisions of this (Convention) (law) the obligee is entitled to require performance of an obligation, a court is not bound to enter a judgment for specific performance unless the court would do so in respect of similar contracts not governed by this (Convention) (law)."

PART II. SUBSTANTIVE PROVISIONS

Article D

Previous draft

"Unless the parties have agreed otherwise,¹⁷ the obligee is not entitled to recover or to forfeit the agreed sum if the obligor is not liable for the failure of performance."

¹⁴*Secretariat supplementary provision.* It is to some extent derived from the Limitation Convention, article 4 (a), and the Sales Convention, article 2 (a).

¹⁵There was general agreement on the substance of this new article. See footnotes 17, 19, 25 and 30, below.

¹⁶See footnote 20, below.

¹⁷*Desirability of the power of modification.* Although opinions were divided as to whether parties should be given such a power of modification, there was support for the view that such a power might be acceptable if under article G, in addition to the case envisaged at present, a court or arbitral tribunal were to be authorized to reduce the agreed sum where parties had modified the rule contained in this article, and recovery or withholding of the sum in such circumstances by the obligee would be manifestly unfair. (See revised article G, subparagraph 2 (b) and footnote 34, below.) As to the drafting, there was general agreement that the power of the parties to modify the rule contained in the article should be deleted and set forth in a separate article. This separate article should also set forth the power to modify the rules contained in articles E and F. Accordingly, article X above has been added to the rules.

¹¹New paragraph (1 *bis*) states explicitly the understanding implicit in the previous draft of the uniform rules. Its language is based on article 4 (a) of the Sales Convention. It has been added in response to queries raised during the deliberations as to the extent to which the rules deal with the validity of the contract. As the opening phrase indicates, insofar as they provide that, subject to various articles of the rules, a penalty invalid under the common law is recoverable, the uniform rules expressly deal with the issue of validity.

¹²*Secretariat supplementary provisions.* Paragraph (2) is identical with the Convention on the Limitation Period in the International Sale of Goods (New York, 1974) (hereinafter referred to as the "Limitation Convention"), article 2 (b), and the Sales Convention, article 1 (2). Paragraph (3) is identical with the Limitation Convention, article 2 (e), and the Sales Convention, article 1 (3).

¹³*Secretariat supplementary provision.* It is identical with the Sales Convention, article 10, and in substance identical with the Limitation Convention, article 2 (c) and (d).

Revised draft

"If a failure of performance in respect of which the parties have agreed that the obligee is entitled to an agreed sum of money occurs, the obligee is entitled to the agreed sum unless the obligor [proves that he]¹⁸ is not liable^{18a} for the failure of performance."

*Article E**Previous draft*

"(1) Where the agreed sum is to be recoverable or forfeited on delay in performance of the obligation, the obligee is entitled to both performance of the obligation and the agreed sum.

"(2) Where the agreed sum is to be recoverable or forfeited on non-performance, or defective performance other than delay, the obligee is entitled either to performance, or to recover or forfeit the agreed sum, unless the agreed sum cannot reasonably be regarded as a substitute for performance.

"(3) The rules set forth above shall not prejudice any contrary agreement made by the parties."¹⁹

Revised draft²⁰

"(1) Where the contract provides that the obligee is entitled to the agreed sum on delay in performance of

¹⁸*Burden of proof.* Under one view expressed during the deliberations, the article should indicate that the obligor bears the burden of proving that he is not liable for the failure of performance if he wishes to defeat the obligee's claim to the agreed sum. Under another view, the issue of the burden of proof should be left to be determined by the applicable law. If the former view is adopted, the words ["proves that he"] may be added. It may be noted that article 79 (1) of the Sales Convention expressly indicates who bears the burden of proof when a party relies on an exemption:

Art. 79 (1): "A party is not liable for a failure to perform any of his obligations if he proves that the failure was due to an impediment beyond his control ..." (emphasis added).

^{18a}Whether the obligor is not liable would be determined by reference to the terms of the contract and the law which, under the rules of private international law, would be applicable to determine the rights and obligations of the parties. The obligor would not be liable if he has a sufficient defence for his failure of performance (e.g. an exemption clause is applicable).

¹⁹The power of the parties to modify the rules contained in this article is now set forth in a separate article (article X above), and accordingly this paragraph is deleted.

²⁰*Entitlement to require performance, paragraphs (1) and (2).* There was wide agreement that an article such as the present defining the relationship between the obligee's right to require performance of an obligation and his right to the agreed sum was desirable. However, it was noted that the various legal systems had different approaches to enforced performance, and there was general agreement that the uniform rules should not interfere with the conditions under which and the methods by which legal systems made orders for enforced performance. If an obligee chose to require performance, the extent of his remedies should be determined by the court. Accordingly, Article Y above, which is based on article 28 of the Sales Convention, has been added under which a court is not bound to enter a judgment for specific performance unless the court would do so in respect of similar contracts not governed by the Convention or law. The phrase "entitled to performance" has been changed to "entitled to require performance" to accord with the terminology of the Sales Convention.

an obligation, the obligee is entitled both to require performance of the obligation and to the agreed sum.²¹

"(2) Where the contract provides that the obligee is entitled to the agreed sum on non-performance of an obligation, or defective performance other than delay, the obligee is entitled either to require performance, or to the agreed sum. If, however, [the obligee proves that]²² the agreed sum cannot reasonably be regarded as a substitute for performance, the obligee is entitled both to require performance of the obligation and to the agreed sum."^{23,24}

*Article F**Previous draft*

"Unless the parties have agreed otherwise,²⁵ if a failure of performance in respect of which the parties have agreed that a sum of money is to be recoverable or forfeited occurs, the obligee is entitled, in respect of the failure, to recover or forfeit the sum, and is entitled to damages²⁶ to the extent of the loss not covered by the agreed sum, but only if he can prove that his loss grossly exceeds the agreed sum."

Revised draft²⁷

"Where the obligee is entitled to the agreed sum, he [is not entitled to damages] [may not assert a claim for damages] to the extent of the loss covered by the agreed

²¹*Substance of paragraph (1).* Subject to the qualifications noted above as to the enforceability of performance, there was wide acceptance of the substance of paragraph (1).

²²*Burden of proof.* To accommodate the suggestion that the paragraphs should clarify who bears the burden of proving that the agreed sum cannot reasonably be regarded as a substitute for performance, the addition of the words "[the obligee proves that]" is suggested.

²³*Drafting of paragraph (2).* There was general agreement that the circumstances when an obligee could only obtain either the performance of the agreed sum, and the circumstances when he could obtain both, should be set forth in separate sentences.

²⁴*Substance of paragraph (2).* The majority view regarded the substance of paragraph (2) as an acceptable compromise. A minority view noted that it was sufficient for the paragraph to provide an alternative choice between requiring performance or recovering or withholding the agreed sum. The cumulation of remedies provided in the second sentence might in some circumstances unjustly enrich the obligee.

²⁵The power of the parties to modify the rules contained in this article is now set forth in a separate article (article X above). Accordingly this opening phrase is deleted.

²⁶*Possible clarification as to the right to damages.* The discussion appeared to reveal the need for a possible clarification of the phrase "is entitled to damages" contained in the previous draft. It was suggested that these words might be interpreted as giving a right to damages under the article itself in the circumstances indicated therein (i.e. when the obligee can prove that his loss grossly exceeds the agreed sum), without the need to prove liability under the applicable law. The possibility of this interpretation might be reduced by the use of a phrase similar to the alternative phrase ["may not assert a claim for damages"] suggested in the revised draft.

²⁷The article has been modified to accord with the view widely expressed during the deliberations that it was unnecessary in this article to set forth the right of the obligee to recover the agreed sum, and that the article should only define the circumstances in which the obligee would be entitled to damages in addition to the agreed sum.

sum.^{27a} He [is also not entitled to damages] [may also not assert a claim for damages]²⁶ to the extent of the loss not covered by the agreed sum, unless he can prove that his loss grossly exceeds the agreed sum."²⁸

Article G

Previous draft

"(1) The agreed sum shall not be reduced by a court or arbitral tribunal.

"(2) However, the agreed sum may be reduced if it is shown to be grossly disproportionate in relation to the loss that has been suffered by the obligee, and if the agreed sum cannot reasonably be regarded as a genuine pre-estimate by the parties of the loss likely to be suffered by the obligee."²⁹

Revised draft³⁰

"(1) The agreed sum shall not be reduced by a court or arbitral tribunal.

"(2) Notwithstanding the provisions of paragraph (1) of this article,³¹ the agreed sum may [shall] be reduced

[though not below the extent of the loss suffered by the obligee];³²

"(a) If the agreed sum is shown to [be grossly disproportionate in relation to] [grossly exceed]³³ the loss that has been suffered by the obligee; or

"(b)³⁴ (i) If parties have provided that the obligee is entitled to the agreed sum even when the obligor is not liable for the failure of performance, and

"(ii) if the obligee claims the agreed sum when the obligor is not liable for the failure of performance, and

"(iii) if entitlement to the agreed sum would be manifestly unfair in the circumstances."

³²*Discretion as to reduction.* It was noted that the article left two issues to the discretion of the court or tribunal: whether to reduce the agreed sum, even if the conditions for reduction were satisfied, and the extent to which the agreed sum was to be reduced if it were decided to make a reduction. Under one view this created an undesirable measure of uncertainty as to the operation of the article. The words "[shall]" and "[though not below the extent of the loss suffered by the obligee]" contain proposals directed to these issues.

³³Under article F, in order to recover damages in excess of the agreed sum, the obligee must prove that his loss "grossly exceeds" the agreed sum. The use of the same phrase is proposed in the present article, instead of the phrase "grossly disproportionate in relation to" used in the previous draft. The latter phrase appears to have the same meaning as the former in the context of the present article.

³⁴*Relation between article D and new subparagraph 2 (b).* Subparagraph 2 (b) has been added for the reasons set forth in footnote 17 above to article D. The widening of the power of reduction under the present article was proposed only as a remedy to cases of hardship which might occur if parties were permitted to modify Rule D, i.e. where the parties had provided that the obligee would be entitled to the agreed sum even if the obligor was not liable for the failure of performance, and the obligee did in fact make a claim when the obligor was not liable. If the agreed sum so claimed grossly exceeded the loss suffered by the obligee, the obligor could claim a reduction under subparagraph 2 (a) of this article. It was proposed during the deliberations, however, that even if the agreed sum did not grossly exceed the loss suffered by the obligee, the obligor should be entitled to some relief, and that a court or arbitral tribunal should be given the power to reduce the agreed sum if enforcing payment of the sum would be manifestly unfair to the obligor. Article 4 (1) of the common provisions set forth in the annex to the Benelux Convention relating to the Penalty Clause, adopted at The Hague on 26 November 1973 provides: "A la demande du débiteur, le juge peut, si l'équité l'exige manifestement, modérer les effets de la clause pénale, . . ."

^{27a}It has been noted that, while it was clearly understood during the deliberations that the obligee was not entitled to damages to the extent of the loss covered by the agreed sum, the previous draft only dealt with the obligee's entitlement to damages to the extent of the loss not covered by the agreed sum. The article has been modified to make explicit the understanding reached during the deliberations.

²⁸There was considerable support for the view that the previous draft tended to obscure the fact that very often the agreed sum was intended by the parties to be a ceiling on liability, and instead tended to focus on the circumstances in which the ceiling could be avoided. Drafting changes have been made to secure a better balance, without changing the substance of the article.

²⁹The prevailing view was that the article should not require as a condition for reduction that the agreed sum could not reasonably be regarded as a genuine pre-estimate by the parties of the loss likely to be suffered by the obligee.

³⁰*Mandatory character of article G:* There was general agreement that parties should have no power to modify article G, and that this fact should be made explicit (see article X, above).

³¹It was suggested that the fact that paragraph (2) qualified paragraph (1) should be made clearer. Accordingly, the word "However" in the previous draft has been replaced by the phrase "Notwithstanding the provisions of paragraph (1) of this article". The latter phrase follows article 44 of the Sales Convention.

II. INTERNATIONAL PAYMENTS^a

Note by the secretariat: electronic funds transfers progress report (A/CN.9/242)^b

1. The Commission, at its eleventh session, included as an item in its programme of work the legal problems arising out of electronic funds transfers.¹ At its twelfth session the Commission, recognizing the complex technical aspects of the subject, requested the secretariat to continue the preparatory work on this subject within the framework of the UNCITRAL Study Group on International Payments, a consultative group composed of representatives of banking and trade institutions.²

2. At its fifteenth session the Commission had before it a report of the Secretary-General (A/CN.9/221)^c which described some of the legal problems arising in this field and contained the recommendations of the Study Group as to the future work which the Commission might undertake.

3. Following the recommendations contained in this report the Commission, at its fifteenth session, decided that the secretariat should begin the preparation of a legal guide on electronic funds transfers, in co-operation with the UNCITRAL Study Group on International Payments.³ It was suggested that the legal guide should

be designed to identify the legal issues, describe the various approaches, point out the advantages and disadvantages of each approach and suggest alternative solutions.

4. After the fifteenth session of the Commission, at the invitation of the Bank for International Settlements the secretariat attended a meeting of Central Bank Legal Experts of the Group of Ten and Switzerland, held at Basle on 20 and 21 October 1982, to exchange views on certain legal aspects of electronic funds transfers. The report of the Secretary-General to the fifteenth session of the Commission (A/CN.9/221) had been distributed in advance to the participants. The conclusion of the meeting was that there was great scope for a legal guide on electronic funds transfers such as that envisaged by the Commission and that the Commission was the most appropriate forum for a project of this kind.

5. The secretariat has begun the work leading to the preparation of the legal guide. The draft of a research paper was prepared by the secretariat based upon the banking law and practice in several countries. This research paper formed a basis for the discussion by the Study Group at its meeting held at Florence, Italy, 27-29 April 1983.

6. The Study Group will continue to collaborate with the secretariat in the preparation of several draft chapters of the legal guide at its next session scheduled for October in Vienna and at a further session tentatively scheduled for April 1984.

7. It is expected that some draft chapters of the legal guide will be made available to the seventeenth session of the Commission for general observation.

^aFor consideration by the Commission see Report, chapter III, B (part one, A).

^b6 May 1983. Referred to in Report, para. 84 (part one, A).

^cYearbook ... 1982, part two, II, C.

¹Report of the United Nations Commission on International Trade Law on the work of its eleventh session, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17 (A/33/17)*, para. 67 (Yearbook ... 1978, part one, II, A).

²Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17 (A/34/17)*, para. 56 (Yearbook ... 1979, part one, II, A).

³Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17 (A/37/17)*, para. 73; A/CN.9/230, para. 73 (Yearbook ... 1982, part one, A).

III. INTERNATIONAL COMMERCIAL ARBITRATION^a

A. Report of the Working Group on International Contract Practices on the work of its fourth session (Vienna, 4-15 October 1982) (A/CN.9/232)^b

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Introduction

1. At its fourteenth session the Commission decided to entrust the Working Group on International Contract Practices with the task of preparing a draft model law on international commercial arbitration.¹

2. The Working Group commenced its work at its third session by discussing all but four of a series of questions prepared by the secretariat designed to establish the basic features of a draft model law.²

3. The Working Group consists of the following States members of the Commission: Austria, Czechoslovakia, France, Ghana, Guatemala, Hungary, India, Japan, Kenya, Philippines, Sierra Leone, Trinidad and

Tobago, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland and United States of America.

4. The Working Group held its fourth session at Vienna from 4 to 15 October 1982. All the members were represented except Ghana, Guatemala, India, Sierra Leone and Trinidad and Tobago.

5. The session was attended by observers from the following States: Argentina, Australia, Belgium, Brazil, Chile, China, Ecuador, Egypt, Finland, German Democratic Republic, Germany, Federal Republic of, Greece, Holy See, Italy, Mexico, Panama, Republic of Korea, Sweden, Switzerland, Thailand and Venezuela.

6. The session was attended by observers from the following intergovernmental organization: Hague Conference on Private International Law, and from the following international non-governmental organizations: International Chamber of Commerce and International Council for Commercial Arbitration.

7. The Working Group elected the following officers:
Chairman: Mr. I. Szasz (Hungary)
Rapporteur: Mr. S. K. Muchui (Kenya)

^aFor consideration by the Commission see Report, chapter IV (part one, A).

^b10 November 1982. Referred to in Report, para. 86 (part one, A).

¹Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 70 (Yearbook ... 1981, part one, A).

²Report of the Working Group on International Contract Practices on the work of its third session, A/CN.9/216 (Yearbook ... 1982, part two, III, A).

8. The following documents were placed before the session:

(a) Report of the Secretary-General: Possible features of a model law on international commercial arbitration (A/CN.9/207).^c

(b) Report of the Working Group on International Contract Practices on the work of its third session (New York, 16-26 February 1982) (A/CN.9/216).

(c) Note by the secretariat: Possible features of a model law on international commercial arbitration: Questions for discussion by the Working Group (A/CN.9/WG.II/ WP.35).^d

(d) Provisional agenda for the session (A/CN.9/WG.II/ WP.36).

(e) Note by the secretariat: Model law on international commercial arbitration: draft articles 1 to 24 on scope of application, arbitration agreement, arbitrators, and arbitral procedure (A/CN.9/WG.II/ WP.37).^e

(f) Note by the secretariat: Model law on international commercial arbitration: draft articles 25 to 36 on award (A/CN.9/WG.II/ WP.38).^f

9. The Working Group adopted the following agenda:

- (a) Election of officers
- (b) Adoption of the agenda
- (c) Consideration of possible features and of draft articles of a model law on international commercial arbitration
- (d) Other business
- (e) Adoption of the report

Deliberations and decisions

10. The Working Group continued and completed its preliminary exchange of views on the questions contained in the note by the secretariat (A/CN.9/WG.II/ WP.35). The Group considered questions 6-6 to 6-9 and some further issues of arbitral procedure.

11. The Working Group also considered tentative draft articles 1 to 36 of a model law on international commercial arbitration as prepared by the secretariat (set forth in A/CN.9/WG.II/ WP.37 and 38). The Group requested the secretariat to redraft these articles in the light of its discussion and decisions at the present session.

12. The Working Group decided to hold its fifth session from 22 February to 4 March 1983 in New York, as authorized by the Commission at its fifteenth session.³

^cYearbook ... 1981, part two, III.

^dYearbook ... 1982, part two, III, B.

^eReproduced in this volume, part two, III, B, 1.

^fReproduced in this volume, part two, III, B, 2.

³Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17* (A/37/17), para. 148 (Yearbook ... 1982, part one, A).

I. Consideration of possible features of a draft model law on international commercial arbitration

13. The Working Group decided to commence its work by considering the four questions prepared by the secretariat which had not been discussed at the third session of the Working Group.

A. MEANS OF RECOURSE

Setting aside or annulment of award (and similar procedures)

Question 6-6: Should the model law provide for only one type of action of "attacking" an award, e.g. setting aside (leaving aside here recourse against *exequatur*, but see questions 6-8)?

14. There was general agreement that the model law should streamline the various types of recourse against an arbitral award and should provide for only one type of action of "attacking" an award. However, it was observed that the acceptability of this approach may depend on the decision as to which arbitral awards were international, and therefore subject to this law, and that the position on this question may not be final.

Question 6-7: If so, on what grounds should such an action be successful? For example, would it be acceptable to restrict the grounds to those listed in article V, paras. (1) (a-d) and (2) (b) of the 1958 New York Convention,⁸ with a possible restriction of the "public policy" ground to "international public policy"?

15. There was general agreement that a restrictive approach in listing the grounds for the setting aside of awards should be adopted. Some doubt was expressed as to whether the reasons for setting aside needed to be restricted to those which are mentioned in the 1958 New York Convention. However, the prevailing view was that the grounds for setting aside should be restricted to those listed in article V, paras. (1) (a-d) and (2) (b) of that Convention.

16. Under one view the "public policy" ground for refusal of recognition or enforcement (article V, paragraph (2) (b)) should be further restricted and qualified as "international public policy". In this connection it was noted that the case law and doctrine of many countries showed a clearly detectable trend to apply a different standard of public policy in cases of international commercial arbitration from that applied in cases of domestic arbitration.⁴

17. Under another view the introduction of a concept of "international public order" was unnecessary and could give rise to difficulties in interpretation. It was noted that there might be a conflict between the

⁸United Nations, Treaty Series, vol. 330, No. 4739 (1959), p. 38.

⁴See Report of the Secretary-General: study on the application and interpretation of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958), A/CN.9/168, paras. 46-47 (Yearbook ... 1979, part two, III, C).

grounds for setting aside of an award for violation of "international public policy" under the model law and the grounds for refusing execution of a foreign award for violation of "public policy" under the 1958 New York Convention.

18. The Working Group requested the secretariat to prepare draft provisions for the attacking of an award reflecting two alternative approaches. One alternative should use the concept of "international public policy" while the other should retain the traditional concept of public policy, leaving it to the courts to interpret this concept adequately.

19. In this connection the Working Group recalled its position in respect of questions 6-3, 6-4 and 6-5 as expressed in paragraph 109 of the Report on the work of its third session (A/CN.9/216) in which it said that the model law should not set forth rules on remedies against decisions granting or refusing enforcement of awards. In view of the discussion at this session which favoured the listing of grounds for attacking awards the Working Group decided to reconsider at a later stage its position adopted at its third session in respect of questions 6-3, 6-4 and 6-5.

Question 6-8: Assuming that an action to set aside may be brought only on the same grounds as an appeal against the order of enforcement of the same award, should the recourse system be streamlined, e.g. by allowing only the action to set aside and regard it as implying an appeal against the *exequatur*, or by requiring in enforcement proceedings that the party against whom enforcement is sought would be given an opportunity to raise objections and, if he does so, to transfer the case to setting aside proceedings?

20. The Working Group expressed different views regarding the extent to which different means of recourse against arbitral awards could be streamlined. Under one view a maximum streamlining in respect of procedure and grounds for attacking awards was desirable. Under another view only the substantive grounds could be unified but not the various procedural aspects of the different means of recourse. The task would be complicated by the fact that in some countries there is no special *exequatur* procedure and an award is enforceable once it is issued.

21. The Working Group decided that the model law should not have detailed procedural rules on *exequatur* and setting aside but should place emphasis on the grounds for attacking awards. The Working Group requested the secretariat to prepare draft provisions along these lines.

Question 6-9: While rules of procedure concerning an action to set aside the award should the model law lay down, including any time-limits for bringing such action?

22. There was general agreement that the model law should contain no procedural rules for attacking an award except for a rule in respect of the time-limit during which the award could be attacked. There was general agreement that the time-limit should be rather short. A period of about three months was suggested. It was noted, however, that the period of time should be long enough to allow for the preparation and translation of the necessary documents. It was also suggested that the model law should specify the moment when the time-limit would begin to run.

B. FURTHER ISSUES OF ARBITRAL PROCEDURE

23. The Working Group noted that at its third session it had agreed that there were other issues of arbitral procedure that might be dealt with in the model law (A/CN.9/216, para. 72). Together with proposals accepted by the Working Group at its fourth session the issues still to be considered for possible inclusion in the model law are:

The point of time at which the limitation period is considered to have been interrupted by the commencement of an arbitration proceeding;

The period during which action must be taken to enforce an arbitral award;

The minimum contents of the statement of claim and defence;

The termination of arbitration proceedings;

The language to be used in the arbitration proceedings.

II. Consideration of tentative draft articles (1-36)

24. The Working Group proceeded to a consideration of tentative draft articles for a model law on international commercial arbitration prepared by the secretariat on the basis of the discussion and decisions of the Working Group at its third session.⁵

25. The Working Group noted that the structure and classification of the issues used in the basic report on possible features of a model law (A/CN.9/207) and in the working paper submitted to its third session (A/CN.9/WG.II/WP.35) as well as the report of that session (A/CN.9/216) had been maintained in the presentation of the draft articles so as to facilitate reference to the earlier discussions. It was agreed that the order of the articles as well as the headings and sub-headings would be altered once a clearer picture of the contents of the model law had emerged.

⁵The draft articles prepared by the secretariat are contained in documents A/CN.9/WG.II/WP.37 and 38.

A. SCOPE OF APPLICATION

*In general**Article 1*

26. The text of two alternative versions of article 1 as considered by the Working Group was as follows:

*Alternative A:**Article 1*

This Law applies:

"(a) To arbitration agreements concluded by parties to a commercial [or economic] transaction whose places of business are in different States [or, if their places of business are in the same State, where their contract is to be performed outside that State or where the subject-matter in dispute is property situated outside that State]; if a party has more than one place of business the relevant place of business is that which has the closest relationship to [the contract and its performance] [the conclusion of the arbitration agreement];"

"(b) To the preparation and conduct of arbitration proceedings based on agreements referred to in paragraph (a);"

"(c) To arbitral awards rendered in proceedings referred to in paragraph (b)."

*Alternative B:**Article 1*

"(1) This Law applies to international commercial arbitration as specified in paragraphs (2), (3) and (4) of this article.

"(2) 'Arbitration' covers arbitration agreements, the preparation and conduct of arbitration proceedings based on such agreements whether or not administered by a permanent arbitral institution, and the arbitral awards resulting therefrom.

"(3) 'Commercial' refers to the settlement of a dispute arising in the context of any commercial transaction [or similar economic relationship] [including supply or exchange of goods, construction of works, financing, joint venture and other forms of business co-operation, provision of services, except labour under a contract of employment].

"(4) 'International' are those cases where the arbitration agreement is concluded by parties whose places of business are in different States [or, if their places of business are in the same State where their contract is to be performed outside that State or where the subject-matter in dispute is property situated outside that State]. If a party has more than one place of business, the relevant place of business is that which has the closest relationship to [the contract and its performance] [the conclusion of the arbitration agreement]."

27. There was general agreement that the drafting technique used in alternative B was more precise than that used in alternative A and that it should, therefore, be used in the model law.

28. It was observed that a State could modify the provisions of the model law when adopting it. However, it was not felt that an express provision to this effect was needed.

*Alternative B:**Paragraph (2)*

29. Under one view paragraph (2) was superfluous and could be deleted. Under another view paragraph (2) was useful in that it gave a broad definition of "international commercial arbitration" and made it clear that it applied both to *ad hoc* and to institutional arbitrations. It was also noted that the definition was similar to that used in respect of the scope of application of the 1961 Geneva Convention.

Paragraph (3)

30. There was general agreement that the term "commercial" should be defined in a broad sense. Different views were expressed as to how this result could best be achieved, especially in view of the fact that in some legal systems the term "commercial" is defined more narrowly than it is in others.

31. Under one view it was unnecessary to include a definition of "commercial". Furthermore, no definition could delineate between the cases which should be included and those which should be excluded.

32. Among the suggestions made for altering the definition were that (a) a full stop be placed after the words "commercial transactions" with the rest of the definition deleted, (b) the word "commercial" be changed to "business", (c) additional examples, such as investment, factoring and leasing be added to the list of commercial transactions, and (d) the term "commercial" should be defined by way of listing legal relationships which were not commercial (e.g. consumer and employment relations). If an illustrative list of commercial activities were to be adopted the inclusion of "investment" was widely supported. A combined approach was also suggested by which the provision would list examples of both legal relationships which would be considered commercial and those which would not be considered commercial.

33. It was also suggested that some of the problems might be solved by an official commentary to the text.

Paragraph (4)

34. There was general agreement that the test of "internationality" should depend upon the character of the parties rather than the subject-matter of the dispute.

35. Under one view the determining test should be the nationality of the parties, whether they were natural

or legal persons. It was suggested that for this purpose the nationality of a legal person might be determined either by the place of incorporation or by the element of control.

36. The prevailing view, however, was that the determining test should be the place of business of the parties, even though it was recognized that the concept of place of business was a complex one and could give rise to difficulty of application in certain cases (e.g. when the party was temporarily doing business in a State or when the dispute involved business activities of a State). It was suggested that it was preferable to align the test of internationality with that in the 1961 Geneva Convention^h and the 1980 Vienna Sales Convention.ⁱ

B. ARBITRATION AGREEMENT

Form, contents, parties, domain

Article 2

37. The text of article 2 as considered by the Working Group was as follows:

Article 2

"'Arbitration agreement' is an undertaking by [parties] [physical persons or legal persons of private or public law] to submit to arbitration all or certain differences which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not [, concerning a subject-matter which could be disposed of by agreement of the parties under the applicable law]."

38. It was agreed that an "arbitration agreement" should be defined as an "agreement" rather than as an "undertaking" so as not to raise doubts as to the difference between an agreement and an undertaking.

39. The prevailing view was that the term "parties" was preferable to "physical persons or legal persons of private or public law." It was observed that the term "parties" was sufficiently clear and its use did not lead the Working Group to deal with questions of capacity, which it had decided at its previous session not to consider in the model law.

40. It was also decided to delete the words "concerning a subject-matter which could be disposed of by agreement under the applicable law." It was felt that there was no need to refer to national law in this context. It was also noted that at a later stage the Working Group would discuss the general question of choice of law.

Article 3

41. The text of article 3 as considered by the Working Group was as follows:

Article 3

"(1) The arbitration agreement, whether an arbitration clause in a contract or a separate agreement, shall be [concluded or evidenced] in writing."

"(2) 'Agreement in writing' includes an agreement contained in a document signed by the parties or contained in an exchange of letters, telegrammes or communications in another, [visible and] sufficiently permanent form. The reference in a contract to general conditions containing an arbitration clause constitutes an arbitration agreement provided that the contract is in writing. [However, an arbitration agreement also exists where one party to a contract refers in its written offer, counter-offer or contract confirmation to general conditions, or uses a contract form or standard contract, containing an arbitration clause and the other party does not object, provided that the applicable law recognizes formation of contracts in such manner]."

42. The prevailing view was to delete the words "concluded or evidenced". It was felt that they did not add any significant meaning to the provision. On the other hand it was noted that the word "evidenced" could be interpreted to mean that an oral agreement evidenced in writing would be considered to be a written arbitration agreement.

43. There was general agreement that the model law should contain a broad definition of that which constituted a writing, possibly broader than existing texts on international commercial arbitration. In this connection it was agreed that the words "in another visible and sufficiently permanent form" were useful in that they referred to new technological means of communicating and storing data, including arbitration agreements. On the other hand it was noted that the provision itself was unclear and it was not certain what technological means would fall within its scope.

44. The idea of the second sentence of paragraph (2) referring to arbitration agreements contained in general conditions was approved in principle. However, the Working Group thought that the term "reference" expressing the manner in which an arbitration agreement became a part of the contract was too vague. In this connection several approaches were suggested. Under one view the text of the arbitration agreement has to be before both parties in order to bind them. Under another view a reference in the contract between the parties to general conditions or other documents containing the arbitration clause was sufficient. As a middle ground between these positions, it was suggested that the document containing the arbitration agreement must be referred to in the contract in such a way that it becomes a part of the contract. The view was also

^hUnited Nations, Treaty Series, vol. 484, No. 7041 (1963-1964), p. 484.

ⁱYearbook ... 1980, part three, I, B (A/CONF.97/18, annex I).

expressed that in the resolution of this problem account must be taken of the fact that general conditions are usually prepared by the economically stronger party.

45. In respect of the last sentence of paragraph (2), it was noted that the problem it considers frequently arises in practice. However, the Working Group decided to delete this provision since it raised difficult problems of interpretation.

46. The Working Group considered whether national rules outside this model law would govern an oral arbitration agreement. The prevailing view was that this model law was intended to govern all international commercial arbitration agreements.

Separability of arbitration agreement

Article 4

47. The text of article 4 as considered by the Working Group was as follows:

Article 4

"For the purposes of determining whether the arbitral tribunal has jurisdiction, an arbitration clause which forms part of a contract shall be treated as an agreement independent of the other terms of the contract. A decision by the arbitral tribunal that the contract is null and void shall not entail *ipso jure* the invalidity of the arbitration clause."

48. The Working Group agreed that the text of article 4 was satisfactory.

Effect of the agreement

Article 5

49. The text of article 5 as considered by the Working Group was as follows:

Article 5

"A court before which an action is brought in a matter which is the subject of an arbitration agreement, shall, at the request of either party, refer the parties to arbitration unless it finds that the agreement is null and void, inoperative or incapable of being performed."

50. There was general agreement that article 5 should be included in the model law. There was also general agreement to include a provision along the lines of article VI, paragraph 1 of the 1961 Geneva Convention which would limit the period of time during which a party could object to the jurisdiction of the court on the grounds of the existence of an arbitration agreement.

51. It was suggested that article 5 should be modified to permit a court to refuse to refer the parties to arbitration if an award made in such an arbitration could not be enforced in the State in question. It was pointed out, however, that such a suggestion goes

against the idea of this model law, which is to promote international commercial arbitration. Moreover, until the award has been made it may not be clear whether it could be enforced in that State. In any case the award might well be enforceable in other States.

Article 6

52. The text of article 6 as considered by the Working Group was as follows:

Article 6

"A request for interim measures of protection addressed by any party to a court, whether before or during arbitration proceedings, shall not be deemed incompatible with the agreement to arbitrate or as a waiver of that agreement."

53. The Working Group was in agreement that the policy expressed by the current text should be retained. It was suggested, however, that the provision should be redrafted to express the view that it was the action of the court in granting interim relief that was compatible with the arbitration agreement. It was pointed out that the text of article 6 was based upon article 26 (3) of the UNCITRAL Arbitration Rules, which were drafted from the viewpoint of the parties, while a different approach was appropriate in a model law.

54. On the other hand it was pointed out that the provision was intended to say that a party had the right to request interim measures of relief from a court pending the final award in the arbitration proceedings. This approach to the question had already been taken in article VI, paragraph 4 of the 1961 Geneva Convention.

55. The Working Group decided to retain the current text at this time.

56. A drafting suggestion was made that "any party" should be used whenever multi-party arbitration could be covered and "either party" should be used only if two-party arbitration alone could be envisaged.

C. ARBITRATORS

Qualifications, challenge (and replacement)

Article 7

57. The text of article 7 as considered by the Working Group was as follows:

Article 7

"A prospective arbitrator shall disclose to those who approach him in connection with his possible appointment any circumstances likely to give rise to justifiable doubts as to his impartiality or independence. An arbitrator, once appointed or chosen, shall disclose such circumstances to the parties unless they have already been informed by him of these circumstances."

58. There was general agreement that the article was acceptable. It was suggested that the duty to disclose was a continuing one and that this should be reflected more clearly in the wording of the article.

Article 8

59. The text of article 8 as considered by the Working Group was as follows:

Article 8

"(1) An arbitrator may be challenged only if circumstances exist that give rise to justifiable doubts as to his impartiality or independence."

"(2) A party may challenge the arbitrator appointed by him only for reasons of which he becomes aware after the appointment has been made."

60. It was noted that the word "only" in paragraph (1) (which was omitted in the French text) was intended to limit the grounds for challenging an arbitrator to justifiable doubts as to his impartiality or independence. It was suggested that this decision should be reviewed since there might be other grounds on which a party should be able to challenge an arbitrator. In this connection a question was raised as to the relationship between article 8 and article 11.

Article 9

61. The text of article 9 as considered by the Working Group was as follows:

Article 9

"(1) Subject to the provisions of article 10, the parties are free to agree on the procedure for challenging an arbitrator.

"(2) Failing such agreement, the following procedure shall be used:

"(a) A party who intends to challenge an arbitrator shall, within fifteen days after knowing about the appointment of that arbitrator or about the circumstances mentioned in articles 7 and 8, send a written statement of the reasons for the challenge to the other party and to all arbitrators;

"(b) When an arbitrator has been challenged by one party, the other party may agree to the challenge. The arbitrator may also, after the challenge, withdraw from his office. In neither case does this imply acceptance of the validity of the grounds for the challenge;

"(c) If within [20] days after the challenge, the other party does not agree to the challenge and the challenged arbitrator does not withdraw, [the decision on the challenge shall be made by the Authority specified in article 17] [the challenging party may pursue his objections before a court only in an action for setting aside the award or any recourse against recognition and enforcement of the award]."

62. It was suggested that articles 9, 10 and 11 should be reorganized to make them more concise. It was further suggested that the relationship between the time-period of 15 days in paragraph (2) (a) and the time-period of 20 days in paragraph (2) (c) should be more clearly expressed and that the starting points of these time-limits should be clarified. It was noted that the implementation of this observation may become unnecessary if in redrafting this article the time-limits were deleted.

63. Practical and theoretical arguments were presented in favour of both alternatives in paragraph (2) (c). Although the view in favour of the first alternative received more support than did the second, the Working Group decided to retain both alternatives for future discussion.

Article 10

64. The text of article 10 as considered by the Working Group was as follows:

Article 10

"If, under any procedure for challenge agreed upon by the parties, the challenged arbitrator does not withdraw or the challenge is not sustained by the person or body entrusted with the decision on the challenge, the challenging party may [request the Authority specified in article 17 to make a final decision on the challenge] [pursue his objections before a court only in an action for setting aside the award or any recourse against recognition and enforcement of the award]."

65. The Working Group deferred the discussion on this article until the re-arrangement of articles 9, 10 and 11 has been made in accordance with the decision under article 9.

Article 11

66. The text of article 11 as considered by the Working Group was as follows:

Article 11

"Unless the parties have agreed otherwise, the following procedure shall be used in the event that an arbitrator [fails to act] [does not perform his functions in accordance with the instructions of the parties and in an impartial, proper and speedy manner] or in the event of the *de jure* or *de facto* impossibility of his performing his functions:

"(a) Any party who wishes that, for any of these reasons, the mandate of an arbitrator be terminated shall send a written statement of the reasons to the other party and to all arbitrators;

"(b) If, within [20] days after the notification, the other party does not agree to the termination of the mandate and the arbitrator does not withdraw from his office, the party may request the Authority specified in article 17 to make a final decision thereon."

67. The view was expressed that the provisions of this article were too detailed and that a party might rely on them merely to prolong the arbitral proceedings.

68. The prevailing view was that the first alternative text in the square brackets was more appropriate. The second alternative text was considered to be too broad in scope because it dealt both with cases in which the actions of an arbitrator gave rise to challenge and cases in which the conduct of the proceedings was not sufficiently expeditious.

69. It was suggested that the expression "fails to act" might in some cases not be sufficiently precise and that some additional clarifying provisions might be appropriate. It was concluded, however, that such further clarifications would not facilitate the interpretation of the article and might make it too inflexible.

Article 12

70. The text of article 12 as considered by the Working Group was as follows:

Article 12

"In the event of the termination of the mandate of an arbitrator or in the event of his death or resignation during the course of the arbitration proceedings, a substitute arbitrator shall be appointed according to the rules that were applicable to the appointment of the arbitrator being replaced, unless the parties agree on another appointment procedure [or decide to terminate the arbitration proceedings]."

71. The Working Group accepted the principle of this article. It was understood that article 12 also covered the case where the mandate of an arbitrator was terminated, or where an arbitrator withdrew from his office, as a result of a challenge in accordance with articles 9 to 11.

72. The view was expressed that it should be made clear that the parties may deviate from this provision. With such a clarification the last words in square brackets could be deleted. A special provision was suggested for cases in which the arbitrator named in the arbitration agreement became incapacitated or died. It was thought that in such cases the arbitration agreement should lapse. It was also suggested that the articles on challenge and replacement should be placed after the articles on appointment of arbitrators.

Number and appointment of arbitrators

Article 13

73. The text of article 13 as considered by the Working Group was as follows:

Article 13

"(1) In arbitration governed by this Law, nationals of any State may be appointed as arbitrators.

"(2) An arbitration agreement is invalid [if] [to the extent that] it accords one of the parties a predominant position with regard to the appointment of arbitrators."

74. The Working Group supported the policy underlying paragraph (1) of article 13. It was also agreed that such a rule should be addressed to the national legislators, who in some cases have restricted the freedom of the parties in this respect, and not to the parties or to the party-appointed arbitrators. One possible way to achieve that was to add to paragraph (1) of this article the words "subject to the arbitration agreement". It was also suggested that this point could be made clearer by a provision that no person should be disqualified by law from being appointed as an arbitrator on the ground of his nationality.

75. As to paragraph (2) under one view it dealt with an exceptional situation that did not need to be regulated by the model law. Under the prevailing view, however, the model law should offer protection to a party when the other party had a predominant position with regard to the appointment of arbitrators.

76. Arguments were expressed in favour of both alternative wordings in square brackets and no decision was reached. Under one view the arbitration agreement giving a predominant position to one party should be invalid. In support of this view it was stated that an arbitration agreement contrary to the fundamental principle of equality of parties should not be enforceable. Under another view only the appointing procedure giving a predominant position to one party should be inoperative while the basic agreement of the parties to resort to arbitration should be respected.

77. In discussing this article a general suggestion was made that it would be useful to make it clear in the model law (possibly in a separate article) from which provisions of the model law the parties cannot derogate.

Article 14

78. The text of article 14 as considered by the Working Group was as follows:

Article 14

"(1) Subject to the provisions of article 13 (2), the parties are free to determine the number of arbitrators.

"(2) Failing such determination,

Variant A:

"three arbitrators shall be appointed.

Variant B:

"the number of arbitrators shall be equal to the number of parties but increased by one if the number of parties is even.

Variant C:

"a sole arbitrator shall be appointed."

79. It was noted that the opening words to this article "subject to the provisions of article 13 (2)" were erroneously included.

80. It was agreed that variant B in paragraph (2) was not acceptable. It was pointed out that if a party were to commence arbitration proceedings against ten respondents in a single case, there would be one party-appointed arbitrator by the claimant and ten party-appointed arbitrators by the respondents.

81. Important arguments were expressed in favour of variants A and C. Under one view, supporting variant A, more weight should be given to the presumption that a panel of three arbitrators is more likely to guarantee equal treatment of both parties. Under another view the costs of arbitration make one arbitrator more favourable. Under a third view the model law should provide for one arbitrator but that on the request of either party the Authority provided in article 17 should have the power to decide that given the circumstances of the case there should be three arbitrators.

82. The Working Group decided to defer its decision on this point. It was suggested that in order to aid the Working Group in making its decision an evaluation should be made of international commercial arbitration practice, taking into account that policies in regard to the number of arbitrators may differ in international and national arbitration.

Article 15

83. The text of article 15 as considered by the Working Group was as follows:

Article 15

"(1) Subject to the provisions of article 13 (2), the parties are free to agree on the procedure of appointing the arbitrator or arbitrators.

"(2) If a party does not fulfill his obligations under an agreed appointment procedure, the other party may request the Authority specified in article 17 to take the required measure instead."

84. The objectives of this article were supported by the Working Group. The view was expressed that paragraph (2) should be elaborated to make it clear that the Authority specified in article 17 is the last resort after all other attempts for appointment have failed. In this respect it was suggested that a recourse to the Authority specified in article 17 should be available when the appointing authority under the arbitration agreement fails to appoint the arbitrator but that the diligent party must first apply to the appointing authority before it can apply to the Authority specified in article 17.

85. As an alternative, it was suggested that when a party does not fulfill his obligations under the agreed appointment procedure, the arbitrator appointed by the diligent party should act as a sole arbitrator. In response it was stated that such a result would be too

harsh and could work well only in a legal system in which the courts exercised a higher level of supervision than was provided for in these draft articles.

Article 16

86. The text of article 16 as considered by the Working Group was as follows:

Article 16

"(1) If the parties have not agreed on the appointment procedure,

"(a) In an arbitration with a sole arbitrator, the arbitrator shall be appointed by the Authority specified in article 17;

"(b) In an arbitration with three arbitrators, each party shall appoint one arbitrator and the two arbitrators thus appointed shall appoint the third arbitrator;

"[(c) In an arbitration with a number of arbitrators that is equal to the number of the parties or a multiple thereof, each party shall appoint one arbitrator or the respective multiple thereof;]

"[(d) In a multi-party arbitration with one arbitrator more than there are parties, each party shall appoint one arbitrator and the additional arbitrator shall be appointed by the Authority specified in article 17.]

"(2) If a party, in an arbitration referred to in paragraph (1) (b), [(c) or (d)], fails to make the required appointment within [30] days after having been so requested by the other party, or if, in an arbitration referred to in paragraph (1) (b), the two arbitrators fail to appoint the third arbitrator within [30] days after their appointment, the appointment shall be made by the Authority specified in article 17."

87. There was general agreement that subparagraphs (c) and (d) of paragraph (1) could be deleted. It was suggested that a provision on multi-party arbitration and on agreements for more than three arbitrators should be included in subparagraph (b).

88. There was general agreement that the article should be redrafted to make it clear that the parties should first try to reach an agreement on the appointment procedure and that the provisions of this article should come to their aid only if the parties were not able to agree.

Article 17

89. The text of article 17 as considered by the Working Group was as follows:

Article 17

"(1) The Authority, referred to in articles 9 (2) (c), 10, 11 (b), 15 (2), 16 (1) (a), (d), (2) and ..., shall be the ... (e.g. specific chamber of a given court, president of a specified court, to be determined by each State when enacting the model law).

"(2) The Authority shall act upon request by any of the parties or by the arbitral tribunal, unless otherwise provided for in a provision of this Law.

"(3) The Authority, in appointing an arbitrator, shall have regard to such considerations as are likely to secure the appointment of an independent and impartial arbitrator and, in the case of a sole or an additional arbitrator under article 16 (1) (a), (b) [or (d)], shall take into account as well the advisability of appointing an arbitrator of a nationality other than the nationalities of the parties."

90. It was agreed that the name of the Authority would be left blank in the model law and that each State which adopted the model law would have the option of designating that Authority it thought most appropriate. It was agreed that in doing so the State should name a judicial organ. A view was expressed that the Authority should possess experience in the field of arbitration and, therefore, that it would be useful if its competence would be centralized to the extent possible.

91. It was noted that the procedure to be used by the Authority would be determined by the rules of civil procedure governing that court.

92. The general view was that the procedure before the Authority should be as expeditious as possible. For this purpose it was suggested that there should be no appeal against the decisions of the Authority. Under another view any provision in respect of appeal against the decisions of the Authority should not be contrary to the basic principles of court control of arbitration. The proponents of this view suggested that a final decision on this question should be taken only after an analysis had been made of all cases which the Authority may be called upon to decide.

93. The question was raised as to the Authority of which State should exercise the functions of an Authority under article 17. In this connection differing views were expressed as to the nature of the rules which should be set forth in the model law.

94. Under one view it is not appropriate to set out special rules of international competence of the Authority because such rules would have to be too detailed. According to this view the question of international competence could be left to general rules on international conflicts of competence.

95. Under another view the model law should have a system of rules on international competence. Such a system should be based on the special functions of the Authority. In this connection it was suggested that the place of arbitration should be the primary criterion. In case the place of arbitration had not been designated, the procedural law to which the arbitral procedure was subjected might be the appropriate criterion. It was also suggested that the party refusing to co-operate in the appointing procedure should be put at risk that the other party could seize the Authority of his country.

96. Under a third view some rules on international competence would be useful and in this context the place of arbitration should be the decisive factor. The secretariat was requested to draft provisions to this effect and to indicate that where the place of arbitration had not been decided, reference should be made to the rules of private international law.

97. In respect of paragraph (2) of this article it was suggested that individual arbitrators could apply to the Authority in cases in which not all the members of the arbitral tribunal were appointed and therefore the arbitral tribunal could not be constituted. It was also suggested that arbitrators should be authorized to apply to the Authority only for appointment of other arbitrators and not in other cases in which the parties could apply to the Authority.

98. It was suggested that it would be useful to authorize the Authority to consult an arbitral institution in the fulfilment of its tasks. In response it was observed that the Authority was free to consult institutions of its choice and that a special provision to this effect was unnecessary.

D. ARBITRAL PROCEDURE

Place of arbitration

Article 18

99. The text of article 18 as considered by the Working Group was as follows:

Article 18

"(1) The parties to an arbitration agreement are free to determine, or to authorize a third person or institution to determine, the place where the arbitration is to be held.

"(2) Failing such stipulation, the arbitral tribunal shall determine the place of arbitration, having regard to the circumstances of the arbitration [including the convenience of the parties]."

100. It was agreed that the words "including the convenience of the parties" in paragraph (2) should be deleted. It was stated that there are many other circumstances to be taken into account and it was not appropriate to mention only one of them.

Arbitration proceedings in general, evidence, experts

Article 19

101. The text of article 19 as considered by the Working Group was as follows:

Article 19

"(1) The arbitral tribunal may conduct the arbitration in such manner as it considers appropriate

“(a) Subject to the provisions of articles 20 to 24 and any instructions given by the parties in the arbitration agreement;

“(b) Provided that the parties are treated with equality and that at any stage of the proceedings each party is given a full opportunity of presenting his case.

“(2) The power conferred upon the arbitral tribunal under paragraph (1) includes the power to adopt its own rules on evidence and to determine the admissibility, relevance, materiality and weight of the evidence offered. [Notwithstanding the provision of paragraph (1) (a), the parties may not preclude the arbitral tribunal from calling an expert if it deems that necessary for deciding the dispute.]”

102. It was suggested that the wording of paragraph (1) of this article should emphasize more clearly that the parties are free to determine either directly or by reference to arbitration rules the procedure to be followed and only in the absence of such agreement by the parties may the arbitral tribunal conduct the arbitration in such a manner as it considers appropriate.

103. The Working Group agreed to decide to what extent the provisions of articles 20 to 24 should be mandatory in deliberations on each of those articles.

104. It was felt that the words “at any stage” in paragraph (1) (b) might be relied upon by a party who wished to prolong the proceedings or to make unnecessary submissions. It was therefore suggested that the provision be rephrased in order to eliminate this possibility.

105. In respect of paragraph (2) it was suggested that the sentence in square brackets should be deleted. It was felt that such a provision unduly restricted the principle of freedom of the parties.

106. It was also suggested that the provision on the power of the arbitral tribunal to adopt rules on evidence should be deleted.

Article 20

107. The text of article 20 as considered by the Working Group was as follows:

Article 20

“(1) If either party so requests at any stage of the proceedings, the arbitral tribunal shall hold hearings for the presentation of evidence by witnesses, including expert witnesses, or for oral argument. In the absence of such a request, the arbitral tribunal shall decide whether to hold such hearings or whether the proceedings shall be conducted on the basis of documents and other materials.

“(2) All documents or information supplied to the arbitral tribunal by one party shall [at the same time] be communicated [by that party] to the other party.”

108. The Working Group was of the view that the rule in paragraph (1) calling for a hearing at the request of either party could be modified by the agreement of the parties. However, if the parties had not so agreed, the rule was binding on the arbitral tribunal.

109. The Working Group was also of the view that the parties could not modify the rule expressed in paragraph (2) to the extent that it required that all documents or information supplied to the arbitral tribunal by one party had to be furnished to the other party. However, the method by which they were to be furnished to the other party could be determined by the parties or by the arbitral tribunal.

110. It was suggested that paragraph (2) might be moved to article 19 (1) (b) as an example of the principle of equality.

111. The Working Group expressed the view that the provision allowing a request for oral hearings “at any stage” of the proceedings was too broad and that this right should be appropriately limited so as to be available at the appropriate stage of the proceedings in the interest of expeditious proceedings. A suggestion was made that a party should have a right to request oral hearings only for substantive arguments but not for procedural arguments.

Article 21

112. The text of article 21 as considered by the Working Group was as follows:

Article 21

“Notwithstanding the provisions of article 18, the arbitral tribunal may

“(a) Hear witnesses and hold meetings for consultation among its members at any place it deems appropriate, having regard to the circumstances of the arbitration;

“(b) Meet at any place it deems appropriate for the inspection of goods, other property or documents. The parties shall be given sufficient notice to enable them to be present at such inspection.”

113. It was agreed that the text should make it clear that when witnesses were to be heard, the parties should always be given sufficient notice to enable them to be present at the hearing. Except for the requirement of notice, the Working Group was of the view that the provision was not binding on the parties.

Article 22

114. The text of article 22 as considered by the Working Group was as follows:

Article 22

“(1) The arbitral tribunal may appoint one or more experts to report to it, in writing, on specific issues to be determined by the tribunal.

"(2) Unless otherwise provided in the arbitration agreement,

"(a) A copy of the expert's terms of reference, established by the arbitral tribunal, shall be communicated to the parties;

"(b) The parties shall give the expert any relevant information or produce for his inspection any relevant documents or goods that he may require of them. Any dispute between a party and such expert as to the relevance of the required information or production shall be referred to the arbitral tribunal for decision;

"(c) Upon receipt of the expert's report, the arbitral tribunal shall communicate a copy of the report to the parties who shall be given the opportunity to express, in writing, their opinion on the report. A party shall be entitled to examine any document on which the expert has relied in his report;

"(d) At the request of either party, the expert, after delivery of the report, [may] [shall] be heard at a hearing where the parties shall have the opportunity to be present, to interrogate the expert, and to present expert witnesses in order to testify on the points at issue."

115. Regarding paragraph (1) it was agreed that the text should be clear that this provision is subject to the contrary agreement of the parties.

116. It was also agreed that the requirement of writing in paragraph (1) should be deleted. It was felt that the form of the expert's opinion could be left to arbitral practice and to the agreement of the parties.

117. There was general agreement that paragraph (2) should express only statements of principle and that the procedural elements should be deleted. However, different views were expressed as to which subparagraphs contained statements of principle. There was wide support for retaining subparagraphs (b) and (d) and less support for retaining subparagraphs (a) and (c). It was suggested that some of the provisions in paragraph (2) could be incorporated in article 20.

118. There was general agreement that the word "shall" in subparagraph (d) was more appropriate than "may" and was in line with the discussion of article 20.

Interim measures of protection

Article 23

119. The text of article 23 as considered by the Working Group was as follows:

Article 23

"The arbitral tribunal [, if so authorized by the parties,] may order [or take], at the request of either party, [any interim measures it deems necessary in respect of the subject-matter of the dispute, including] measures for the conservation

of the goods forming the subject-matter in dispute, such as their deposit with a third person or the sale of perishable goods. The arbitral tribunal shall be entitled to require security for the costs of such measures."

120. Different views were expressed whether the existence of an arbitration agreement implied that the arbitral tribunal had the right to order an interim measure of protection. Under one view the arbitral tribunal could order such measures only if it had been authorized to do so by the parties. Under another view the authorization to order such measures is presumed unless the parties excluded it expressly.

121. As to the type of interim measures which the arbitral tribunal should be authorized to order, the view was expressed that the arbitral tribunal should be empowered to order any interim measures of protection it deemed necessary. Under another view the interim measures of protection which could be ordered by the arbitral tribunal should be limited, e.g. to measures for the conservation of the goods forming the subject-matter in dispute.

122. It was suggested that as the basis for further discussion a text might be drafted which recognized that an arbitral tribunal had an implied authority to order interim measures of protection but that the types of interim measures of protection which could be ordered by an arbitral tribunal should be limited. It was further suggested that it might facilitate the agreement on the policy to be followed if the question of ordering interim measures of protection was separated from the question of enforcement of the order.

123. It was agreed to delete the words "or take" in the second square brackets.

Article 24

124. The text of article 24 as considered by the Working Group was as follows:

Alternative A:

Article 24

"(1) If, within the period of time fixed by the arbitral tribunal, the claimant has failed to communicate his statement of claim without showing sufficient cause for such failure, the arbitral tribunal shall issue an order for the termination of the arbitration proceedings.

"(2) If, within the period of time fixed by the arbitral tribunal, the respondent fails to communicate his statement of defence without showing sufficient cause for such failure, the arbitral tribunal shall order that the proceedings continue.

"(3) If one of the parties, invited in writing at least [20] days in advance, fails to appear at a hearing, without showing sufficient cause for such failure, the arbitral tribunal may proceed with the arbitration; if the tribunal decides to do so, it shall notify the parties in writing.

"(4) If one of the parties, invited in writing to produce documentary evidence within a specified period of time of not less than [20] days, fails to do so, the arbitral tribunal may make the award on the evidence before it; if the tribunal decides to do so, it shall notify the parties in writing.

"[(5) The defaulting party may, within 15 days after issuance of the order referred to in paragraph (1) or (2) or the notification referred to in paragraph (3) or (4), request the Authority specified in article 17 to review the decision of the arbitral tribunal as to whether the conditions laid down in the respective paragraph of this article were fulfilled.]"

Alternative B:

Article 24

"If, without showing sufficient cause for the failure,

"(a) the respondent fails to communicate his statement of defence within the period of time fixed by the arbitral tribunal; or

"(b) one of the parties, invited at least [20] days in advance, fails to appear at a hearing; or

"(c) one of the parties, invited in writing to produce documentary evidence within a specified period of time of not less than [20] days fails to do so,

the other party may request the Authority specified in article 17 to [authorize] [instruct] the arbitral tribunal to proceed with the arbitration."

125. The Working Group supported the policy underlying paragraphs (1) to (4) of alternative A. It was generally agreed that these provisions were subject to the contrary agreement of the parties. It was noted that in paragraph (4) of article 24 (alternative A) the words "without showing sufficient cause for such failure" had been erroneously omitted and should be added after the words "fails to do so".

126. It was agreed that paragraph (5) of alternative A as well as the entire text of alternative B should be deleted since they introduced a degree of court supervision of international commercial arbitration which was neither necessary nor desirable.

127. The view was expressed that this article should set forth principles in a general way without detailed procedural rules.

128. The Working Group was in agreement that this article should in its result preserve a balance of equality between the parties. It was noted, however, that it was difficult to preserve a formal equality since the parties were in different situations. The claimant has every reason to pursue his claim if he believes it is justified, since otherwise he will have incurred expenses for no

substantive purpose. On the other hand the respondent may fail to act in the arbitration so as to impede its progress.

129. It was suggested that the parties might be in a situation of greater equality if the failure of the defendant to communicate his statement of defence was treated as a denial of the claim. In such a case, even though the respondent was in default in respect of the arbitral procedure, the claimant would have to establish the merits of his case before the arbitral tribunal.

130. It was suggested that the time-limits provided for in this article might be too short, taking into account the distances and possible delays in communications. It was also suggested that a flexible approach in giving the arbitral tribunal some discretion in setting time-limits might be appropriate.

131. The view was also expressed that it would be appropriate to make clear in paragraph (3) that the arbitral tribunal should give a party a period of time to show that he had sufficient cause for his failure to appear at a hearing.

E. AWARD

Types of award

Article 25

132. The text of article 25 as considered by the Working Group was as follows:

Article 25

"Where the arbitral tribunal makes an award which [is apparently] [indicates that it is] not intended to settle the dispute in full, the making of such an (interim, interlocutory, or partial) award does not terminate the mandate of the arbitral tribunal."

133. The Working Group agreed that it was useful to have a provision on awards which do not settle the dispute in full.

134. The Working Group was of the view that if an enumeration of different types of awards not settling the claim in full (i.e. interim, interlocutory and partial) were to be retained at all, it should be made by way of illustration only. By such an approach difficulties arising from possible differences in the meaning of these words in various legal systems would be avoided.

135. The Working Group noted that both articles 25 and 34 seek to ensure the continuation of the mandate of the arbitral tribunal in cases of awards which do not settle the dispute in full and that co-ordination in the drafting of these two articles would be appropriate.

Making of an award

Article 26

136. The text of article 26 as considered by the Working Group was as follows:

Article 26

"(1) When there are three or another uneven number of arbitrators, any award [or other decision of the arbitral tribunal] shall be made by [all or] a majority of the arbitrators, provided that all arbitrators have taken part in the deliberations leading to the award [or decision].

"[(2) In the case of questions of procedure, when there is no majority or when the arbitral tribunal so authorizes, the presiding arbitrator may decide on his own, subject to revision, if any, by the arbitral tribunal.]"

137. There was general agreement that this article was not mandatory on the parties and that the article should so state.

138. There was general agreement that the actual participation of all the arbitrators in the deliberations should not be a condition for the validity of the award. The prevailing view was that it should be expressly stated in this article that the award could be made by a majority of the arbitrators provided that all the arbitrators had had the opportunity to take part in the deliberations. Under another view such a condition was self-evident and, if expressly mentioned in the model law, could give rise to a wrong impression that an arbitrator had a right to refuse to take part in the deliberations. The proponents of this view therefore proposed that the model law should not mention the condition that the arbitrators must be given an opportunity to take part in the deliberations.

139. It was suggested that the wording of the article should leave no doubt that the term "majority" means "more than half of all appointed arbitrators" and does not mean "more than half of those who made the award".

140. There was general agreement that the provisions of paragraph (2) should be retained, even though it was recognized that it is not always easy to distinguish between substance and procedure. The view was expressed that once the presiding arbitrator decided a procedural question on his own, the other arbitrators should not have the possibility to change his decision. However, the prevailing view was that the arbitral tribunal should retain the possibility of controlling all the decisions made by the presiding arbitrator.

Form of award

Article 27

141. The text of article 27 as considered by the Working Group was as follows:

Article 27

"(1) An award shall be made in writing and shall be signed by the arbitral tribunal. If, in

arbitration proceedings with more than one arbitrator, the signature of an arbitrator cannot be obtained, the signatures of a majority of the arbitrators shall suffice, provided that the fact and the reason for the missing signature are stated.

"(2) An award shall be made at the place of arbitration (article 18). It shall state the place where and the date on which it is made. [The award shall be deemed to have been made at the place and on the date indicated therein.] [Failing such indication, the award shall be deemed to have been made at the place of arbitration and on the date on which it is signed by the arbitral tribunal.]

"(3) The arbitral tribunal shall state the reasons upon which the award is based, unless the parties have agreed that no reasons are to be given. The arbitral tribunal is not obliged to give reasons for an award on agreed terms."

142. The policy underlying paragraph (1) of this article was supported. It was suggested that the words "arbitral tribunal" in the first sentence of paragraph (1) should be replaced by the word "arbitrators" to make it clear that it was the arbitrators who must sign the award and not for example the presiding arbitrator or secretary of the arbitral tribunal on behalf of the tribunal. It was also observed that in cases of arbitral tribunals composed of five or more arbitrators the award could be valid even if more than one signature was missing. It was agreed that paragraph (1) covered all such cases.

143. Regarding paragraph (2) of this article there was general agreement that as a matter of principle the arbitral tribunal should make the award at the place of arbitration. However, it was recognized that for reasons of convenience of the arbitrators and the parties an award was often decided upon and signed in some other place.

144. Under the prevailing view the model law should not make doubtful the validity of the award for the sole reason that the final agreement by the arbitrators on the award was not reached at the place of arbitration. It was suggested, however, that the model law should not imply that the arbitral tribunal has a right to state a fictitious place of making the award. Therefore, under this view no provision establishing a presumption on the place of making the award should be included in the model law. After the discussion it was agreed that the basis of further discussions would be a provision to be drafted by the secretariat providing that the place of arbitration should be stated in the award and that the award is deemed to be made at the place of arbitration.

145. There was general agreement that paragraph (3) of this article was acceptable.

*Pleas as to arbitrator's jurisdiction**Article 28*

146. The text of article 28 as considered by the Working Group was as follows:

Article 28

"(1) [Subject to the provisions of paragraph (3) of this article,] a plea that the arbitral tribunal does not have jurisdiction, including any objections with respect to the existence or validity of the arbitration agreement, may be raised only in the arbitration proceedings and not later than in the statement of defence or, with respect to a counter-claim, in the reply to the counter-claim. [A plea that the arbitral tribunal has exceeded its terms of reference shall be raised during the arbitration proceedings promptly after the matter is raised on which the tribunal is alleged to have no jurisdiction.] [Where the delay in raising the plea is due to a cause which the arbitral tribunal deems justified, it shall declare the plea admissible.]

"[(2) The fact that a party has appointed, or participated in the appointment, of an arbitrator does not preclude that party from raising a plea referred to in paragraph (1) of this article.]

"[(3) Where either party to an arbitration agreement has initiated arbitration proceedings before any resort is had to a court, a court subsequently asked to deal with the same subject-matter between the same parties or with the question whether the arbitration agreement was non-existent or null and void or had lapsed, shall stay its ruling on the jurisdiction of the arbitral tribunal until the arbitral award is made, unless it has good and substantial reasons to the contrary.]"

147. Under one view the policy expressed by paragraph (1), that court intervention on the question of the jurisdiction of the arbitral tribunal should not be permitted prior to the making of the final arbitral award, was correct. It was said that in many countries courts are not prepared to act promptly on such questions with the result that the arbitration might be unduly delayed.

148. Under the prevailing view, however, while arbitral tribunals should have the power to rule on their own jurisdiction, as is recognized under article 29, it would be improper to divest the courts of a concurrent power to rule on the jurisdiction of the arbitral tribunal. In regard to the wording of paragraph (1), this result was achieved by deletion of the word "only" in the first sentence. It was noted, however, that this deletion did not affirmatively state the power of the courts in this regard.

149. It was suggested that it should be made clear in the model law that the arbitral tribunal could proceed with the case during the period a court was considering whether the arbitral tribunal had jurisdiction over the dispute.

150. With this recognition of the concurrent power of the court and the arbitral tribunal the rest of paragraphs (1) and (2) were generally acceptable to the Working Group.

151. The prevailing view was in favour of deleting paragraph (3). It was recognized, however, that paragraph (3) derived from an existing convention and that it should not therefore be discarded without a second consideration. As a possible solution the secretariat was requested to draft a text incorporating the basic idea of paragraph (3) into an expanded article 5.

Article 29

152. The text of article 29 as considered by the Working Group was as follows:

Article 29

"(1) The arbitral tribunal has the power to rule on its own jurisdiction, including any objections with respect to the existence or validity of the arbitration clause, in accordance with the provisions of article 4, or of the separate arbitration agreement.

"(2) The arbitral tribunal may rule on a plea concerning its jurisdiction either as a preliminary question or in the final award."

153. The Working Group was in general agreement with this article. Some support was expressed for an additional provision that a ruling by the arbitral tribunal on jurisdiction as a preliminary question should always be made in the form of an interlocutory award so as to allow an appeal to the courts from the interlocutory award.

Article 30

154. The text of article 30 as considered by the Working Group was as follows:

Article 30

"A ruling by the arbitral tribunal that it has jurisdiction may be contested by either party,

Alternative A:

"whether it was made as a preliminary question or in the final award, only by way of recourse against the award under the procedure laid down in article

Alternative B:

"(a) If it was made as a preliminary question, [within one month] before the Authority specified in article 17, which has the power to order the termination of the arbitration proceedings for lack of jurisdiction;

"(b) If it was made in the final award, by way of recourse against the award under the procedure laid down in article"

155. Under one view it was not necessary to regulate the time for appeal against a ruling by the arbitral tribunal since the decision of the Working Group in

respect of article 28 would permit a party to resort directly to a court at any time. The prevailing view, however, was that, despite the possibility of direct resort to a court, it would be useful to regulate the time for appeal for those cases in which a party chose to raise its objections regarding jurisdiction before the arbitral tribunal. Nevertheless, it was generally agreed that the final decision on this point could be taken only after the final wording of article 28 had been established.

156. Under the prevailing view a party should be able to contest a ruling by the arbitral tribunal that it had jurisdiction only by recourse against the final award, as provided in alternative A.

157. The Working Group was divided as to whether the parties should have the possibility of contesting a ruling by the arbitral tribunal that it had no jurisdiction. The Working Group reserved its final position on this point.

Law applicable to substance of dispute

Article 31

158. The text of article 31 as considered by the Working Group was as follows:

Article 31

"(1) The arbitral tribunal shall apply the law designated by the parties as applicable to the substance of the dispute. [Parties may so designate any national law or, even if not yet in force, a pertinent international convention or uniform law.]

"(2) Failing such designation by the parties, the arbitral tribunal shall apply

Alternative A:

"the law determined by the conflict of laws rules which it considers applicable.

Alternative B:

"the substantive law rules which it considers most appropriate [, taking into account the various factors of the transaction and the interests of the parties]. [Such rules may form part of a given national legal system or of an international convention or uniform law, even if not yet in force.]

"(3) The arbitral tribunal [shall decide in accordance with the terms of the contract and] shall take into account the usages of the trade applicable to the transaction. [It shall apply any usage to which the parties have agreed; the parties are considered, unless otherwise agreed, to have impliedly made applicable to their contract or its formation a usage of which they knew or ought to have known and which in international trade is widely known to, and regularly observed by, parties to contracts of the type involved in the particular trade concerned.]"

159. Under one view the model law should not contain conflict of law rules on the substance of the dispute. It was noted that such rules are complex and cannot be reduced properly to short formulas. It was also noted that in some States the rules on conflict of laws are contained in a single law or code governing private international law in general. The introduction into this model law of rules on the conflict of laws for use in international commercial arbitration would make it difficult for those States to assimilate the model law into their legal system.

160. Under the prevailing view, however, it would be useful to have general guidelines as to the law applicable to the substance of the dispute in international commercial arbitrations. The Working Group decided, therefore, to retain a text based upon this article.

161. The Working Group was agreed that the basic rule should be the autonomy of the parties to designate the applicable law. It decided, therefore, to retain the first sentence of paragraph (1). It also decided that the sentence should be drafted so as to indicate clearly that the designation by the parties of the law of a given State referred to the substantive rules of law of that State and not to its conflict of law rules, unless the parties have otherwise indicated.

162. There was general agreement to delete the second sentence of paragraph (1). It was felt that the designation of an international convention or uniform law which was not yet in force in any State would cause difficulties in determining the relationship between that text and the other national law applicable to the substance of the dispute. It was suggested that such a text could become applicable to the dispute only as a part of the contract and then only if the parties had so indicated. However, it was also suggested that the statement as to the autonomy of the parties might be broadened in this article to enable the parties implicitly to designate parts of different systems of law as applicable to the substance of their dispute. It was suggested that the autonomy of the parties could be broadened implicitly by a rule according to which "the tribunal shall decide a dispute in accordance with such rules of law as may be agreed by the parties".

163. There was general agreement that alternative A of paragraph (2) was preferable. It was agreed, however, that the choice of either alternative A or alternative B would probably lead to the same result in practice.

164. Under one view trade usages are part of the applicable law. Under this view the obligation to apply trade usages was impliedly incorporated in paragraph (1). Therefore, paragraph (3) could be deleted.

165. Under the prevailing view, however, the model law should contain an express provision that the arbitral tribunal should decide according to the terms of the contract and take into account the usages of the trade applicable to the transaction.

166. It was agreed to delete the second sentence of paragraph (3). This sentence, which was taken from the 1980 Vienna Sales Convention, was thought to be applicable to contracts of sale and perhaps other international trade contracts but not to be applicable to some other types of contracts which might give rise to disputes subject to this law, such as investment contracts.

167. Noting the strong support for maintaining the autonomy of the parties in choosing the law applicable to the substance of the dispute, a view was expressed that similar freedom of choice should be given to parties in transactions having international links to include a provision in their agreement that the model law shall apply, thereby avoiding possible uncertainty in determining whether the model law or domestic law applies. This view could be considered in connection with the next draft of article 1.

Article 32

168. The text of article 32 as considered by the Working Group was as follows:

Article 32

"The arbitral tribunal shall decide *ex aequo et bono* [or as *amiable compositeur*] [only] if the parties have expressly authorized it to do so."

169. There was general agreement that this article was acceptable, even though many States do not provide for such arbitrations. The prevailing view was to retain both expressions *ex aequo et bono* and *amiable compositeur* in the model law because under some national laws there might be a difference in meaning between them.

170. The prevailing view was to maintain the word "only" in the second square brackets in order to indicate that the procedure was an exceptional one.

Settlement

Article 33

171. The text of article 33 as considered by the Working Group was as follows:

Article 33

Alternative A:

"(1) If, during the arbitration proceedings, the parties agree on a settlement of the dispute, the arbitral tribunal shall either issue an order for the termination of the arbitration proceedings or, if requested by both parties and accepted by the tribunal, record the settlement in the form of an arbitral award on agreed terms.

Alternative B:

"(1) If, during the arbitration proceedings, the parties agree on a settlement of the dispute, the arbitral tribunal shall, if requested by [both parties] [a party, unless the arbitration agreement requires a request by both parties], record the settlement in the form of an arbitral award on agreed terms, unless the arbitral tribunal has

[good and substantial] [compelling] reasons, in particular grounds of international public policy, not to follow that request.

"(2) An award on agreed terms shall be made in accordance with the provisions of articles 27 and 35 and shall state that it is an award [on agreed terms]. Such an award [has the same status and executory force as] [shall be treated like] any other award on the merits of the case."

172. There was general agreement that alternative A of paragraph (1) was preferable.

173. However, in this context a view was expressed that the procedure for recording a settlement as an award on agreed terms would not be necessary if the model law would provide for the enforceability of the settlement agreement as such.

174. It was suggested that the arbitral tribunal should be empowered to record a settlement in the form of an arbitral award on agreed terms on the request of either party. It was pointed out that it is often the case that only the party who is to receive payment under the award has an interest in converting the settlement into an award which can then be enforced under the 1958 New York Convention.

175. On the other hand, it was noted that a settlement may be ambiguous or subject to conditions that might not be apparent to the arbitral tribunal. According to this view, which received a majority of the support, there were fewer dangers of injustice by requiring both parties to request an award on agreed terms.

176. The Working Group was of the view that the arbitral tribunal should have the right to decide whether it would record the settlement in the form of an agreed award.

Correction and interpretation of award

Article 34

177. The text of article 34 as considered by the Working Group was as follows:

Article 34

"(1) [Unless otherwise agreed by the parties,] within thirty days after the receipt of the award, either party, with notice to the other party, may request the arbitral tribunal

"(a) To correct in the award any errors in computation, any clerical or typographical errors, or any errors of similar nature; the arbitral tribunal may, within thirty days after the communication of the award, make such corrections on its own initiative;

"(b) To give, within forty-five days, an interpretation of a specific point or part of the award; such interpretation shall form part of the award;

"(c) To make an additional award as to claims presented in the arbitration proceedings but omitted from the award; if the arbitral tribunal considers such request to be justified and that the omission can be rectified without any further hearings or evidence, it shall complete its award within sixty days after the receipt of the request.

"(2) The provisions of articles 27, paragraphs (1) and (2), and 35 shall apply to a correction, interpretation or an additional award."

178. The Working Group was in general agreement that the arbitral tribunal should have the right to correct any errors in computation, any clerical or typographical errors, or any errors of similar nature as provided in paragraph (1) (a), and that the parties should not be able to stipulate to the contrary. The Working Group did not feel, however, that the time-limit of 30 days was of a similar mandatory character.

179. In respect of paragraph (1) (b) the prevailing view was that the right of a party to request an interpretation of the award was not subject to the contrary agreement of the parties. The Working Group was not in agreement as to whether the interpretation should form part of the award and it was decided to put this portion of the paragraph in square brackets.

180. The Working Group agreed to retain paragraph (1) (c). The Working Group also agreed that the provision was not binding on the parties.

181. A question was raised and referred for later decision as to whether it was preferable to provide in each article of the model law whether that article or a part of it was binding on the parties or whether it was preferable to have a single provision on that subject.

182. It was noted that the time-limits should be in harmony with the time-limits for "attacking" an award in the courts.

183. The Working Group also noted that this article should be harmonized with the provisions of articles 25 and 36.

Delivery and registration of award

Article 35

184. The text of article 35 as considered by the Working Group was as follows:

Article 35

"(1) After an award is made under article 27, copies thereof signed by the arbitral tribunal shall be communicated to the parties.

"(2) Upon request by [the parties] [either party], the original award shall be filed with the Authority specified in article 17. [This provision shall not be interpreted as making such filing a precondition for recognition or enforcement of the award.]"

185. There was general agreement that paragraph (1) should be retained. It was suggested that the words "by the arbitral tribunal" should be replaced by the words "by the arbitrators in accordance with article 27". It was also noted that arbitrators sometimes withheld their award until the parties had paid the fees and expenses for the arbitration and that this practice should not be precluded by the model law.

186. The Working Group decided to delete paragraph (2).

Executory force and enforcement of award

Article 36

187. The text of article 36 as considered by the Working Group was as follows:

Article 36

Alternative A:

"Subject to any multilateral or bilateral agreement entered into by the State in which this Law is in force, an arbitral award as defined in article 1

Alternative B:

"An arbitral award as defined in article 1 and considered as a domestic award in the State in which this Law is in force

"shall be recognized as binding and enforced in accordance with the following rules of procedure:

"(a) An application for recognition and enforcement of an arbitral award shall be made in writing to [the Authority specified in article 17];

"(b) The party applying for recognition and enforcement shall, at the time of the application, supply the duly authenticated original award or a duly certified copy thereof and the original arbitration agreement referred to in article 3 or a duly certified copy thereof. [If the said award or agreement is not made in an official language of [the Authority] [this State], the party applying for recognition and enforcement of the award shall produce a translation of these documents into such language, certified by an official or sworn translator or by a diplomatic or consular agent.]"

188. There was general agreement that the model law should provide a uniform system of enforceability for the international awards rendered in the country which adopted the model law. It was also agreed that if according to the law of that country enforceability of such international awards was recognized under less stringent conditions than those of the model law, the less stringent conditions should prevail.

189. The Working Group requested the secretariat to prepare as a separate article draft provisions on the enforceability of international awards rendered abroad.

B. Working papers submitted to the Working Group on International Contract Practices at its fourth session (Vienna, 4-15 October 1982)

1. NOTE BY THE SECRETARIAT: MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION: DRAFT ARTICLES 1 TO 24 ON SCOPE OF APPLICATION, ARBITRATION AGREEMENT, ARBITRATORS, AND ARBITRAL PROCEDURE (A/CN.9/WG.II/WP.37)^a

Introductory note

1. This working paper contains tentative draft articles on scope of application, arbitration agreement, arbitrators, and arbitral procedure, prepared by the secretariat in accordance with the conclusions reached by the Working Group on International Contract Practices at its third session (New York, 16-26 February 1982). Separate working papers will deal with the other chapters (i.e. award, means of recourse) and with those issues on which the Working Group requested further studies (e.g. court assistance in taking evidence, filling of gaps and adaptation of contracts) or which were suggested as additional features to be included in the model law (notice of arbitration, statements of claim and defence, language, termination of arbitration proceedings).

2. References accompanying the draft articles are made to the relevant parts of the report of the Working Group on the work of its third session under its symbol A/CN.9/216.^b In order to facilitate reference to the corresponding discussion in that report and in the basic report on possible features of a model law (A/CN.9/207),^c the structure and classification of the issues used therein has been maintained in the presentation of the draft articles. Their order in no way indicates the eventual structure of the model law and will be altered once a clearer picture about the contents of the model law has emerged. Also the headings and subheadings used in these reports have been maintained in this working paper for the same purpose. They are not intended to be suggested headings of the eventual chapters or sections of the model law.

Draft articles 1 to 24 of a model law on international commercial arbitration

I. Scope of application¹

Alternative A:²

Article 1 (A)

This Law applies:

(a) To arbitration agreements concluded by parties to a commercial [or economic] transaction whose places

of business are in different States [or, if their places of business are in the same State, where their contract is to be performed outside that State or where the subject-matter in dispute is property situated outside that State]³; if a party has more than one place of business the relevant place of business is that which has the closest relationship to [the contract and its performance] [the conclusion of the arbitration agreement];⁴

(b) To the preparation and conduct of arbitration proceedings based on agreements referred to in paragraph (a);

(c) To arbitral awards rendered in proceedings referred to in paragraph (b).

Alternative B:

Article 1 (B)

(1) This Law applies to international commercial arbitration as specified in paragraphs (2), (3) and (4) of this article.

(2) "Arbitration" covers arbitration agreements, the preparation and conduct of arbitration proceedings based on such agreements whether or not administered by a permanent arbitral institution, and the arbitral awards resulting therefrom.

(3) "Commercial" refers to the settlement of a dispute arising in the context of any commercial transaction [or similar economic relationship] [including supply or exchange of goods, construction of works, financing, joint venture and other forms of business co-operation, provision of services, except labour under a contract of employment].⁵

(4) "International" are those cases where the arbitration agreement is concluded by parties whose places of business are in different States [or, if their places of

¹If the latter situation were to be accepted as an "international" case, this extension would probably have to be expressed in the context of the arbitration proceedings but not the arbitration agreement, since at the time of the conclusion of that agreement it may not be clear whether a dispute will arise relating to property.

²The first mentioned factor ("the contract and its performance") is the one adopted in article 10 (a) of the United Nations Convention on Contracts for the International Sale of Goods (Yearbook ... 1980, part three, I, B). The second alternative ("the conclusion of the arbitral agreement") is submitted for consideration since it would allow a clear decision even in the case where the contract, or a separate arbitration agreement, is negotiated and concluded with one branch of a firm while another branch, in a different State, is in charge of the performance.

³This non-exhaustive list, still to be refined, is given here in order to stimulate discussion on whether the general term "commercial" (or "economic") should be explained by way of example or be left undefined.

^a15 July 1982. Referred to in Report, para. 87 (part one, A).

^bYearbook ... 1982, part two, III, A.

^cYearbook ... 1981, part two, III.

¹Relevant discussion and conclusions of the Working Group in A/CN.9/216, paras. 16-21.

²The main difference between alternative A and alternative B is one of structure and drafting style; also, alternative B is more detailed and covers some aspects not dealt with in alternative A (see art. 1 (B) (2), (3)).

business are in the same State where their contract is to be performed outside that State or where the subject-matter in dispute is property situated outside that State].⁶ If a party has more than one place of business, the relevant place of business is that which has the closest relationship to [the contract and its performance] [the conclusion of the arbitration agreement].⁷

II. Arbitration agreement

1.-3. Form, contents, parties, domain⁸

Article 2⁹

"Arbitration agreement" is an undertaking by [parties] [physical persons or legal persons of private or public law] to submit to arbitration all or certain differences which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not [, concerning a subject matter which could be disposed of by agreement of the parties under the applicable law].

Article 3

(1) The arbitration agreement, whether an arbitration clause in a contract or a separate agreement, shall be [concluded or evidenced] in writing.

(2) "Agreement in writing" includes an agreement contained in a document signed by the parties or contained in an exchange of letters, telegrams or communications in another, [visible and] sufficiently permanent form.¹⁰ The reference in a contract to general conditions containing an arbitration clause constitutes an arbitration agreement provided that the contract is in writing. [However, an arbitration agreement also exists where one party to a contract refers in its written offer, counter-offer or contract confirmation to general conditions, or uses a contract form or standard contract, containing an arbitration clause and the other party does not object, provided that the applicable law recognizes formation of contracts in such manner].¹¹

⁶See note 3.

⁷See note 4.

⁸Discussion and conclusions of the Working Group in A/CN.9/216, paras. 22-31.

⁹This draft provision is modelled on article II (1) of the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (hereinafter referred to as "1958 New York Convention") (United Nations, *Treaty Series*, vol. 330, No. 4739 (1959), p. 38), with some alternatives or amendments based on suggestions by the Working Group.

¹⁰The last words of this sentence are submitted to invite discussion by the Working Group on which modern means of communication should be recognized and which elements should be required, in particular in cases of electronic transmission.

¹¹It may be noted that this latter provision deviates from the requirement of written form by recognizing a writing by only one party, but that it deviates considerably less than, for example, article I (2) (a) of the European Convention on International Commercial Arbitration (Geneva, 1961) (United Nations, *Treaty Series*, vol. 484, No. 7041 (1963-1964), p. 484) which recognizes, "in relations between States whose laws do not require that an arbitration agreement be made in writing, any arbitration agreement concluded in the form authorized by these laws".

4. Separability of arbitration clause¹²

Article 4¹³

For the purposes of determining whether the arbitral tribunal has jurisdiction, an arbitration clause which forms part of a contract shall be treated as an agreement independent of the other terms of the contract. A decision by the arbitral tribunal that the contract is null and void shall not entail *ipso jure* the invalidity of the arbitration clause.

5. Effect of the agreement¹⁴

Article 5¹⁵

A court, before which an action is brought in a matter which is the subject of an arbitration agreement, shall, at the request of either party, refer the parties to arbitration unless it finds that the agreement is null and void, inoperative or incapable of being performed.

Article 6¹⁶

A request for interim measures of protection addressed by any party to a court, whether before or during arbitration proceedings, shall not be deemed incompatible with the agreement to arbitrate or as a waiver of that agreement.

III. Arbitrators

1.-2. Qualifications, challenge (and replacement)¹⁷

Article 7

A prospective arbitrator shall disclose to those who approach him in connection with his possible appointment any circumstances likely to give rise to justifiable doubts as to his impartiality or independence. An arbitrator, once appointed or chosen, shall disclose such circumstances to the parties unless they have already been informed by him of these circumstances.¹⁸

Article 8¹⁹

(1) An arbitrator may be challenged only if circumstances exist that give rise to justifiable doubts as to his impartiality or independence.

¹²Discussion and conclusion of the Working Group in A/CN.9/216, para. 34.

¹³This draft provision is modelled on article 21 (2) of the UNCITRAL Arbitration Rules. The related issue "Pleas as to arbitrator's jurisdiction" will be dealt with under V.4, following the classification scheme adopted in the report. However, it may well be combined later with the provision on separability.

¹⁴Discussion and conclusions of the Working Group in A.CN.9/216, paras. 35-39.

¹⁵This draft provision is modelled on article II (3) of the 1958 New York Convention.

¹⁶This draft provision is modelled on article 26 (3) of the UNCITRAL Arbitration Rules.

¹⁷Discussion and conclusions of the Working Group in A.CN.9/216, paras. 42-45, 50, 52, 75. The draft provisions of this section might later be placed after the draft provisions on the appointment of arbitrators.

¹⁸This draft provision is modelled on article 9 of the UNCITRAL Arbitration Rules.

¹⁹This draft provision is modelled on article 10 of the UNCITRAL Arbitration Rules.

(2) A party may challenge the arbitrator appointed by him only for reasons of which he becomes aware after the appointment has been made.

Article 9

(1) Subject to the provisions of article 10, the parties are free to agree on the procedure for challenging an arbitrator.

(2) Failing such agreement, the following procedure shall be used:²⁰

(a) A party who intends to challenge an arbitrator shall, within fifteen days after knowing about the appointment of that arbitrator or about the circumstances mentioned in articles 7 and 8, send a written statement of the reasons for the challenge to the other party and to all arbitrators;

(b) When an arbitrator has been challenged by one party, the other party may agree to the challenge. The arbitrator may also, after the challenge, withdraw from his office. In neither case does this imply acceptance of the validity of the grounds for the challenge;

(c) If within [20] days after the challenge, the other party does not agree to the challenge and the challenged arbitrator does not withdraw, [the decision on the challenge shall be made by the Authority specified in article 17] [the challenging party may pursue his objections before a court only in an action for setting aside the award or any recourse against recognition and enforcement of the award].²¹

Article 10

If, under any procedure for challenge agreed upon by the parties, the challenged arbitrator does not withdraw or the challenge is not sustained by the person or body entrusted with the decision on the challenge, the challenging party may [request the Authority specified in article 17 to make a final decision on the challenge] [pursue his objections before a court only in an action for setting aside the award or any recourse against recognition and enforcement of the award].²²

²⁰The procedure suggested here is essentially the one adopted in articles 11 and 12 of the UNCITRAL Arbitration Rules, except that no provision is included on the involvement of an appointing authority designated by the parties.

²¹The first alternative, providing for a final decision on the challenge, may help to avoid delays and controversy during the arbitration proceedings and to reduce the risk of a later setting aside of the award and, thus, of waste of time and resources. However the second alternative might be acceptable in view of the practical experience that an arbitrator challenged on justifiable grounds usually withdraws from his office.

²²This draft provision is designed to regulate the recourse available to a party who has challenged an arbitrator without success under a procedure agreed upon by the parties. Such party would, depending on which alternative is selected by the Working Group for articles 9 and 10, have the right to resort to the specified Authority for a final decision or would be precluded from resorting to a court during the arbitration proceedings, even if such court intervention were envisaged in the challenge procedure agreed upon by the parties.

Article 11²³

Unless the parties have agreed otherwise, the following procedure shall be used in the event that an arbitrator [fails to act] [does not perform his functions in accordance with the instructions of the parties and in an impartial, proper and speedy manner] or in the event of the *de jure* or *de facto* impossibility of his performing his functions:

(a) Any party who wishes that, for any of these reasons, the mandate of an arbitrator be terminated shall send a written statement of the reasons to the other party and to all arbitrators;

(b) If, within [20] days after the notification, the other party does not agree to the termination of the mandate and the arbitrator does not withdraw from his office, the party may request the Authority specified in article 17 to make a final decision thereon.

Article 12

In the event of the termination of the mandate of an arbitrator or in the event of his death or resignation during the course of the arbitration proceedings, a substitute arbitrator shall be appointed according to the rules that were applicable to the appointment of the arbitrator being replaced, unless the parties agree on another appointment procedure [or decide to terminate the arbitration proceedings].²⁴

3.-4. Number and appointment of arbitrators²⁵

Article 13

(1) In arbitration governed by this Law, nationals of any State may be appointed as arbitrators.

(2) An arbitration agreement is invalid [if] [to the extent that]²⁶ it accords one of the parties a predominant position with regard to the appointment of arbitrators.

Article 14

(1) Subject to the provisions of article 13 (2), the parties are free to determine the number of arbitrators.

(2) Failing such determination,

Variant A:

three arbitrators shall be appointed.

²³This draft provision follows in substance article 13 (2) of the UNCITRAL Arbitration Rules but spells out the procedure to be used in such case instead of generally referring to the provisions on challenge.

²⁴This draft provision follows in substance articles 12 (2) and 13 (1) of the UNCITRAL Arbitration Rules, except for the alternative option of termination of the proceedings which, if adopted, would have to be considered in the context of the general issue "Termination of arbitration proceedings" under IV.11.

²⁵Discussion and conclusions of the Working Group in A/CN.9/216, paras. 46-50.

²⁶These alternatives are submitted to invite discussion by the Working Group on what should be the effect of a clause which violates the principle of equality of the parties: invalidity of the whole arbitration agreement or of that clause only.

Variant B:

the number of arbitrators shall be equal to the number of parties but increased by one if the number of parties is even.

Variant C:

a sole arbitrator shall be appointed.

Article 15

(1) Subject to the provisions of article 13 (2), the parties are free to agree on the procedure of appointing the arbitrator or arbitrators.

(2) If a party does not fulfill his obligations under an agreed appointment procedure, the other party may request the Authority specified in article 17 to take the required measure instead.²⁷

Article 16²⁸

(1) If the parties have not agreed on the appointment procedure,

(a) In an arbitration with a sole arbitrator, the arbitrator shall be appointed by the Authority specified in article 17;

(b) In an arbitration with three arbitrators, each party shall appoint one arbitrator and the two arbitrators thus appointed shall appoint the third arbitrator;

[(c) In an arbitration with a number of arbitrators that is equal to the number of the parties or a multiple thereof, each party shall appoint one arbitrator or the respective multiple thereof;]

[(d) In a multi-party arbitration with one arbitrator more than there are parties, each party shall appoint one arbitrator and the additional arbitrator shall be appointed by the Authority specified in article 17.]

(2) If a party, in an arbitration referred to in paragraph (1) (b), [(c) or (d)], fails to make the required appointment within [30] days after having been so requested by the other party, or if, in an arbitration referred to in paragraph (1) (b), the two arbitrators fail to appoint the third arbitrator within [30] days after their appointment, the appointment shall be made by the Authority specified in article 17.

Article 17

(1) The Authority, referred to in articles 9 (2) (c), 10, 11 (b), 15 (2), 16 (1) (a), (d), (2) and . . . , shall be the . . . (e.g. specific chamber of a given court, president of a

²⁷The main case envisaged here would be where the respondent, though committed under the arbitration agreement to appoint the second arbitrator, fails to make that appointment within the agreed period of time.

²⁸This draft article is intended to regulate the appointment procedure not only for the case of article 14 (2), i.e. where parties have not agreed on the number of arbitrators, but also for cases where they have agreed on the number but not on the procedure. Yet, it may not be desirable in a model law to list the procedure for any possible number which parties could select due to their unlimited freedom under article 14 (1). Thus, it may be considered to provide procedural rules only for the two probably most common and practical numbers, i.e. one and three.

specified court, to be determined by each State when enacting the model law).²⁹

(2) The Authority shall act upon request by any of the parties or by the arbitral tribunal, unless otherwise provided for in a provision of this Law.

(3) The Authority, in appointing an arbitrator, shall have regard to such considerations as are likely to secure the appointment of an independent and impartial arbitrator and, in the case of a sole or an additional arbitrator under article 16 (1) (a), (b) [or (d)], shall take into account as well the advisability of appointing an arbitrator of a nationality other than the nationalities of the parties.³⁰

*IV. Arbitral procedure**1. Place of arbitration³¹**Article 18*

(1) The parties to an arbitration agreement are free to determine, or to authorize a third person or institution to determine, the place where the arbitration is to be held.

(2) Failing such stipulation, the arbitral tribunal shall determine the place of arbitration, having regard to the circumstances of the arbitration [, including the convenience of the parties].

*2-4. Arbitration proceedings in general, evidence, experts³²**Article 19*

(1) The arbitral tribunal may conduct the arbitration in such manner as it considers appropriate

(a) Subject to the provisions of articles 20 to 24 and any instructions given by the parties in the arbitration agreement;³³

(b) Provided that the parties are treated with equality and that at any stage of the proceedings each party is given a full opportunity of presenting his case.³⁴

(2) The power conferred upon the arbitral tribunal under paragraph (1) includes the power to adopt its

²⁹The Authority envisaged in this provision would be a judicial body specializing in arbitration matters and assisting in a variety of ways specified in the model law.

³⁰This draft provision is modelled on article 6 (4) of the UNCITRAL Arbitration Rules. The Working Group may wish to consider adding a provision along the lines of article 6 (3), suggesting the use of the list-procedure.

³¹Discussions and conclusions of the Working Group in A/CN.9/216, paras. 53-55.

³²Discussion and conclusions of the Working Group in A/CN.9/216, paras. 56-60, 63, 64.

³³Consideration of this sub-paragraph may be combined with the discussion on the articles referred to therein. When discussing articles 20 to 24, the Working Group may wish to consider to what extent these provisions should be mandatory (as regards art.20, see A/CN.9/216, para. 57).

³⁴This draft provision is modelled on article 15 (1) of the UNCITRAL Arbitration Rules.

own rules on evidence and to determine the admissibility, relevance, materiality and weight of the evidence offered. [Notwithstanding the provision of paragraph (1) (a), the parties may not preclude the arbitral tribunal from calling an expert if it deems that necessary for deciding the dispute.]

Article 20³⁵

(1) If either party so requests at any stage of the proceedings, the arbitral tribunal shall hold hearings for the presentation of evidence by witnesses, including expert witnesses, or for oral argument. In the absence of such a request, the arbitral tribunal shall decide whether to hold such hearings or whether the proceedings shall be conducted on the basis of documents and other materials.

(2) All documents or information supplied to the arbitral tribunal by one party shall [at the same time] be communicated [by that party]³⁶ to the other party.

Article 21³⁷

Notwithstanding the provisions of article 18, the arbitral tribunal may

(a) Hear witnesses and hold meetings for consultation among its members at any place it deems appropriate, having regard to the circumstances of the arbitration;

(b) Meet at any place it deems appropriate for the inspection of goods, other property or documents. The parties shall be given sufficient notice to enable them to be present at such inspection.

Article 22³⁸

(1) The arbitral tribunal may appoint one or more experts to report to it, in writing, on specific issues to be determined by the tribunal.³⁹

(2) Unless otherwise provided in the arbitration agreement,

(a) A copy of the expert's terms of reference, established by the arbitral tribunal, shall be communicated to the parties;

(b) The parties shall give the expert any relevant information or produce for his inspection any relevant

documents or goods that he may require of them. Any dispute between a party and such expert as to the relevance of the required information or production shall be referred to the arbitral tribunal for decision;

(c) Upon receipt of the expert's report, the arbitral tribunal shall communicate a copy of the report to the parties who shall be given the opportunity to express, in writing, their opinion on the report. A party shall be entitled to examine any document on which the expert has relied in his report;

(d) At the request of either party, the expert, after delivery of the report, [may] [shall] be heard at a hearing where the parties shall have the opportunity to be present, to interrogate the expert, and to present expert witnesses in order to testify on the points at issue.

5. Interim measures of protection⁴⁰

Article 23⁴¹

The arbitral tribunal [, if so authorized by the parties,] may order [or take, at the request of either party, [any interim measures it deems necessary in respect of the subject-matter of the dispute, including] measures for the conservation of the goods forming the subject-matter in dispute, such as their deposit with a third person or the sale of perishable goods. The arbitral tribunal shall be entitled to require security for the costs of such measures.

7. Default⁴²

Alternative A:

Article 24 (A)⁴³

(1) If, within the period of time fixed by the arbitral tribunal, the claimant has failed to communicate his statement of claim without showing sufficient cause for such failure, the arbitral tribunal shall issue an order for the termination of the arbitration proceedings.

(2) If, within the period of time fixed by the arbitral tribunal, the respondent fails to communicate his statement of defence without showing sufficient cause for such failure, the arbitral tribunal shall order that the proceedings continue.

(3) If one of the parties, invited in writing at least [20] days in advance, fails to appear at a hearing, without showing sufficient cause for such failure, the arbitral tribunal may proceed with the arbitration; if the

³⁵This draft article is modelled on article 15 (2) and (3) of the UNCITRAL Arbitration Rules.

³⁶The words placed between square brackets would probably have to be deleted if the provisions were to be mandatory (cf. footnote 33) since under some arbitration rules or administrative procedures copies of the communications of a party are sent to the other party by the arbitral tribunal or an administrative body, thus not "by that party" and not "at the same time".

³⁷This draft article is modelled on article 16 (2) and (3) of the UNCITRAL Arbitration Rules.

³⁸This draft article is modelled on article 27 of the UNCITRAL Arbitration Rules. If the Working Group were to adopt paragraph (2), it may wish to consider including suppletive rules also on evidence and hearings, modelled on articles 24 and 25 (1) to (5) of the UNCITRAL Arbitration Rules.

³⁹As to the question whether the parties may preclude the arbitral tribunal from calling an expert, see draft article 19 (2).

⁴⁰Discussions and conclusions of the Working Group in A/CN.9/216, paras. 65-67.

⁴¹This draft article is modelled on article 26 (1) and (2) of the UNCITRAL Arbitration Rules, with some alternative wording reflecting the views expressed in the Working Group.

⁴²Discussion and conclusions of the Working Group in A/CN.9/216, para. 71.

⁴³Paragraphs (1) to (4) of this draft article are modelled on article 28 of the UNCITRAL Arbitration Rules. Paragraph (5) presents a possible method of judicial control which the Working Group may wish to consider, as an alternative to draft article 24 (B), if some kind of court control over *ex parte* proceedings would be envisaged at all.

tribunal decides to do so, it shall notify the parties in writing.

(4) If one of the parties, invited in writing to produce documentary evidence within a specified period of time not less than [20] days, fails to do so, the arbitral tribunal may make the award on the evidence before it; if the tribunal decides to do so, it shall notify the parties in writing.

[(5) The defaulting party may, within 15 days after issuance of the order referred to in paragraph (1) or (2) or the notification referred to in paragraph (3) or (4), request the Authority specified in article 17 to review the decision of the arbitral tribunal as to whether the conditions laid down in the respective paragraph of this article were fulfilled.]

Alternative B

Article 24 (B)

If, without showing sufficient cause for the failure,

(a) the respondent fails to communicate his statement of defence within the period of time fixed by the arbitral tribunal; or

(b) one of the parties, invited in writing at least [20] days in advance, fails to appear at a hearing; or

(c) one of the parties, invited in writing to produce documentary evidence within a specified period of time of not less than [20] days, fails to do so,

the other party may request the Authority specified in article 17 to [authorize] [instruct] the arbitral tribunal to proceed with the arbitration.

2. NOTE BY THE SECRETARIAT: MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION: DRAFT ARTICLES 25 TO 36 ON AWARD (A/CN.9/WG.II/WP.38)^a

Introductory note

1. This working paper contains tentative draft articles on the arbitral award, prepared by the secretariat in accordance with the conclusions reached by the Working Group on International Contract Practices at its third session (New York, 16-26 February 1982)^b. Draft articles on scope of application, arbitration agreement, arbitrators, and arbitral procedure are contained in the note A/CN.9/WG.II/WP.37 of 15 July 1982. Separate working papers, to be submitted to future sessions of the Working Group, will deal with the final chapter (VI. Means of recourse) and with those issues on which the Working Group has requested further studies (e.g. court assistance in taking evidence; filling of gaps and adaptation of contracts) or which were suggested as additional features to be included in the model law (effect of commencement of arbitration proceedings on prescription period; minimum contents of statements of claim and of defence; language; termination of arbitration proceedings).

2. References accompanying the draft articles are made to the relevant parts of the report of the Working Group on the work of its third session under its symbol A/CN.9/216^c. In order to facilitate reference to the corresponding discussion in that report and in the basic report on possible features of a model law (A/CN.9/207)^d, the structure and classification of the

issues used therein has been maintained in the presentation of the draft articles. Their order in no way indicates the eventual structure of the model law and will be altered once a clearer picture about the contents of the model law has emerged. Also the headings and subheadings used in these reports have been maintained in this working paper for the same purpose. They are not intended to be suggested headings of the eventual chapters or sections of the model law.

Draft articles 25 to 36 of a model law on international commercial arbitration

V. Award

1. Types of award¹

Article 25

Where the arbitral tribunal makes an award which [is apparently] [indicates that it is]² not intended to settle the dispute in full, the making of such an (interim, interlocutory, or partial) award does not terminate the mandate of the arbitral tribunal.³

¹Relevant discussion and conclusions of the Working Group in A/CN.9/216, para.73.

²Alternative wording is submitted here to stimulate discussion on whether an indication of the intent should be required (which could be interpreted as requiring a statement to that effect) or whether it would be more appropriate to require merely that the intent is apparent (or evident).

³If this draft article were to be retained, it might later be incorporated into the provisions, if any, on termination of arbitration proceedings (under IV.11).

^a31 August 1982. Referred to in Report, para. 87 (part one, A).

^bReproduced in this volume, part two, III, B, 1.

^cYearbook ... 1982, part two, III, A.

^dYearbook ... 1981, part two, III.

2. Making of an award⁴

Article 26⁵

(1) When there are three or another uneven number of arbitrators,⁶ any award [or other decision of the arbitral tribunal] shall be made by [all or] a majority of the arbitrators, provided that all arbitrators have taken part in the deliberations leading to the award [or decision].

[(2) In the case of questions of procedure, when there is no majority or when the arbitral tribunal so authorizes, the presiding arbitrator may decide on his own, subject to revision, if any, by the arbitral tribunal.]

3. Form of award⁷

Article 27

(1) An award shall be made in writing and shall be signed by the arbitral tribunal. If, in arbitration proceedings with more than one arbitrator, the signature of an arbitrator cannot be obtained, the signatures of a majority of the arbitrators shall suffice, provided that the fact and the reason for the missing signature are stated.

(2) An award shall be made at the place of arbitration (article 18). It shall state the place where and the date on which it is made. [The award shall be deemed to have been made at the place and on the date indicated therein.]⁸ [Failing such indication, the award shall be deemed to have been made at the place of arbitration and on the date on which it is signed by the arbitral tribunal.]⁹

(3) The arbitral tribunal shall state the reasons upon which the award is based, unless the parties have agreed that no reasons are to be given.¹⁰ The arbitral tribunal is not obliged to give reasons for an award on agreed terms.¹¹

⁴Discussion and conclusions of the Working Group in A/CN.9/216, paras. 74-77. As to the suggestion in para.75 (on possible legal consequences of undue delay by an arbitrator in conducting the proceedings) see draft article 11 (in A/CN.9/WG.II/WP.37).

⁵This draft provision is modelled on article 31 of the UNCITRAL Arbitration Rules (Yearbook ... 1976, part one, II, A, paras. 56-57).

⁶Despite the parties' freedom to agree on any number of arbitrators, no provision on an even number is suggested here, following the approach suggested in draft article 16 and accompanying footnote 28 (A/CN.9/WG.II/WP.37).

⁷Discussion and conclusions of the Working Group in A/CN.9/216, paras. 78-80.

⁸The sentence in parenthesis reflects the suggestion set forth in para. 79 of A/CN.9/216.

⁹The last sentence is modelled on article 22 of the ICC Rules of Arbitration (1975). It would indirectly express the view prevailing in the Working Group (A/CN.9/216, para.79) that an award was not invalid by the mere reason that the place and time where not stated therein.

¹⁰This sentence is modelled on article 32 (3) of the UNCITRAL Arbitration Rules.

¹¹This sentence could also be incorporated into the draft article relating to settlement by the parties (article 33).

4. Pleas as to arbitrator's jurisdiction¹²

Article 28

(1) [Subject to the provisions of paragraph (3) of this article,] a plea that the arbitral tribunal does not have jurisdiction, including any objections with respect to the existence or validity of the arbitration agreement, may be raised only in the arbitration proceedings and not later than in the statement of defence or, with respect to a counter-claim, in the reply to the counter-claim.¹³ [A plea that the arbitral tribunal has exceeded its terms of reference shall be raised during the arbitration proceedings promptly after the matter is raised on which the tribunal is alleged to have no jurisdiction.] [Where the delay in raising the plea is due to a cause which the arbitral tribunal deems justified, it shall declare the plea admissible.]¹⁴

[(2) The fact that a party has appointed, or participated in the appointment, of an arbitrator does not preclude that party from raising a plea referred to in paragraph (1) of this article.]¹⁵

[(3) Where either party to an arbitration agreement has initiated arbitration proceedings before any resort is had to a court, a court subsequently asked to deal with the same subject-matter between the same parties or with the question whether the arbitration agreement was non-existent or null and void or had lapsed, shall stay its ruling on the jurisdiction of the arbitral tribunal until the arbitral award is made, unless it has good and substantial reasons to the contrary.]¹⁶

Article 29¹⁷

(1) The arbitral tribunal has the power to rule on its own jurisdiction, including any objections with respect to the existence or validity of the arbitration clause, in accordance with the provisions of article 4,¹⁸ or of the separate arbitration agreement.

(2) The arbitral tribunal may rule on a plea concerning its jurisdiction either as a preliminary question or in the final award.

Article 30

A ruling by the arbitral tribunal that it has jurisdiction may be contested by either party,

¹²Discussion and conclusions of the Working Group in A/CN.9/216, paras. 81-83.

¹³This sentence is modelled on article 21 (3) of the UNCITRAL Arbitration Rules.

¹⁴The two sentences in parenthesis are modelled on article V(1.) of the European Convention on International Commercial Arbitration (Geneva, 1961; hereinafter referred to as 1961 Geneva Convention) (United Nations, *Treaty Series*, vol. 484, No. 7041 (1963-1964), p. 364).

¹⁵This draft provision is modelled on article 18 (4) of the Uniform Law annexed to the European Convention (Strasbourg, 1966) (*European Treaty Series*, No. 56).

¹⁶This draft provision is modelled on article VI (3.) of the 1961 Geneva Convention.

¹⁷This draft article is modelled on article 21 (1) and (4) of the UNCITRAL Arbitration Rules.

¹⁸The reference to article 4 need not be retained if draft article 4 itself is incorporated here (cf. footnote 13 in A/CN.9/WG.II/WP.37).

Alternative A:

whether it was made as a preliminary question or in the final award, only by way of recourse against the award under the procedure laid down in article ...¹⁹

Alternative B:

(a) if it was made as a preliminary question, [within one month] before the Authority specified in article 17, which has the power to order the termination of the arbitration proceedings for lack of jurisdiction;

(b) if it was made in the final award, by way of recourse against the award under the procedure laid down in article ...¹⁹.

5. *Law applicable to substance of dispute*²⁰*Article 31*

(1) The arbitral tribunal shall apply the law designated by the parties as applicable to the substance of the dispute.²¹ [Parties may so designate any national law or, even if not yet in force, a pertinent international convention or uniform law.]²²

(2) Failing such designation by the parties, the arbitral tribunal shall apply

Alternative A:

the law determined by the conflict of laws rules which it considers applicable.²³

Alternative B:

the substantive law rules which it considers most appropriate [, taking into account the various factors of the transaction and the interests of the parties]. [Such rules may form part of a given national legal system or of an international convention or uniform law, even if not yet in force].²⁴

(3) The arbitral tribunal [shall decide in accordance with the terms of the contract and] shall take into account the usages of the trade applicable to the transaction.²⁵ [It shall apply any usage to which the parties have agreed; the parties are considered, unless otherwise agreed, to have impliedly made applicable to their contract or its formation a usage of which they

knew or ought to have known and which in international trade is widely known to, and regularly observed by, parties to contracts of the type involved in the particular trade concerned.]²⁶

Article 32

The arbitral tribunal shall decide *ex aequo et bono* [or as *amiable compositeur*] [only] if the parties have expressly authorized it to do so.

6. *Settlement*²⁷*Article 33**Alternative A:*

(1) If, during the arbitration proceedings, the parties agree on a settlement of the dispute, the arbitral tribunal shall either issue an order for the termination of the arbitration proceedings, or if requested by both parties and accepted by the tribunal, record the settlement in the form of an arbitral award on agreed terms.²⁸

Alternative B:

(1) If, during the arbitration proceedings, the parties agree on a settlement of the dispute, the arbitral tribunal shall, if requested by [both parties] [a party, unless the arbitration agreement requires a request by both parties], record the settlement in the form of an arbitral award on agreed terms, unless the arbitral tribunal has [good and substantial] [compelling] reasons, in particular grounds of international public policy, not to follow that request.

(2) An award on agreed terms shall be made in accordance with the provisions of articles 27 and 35 and shall state that it is an award [on agreed terms]. Such an award [has the same status and executory force as] [shall be treated like] any other award on the merits of the case.

7. *Correction and interpretation of award*²⁹*Article 34*³⁰

(1) [Unless otherwise agreed by the parties,] within thirty days after the receipt of the award, either party,

¹⁹The reference is to a future draft article on the subject "VI. Setting aside or annulment of award", still to be considered by the Working Group.

²⁰Discussion and conclusions of the Working Group in A/CN.9/216, paras. 84-94.

²¹This sentence is modelled on article 33 (1) of the UNCITRAL Arbitration Rules.

²²The sentence in parenthesis reflects a suggestion set forth in para. 87 of A/CN.9/216.

²³Alternative A is modelled on article 33 (1) of the UNCITRAL Arbitration Rules.

²⁴Alternative B reflects the view reported in para. 89 of A/CN.9/216.

²⁵This sentence is modelled on article 33 (3) of the UNCITRAL Arbitration Rules.

²⁶The sentence in parenthesis reflects a suggestion set forth in para. 92 of A/CN.9/216 and is modelled on article 9 of the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980) (Yearbook ... 1980, part three, I, B).

²⁷Discussion and conclusions of the Working Group in A/CN.9/216, paras. 95-97.

²⁸This alternative is modelled on article 34 (1) of the UNCITRAL Arbitration Rules. If this alternative were to be adopted, the part referring to termination might later be incorporated into the provisions, if any, on "Termination of arbitration proceedings" (under IV.11).

²⁹Discussion and conclusions of the Working Group in A/CN.9/216, para. 98.

³⁰This draft article is modelled on articles 35 to 37 of the UNCITRAL Arbitration Rules. The draft provision on making an additional award is included here although the Working Group has not yet considered that issue.

with notice to the other party, may request the arbitral tribunal

(a) To correct in the award any errors in computation, any clerical or typographical errors, or any errors of similar nature; the arbitral tribunal may, within thirty days after the communication of the award make such corrections on its own initiative;

(b) To give, within forty-five days, an interpretation of a specific point or part of the award; such interpretation shall form part of the award;

(c) To make an additional award as to claims presented in the arbitration proceedings but omitted from the award; if the arbitral tribunal considers such request to be justified and that the omission can be rectified without any further hearings or evidence, it shall complete its award within sixty days after the receipt of the request.

(2) The provisions of articles 27, paragraphs (1) and (2), and 35 shall apply to a correction, interpretation or an additional award.

8. Delivery and registration of award³¹

Article 35³²

(1) After an award is made under article 27, copies thereof signed by the arbitral tribunal shall be communicated to the parties.³³

(2) Upon request by [the parties] [either party], the original award shall be filed with the Authority specified in article 17.³⁴ [This provision shall not be interpreted as making such filing a pre-condition for recognition or enforcement of the award.]

9. Executory force and enforcement of award.³⁵

Article 36

Alternative A:

Subject to any multilateral or bilateral agreement entered into by the State in which this Law is in force,³⁶ an arbitral award as defined in article 1

Alternative B:

An arbitral award as defined in article 1 and considered as a domestic award in the State in which this Law is in force,³⁶

shall be recognized as binding and enforced in accordance with the following rules of procedure:³⁷

(a) An application for recognition and enforcement of an arbitral award shall be made in writing to [the Authority specified in article 17];³⁸

(b) The party applying for recognition and enforcement shall, at the time of the application, supply the duly authenticated original award or a duly certified copy thereof and the original arbitration agreement referred to in article 3 or a duly certified copy thereof. [If the said award or agreement is not made in an official language of [the Authority] [this State], the party applying for recognition and enforcement of the award shall produce a translation of these documents into such language, certified by an official or sworn translator or by a diplomatic or consular agent.]³⁹

³⁵Discussion and conclusions of the Working Group in A/CN.9.216, paras. 103-104.

³⁶A State when adopting this model law may replace this reference by the name of that State or other appropriate wording.

³⁷It should be noted that this draft article deals only with procedure but not with substantive aspects (e.g. the question, dealt with under VI.2, of which objections may be raised against recognition and enforcement).

³⁸Designation of the Authority specified in article 17 may be particularly appropriate if alternative B were to be adopted. For alternative A, however, it might be preferable to refer to all courts or other judicial authorities competent to grant recognition and enforcement.

³⁹Subparagraph (b) is modelled on article IV of the 1958 New York Convention (United Nations, *Treaty Series*, vol. 330, No. 4739 (1959), p. 38). The last sentence, placed between square brackets, is unnecessary if alternative B were to be adopted.

³¹Discussion and conclusions of the Working Group in A/CN.9.216, paras. 100-102.

³²This draft article might later be combined with draft article 27.

³³This draft provision is modelled on article 32 (6) of the UNCITRAL Arbitration Rules.

³⁴The Working Group may wish to consider the appropriateness of including a similar provision for the filing of all documents and records of the arbitration proceedings, in particular in *ad hoc* arbitration.

**C. Report of the Working Group on International Contract Practices on the work of its fifth session
(New York, 22 February-4 March 1983) (A/CN.9/233)^a**

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Introduction

1. At its fourteenth session the Commission decided to entrust the Working Group on International Contract Practices with the task of preparing a draft model law on international commercial arbitration.¹

2. The Working Group commenced its work at its third session by discussing all but four of a series of questions prepared by the secretariat designed to establish the basic features of a draft model law.²

^a28 March 1983. Referred to in Report, para. 86 (part one, A).

^bReproduced in this volume, part two, III, D, 2.

^cReproduced in this volume, part two, III, D, 1.

^dReproduced in this volume, part two, III, D, 3.

¹Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 70 (Yearbook ... 1981, part one, A).

²Report of the Working Group on International Contract Practices on the work of its third session, A/CN.9/216 (Yearbook ... 1982, part two, III, A).

3. At its fourth session the Working Group completed its discussion on questions prepared by the secretariat on possible features of a draft model law on some further issues of arbitral procedure possibly to be dealt with in a draft model law. At that session the Working Group also considered draft articles 1 to 36 of a draft model law prepared by the secretariat.³

4. The Working Group consists of the following States members of the Commission: Austria, Czechoslovakia, France, Ghana, Guatemala, Hungary, India, Japan, Kenya, Philippines, Sierra Leone, Trinidad and Tobago, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland, and United States of America.

5. The Working Group held its fifth session in New York from 22 February to 4 March 1983. All the members were represented except Ghana.

³Report of the Working Group on International Contract Practices on the work of its fourth session, A/CN.9/232 (reproduced in this volume, part two, III, A).

6. The session was attended by observers from the following States: Argentina, Australia, Brazil, Bulgaria, Burma, Chile, China, Ecuador, Egypt, Fiji, Finland, German Democratic Republic, Germany, Federal Republic of, Greece, Holy See, Iraq, Italy, Malaysia, Mexico, Norway, Peru, Republic of Korea, Rwanda, Spain, Sudan, Sweden, Switzerland, Thailand, Turkey and Uruguay.

7. The session was attended by observers from the following United Nations secretariat units: United Nations Conference on Trade and Development and United Nations Industrial Development Organization. The session was also attended by observers from the following intergovernmental organizations: Asian-African Legal Consultative Committee, European Economic Community and Hague Conference on Private International Law; and from the following international non-governmental organizations: International Bar Association, International Chamber of Commerce, International Council for Commercial Arbitration and International Law Association.

8. The Working Group elected the following officers:
Chairman: Mr. I. Szasz (Hungary)
Rapporteur: Mr. P.K. Mathanjuki (Kenya)

9. The following documents were placed before the session:

(a) Report of the Secretary-General: possible features of a model law on international commercial arbitration (A/CN.9/207);^c

(b) Report of the Working Group on International Contract Practices on the work of its third session (New York, 16-26 February 1982) (A/CN.9/216);^f

(c) Report of the Working Group on International Contract Practices on the work of its fourth session (Vienna, 4-15 October 1982) (A/CN.9/232);^g

(d) Provisional agenda for the session (A/CN.9/WG.II/WP.39);

(e) Note by the secretariat: revised draft articles I to XXVI on scope of application, arbitration agreement, arbitrators, arbitral procedure and award (A/CN.9/WG.II/WP.40);^h

(f) Note by the secretariat: possible further features and draft articles of a model law (A/CN.9/WG.II/WP.41);^h

(g) Note by the secretariat: draft articles 37 to 41 on recognition and enforcement of award and on recourse against award (A/CN.9/WG.II/WP.42).^h

10. The Working Group adopted the following agenda:

- (a) Election of officers
- (b) Adoption of the agenda
- (c) Consideration of possible features and of draft articles of a model law on international commercial arbitration
- (d) Other business
- (e) Adoption of the report

Deliberations and decisions

11. The Working Group considered possible further features and tentative draft articles of a model law prepared by the secretariat, as contained in document A/CN.9/WG.II/WP.41. The Working Group requested the secretariat to redraft those articles in the light of its discussion and decisions at the present session.

12. The Working Group also considered revised draft articles I to XII, XXV and XXVI of a model law prepared by the secretariat, as contained in document A/CN.9/WG.II/WP.40. The Working Group decided to continue at its next session its discussion on revised draft articles XIII to XXIV not yet considered. The Working Group requested the secretariat to redraft revised draft articles I to XII, XXV and XXVI in the light of its discussion and decisions at the present session.

13. The Working Group further considered tentative draft articles 37 to 41 of a model law prepared by the secretariat, as contained in document A/CN.9/WG.II/WP.42. The Working Group requested the secretariat to redraft those articles in the light of its discussion and decisions at the present session.

14. The Working Group noted that probably two more sessions would be required to complete the task entrusted to it by the Commission. Subject to approval by the Commission, the Working Group decided to hold its sixth session from 29 August to 9 September 1983 at Vienna and the seventh session some time in February 1984, subject to the progress to be made at the sixth session. With regard to the languages to be used at meetings of the Working Group, a view was expressed that Arabic interpretation should be provided whenever such service was available.

1. Consideration of further features and draft articles of a model law (A/CN.9/WG.II/WP.41)

A. ADAPTION OF CONTRACTS AND FILLING OF GAPS IN CONTRACTS

15. The Working Group considered the question whether the model law should deal with the power of an arbitral tribunal to adapt a contract or fill gaps in a

^cYearbook ... 1981, part two, III.

^fYearbook ... 1982, part two, III, A.

^gReproduced in this volume, part two, III, A.

^hReproduced in this volume, part two, III, D, subsections 1-3.

contract (on the basis of a note by the secretariat, WP.41, paras. 2-11 and draft article A).

16. The Working Group noted that, especially in contracts performed over a longer period of time, the parties are often faced with the need to adapt or supplement their contract. It was also noted that it was inherent in the principle of autonomy of the parties that the parties may entrust a third person to decide on how the contract should be adapted or supplemented.

17. However, divergent views were expressed on the question whether the arbitral tribunal in this very capacity may be empowered by the parties to adapt or supplement their contract and whether an express rule to this effect should be included in the model law.

18. Under one view, the arbitral tribunal may assume the role of a third party intervener if the parties so wish, and by assuming such a role it still functions as an arbitral tribunal. Under this view, a rule to this effect would be useful because it would ensure that the process of adapting or supplementing a contract by the arbitral tribunal would be subject to the same procedural safeguards as the process of settling legal disputes. Also, the decision of the arbitral tribunal adapting or supplementing a contract should form an integral part of the contract between the parties and it should be subjected to the same rules as an arbitral award.

19. Under another view, the question of adapting or supplementing contracts by arbitral tribunals should not be dealt with in the model law. There were difficulties and uncertainties in drawing the line between procedural and substantive questions. It was also difficult to distinguish between gaps left intentionally by the parties and those "gaps" which tended to exist in every contract, since a contract is unlikely to expressly deal with each and every possible contingency, and which may become apparent only in the course of the performance of the contract.

20. The Working Group postponed its decision on whether the model law should contain a provision on this issue. It requested the secretariat to study the matter and, if appropriate, prepare a revised draft provision on adaptation and supplementation of contracts taking into account the views and concerns expressed in the discussion.

B. COMMENCEMENT OF ARBITRAL PROCEEDINGS AND CESSATION OF RUNNING OF LIMITATION PERIOD

21. The Working Group considered the question whether the model law should deal with issues relating to the cessation of the running of limitation periods by instituting arbitration proceedings (on the basis of a note by the secretariat, WP.41, paras. 12-18 and draft article B). Divergent views were expressed as to whether such a rule should merely define the point of time at which a limitation period, if provided in a national law, would cease to run or whether the rule, for the sake of

unification of laws, should itself regulate the cessation of the running of any limitation period. Some support was expressed for a broader rule which would indicate the cessation of the running of a limitation period as a legal consequence of the commencement of arbitral proceedings.

22. However, there was wide support in the Working Group that the model law should contain a rule which would define the moment of the commencement of arbitral proceedings. It was pointed out in support of that view that such a rule was sufficient for the model law and that any consequences of the commencement of arbitral proceedings, such as cessation of the running of the limitation period, touched upon questions which were outside the field of arbitral procedure and should therefore not be dealt with in the model law. It was also felt that a rule on the cessation itself, in order to be useful and workable, would have to be much more elaborate and settle many details which, in turn, could easily be in conflict with existing laws on prescription.

23. The Working Group requested the secretariat to prepare a draft provision in the light of the discussion at this session.

C. MINIMUM CONTENTS OF STATEMENTS OF CLAIM AND DEFENCE

24. The Working Group considered the question whether the model law should contain a provision, whether mandatory or not, on the minimum contents of the statements of claim and defence (on the basis of a note by the secretariat, WP.41, paras. 19-21).

25. There was general agreement that the model law should contain a rule on the initial pleadings by the parties. The prevailing view was that such a rule should only deal with those elements of initial pleadings which were essential for defining the dispute on which the arbitral tribunal is to give a decision. Some support was expressed for adding procedural rules along the lines of articles 18 to 20 of the UNCITRAL Arbitration Rules¹ to provide guidance to the parties and the arbitrators in cases where the parties have not themselves made any provision.

26. The Working Group deferred its decision on the question whether rules on initial pleadings by the parties should be mandatory or non-mandatory. The Working Group requested the secretariat to draft tentative provisions on the basis of the discussion and conclusions at the present session.

D. LANGUAGES IN ARBITRAL PROCEEDINGS

27. The Working Group considered whether the model law should contain a provision on the language or languages to be used in arbitral proceedings (on the basis of a note by the secretariat, WP.41, paras. 22-26 and draft article D).

¹Yearbook ... 1976, part one, II, A, paras. 56-57.

28. There was general agreement that a provision on the language to be used in arbitral proceedings was useful. The Working Group supported the principle that the parties and, in the absence of an agreement by the parties, the arbitrators should be free to determine the language or the languages of the proceedings. A clear statement of that principle appeared desirable to avoid a possible interpretation that the official (court) language used at the place of arbitration should also be decisive for the arbitral proceedings.

29. The Working Group expressed the view that there was no need for the model law to suggest to the parties to use their best efforts to agree on a single language because such a suggestion was either superfluous or without effect for lack of sanction. The view was also expressed that, while it was implied that in determining the language of the proceedings the arbitral tribunal must have regard to the circumstances of the case, it was not appropriate to expressly state that requirement because it could create unnecessary disagreements over the weighing of different circumstances and because it was in a way self-evident.

30. It was also suggested that, in order to avoid misunderstandings, the model law should make it clear that the determination of a language or languages may relate to all or only certain documents or communications to be specified (e.g., as envisaged in article 17 of the UNCITRAL Arbitration Rules). In that context it was suggested that the arbitral award might be regarded as not forming part of the arbitral proceedings and that the question of the language of the award should be covered by such provision.

E. COURT ASSISTANCE IN TAKING EVIDENCE

31. The Working Group considered the question whether the model law should deal with issues relating to the right of an arbitral tribunal or the parties to request a court for assistance in taking evidence (on the basis of a note by the secretariat, WP.41, paras. 27-37 and draft articles E1 to E3).

32. Divergent views were expressed as to the question whether the model law should deal with court assistance in taking evidence. The prevailing view was that a possibility of requesting such assistance would facilitate the functioning of international commercial arbitration and that, therefore, rules on these issues were desirable. Under another view, the possibility of a court being active in taking evidence to be used in arbitral proceedings was contrary to the private nature of arbitration and might lead to undesirable intervention of courts in arbitral proceedings.

33. The Working Group discussed the two alternative approaches contained in draft article E1. The first alternative was that the requested court merely contributed the element of compulsion and thus enabled the arbitral tribunal to take evidence, and the second alternative was that the requested court took the evidence itself. Some support was expressed for each

alternative. However, the view prevailed that a combination of both alternatives was desirable. Such a combined approach would allow the court which was requested to give assistance to decide whether assistance is to be given in such a way that the court itself takes evidence or whether compulsion is to be provided by the court to enable the arbitral tribunal to take evidence. Such a combined approach would also have the advantage of allowing the court to give assistance according to its own rules of procedure.

34. Divergent views were expressed as to the question whether a party should have a right to directly request a court for assistance. The prevailing view was that a party should request for court assistance only through the arbitral tribunal or with its approval, in order to prevent abuse of court assistance. Under another view, account should be taken of arbitration practice according to which arbitral tribunals are not involved in gathering evidence. According to this view, the mere fact that court assistance was needed in procuring evidence did not warrant involving the arbitral tribunal in the process of gathering evidence.

35. In respect of article E2, which contained provisions on the contents of a request for court assistance, there was general agreement that this provision was too detailed and should not be included in the model law.

36. In respect of article E3, which contained provisions on assistance by the courts of the State which adopted the model law to foreign arbitral tribunals, the prevailing view was that, if court assistance were to be regulated at all in the model law, a provision on such international court assistance would be useful. The Working Group supported the view that requests by foreign arbitral tribunals should be treated like similar requests by foreign courts (as expressed in paragraph (2) of article E3). It was suggested that this rule would be more easily acceptable if a request for assistance from a foreign court would have to be made through a court in the State in which the arbitration took place.

37. It was further suggested that the model law should not contain detailed procedural rules on international court assistance to arbitral tribunals and that it might be desirable to elaborate such rules either in a separate convention or by extending an existing convention. The Working Group requested the secretariat to take note of that suggestion as a possible future item of work to be discussed by the Commission.

F. TERMINATION OF ARBITRAL PROCEEDINGS

38. The Working Group considered the question whether it would be appropriate to include in the model law a provision on termination of arbitral proceedings (on the basis of a note by the secretariat, WP.41, paras. 38-41 and draft article F).

39. There was wide support in the Working Group for the view that the model law should contain a

provision on termination of arbitral proceedings. Such a provision would be useful because it would provide certainty in respect of important consequences of the termination of arbitral proceedings.

40. The prevailing view was that there should be no automatic termination of arbitral proceedings and that a procedural decision by the arbitral tribunal was needed for terminating the arbitral proceedings. However, it was suggested that the wording should indicate that a special order of termination was not always necessary, for example, when the dispute was settled by an agreement of the parties or by an award on the merits of the claim.

41. It was also suggested that the model law should contain a rule empowering the arbitral tribunal to decide whether it was appropriate to terminate the proceedings after the tribunal gave suitable notice to the parties of its intention to terminate the proceedings.

G. PERIOD FOR ENFORCEMENT OF ARBITRAL AWARDS

42. The Working Group considered the question whether the model law should contain a provision on the period during which an arbitral award may be enforced (on the basis of a note by the secretariat, WP.41, paras. 42-45 and draft article G).

43. The prevailing view was that such a provision was useful for reasons of certainty. Under another view, such a rule was not necessary because States had solutions to this question and there was no need that the model law attempted a unification of this issue. In support of this view it was pointed out that a number of national laws treated arbitral awards like court decisions in this respect.

44. The Working Group felt that alternative B providing a period with a fixed time-limit was to be preferred for reasons of simplicity in its application.

45. Divergent views were expressed concerning the starting point for the period for enforcement of arbitral awards. Under one view, the period should start to run from the date when the award was made. Under another view, the starting point should be the date when the award was received by the party requesting the enforcement. Under yet another view, the starting point should be the date when the award was received by the party against whom enforcement is sought. The secretariat was requested to prepare a draft provision reflecting the views expressed by the Working Group.

II. Consideration of revised draft articles I to XXVI of a model law on international commercial arbitration (A/CN.9/WG.II/WP.40)

46. The Working Group proceeded to a consideration of revised draft articles I to XXVI for a model law on international commercial arbitration (set forth in

document A/CN.9/WG.II/WP.40). Those revised draft articles had been prepared by the secretariat on the basis of the discussion and decisions of the Working Group at its fourth session (see the report of the Working Group, A/CN.9/232, paras. 24-189). Of these revised draft articles, the Working Group considered, at the present session, articles I to XII and then articles XXV and XXVI.

A. SCOPE OF APPLICATION

Article I

47. The text of article I as considered by the Working Group was as follows:

Article I

“(1) This Law applies to international commercial arbitration as specified in paragraphs (2), (3) and (4) of this article.

“(2) ‘Arbitration’ includes [all matters of arbitration, in particular]

“(a) Arbitration agreements [as defined in article II, para. (1)];

“(b) The preparation and conduct of arbitration proceedings based on such agreements whether or not administered by a permanent arbitral institution; and

“(c) The arbitral awards resulting therefrom.

“(3) ‘Commercial’ refers to any [defined legal] relationship of a commercial [or economic] nature [including, for example, any trade transaction for the supply or exchange of goods, factoring, leasing, construction of works, consulting, engineering, commercial representation, investment, joint venture and other forms of industrial or business co-operation, financing, or providing of services].

“(4) ‘International’ are those cases where the arbitration agreement is concluded by parties whose places of business are in different States. If a party has more than one place of business, the relevant place of business is [that which has the closest relationship to the arbitration agreement] [the seat of the head office].”

Paragraph (1)

48. The Working Group was agreed that the model law should specify its scope of application. It was also agreed that this scope—in line with the mandate given to the Working Group by the Commission—was “international commercial arbitration”, as stated in paragraph (1).

49. However, divergent views were expressed as to the “definitions” of the three elements (“arbitration”, “commercial”, “international”) suggested in paragraphs (2), (3) and (4). As a result of the decisions on those paragraphs (see below, paras. 50-60), the Working Group decided to delete the words “as specified in

paragraphs (2), (3) and (4) of this article" and requested the secretariat to consider combining the remaining words of paragraph (1) with other provisions in a revised concise draft of the whole article.

Paragraph (2)

50. Some support was expressed for retaining paragraph (2) with some modifications. The prevailing view, however, was that the provision should not be retained, except for the useful clarification that the model law covered arbitration whether or not administered by a permanent arbitral institution. It was thought that paragraph (2) did not contain a definition of the term "arbitration" but merely a table of contents and was therefore superfluous (since *lex ipsa loquitur*). In addition, it might even be harmful by not being complete.

51. The Working Group, after deliberation, decided to delete paragraph (2) but to retain the idea expressed by the words "whether or not administered by a permanent arbitral institution" in subparagraph (b). It was suggested that those words might be inserted in article II, paragraph (1), after the words "submit to arbitration".

Paragraph (3)

52. The Working Group was agreed that the term "commercial" should be given a wide interpretation but divergent views were expressed as to whether and, if so, in what manner the term should be defined in the model law. There was even some concern as to the use of the term as such in that, under some legal systems, it might be construed as applying only to transactions by "commercial persons" (merchants) as defined by a given national law.

53. Under one view, the model law should not attempt to define the term "commercial" since no satisfactory definition had been found to date. Under another view, which also recognized the great difficulties in finding a workable definition, it was sufficient to state in general terms that "commercial" referred to a "relationship of a commercial nature or", as supported by some representatives, "of an economic character". In support of those views, it was pointed out that the illustrative list of commercial transactions set forth in paragraph (3) was inappropriate for various reasons: (a) inclusion of a list of examples was contrary to the legislative techniques in a number of legal systems; (b) courts might interpret the list as exhaustive despite its express illustrative nature; (c) the examples contained in the list were unbalanced in that important transactions were missing (e.g., maritime transport, banking, insurance, licensing); (d) some of the examples (e.g., consulting, providing of services) were too wide or vague and thus more harmful than helpful.

54. Under yet another view, however, it was useful to include in the model law a list, despite its shortcomings, since it would provide some guidance and help to prevent too restrictive interpretations as found in some national laws or legal doctrine. The proponents of that view suggested various amendments to the list.

55. In view of the divergency of views in the Working Group, it was also suggested that the list could be placed in a footnote to article I rather than in the body of the text itself. Yet another suggestion was to include the list in a commentary, if one were to be published with the final model law.

56. The Working Group, after deliberation, decided not to retain paragraph (3). It requested the secretariat to draft a footnote to the term "commercial" in paragraph (1), which would contain the substance of paragraph (3) and take into account the suggested amendments and the need for clarifying that not only transactions between merchants but also others were covered.

Paragraph (4)

57. There was general agreement that the term "international" should be given a wide interpretation. However, divergent views were expressed as to how this could be done in a satisfactory and clear manner.

58. Under one view, the definition suggested in paragraph (4) did not fully correspond with international practice and excluded some important international situations (e.g., arbitration between parties of same State about foreign subject-matter; arbitration between parties of same State, one of which is controlled and managed by foreign company). It was suggested, therefore, to adopt a more general formula such as, e.g., "transaction involving international trade interests". Another suggestion in this direction was to add to paragraph (4) a provision allowing parties to agree on the application of the model law provided that there was an international element in their relationship (possibly to be established by objective criteria such as the ones mentioned in footnote 7 of WP.40).

59. The prevailing view was that the first sentence of paragraph (4) presented a solid basis for determining the international character. As to the second sentence, divergent views were expressed as to which of the alternative solutions was to be preferred. In support of the second alternative (i.e. seat of head office, or better: principal place of business) it was noted that that text provided greater certainty and would enhance the applicability of the model law. There was wider support, however, for the first alternative (closest relationship) since it was similar to the solution adopted in the United Nations Convention on Contracts for the International Sale of Goods (Vienna 1980; article 10 (a)) and because it reflected the probable interests and wishes of the parties. It was suggested that the relevant connecting factor was not only the arbitration agreement but also its implementation and, possibly, the subject-matter of the dispute.

60. The Working Group, after deliberation, decided to retain paragraph (4), except for the second alternative, as a basis for future reconsideration and requested the secretariat to prepare, for future consideration, an additional draft provision containing a wider and more

general definition, possibly with an enumeration of objective criteria. Such a formula could be used in an "opting-in" provision or as a substitute for paragraph (4) itself.

B. ARBITRATION AGREEMENT

Article II

61. The text of article II as considered by the Working Group was as follows:

Article II

"(1) ['Arbitration agreement' is an agreement by parties to] [In an 'arbitration agreement' parties may] submit to arbitration all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not.

"(2) The arbitration agreement, whether an arbitration clause in a contract or a separate agreement, shall be in writing [, i.e.] [. An agreement is in writing if it is] contained in a document signed by the parties or in an exchange of letters, telegrams or other communications [in sufficiently permanent form] [of equal evidential value]. The reference in a contract to general conditions, or similar legal texts, containing an arbitration clause constitutes an arbitration agreement provided that the contract is in writing and the reference is such as to make that clause a part of the contract."

Paragraph (1)

62. The Working Group was agreed that a provision along the lines of paragraph (1) should be retained in the model law. As to the text placed between square brackets, some support was expressed for the second alternative. The prevailing view, however, was in favour of the first alternative since it was deemed useful to cast the provision in the form of a definition.

63. Some support was also expressed in favour of deleting the words "defined legal" since they might lead to an undesirable restriction. However, the prevailing view was to retain those words which were also found in the 1958 New York Convention (art. II (1)).

64. Accordingly, the Working Group decided to retain paragraph (1) with the first alternative. In that context, it was noted that that provision would be an appropriate place for expressing the idea that the model law covered arbitration whether or not administered by a permanent arbitral institution (see above, para. 51).

Paragraph (2)

65. The Working Group was agreed that a provision along the lines of paragraph (2) should be included in the model law.

66. There was some support for expressing the idea that the model law should not invalidate arbitration

agreements which did not comply with the requirement of written form. Oral agreements which were common in some places and trades should not be covered by the model law, thus leaving open their regulation and recognition under another law. The prevailing view, however, was that the model law should govern all international commercial arbitration agreements and, as provided in paragraph (2), require that they be in writing. It was noted in that context that the model law, in its present form, did not fully specify the legal consequences of non-compliance with that form requirement. A suggestion was made to envisage the possibility of parties curing such defect by participating in the arbitration proceedings—an idea, which might be embodied in a waiver rule of more general application (e.g., article 30 of the UNCITRAL Arbitration Rules).

67. As regards the first two alternatives in square brackets, some support was expressed for each of them and additional drafting proposals were made. As regards the second set of alternatives attempting to qualify "the other communications", some support was also expressed for each of them. However, the prevailing view was that neither of those attempts was fully satisfactory. It was, therefore, suggested to adopt the first sentence without any of the alternatives unless the secretariat could find a more satisfactory wording to express the idea, supported by all, that modern means of communication should be included.

68. As regards the last sentence, some doubts were expressed as to its clarity. The Working Group adopted a suggestion to redraft the sentence as follows: "The reference in a contract to an arbitration clause contained in another legal text constitutes an arbitration agreement provided that the contract is in writing and the reference is such as to make that clause a term of the contract".

C. ARBITRATION AND THE COURTS

Article III

69. The text of article III as considered by the Working Group was as follows:

[Article III]

"In matters governed by this Law, no court shall intervene except where so provided in this Law."

70. Divergent views were expressed as to the appropriateness of including in the model law a provision along the lines of article III. Under one view, such a provision was unacceptable for a number of reasons:

(a) Its scope and effect could not be determined in view of the disparity between national laws as regards instances of court intervention;

(b) It created the impression that court intervention was something negative and to be limited to the utmost;

(c) It could adversely affect the positive and helpful attitude of courts towards arbitration.

71. Under another view, however, article III should be retained since it provided certainty as to when a court might intervene in arbitration matters and obliged the drafters of the model law to enumerate all such instances. It was also pointed out that the model law, in its present form, already covered most of the cases where control or assistance by courts seemed justified and that in international commercial arbitration control by courts should be kept to a minimum.

72. Under yet another view, it was premature to take a decision on article III since it was not clear at this point what the model law would cover in its final form. It was more important to clarify in model law instances where court intervention was appropriate.

73. That view was adopted by the Working Group after deliberation. Accordingly, the decision on article III was postponed and its underlying policy accepted as an intention of the Working Group to clarify, in the course of the preparation of the draft model law, instances of court intervention.

Article IV

74. The text of article IV as considered by the Working Group was as follows:

Article IV

“(1) A court, before which an action is brought in a matter which is the subject of an arbitration agreement, shall, at the request of a party, refer the parties to arbitration unless it finds that the agreement is null and void, inoperative or incapable of being performed.

“(2) A plea that the court [referred to in paragraph (1)] has no jurisdiction because of the existence of a valid arbitration agreement may be raised by a party not later than in his statement on the substance of the dispute.

“(3) Where arbitration proceedings have commenced and such a plea is raised before the court or a party requests from [a court] [the Court specified in article V] a ruling that the arbitral tribunal has no jurisdiction the arbitral tribunal may either continue or suspend the arbitration proceedings until its jurisdiction is decided on by that court.

“(4) Any party may address to a court a request for interim measures of protection, whether before or during arbitration proceedings. This shall not be deemed incompatible with the agreement to arbitrate or as a waiver of that agreement.”

75. The Working Group was agreed that article IV should be retained with some suggested modifications. A drafting proposal of general relevance was to make clear in all languages that the term “court” referred to the court of a State as distinguished from an arbitral tribunal.

Paragraph (1)

76. Some support was expressed for deleting the words “at the request of a party”. The prevailing view, however, was to retain those words, in line with the corresponding provision in the 1958 New York Convention^k (article II (1)). Also for the sake of consistency with that important Convention, it was decided to retain the words “shall refer the parties to arbitration” and not to substitute, as suggested by some, the words “shall decline jurisdiction”. A suggestion was made to replace the words “shall, at the request of a party, refer the parties to arbitration” by the words “shall, at the request of the parties, refer the issue to arbitration”.

77. A suggestion was made that paragraph (1) should not be understood as requiring the court to examine in detail the validity of an arbitration agreement and that this idea could be expressed by requiring only a *prima facie* finding or by rephrasing the closing words as follows: “unless it finds that the agreement is manifestly null and void”. In support of that idea it was pointed out that it would correspond with the principle to let the arbitral tribunal make the first ruling on its competence, subject to later control by a court. However, the prevailing view was that, in the cases envisaged under paragraph (1) where the parties differed on the existence of a valid arbitration agreement, that issue should be settled by the court, without first referring the issue to an arbitral tribunal, which allegedly lacked jurisdiction. The Working Group, after deliberation, decided to retain the text of paragraph (1).

Paragraph (2)

78. The Working Group adopted this paragraph subject to the deletion of the word “valid” and the insertion of the word “first” before the word “statement”. A suggestion was made that the words “has no jurisdiction” be modified to reflect the position in some legal systems that, while a court may have jurisdiction, it should decline to exercise that jurisdiction if there is a valid arbitration agreement.

Paragraph (3)

79. It was noted that this provision was related to the issue dealt with in article XIII. It might, therefore, have to be reconsidered in the light of the discussion on that article. It was also suggested to consider rearranging the order of the provisions.

80. As regards the alternatives placed between square brackets, the Working Group was divided on which was the better solution and decided, for the time being, to adopt the first alternative (i.e. “a court”). The Working Group was agreed that the arbitral tribunal should have the procedural power to either continue or suspend the arbitration proceedings when its jurisdiction was challenged before a court. It was noted, however, that the possibility of a suspension might encourage a party to challenge the jurisdiction merely

^kUnited Nations, Treaty Series, vol. 330, No. 4739 (1959), p. 38.

for dilatory purposes. It was, therefore, suggested to seek a wording which could meet this concern.

Paragraph (4)

81. The Working Group requested the secretariat to redraft this provision so as to express more clearly the idea that the involvement and decision of a court (or other judicial authority) with regard to interim measures of protection was not incompatible with the arbitration agreement. A suggestion was made to include also interim measures of securing evidence (e.g., inspection of goods by independent expert).

Article V

82. The text of article V as considered by the Working Group was as follows:

Article V

"(1) The special Court entrusted by this Law with functions of arbitration assistance and control [under articles VIII (2), (3), X (2)/(3), XI (2), XIII (3), XIV, XXV, XXVI ...]

"shall be the ... (blanks to be filled by each State when enacting the model law).

"(2) Unless otherwise provided in this Law,

"(a) this Court shall act upon request by any party or the arbitral tribunal; and

"(b) the decisions of this Court shall be final."

Paragraph (1)

83. The Working Group decided to delete the word "special" and requested the secretariat to redraft the provision without using the term "control".

Paragraph (2)

84. Divergent views were expressed as to the appropriateness of a provision along the lines of paragraph (2). Under one view, the provision was useful in that it regulated some basic features of the procedure to be followed by the Court, with the possibility of making exceptions thereto in the model law itself. In support of subparagraph (b), it was pointed out that it would serve the purpose of expediting the proceedings which was of special importance in international commercial arbitration.

85. Under the prevailing view, however, the provision should not be retained. It was pointed out that paragraph (2), in particular its subparagraph (b), infringed upon fundamental concepts and rules of court procedure. Nevertheless, its procedural features (right to request and finality of decision) might be included in individual provisions of the model law entrusting the Court with certain functions.

86. The Working Group, after deliberation, decided not to retain paragraph (2) and to consider settling the procedural questions in the context of the individual provisions referring to the Court specified in article V.

D. COMPOSITION OF ARBITRAL TRIBUNAL

Article VI

87. The text of article VI as considered by the Working Group was as follows:

Article VI

"(1) No person shall be by reason of his nationality precluded from acting as arbitrator, unless otherwise agreed by the parties.

"(2) An arbitration agreement is invalid [if] [to the extent that] it accords one of the parties a [predominant position] [manifestly unfair advantage] with regard to the appointment of arbitrators."

Paragraph (1)

88. The Working Group decided to retain this provision.

Paragraph (2)

89. Divergent views were expressed as to the appropriateness of a provision along the lines of paragraph (2). Under one view, such a rule was useful in that it served the purposes of equality and fairness, although the need for such a rule in international commercial arbitration may be limited to few instances. The proponents of this view expressed a preference for the second of either set of alternatives (i.e. "to the extent that" and "manifestly unfair advantage").

90. The prevailing view, however, was to delete paragraph (2) since (a) there was no real need for such a rule in view of the fact that the few instances aimed at could appropriately be dealt with by other provisions of the model law (e.g., on challenge of arbitrator or setting aside of award); (b) the wording was too vague and could thus lead to controversy or dilatory tactics and, above all, to a misinterpretation which could endanger well-established and recognized appointment practices; (c) the legal sanction, in particular the idea of partial invalidity, was not sufficiently clear.

91. The Working Group, after deliberation, decided to delete paragraph (2). That decision, however, should not be understood as condoning practices where one party had a clearly greater influence on the appointment without good reasons.

Article VII

92. The text of article VII as considered by the Working Group was as follows:

Article VII

"The parties are free to determine the number of arbitrators. Failing such determination, [three arbitrators] [a sole arbitrator] shall be appointed."

93. The Working Group adopted this article with the first alternative (i.e. "three arbitrators"). It was pointed out that, in view of the parties' freedom recognized in the first sentence, the number of arbitrators provided in

the second sentence was of limited practical relevance and merely a last resort in case of non-agreement. In particular, where parties wanted a sole arbitrator for the sake of saving time and costs, they would normally agree thereon.

Article VIII

94. The text of article VIII as considered by the Working Group was as follows:

Article VIII

“(1) Subject to the provisions of article VI (2), the parties are free to agree on a procedure of appointing the arbitrator or arbitrators.

“(2) Failing such agreement,

“(a) if, in an arbitration with a sole arbitrator, the parties are unable to agree on the arbitrator, he shall be appointed by the Court specified in article V;

“(b) in an arbitration with three arbitrators, each party shall appoint one arbitrator and the two arbitrators thus appointed shall appoint the third arbitrator.

“(3) Where [the composition of an arbitral tribunal becomes unduly delayed because] the parties, or two arbitrators, are unable to reach agreement or where one of the parties, or any designated appointing authority, fails to act as required under an agreed appointment procedure or under this Law, the Court specified in article V may be requested [by any party or arbitrator] to take the necessary measure instead.

“(4) The Court, in appointing an arbitrator, shall have regard to such considerations as are likely to secure the appointment of an independent and impartial arbitrator and, in the case of a sole or a third arbitrator, shall take into account as well the advisability of appointing an arbitrator of a nationality other than the nationalities of the parties.”

Paragraph (1)

95. The Working Group noted that, pursuant to its decision on article VI (2) (see para. 91 above), the opening words “Subject to the provisions of article VI (2)” were obsolete. Subject to this deletion, the text of paragraph (1) was adopted.

Paragraph (2)

96. The Working Group adopted this paragraph. A suggestion was made to reverse the order of subparagraphs (a) and (b).

Paragraph (3)

97. It was noted that paragraph (3) was not sufficiently clear because it attempted to cover too many different fact situations. The first distinction to be drawn was between appointment procedures agreed upon by the parties and those procedures provided in the model law;

it was submitted that in that second category the need for court assistance was greater than in the first one. Another distinction to be made related to the person or institution that failed to act (i.e. a party, the parties, two arbitrators, or an appointing authority).

98. The Working Group was agreed that the words “becomes unduly delayed” were too vague and that more definite time-periods should be set. It was suggested, for example, to fix a time-period of, for example, thirty days or, as between two parties or arbitrators, to require a notice in which a time-period for action would be fixed.

99. The Working Group requested the secretariat to redraft paragraph (3) in the light of the views expressed in the Working Group.

Paragraph (4)

100. While some concern was expressed about giving a court instructions of the type set forth in paragraph (4), the Working Group decided to retain this provision. A suggestion was made to add to the criteria mentioned in that provision other important features such as competence, qualification, experience.

New rule of interpretation

101. In connection with the discussion on article VIII, the Working Group considered a suggestion by the secretariat (set forth in the introductory note to document A/CN.9/WG.II/WP.40, para. 4). The suggestion was to express in a general rule of interpretation that (a) the freedom of the parties to determine a certain point included the freedom to authorize a third person or institution to make that determination; and (b) agreement by the parties included any reference to arbitration rules.

102. The Working Group was agreed that such clarification was helpful in view of the common practice of using arbitration rules and entrusting certain decisions to third persons or institutions. It was also preferable to clarify that matter in a general rule rather than in each of the many provisions, where that point was relevant.

Article IX

103. The text of article IX as considered by the Working Group was as follows:

Article IX

“(1) A prospective arbitrator shall disclose to those who approach him in connection with his possible appointment any circumstances likely to give rise to justifiable doubts as to his impartiality or independence. An arbitrator [, from the time of his appointment,] shall disclose any such circumstances to the parties unless they have already been informed by him of these circumstances.

“(2) An arbitrator may be challenged only if circumstances exist that give rise to justifiable

doubts as to his impartiality or independence. A party may challenge the arbitrator appointed by him only for reasons of which he becomes aware after the appointment has been made."

104. The Working Group was agreed that a provision along the lines of article IX was useful. It was noted that the provision should not be understood as requiring the arbitrator to act as a judge on his own impartiality or independence.

105. Some concern was expressed that the provisions of article IX, in particular its paragraph (2) using the word "only", were too restrictive by not covering, for example, the notion of competence or other qualifications possibly included in the agreement on the appointment. The prevailing view was, however, that the issue of competence or other qualifications was more closely related to the conduct of the proceedings than to the initial appointment and that the article should be retained with its present scope.

106. As regards the second sentence of paragraph (1), it was suggested to express more clearly the idea that the duty to disclose was a continuing one, for example, by adding to the words submitted between square brackets the words "and thereafter" or by other appropriate wording.

Article X

107. The text of article X as considered by the Working Group was as follows:

Article X

"(1) The parties are free to agree on the procedure for challenging an arbitrator subject to the provisions of paragraph (3) of this article.

Alternative A:

"(2) Failing such agreement, a party who intends to challenge an arbitrator shall, within fifteen days after knowing about the appointment or the circumstances referred to in article IX (2), send a written statement of the reasons for the challenge to the other party and to all arbitrators. The mandate of the arbitrator terminates when the other party agrees to the challenge or the arbitrator withdraws from his office; in neither case does this imply acceptance of the validity of the grounds for the challenge.

"(3) If a challenge

"(a) under paragraph (2) of this article is not successful within 30 days after the receipt of the written statement by the other party and by the challenged arbitrator, or

"(b) under any challenge procedure agreed upon by the parties, is neither accepted by the other party or the challenged arbitrator nor sustained by any person or body entrusted with the decision on the challenge,

"the challenging party may [request the Court specified in article V to decide on the challenge]

[pursue his objections before a court only in an action for setting aside the arbitral award]."

Alternative B

"(2) Where an arbitrator is challenged without success, whether or not under a procedure agreed upon by the parties, the challenging party may [request the Court specified in article V to decide on the challenge] [pursue his objections before a court only in an action for setting aside the arbitral award]."

Paragraph (1)

108. The Working Group adopted that paragraph.

Paragraphs (2) and (3) of alternative A and paragraph (2) of alternative B

109. The Working Group was divided on whether alternative A or alternative B presented the better approach. Under one view, alternative A was too detailed for a model law, in particular subparagraphs (a) and (b) of paragraph (3), although it was recognized that a time-period was useful. Under another view, alternative A was useful in providing procedural guidance, while alternative B was regarded as too concise. The Working Group, after deliberation, decided to take alternative A as the basis for future consideration and requested the secretariat to prepare a revised draft with a shorter version of paragraph (3).

110. Divergent views were expressed on whether the challenging party may (a) request the Court specified in article V to decide on the challenge or (b) pursue his objections before a court only in an action for setting aside the arbitral award. The main reason in support of the first alternative was that it would help to settle the question expeditiously and to avoid the unfortunate situation that arbitration proceedings, with a party having challenged an arbitrator, would have to be carried through. The main reason in support of the second alternative was that it would help to prevent dilatory tactics by a party. In response to this, some proponents of the first alternative pointed out that this concern could be alleviated by setting a time-limit for resort to court and by allowing the arbitral tribunal to continue with the proceedings until the decision by the court.

111. The Working Group, after deliberation, decided to retain both alternatives placed between square brackets, with possible drafting amendments. It was understood, however, that the final text of the model law should contain only one of the alternatives.

Article XI

112. The text of article XI as considered by the Working Group was as follows:

Article XI

"(1) The mandate of an arbitrator terminates in the event of the *de jure* or *de facto* impossibility of his performing his functions or, unless other-

wise agreed by the parties, in the event that he fails to act [in accordance with his mandate under the arbitration agreement].

"(2) If a dispute arises concerning any of the cases envisaged in paragraph (1), any party or arbitrator may request the Court specified in article V to decide on the termination of the mandate."

Paragraph (1)

113. Concern was expressed about the approach suggested in this provision which linked an automatic legal consequence (i.e. termination of mandate) to a vague cause (in particular: "fails to act"). It was suggested to adopt, instead, an approach similar to the one taken in the second sentence of paragraph (2) of alternative A of article X.

114. As regards the words "fails to act", various amendments were suggested, e.g., to add the word "adequately" or to focus on a misconduct of the proceedings by the arbitrator. The prevailing view, however, was that the words "fails to act", though not abundantly clear, were to be preferred to any suggested amendment. In that context it was noted that paragraph (2) provided a procedure in cases of uncertainty or controversy about a failure to act. No support was expressed in favour of the words placed between square brackets.

115. The Working Group, after deliberation, requested the secretariat to prepare a revised draft, taking into account the concerns and views expressed during the discussion.

Paragraph (2)

116. It was suggested not to use the technical term "dispute" in that context and to replace it by more general wording such as "difficulty" or "controversy". Some concern was expressed about giving an arbitrator the right to request a court decision, while, under another view, such a right may be appropriate in some cases.

117. The Working Group, after deliberation, requested the secretariat to revise that provision, taking into account the views expressed in the Group.

Article XII

118. The text of article XII as considered by the Working Group was as follows:

Article XII

"In the event of the death or resignation of an arbitrator or the termination of his mandate under article X or XI, a substitute arbitrator shall be appointed according to the rules that were applicable to the appointment of the arbitrator being replaced, unless the parties agree otherwise. [However, if the arbitrator to be replaced was named in the arbitration agreement, that agreement shall lapse *ipso jure*]."

119. A suggestion was made to retain the sentence placed between square brackets since in the case envisaged therein the parties had expressed clearly that they had confidence only in the person named in the arbitration agreement. The prevailing view was, however, that that sentence was not needed in view of the faculty of the parties, provided at the end of the first sentence, to agree "otherwise". It was also pointed out that an automatic lapsing of the arbitration agreement was not necessarily in the interest of the parties.

120. The Working Group, after deliberation, decided to retain the first sentence of that article.

J. RECOGNITION AND ENFORCEMENT OF AWARD

Article XXV

121. The text of article XXV as considered by the Working Group was as follows:

Article XXV

"An arbitral award made in the territory of this State shall be recognized as binding and enforced in accordance with the following procedure [unless recognition and enforcement of such awards are granted under less onerous conditions]:

An application shall be made in writing to the [competent court] [Court specified in article V], accompanied by the duly authenticated original award, or a duly certified copy thereof, and the original arbitration agreement referred to in article II, or a duly certified copy thereof."

122. The Working Group noted that the provisions of article XXV which dealt with arbitral awards made in the territory of the State where recognition or enforcement was sought were not essentially different from the provisions of article XXVI which dealt with arbitral awards made in a foreign State. However, the view prevailed that, for the sake of clarity and possible different treatment of domestic and foreign awards in other respects, it was advisable to have separate articles on those two types of awards.

123. The Working Group was agreed that the objective of article XXV was to set forth maximum procedures for recognition or enforcement of an award made in the same State and that it was not contrary to the harmonization to be achieved by the model law if a State retained an even less onerous procedure.

124. As to the demarcation line between the awards dealt with in article XXV and the awards dealt with in article XXVI, the Working Group supported the territorial principle as opposed to the principle of wider recognition of the autonomy of the parties, i.e., arbitral awards dealt with in article XXV are only those made in the State where recognition or enforcement was sought excluding awards made in a foreign State but submitted by the agreement of the parties to the

procedural law of the State where recognition or enforcement was sought. It was noted, however, that this preference for the territorial approach was limited to the articles under consideration here and would not preclude the possibility of drawing the line differently in respect of other provisions (e.g., on setting aside of awards).

125. It was noted that an arbitral award made in the State where recognition or enforcement was sought may be written in a language other than the language officially used in that State. The Working Group was agreed that the model law had to make it clear that in such cases the award had to be translated into the language of the court (as suggested in article XXVI in respect of foreign awards).

126. The Working Group expressed the view that there was no need to unify national rules on court competence for recognition or enforcement of awards made in the territory of the State where the award was made and that, therefore, an application for recognition or enforcement should be made to the competent court and not to the Court specified in article V.

Article XXVI

127. The text of article XXVI as considered by the Working Group was as follows:

Article XXVI

"An arbitral award made outside the territory of this State shall be recognized as binding and enforced in accordance with the following procedure, subject to any multilateral or bilateral agreement entered into by this State:

An application shall be made in writing to the [competent court] [Court specified in article V], accompanied by the duly authenticated original award, or a duly certified copy thereof, and the original arbitration agreement referred to in article II, or a duly certified copy thereof. If the said award or agreement is not made in an official language of this State, the party applying for recognition and enforcement of the award shall supply a translation of these documents into such language, certified by an official or sworn translator or by a diplomatic or consular agent."

128. There was general agreement in the Working Group that the rules of procedure for recognition or enforcement of arbitral awards made abroad should be subject to any multilateral or bilateral agreements entered into by the State. It was felt, however, that that principle was not only relevant for article XXVI and should, therefore, be expressed as a general rule in a separate provision.

129. Divergent views were expressed as to whether the model law should contain provisions on recognition and enforcement of foreign arbitral awards since, for those States that had ratified or acceded to the 1958

New York Convention or other relevant Conventions, there was no need for adopting (and "duplicating") such provisions and other States were unlikely to accept such "liberal" provisions. The prevailing view, however, was that such provisions should be retained in the model law as an important step towards creating, in addition to the multilateral and bilateral network, a unilateral system of recognition and enforcement of foreign arbitral awards. As regards the concern of granting unlimited recognition and enforcement by, for example, not requiring reciprocity, it was pointed out that the following articles (in particular article 38) could provide the necessary safeguards.

130. As regards the alternatives placed between square brackets, a preference was expressed for the court specified in article V.

131. The Working Group, after deliberation, requested the secretariat to prepare a revised draft of article XXVI, taking into account the views expressed by the Group.

III. Consideration of draft articles 37 to 41 on recognition and enforcement of award and on recourse against award (A/CN.9/WG.II/WP.42)

132. The Working Group commenced its consideration of draft articles 37 to 41 on recognition and enforcement of awards and on recourse against awards, as set forth in document A/CN.9/WG.II/WP.42. Those draft articles had been prepared by the secretariat in the light of the pertinent discussions and conclusions by the Working Group at its third and fourth sessions (see the reports of the Working Group, A/CN.9/216, paras. 103-104 and 106-109, and A/CN.9/232, paras. 14-22).

Article 37

133. The text of article 37 as considered by the Working Group was as follows:

Article 37

"(1) Recognition and enforcement of an arbitral award made in the territory of this State may be refused, at the request of the party against whom it is invoked, only if that party furnishes proof that:

"(a) A party to the arbitration agreement referred to in article II was, under the law applicable to him, under some incapacity, or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of this State; or

"(b) The party against whom the award is invoked was not given proper notice of the appointment of the arbitrator(s) or of the arbitration proceedings or was otherwise unable to present his case; or

"(c) The award [deals with] [decides on] a dispute or matter [not submitted to arbitration] [outside the scope of the arbitration agreement or not referred to the arbitral tribunal]; however,

if any decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration may be recognized and enforced; or

“(d) The composition of the arbitral tribunal or the arbitral procedure was not in accordance with the mandatory provisions of this Law, or the agreement by the parties, unless in conflict with any mandatory provision of this Law, or, failing such agreement, the non-mandatory provisions of this Law [, provided that, if the parties have agreed on the application of the law of another State, the provisions of that law are relevant]; or

“(e) The award [has not yet become binding on the parties] [is still open to appeal before a higher instance arbitral tribunal] or has been set aside [or suspended] by a court of this State [or, if the award was made under the law of another country, by a competent authority of that country].

“(2) Recognition and enforcement of an award may also be refused if the court finds that the recognition or enforcement would be contrary to the [international] public policy of this State [, including any public policy rule on the arbitrability of the subject matter of the dispute].”

General considerations

134. The Working Group was agreed that article 37 was connected, in terms of substance and approach, with other draft articles, in particular articles XXV, XXVI, 38 and 41. The Group noted that article 37 was drafted in a similar way as article 38, which was closely modelled on article V of the 1958 New York Convention. Those observations led to various policy considerations and general drafting suggestions.

135. One such policy question was whether the model law should contain provisions on the recognition and enforcement of awards rendered in the State where recognition and enforcement were sought. As done earlier with regard to article XXV, a suggestion was made to delete article 37. The prevailing view, however, was to retain a provision on refusal of recognition or enforcement of domestic awards, following the decision by the Working Group on article XXV.

136. It was noted that article 41 envisaged similar safeguards as article 37. In view of the reference in article 41 to the reasons set forth in article 37, two suggestions were made. The first one was to later consider streamlining the system of recourse against awards and their enforcement, which was not only of interest to States which did not provide for an “*exequatur*” procedure. The other suggestion was to consider with utmost care whether the exclusive list of reasons was not too restrictive to be widely acceptable. The Working Group noted that those suggestions could be adequately considered only in the context of article 41.

137. A further question of policy was how closely any provisions on recognition and enforcement of awards should be modelled on the 1958 New York Convention. It was understood that the issue of harmony with that Convention was directly relevant only to the provisions on foreign awards. Nevertheless, that issue became relevant to provisions covering “domestic” awards in an indirect way, i.e. the idea of striving for harmony between articles 37 and 38, which would leave open the possibility, as supported by some, of later combining them for the sake of a uniform treatment of awards in international commercial arbitration irrespective of where they were rendered.

138. As regards the general issue of harmony with the 1958 New York Convention, divergent views were expressed. Under one view, that Convention could serve as a starting point but should not be followed closely since it might well be revised in the not so distant future and since there was a need for not hampering future developments in the field of international commercial arbitration. Under another view, however, the 1958 New York Convention should be deviated from only where cogent reasons existed for such deviation. In support of that view, reference was made to the mandate of the Working Group which included the instruction to have due regard to that Convention. The Working Group, after deliberation, decided to take the Convention as the basis for its work but to deviate therefrom where there were good reasons for doing so.

139. As regards the special issue of harmonizing article 37 with article V of the New York Convention, some support was expressed for aligning both provisions in order to achieve a similar or uniform system for “domestic” and foreign awards. The prevailing view, however, was that with regard to article 37 there was less need for harmony than in respect of article 38. A general drafting suggestion was, therefore, not to feel bound by the structure of article V of the New York Convention and to consider preparing a more concise and simple version of article 37.

Opening words of paragraph (1)

140. The Working Group noted that under this provision recognition and enforcement “may be refused” and that that wording was ambiguous in that it might be construed as giving discretion to the court. While some support was expressed in favour of such discretion, the prevailing view was that, for the sake of certainty and predictability, the court should not be given such discretion and that that interpretation could be made clear by using the wording “shall be refused”. It was understood that that solution did not preclude the possibility of providing some flexibility as regards individual reasons for refusal (e.g., exclusion of minimal or trivial infraction of procedural rule).

Subparagraph (a)

141. Divergent views were expressed with regard to subparagraph (a). Under one view, that provision should not be retained since it gave insufficient answers to complicated issues of private international law which

could better be dealt with in a separate legal text, e.g., a convention. For example, the rule offered with regard to the complex issue of capacity was too simplistic and not accepted in all legal systems. Similar concerns applied to the rule on the law applicable to the validity of the arbitration agreement, an issue which was noted to be on the agenda of the Hague Conference on Private International Law. It was also pointed out that that provision was not consistent with article XIII (3) of the model law.

142. Under another view, it was desirable to have a provision which, like the corresponding provision in the 1958 New York Convention, would settle the essential questions of conflicts of laws in respect of capacity and validity without necessarily adopting the same rules as that Convention.

143. The prevailing view, however, was to retain subparagraph (a) without including any conflicts rule. Various drafting proposals were made to express that idea to merely mention incapacity and invalidity as reasons for refusal.

144. The Working Group, after deliberation, adopted that view and requested the secretariat to revise the provision accordingly. It was understood that the decision to exclude rules on conflicts of laws was limited to that provision and that the Working Group would at a later stage, on the basis of a study, consider the general question whether the model law should contain any provisions on conflicts of laws.

Subparagraph (b)

145. The Working Group supported the policy underlying that provision.

146. It was suggested, however, that there was no need for expressing those principles in the provision since they could be regarded as covered by the public policy ground in paragraph (2) and by mandatory provisions of the model law. The prevailing view was, however, that the principles were of such importance that they should be emphasized, as in the 1958 New York Convention.

Subparagraph (c)

147. The Working Group adopted that provision, subject to the deletion of the words placed between the first square brackets, i.e. "deals with". It was felt that the alternative wording "decides on" was more appropriate since it was more precise and referred to the point relevant to the question of the arbitrators' competence. For example, the mere fact that the reasons of an award mentioned a matter outside the scope of the submission should not constitute a ground for refusing enforcement.

148. As regards the second set of alternatives in square brackets, the Working Group was divided on the question whether it was sufficient to refer to disputes not submitted to arbitration, or whether it should be made more clear that the authority of the arbitral tribunal had to be measured by two standards:

the arbitration agreement and the often narrower mandate given to the arbitral tribunal by way of reference, submission or statement of claim. The Working Group decided to retain both alternatives for future reconsideration.

Subparagraph (d)

149. The Working Group was agreed that the provision should more clearly express the principle that the composition of the arbitral tribunal and the arbitral procedure had to comply with the agreement of the parties. It was understood—and possibly to be expressed in that provision—that the agreement was subject to the mandatory provisions of the law.

150. Divergent views were expressed as to whether, failing such agreement, non-mandatory rules should be included in that provision. Under one view, such rules should be included since they were binding in view of the fact that the parties had not excluded them. Under another view, such rules should not be referred to in that provision, in order to give the arbitral tribunal discretion in conducting the proceedings and to prevent the undesirable result that enforcement could be refused because of a minor violation of a non-mandatory rule.

151. The Working Group, after deliberation, requested the secretariat to prepare a revised draft with possible alternatives, reflecting the views expressed during the discussion.

Subparagraph (e)

152. The Working Group adopted the wording of the first alternative between square brackets, i.e. "has not yet become binding on the parties", and decided to delete the text between the three other square brackets.

153. The view was expressed that the words "or has been set aside by a court of this State" were superfluous since in such case the award was not binding on the parties. The prevailing view was, however, that the reason of setting aside should be separately stated since, at least in view of the usual interpretation of the same wording in the 1958 New York Convention, there were serious doubts as to whether the words "not yet binding" would be interpreted as covering setting aside.

Paragraph (2)

154. While some support was expressed in favour of retaining the word "international", the view prevailed that that word should be deleted because its underlying idea was not generally accepted and, above all, the term "international public policy" lacked precision.

155. As regards the words in the second square brackets, a view was expressed that the ground of non-arbitrability should be set forth in a separate subparagraph, following the structure of paragraph (2) of article 38. The prevailing view was, however, that the phrase need not be retained since rules on non-arbitrability normally formed part of the public policy of a State.

156. The Working Group, after deliberation, adopted paragraph (2) without the words placed between square brackets.

Article 38

157. The text of article 38 as considered by the Working Group was as follows:

Article 38

“(1) Subject to any multilateral or bilateral agreement entered into by this State, recognition and enforcement of an arbitral award made outside the territory of this State may be refused, at the request of the party against whom it is invoked, only if that party furnishes proof that:

“(a) A party to the arbitration agreement referred to in article II was, under the law applicable to him, under some incapacity, or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of this State; or

“(b) The party against whom the award is invoked was not given proper notice of the appointment of the arbitrator(s) or of the arbitration proceedings or was otherwise unable to present his case; or

“(c) The award [deals with] [decides on] a dispute or matter [not submitted to arbitration] [outside the scope of the arbitration agreement or not referred to the arbitral tribunal]; however, if any decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration may be recognized and enforced; or

“(d) The composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties, or, failing such agreement, was not in accordance with the law of the country where the arbitration took place [, provided that, if the parties have agreed on the application of the law of another State, the provisions of that law are relevant]; or

“(e) The award [has not yet become binding on the parties] [is still open to appeal or other ordinary recourse] or has been set aside [for one of the reasons set forth in sub-paragraphs (a) to (d) or in paragraph (2) of this article], or suspended, by a competent authority of the country in which [, or under the law of which,] that award was made.

“(2) Recognition and enforcement may also be refused if the court [from which recognition and enforcement is sought] finds that:

“(a) The subject matter of the dispute is not capable of settlement by arbitration under the law of this State; or

“(b) The recognition or enforcement of the award would be contrary to the [international] public policy of this State.”

General considerations

158. As done earlier with regard to article XXVI, a suggestion was made to delete article 38, since it envisaged recognition and enforcement of foreign awards without proper safeguards (e.g., reciprocity), which could only be established in multilateral or bilateral agreements, and because the model law would, thus, establish a system more favourable to recognition and enforcement than the 1958 New York Convention. The prevailing view was, however, that provisions along the lines of article 38 (and XXVI) should be retained in the model law since (a) even a unilateral system of recognition and enforcement was useful in supplementing the multilateral and bilateral network; (b) the two paragraphs of article 38 provided sufficient safeguards; (c) in international commercial arbitration, the place of arbitration was of limited importance; (d) those States not yet adhering to the 1958 New York Convention could avail themselves of the reciprocity mechanism in relation to a great number of States by ratifying or acceding to that Convention.

159. Divergent views were expressed on whether and to what extent article 38 should be aligned with article 37 or modelled on article V of the 1958 New York Convention. Under one view, there should be full harmony between articles 37 and 38, for the sake of uniform treatment in the model law of all awards in international commercial arbitration, and, thus, the decisions of the Working Group on article 37 should be followed with regard to article 38.

160. Under another view, however, article 38 should accord with the text of article V of the 1958 New York Convention, since both articles dealt with the same subject matter (i.e. refusal of recognition or enforcement of foreign arbitral awards) and any disparity between the two legal régimes should be avoided. It was pointed out that such harmonization was in the interest of all States whether or not they adhered to the 1958 New York Convention.

161. Under yet another view, which the Working Group adopted, article 38 should be closely modelled on article V, without precluding the possibility of a substantive modification in exceptional cases for cogent reasons, and mere drafting amendments should be avoided. As a result, the decisions of the Working Group on article 37 were not binding in respect of article 38. It was noted, however, that that approach did not necessarily exclude the option of later striving for greater harmony between articles 37 and 38.

162. A suggestion was made to consider, at a later stage, the appropriateness of presenting, e.g., in a footnote to the model law or in a commentary, the views and intentions of the Working Group as regards the interaction between the model law and the 1958 New York Convention. Such clarification on the relationship between the two legal régimes could provide assistance and guidance to States when adopting the model law.

*Paragraph (1)**Opening words of paragraph (1)*

163. The Working Group was agreed that the words "Subject to any multilateral or bilateral agreement entered into by this State" should be deleted in view of its decision (taken in respect of article XXVI) to express that proviso in a separate provision of more general application. A suggestion was made to consider adding to such proviso the "principles of mutual benefit".

Subparagraph (a)

164. The Working Group noted that the last words of this subparagraph "under the law of this State" were erroneously included and should be replaced by the words "under the law of the country where the award was made".

165. Divergent views were expressed on the conflicts of law rules included in that provision. Under one view, the concern expressed with regard to the same provision in article 37 was equally relevant here. Some proponents of that view proposed the deletion of the subparagraph, while others were in favour of merely excluding the conflicts rules, as decided with regard to article 37.

166. Under another view, however, it was desirable to adopt the wording of the corresponding provision of the 1958 New York Convention, despite its shortcomings. Under yet another view, some modification should be considered whereby a substantial improvement could be achieved.

167. The Working Group, after deliberation, decided to adopt the wording of article V (1)(a) of the 1958 New York Convention without excluding the possibility of a substantive improvement.

Subparagraph (b)

168. The Working Group adopted that subparagraph.

Subparagraph (c)

169. Some support was expressed for aligning that subparagraph with article 37 (1)(c), as approved by the Working Group. The prevailing view, however, was to adopt the wording of article V (1)(c) of the 1958 New York Convention.

Subparagraph (d)

170. The Working Group adopted that subparagraph without the words between square brackets. It was understood that the text between square brackets was redundant since a stipulation on the procedural law formed part of the agreement of the parties.

Subparagraph (e)

171. Some support was expressed for retaining the text between the third square brackets which was modelled on article IX of the European Convention on International Commercial Arbitration (Geneva 1961).¹

The prevailing view, however, was to delete that text since the restriction expressed therein was not generally acceptable and, thus, too ambitious and its application could lead to difficulties.

172. The Working Group adopted the text of that subparagraph, including the texts between the first and the fourth square brackets, which accorded with article V (1)(e) of the 1958 New York Convention.

Paragraph (2)

173. Some support was expressed for deleting subparagraph (a), in accordance with the decision of the Working Group on the similar rule in article 37 (2), i.e. the text between the second square brackets. The prevailing view was, however, to retain that provision for the sake of consistency with article V (2)(a) of the 1958 New York Convention.

174. As regards subparagraph (b), some support was expressed for retaining the word "international", with a possible clarification by expressing the idea as follows "public policy of this State with regard to international commercial transactions". The prevailing view, however, was to delete the word "international" for the reasons stated in the context of the discussion of article 37 (2).

175. The Working Group adopted the text of paragraph (2), including the words between the first square brackets but without the word "international" in subparagraph (b).

Article 39

176. The text of article 39 as considered by the Working Group was as follows:

Article 39

"If an application for the setting aside or suspension of an award has been made to a competent authority referred to in article 37, paragraph (1)(e) or 38, paragraph (1)(e), the authority before which the award is sought to be relied upon may, if it considers it proper, adjourn the decision on the enforcement of the award and may also, on the application of the party claiming enforcement of the award, order the other party to give suitable security."

177. The Working Group adopted that article, subject to the deletion of the words "in article 37, paragraph (1)(e) or", so as to limit the scope of that article to recognition and enforcement of only foreign awards.

*Recourse against arbitral award**Article 40*

178. The text of article 40 as considered by the Working Group was as follows:

Article 40

"No recourse against an arbitral award made under this Law [, whether or not rendered

¹United Nations, Treaty Series, vol. 484, No. 7041 (1963-1964), p. 364.

in the territory of this State,] may be made to a court except an action for setting aside in accordance with the provisions of article 41."

179. The Working Group expressed its support for the policy underlying that article. It was noted, however, that that rule of exclusion could be finally assessed only after having considered article 41. It was also noted that the reference to "an action for setting aside" was too restrictive if article 41 would include other remedies such as remission to the arbitral tribunal, as envisaged in its paragraph (4), or correction or interpretation of an award by the court. In such case it would be more appropriate to delete the words "an action for setting aside" and merely retain the general reference "in accordance with the provisions of article 41".

180. The Working Group was divided on whether the words placed between square brackets should be retained. Under one view, that text provided a useful clarification (as suggested in footnote 24 of WP.42). Under another view, that text should not be retained for either of the following reasons: (a) the words "made under this Law" were sufficiently clear so as to make any clarification superfluous; (b) the text between square brackets created uncertainty, by allowing the possible misinterpretation that article 40 adopted in State A would also apply to an award made in State B under the model law adopted there and, even if correctly interpreted, touched upon the difficult issue of court competence (for setting aside awards made abroad but under the model law of State A), which was a matter probably outside the scope of the model law.

Article 41

181. The text of article 41 as considered by the Working Group was as follows:

Article 41

"(1) An action for setting aside [an arbitral award referred to in article 40] may be brought [before the Court specified in article V] within four months from the date on which the party bringing that action has received the award in accordance with article XXII (4).

"(2) An arbitral award may be set aside only on one of the grounds on which recognition or enforcement may be refused under article 37, paragraph (1) (a), (b), (c), (d) or (2) [or on which an arbitrator may be challenged under article IX (2)].

"(3) The court may, where appropriate, set aside only a part of the award, provided that this part can be separated from the other parts of the award.

"(4) If the court sets aside the award, [it may order that the arbitration proceedings continue for re-trial of the case] [a party may within three months request re-institution of the arbitration proceedings], unless such measure is incompatible with a ground on which the award is set aside.

"(5) Any decision by the court on an action for setting aside is subject to appeal within three months."

Structure and order of provisions

182. It was suggested to place that article (and art. 40) before the articles on recognition and enforcement of awards and, then, to specify in paragraph (2) the reasons for setting aside instead of referring to article 37. A further suggestion was to reverse the order of paragraphs (1) and (2). Yet another suggestion was to combine the provisions on setting aside with the articles on recognition and enforcement of domestic awards and, thereby, to streamline the system established in the model law. The Working Group was agreed that those suggestions could be considered at a later stage.

Paragraph (1)

183. As regards the words between the first square brackets, the Working Group was agreed that they could either be deleted, in view of the close proximity of that provision with article 40, or replaced by the same words as used in article 40 specifying which awards were covered. As regards the words between the second square brackets, the Working Group agreed with their contents but felt that a reference to article 41 in article V was sufficient.

184. As regards the time period stated in paragraph (1), various suggestions were made for shortening or for extending that period. After deliberation, a time period of three months was accepted. It was noted that the provision might be expanded so as to accommodate cases of appeal to another arbitral tribunal (as suggested in footnote 27 of WP.42).

185. The Working Group decided to retain paragraph (1), subject to the above modifications.

Paragraph (2)

186. Divergent views were expressed as to the grounds for setting aside an award. Under one view, the list of reasons set forth in paragraph (2) was too restrictive since it did not cover some important grounds recognized in some legal systems, sometimes even forming part of the public policy of a State. It was suggested, therefore, to add to the list some more grounds as, e.g., mentioned in footnote 29 of WP.42 (in particular, under (c) and (d)). An alternative suggestion was to replace the list by a general formula such as "in cases of procedural injustice" and to rely on the common sense of the judge.

187. The prevailing view, however, was to limit the reasons for setting aside to those grounds on which under article 38 recognition and enforcement may be refused. That solution would facilitate international commercial arbitration by enhancing predictability and expeditiousness and would go a long way towards establishing a harmonized system of limited recourse against awards and their enforcement. It was stated in

support that the reasons set forth in article V of the New York Convention provided sufficient safeguards, and that some of the grounds suggested as additions to the list were likely to fall under the public policy reason.

188. As regards the reason set forth in subparagraph (d) of article V (1), there was wide support for providing for a certain qualification (as suggested in footnote 28 of WP.42), by adopting a general rule of "estoppel" or implied waiver and, possibly, by excluding minor defects which had no influence on the award. Subject to such possible addition, which would also apply to articles 37 and 38, the Working Group adopted paragraph (2).

Paragraph (3)

189. The Working Group adopted that paragraph.

Paragraph (4)

190. Divergent views were expressed as to the appropriateness of retaining a rule along the lines of paragraph (4). Under one view, the provision should be deleted since it dealt in an insufficient manner with procedural questions which were answered in a way not easily reconciled with the different concepts of the various legal systems. It was also pointed out that setting aside should be regarded as a remedy separate from remission to the arbitral tribunal and that the wording between the second square brackets and the following proviso lacked clarity.

191. However, there was more support for retaining a provision along the lines of paragraph (4), subject to various modifications. The main reasons for retention were that the provision made it clear that the arbitration agreement had not necessarily lapsed and that it opened the way for remission to an arbitral tribunal. While some support was expressed for leaving the decision on retrial of the case solely to the court and its discretion, the prevailing view was to leave that matter to the

parties, possibly subject to some control or authorization by the court.

192. Various suggestions were made for clarifying, in a revised draft, in particular, the following issues: (a) to whom would a party have to address its request for "re-institution"; (b) "re-institution" should not necessarily mean that the proceedings would be conducted by the previous arbitrators; (c) remission or retrial might relate to the whole award or only to part of it, including the instruction to correct a certain procedural defect; (d) the proviso at the end of the paragraph should be more detailed and, for example, should mention the reasons of non-existence of a valid arbitration agreement and non-feasibility of remission to the previous arbitral tribunal.

193. The Working Group, after deliberation, requested the secretariat to prepare a revised draft on the basis of the views expressed during the discussion.

Paragraph (5)

194. Divergent views were expressed with regard to that paragraph. Under one view, that provision should be retained, though possibly with a different time period or no time period at all. Under the prevailing view, however, that provision should be deleted since it dealt, without need, with a fundamental issue governed by national procedural laws, and sometimes even backed by constitutional guarantees.

195. The Working Group, after deliberation, decided not to retain paragraph (5).

REFERENCE TO CONCILIATION

196. A suggestion was made to include in a preamble, or in an appropriate provision of the model law, a reference to conciliation as an additional method of settling disputes where parties so wished.

D. Working Papers submitted to the Working Group on International Contract Practices at its fifth session (New York, 22 February-4 March 1983).

1. NOTE BY THE SECRETARIAT: MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION: REVISED DRAFT ARTICLES I TO XXVI (A/CN.9/WG.II/WP.40)^a

Introductory note

1. This working paper contains revised draft articles I-XXVI of a model law on international commercial arbitration, prepared by the secretariat in accordance with the conclusions of the Working Group on International Contract Practices at its fourth session (Vienna, 4-15 October 1982).¹ A comparative table at

the end of this note shows the numbers of the revised draft articles and of the corresponding previous draft articles² on which the revised draft articles are based.

2. In addition to the redrafting of the text of the articles, the revision includes a rearrangement of the order of the articles and a modification of the headings. While the original classification scheme is no longer used, the new headings and the order of articles are still

^a14 December 1982. Referred to in Report, para. 87 (part one, A).

¹See Report of the Working Group on International Contract Practices on the work of its fourth session (A/CN.9/232) (reproduced in this volume, part two, III, A).

²The previous draft articles prepared by the secretariat are contained in documents A/CN.9/WG.II/WP.37 and 38, and are also reproduced in A/CN.9/232.

to be regarded as tentative pending future decisions as to which of the revised draft articles will ultimately be retained and which of the additional draft provisions will be adopted.³

3. It may be noted that this revised draft does not contain a provision listing all the "mandatory" provisions of the model law. It merely reflects in individual provisions any decision taken by the Working Group in this respect, for example by including the words "unless otherwise agreed by the parties".

4. Finally, the revised draft has been prepared with the following two assumptions in mind which might later be expressly stated in the model law, possibly together with other rules of interpretation: (a) freedom of parties to determine a certain point includes freedom to authorize a third person or institution to make that determination; (b) agreement by parties includes reference to arbitration rules.

Comparative table of numbers of draft articles

<i>Revised draft article (in WP.40)</i>	<i>Previous draft article (WP.37, 38)</i>	<i>Revised draft article (in WP.40)</i>	<i>Previous draft article (WP.37, 38)</i>
I	1	XIII (1)	29 (1), 4
II (1)	2	(2)	28 (1), (2)
(2)	3	(3)	29 (2), 30
III	—	XIV	23
IV (1)	5	XV	19
(2), (3)	—	XVI (1)	18 (1), (2)
(4)	6	(2)	21
V (1), (2)	17 (1), (2)	XVII (1)	20 (1), 22 (2) d
VI	13	(2)	21 (last sent.)
VII	14	(3)	20 (2)
VIII (1)	15 (1)	(4)	22 (1)
(2)	16 (1)	(5)	22 (2) b
(3)	15 (2), 16 (2)	XVIII	24 (A) (1)-(4)
(4)	17 (3)	XIX (1)-(3)	31 (1)-(3)
IX (1)	7	(4)	32
(2)	8	XX	26
X (1)	9 (1)	XXI	33
Alt. A: (2)	9 (2) a, b	XXII (1)-(3)	27
(3)	9 (2)c, 10	(4)	35 (1)
Alt. B: (2)	9 (2)c, 10	XXIII	25
XI (1)	11	XXIV	34
(2)	—	XXV	36
XII	12	XXVI	36

Revised draft articles of a model law on international commercial arbitration

A. SCOPE OF APPLICATION

Article I

(1) This Law applies to international commercial arbitration as specified in paragraphs (2), (3) and (4) of this article.

³The additional draft provisions will be dealt with in A/CN.9/WG.II/WP.41 and 42 (reproduced in this volume, part two, III, D, 2 and 3, respectively).

(2) "Arbitration" includes [all matters of arbitration, in particular]

(a) Arbitration agreements [as defined in article II, paragraph (1)];⁴

(b) The preparation and conduct of arbitration proceedings based on such agreements whether or not administered by a permanent arbitral institution; and

(c) The arbitral awards resulting therefrom.

(3) "Commercial" refers to any [defined legal] relationship of a commercial [or economic] nature [including, for example, any trade transaction for the supply or exchange of goods, factoring, leasing, construction of works, consulting, engineering, commercial representation, investment, joint venture and other forms of industrial or business co-operation, financing, or providing of services].⁵

(4) "International" are those cases where the arbitration agreement is concluded by parties whose places of business are in different States. If a party has more than one place of business, the relevant place of business is [that which has the closest relationship to the arbitration agreement] [the seat of the head office].^{6,7}

B. ARBITRATION AGREEMENT

Article II

(1) ["Arbitration agreement" is an agreement by parties to] [In an "arbitration agreement" parties may] submit to arbitration all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not.

⁴The reference to only paragraph (1) of article II would, apart from its general value, help to clarify that the requirement of written form as laid down in article II, paragraph (2), is not a question of scope of application. Thus, a non-written agreement would be covered by this Law but would not be valid because of article II, paragraph (2).

⁵Inclusion of such or a similar illustrative list could help to underline the desirable wide interpretation of the term "commercial" and, at least, make clear that the transactions listed are covered by the model law. If the Working Group decides not to retain such a list, some clarification might be achieved in a commentary, if one were to be published; in that case examples should also be given of transactions not covered by the model law, e.g. consumer sales.

⁶The first alternative reflects the formula used in article 10 (a) of the 1980 Vienna Sales Convention (Yearbook ... 1980, part three, I, B) but adjusted to arbitration. The second alternative is submitted for consideration in view of its potential advantages: it provides a clearer criterion and enhances the applicability of the model law. Adoption of the second alternative would lessen the need for the provision dealt with in the following footnote.

⁷In this context, the Working Group may wish to consider the suggestion (set forth in A/CN.9/232, para. 167) to include an "opting in"-provision according to which parties may stipulate the application of the model law (in lieu of the law on domestic arbitration) by regarding their case as an international one. Since a State is unlikely to grant such freedom of choice in strictly domestic cases, it is submitted that some international element should be established. While it will prove very difficult to define this element, one possible way might be to require that not all of the following places are situated in the same State: (a) place of offer of contract containing arbitration clause or of separate arbitration agreement; (b) place of corresponding acceptance; (c) place of performance of contract or of location of subject matter; (d) place of registration or incorporation (or nationality) of each party; (e) place of arbitration.

(2) The arbitration agreement, whether an arbitration clause in a contract or a separate agreement, shall be in writing [i.e.] [An agreement is in writing if it is] contained in a document signed by the parties or in an exchange of letters, telegrammes or other communications [in sufficiently permanent form] [of equal evidential value]. The reference in a contract to general conditions, or similar legal texts, containing an arbitration clause constitutes an arbitration agreement provided that the contract is in writing and the reference is such as to make that clause a part of the contract.

C. ARBITRATION AND THE COURTS

[Article III]

In matters governed by this Law, no court shall intervene except where so provided in this Law.⁸

Article IV

(1) A court, before which an action is brought in a matter which is the subject of an arbitration agreement, shall at the request of a party, refer the parties to arbitration unless it finds that the agreement is null and void, inoperative or incapable of being performed.

(2) A plea that the court [referred to in paragraph (1)] has no jurisdiction because of the existence of a valid arbitration agreement may be raised by a party not later than in his statement on the substance of the dispute.

(3) Where arbitration proceedings have commenced and such a plea is raised before the court or a party requests from [a court] [the Court specified in article V] a ruling that the arbitral tribunal has no jurisdiction the arbitral tribunal may either continue or suspend the arbitration proceedings until its jurisdiction is decided on by that court.

(4) Any party may address to a court a request for interim measures of protection, whether before or during arbitration proceedings. This shall not be deemed incompatible with the agreement to arbitrate or as a waiver of that agreement.

Article V

(1) The special Court entrusted by this Law with functions of arbitration assistance and control [under articles VIII (2), (3), X (2)/(3), XI (2), XIII (3), XIV, XXV, XXVI ...] shall be the ... (blanks to be filled by each State when enacting the model law).⁹

⁸This novel draft provision is intended to express a principle underlying the discussions in the Working Group. While its acceptability may be assessed only after the contents of (i.e. "the matters governed by") the model law are clear, it would compel the drafters to express in the Law any instance of possible court control.

⁹It is suggested that the question of the international jurisdiction or competence of this Court be discussed at a later stage (probably in connection with issues of conflict of laws) when the exact and complete tasks of that Court are clear.

(2) Unless otherwise provided in this Law,

(a) This Court shall act upon request by any party or the arbitral tribunal;¹⁰ and

(b) The decisions of this Court shall be final.¹¹

D. COMPOSITION OF ARBITRAL TRIBUNAL

Article VI

(1) No person shall be by reason of his nationality precluded from acting as arbitrator, unless otherwise agreed by the parties.

(2) An arbitration agreement is invalid [if] [to the extent that] it accords one of the parties a [predominant position] [manifestly unfair advantage] with regard to the appointment of arbitrators.

Article VII

The parties are free to determine the number of arbitrators. Failing such determination, [three arbitrators] [a sole arbitrator] shall be appointed.

Article VIII

(1) Subject to the provisions of article VI (2), the parties are free to agree on a procedure of appointing the arbitrator or arbitrators.

(2) Failing such agreement,

(a) If, in an arbitration with a sole arbitrator, the parties are unable to agree on the arbitrator, he shall be appointed by the Court specified in article V;

(b) In an arbitration with three arbitrators, each party shall appoint one arbitrator and the two arbitrators thus appointed shall appoint the third arbitrator.

(3) Where [the composition of an arbitral tribunal becomes unduly delayed because] the parties, or two arbitrators, are unable to reach agreement or where one of the parties, or any designated appointing authority, fails to act as required under an agreed appointment procedure or under this Law, the Court specified in article V may be requested [by any party or arbitrator] to take the necessary measure instead.

(4) The Court, in appointing an arbitrator, shall have regard to such considerations as are likely to secure the appointment of an independent and impartial arbitrator and, in the case of a sole or a third arbitrator, shall take into account as well the advisability of appointing an arbitrator of a nationality other than the nationalities of the parties.

¹⁰Provisions which "provide otherwise" may either restrict the rule under (a), e.g. article X (3) which entitles only a party to resort to this Court, or widen the rule by entitling others, such as individual arbitrators, e.g. article VIII (3) or XI (2).

¹¹Provisions which "provide otherwise", i.e. allow an appeal, might, for example, be envisaged in respect of decisions on setting aside, or on recognition and enforcement, of arbitral awards (to be dealt with in A/CN.9/WG.II/WP.42).

Article IX

(1) A prospective arbitrator shall disclose to those who approach him in connection with his possible appointment any circumstances likely to give rise to justifiable doubts as to his impartiality or independence. An arbitrator [, from the time of his appointment,] shall disclose any such circumstances to the parties unless they have already been informed by him of these circumstances.

(2) An arbitrator may be challenged only if circumstances exist that give rise to justifiable doubts as to his impartiality or independence. A party may challenge the arbitrator appointed by him only for reasons of which he becomes aware after the appointment has been made.

Article X

(1) The parties are free to agree on the procedure for challenging an arbitrator subject to the provisions of paragraph (3) of this article.¹²

Alternative A:

(2) Failing such agreement, a party who intends to challenge an arbitrator shall, within fifteen days after knowing about the appointment or the circumstances referred to in article IX (2), send a written statement of the reasons for the challenge to the other party and to all arbitrators. The mandate of the arbitrator terminates when the other party agrees to the challenge or the arbitrator withdraws from his office; in neither case does this imply acceptance of the validity of the grounds for the challenge.

(3) If a challenge

(a) under paragraph (2) of this article is not successful within 30 days after the receipt of the written statement by the other party and by the challenged arbitrator,¹³ or

(b) under any challenge procedure agreed upon by the parties, is neither accepted by the other party or the challenged arbitrator nor sustained by any person or body entrusted with the decision on the challenge,

the challenging party may [request the Court specified in article V to decide on the challenge] [pursue his objections before a court only in an action for setting aside the arbitral award].

Alternative B:

(2) Where an arbitrator is challenged without success, whether or not under a procedure agreed upon by the parties, the challenging party may [request the Court specified in article V to decide on the challenge] [pursue his objections before a court only in an action for setting aside the arbitral award].

¹²The reference to paragraph (3) relates to alternative A; if alternative B were to be adopted, the reference should be to paragraph (2).

¹³No time-period seems necessary if resort to the court may only be had in an action for setting aside. If a time-period were to be adopted, consideration might be given to selecting as the starting point of time the date of mailing the statement (to further the interest of the challenging party).

Article XI

(1) The mandate of an arbitrator terminates in the event of the *de jure* or *de facto* impossibility of his performing his functions or, unless otherwise agreed by the parties, in the event that he fails to act [in accordance with his mandate under the arbitration agreement].

(2) If a dispute arises concerning any of the cases envisaged in paragraph (1), any party or arbitrator may request the Court specified in article V to decide on the termination of the mandate.

Article XII

In the event of the death or resignation of an arbitrator or the termination of his mandate under article X or XI, a substitute arbitrator shall be appointed according to the rules that were applicable to the appointment of the arbitrator being replaced, unless the parties agree otherwise. [However, if the arbitrator to be replaced was named in the arbitration agreement, that agreement shall lapse *ipso jure*].¹⁴

E. COMPETENCE OF ARBITRAL TRIBUNAL

Article XIII

(1) The arbitral tribunal has the power to rule on its own jurisdiction, including any objections with respect to the existence or validity of the arbitration agreement. For that purpose, an arbitration clause which forms part of a contract shall be treated as an agreement independent of the other terms of the contract. A decision by the arbitral tribunal that the contract is null and void shall not entail *ipso jure* the invalidity of the arbitration clause.

(2) A plea that the arbitral tribunal does not have jurisdiction shall be raised not later than in the [statement of defence or, with respect to a counter-claim, in the reply to the counter-claim] [reply to the claim or the counter-claim]. A party is not precluded from raising such plea by the fact that he has appointed, or participated in the appointment, of an arbitrator. A plea that the arbitral tribunal has exceeded its terms of reference shall be raised promptly after the matter, allegedly outside the mandate, is taken up. The arbitral tribunal may admit a later plea if it deems the delay justified.

(3) The arbitral tribunal may rule on a plea referred to in paragraph (2) either as a preliminary question or in the final award. In either case, a ruling by the arbitral tribunal that it has jurisdiction may be contested by any party only in an action for setting aside the arbitral award. [A ruling by the arbitral tribunal that it has no jurisdiction may be contested by any party within 30 days before the Court specified in article V].

¹⁴It is submitted that this last sentence does not seem necessary or advisable. Its practical value seems limited since naming of an arbitrator in the original agreement is not very common. More importantly, a less automatic and more flexible approach is desirable and possible in view of the proviso in the first sentence "unless the parties agree otherwise".

Article XIV

Unless otherwise agreed by the parties, the arbitral tribunal may, at the request of a party, order interim measures for conserving, or maintaining the value of, the goods forming the subject-matter in dispute, such as their deposit with a third person or the sale of perishable merchandise. The arbitral tribunal may require [of a party or the parties] security for the costs of such measures. If enforcement of any such interim measure becomes necessary, the arbitral tribunal may request [a competent court] [the Court specified in article V] to render executory assistance.

F. PLACE AND CONDUCT OF ARBITRATION PROCEEDINGS

Article XV

(1) Subject to the provisions of article XVII (1) [(a)], (b), (2), (3), [(5)], the parties are free to [agree on] [determine, either directly or by reference to arbitration rules,]¹⁵ the procedure to be followed by the arbitral tribunal in conducting the proceedings.

(2) Failing such agreement [on the respective point at issue], the arbitral tribunal may, subject to the provisions of this Law, conduct the arbitration in such manner as it considers appropriate, provided that the parties are treated with equality and that each party is given a full opportunity of presenting his case. The power conferred upon the arbitral tribunal includes the power to determine the admissibility, relevance, materiality and weight of any evidence.

Article XVI

(1) The parties are free to agree on the place where the arbitration is to be held. Failing such agreement, the place of arbitration shall be determined by the arbitral tribunal [, having regard to the circumstances of the arbitration].

(2) Notwithstanding the provisions of the preceding paragraph, the arbitral tribunal may [, unless otherwise agreed by the parties,]¹⁶ meet at any place it deems appropriate for

(a) Hearing witnesses;

(b) Consultations among its members;

(c) The inspection of goods, other property or documents.

Article XVII

(1) [Failing agreement by the parties,]¹⁶ the arbitral tribunal shall decide whether to hold hearings or whether the proceedings shall be conducted on the basis of documents and other materials. However, if a party so requests,

(a) The arbitral tribunal shall, at the appropriate stage of the proceedings, hold hearings for the presentation of evidence by witnesses, including expert witnesses, or for oral argument [on the substance of the dispute];

(b) Any expert, appointed by the arbitral tribunal, after delivery of his written or oral report, shall be heard at a hearing where the parties have the opportunity [to be present,] to interrogate the expert and to present expert witnesses in order to testify on the points at issue.

(2) In order to enable the parties to be present at any hearing and any meeting of the arbitral tribunal for inspection purposes, they shall be given [sufficient] notice [thereof at least 40 days in advance].¹⁷

(3) All documents or information supplied to the arbitral tribunal by one party shall be [communicated] [made available] to the other party. Also any expert report or other document, on which the arbitral tribunal may rely on in making its decision, shall be made available to the parties.

(4) [Unless otherwise agreed by the parties,]¹⁶ the arbitral tribunal may appoint one or more experts to report to it on specific issues to be determined by the tribunal.

(5) The parties shall give the expert any relevant information or produce for his inspection any relevant documents or goods that he may require of them. [Any dispute between a party and such expert as to the relevance of the required information or production shall be referred to the arbitral tribunal for decision.]

Article XVIII

Alternative A:

[Unless otherwise agreed by the parties,]¹⁶ if, without showing sufficient cause for the failure,

(a) The claimant fails to communicate his statement of claim within the period of time stipulated by the parties or fixed by the arbitral tribunal, the arbitration proceedings shall be terminated [and the costs of the arbitration be borne by the claimant];

(b) The respondent fails to communicate his statement of defence within the period of time [of not less than 40 days as] stipulated by the parties or fixed by the arbitral tribunal, [this [may] [shall] be treated as a denial of the claim and]¹⁸ the arbitration proceedings shall continue;

(c) A party, duly notified in accordance with article XVII (2),¹⁹ fails to appear at a hearing, the arbitral tribunal may proceed with the arbitration;

¹⁷The second alternative would be useful also in the context of the default provision of article XVII (c).

¹⁸If the idea in square brackets were to be accepted, the Working Group may wish to define what exactly is meant by "denial of claim".

¹⁹A (minimum) period of time would have to be included here, if in article XVII (2) the first alternative (i.e. "sufficient notice") were adopted.

¹⁵The second alternative may be regarded as superfluous, if the suggestion set forth in the introduction (above, para 4) were accepted.

¹⁶Mention of this proviso may be deemed unnecessary in view of the fact that this article is not included in the reference to mandatory provisions listed in article XV (1).

(d) A party fails to produce documentary evidence, after having been invited to do so within a specified period of time of not less than 40 days, the arbitral tribunal may make the award on the evidence before it.^{19a}

Alternative B:

Even if, without showing sufficient cause for the failure, the respondent fails to communicate his statement of defence, or a party fails to appear at a hearing or to produce documentary evidence, although an invitation to do so had been sent at least 40 days in advance, the arbitral tribunal may continue the proceedings and make the award, unless default proceedings are excluded by agreement of the parties.

G. RULES APPLICABLE TO SUBSTANCE OF DISPUTE

Article XIX

(1) The arbitral tribunal shall [decide the dispute in accordance with such rules of law as may be agreed by the parties] [apply the law designated by the parties as applicable to the substance of the dispute]. Any designation of the law or legal system of a given State shall be construed, unless otherwise expressed, as directly referring to the [pertinent] substantive law of that State and not to its conflict of laws rules.

(2) Failing any designation by the parties, the arbitral tribunal shall apply the law determined by the conflict of laws rules which it considers applicable.

(3) The arbitral tribunal shall decide in accordance with the terms of the contract and shall take into account the usages of trade applicable to the transaction.

(4) The arbitral tribunal shall decide *ex aequo et bono* or as *amiable compositeur* only if the parties have expressly authorized it to do so.

H. MAKING OF AWARD AND OTHER DECISIONS

Article XX

(1) When there are three [or another uneven number of]²⁰ arbitrators, any award or other decision of the arbitral tribunal shall be made, unless otherwise agreed by the parties, by [a majority of the arbitrators, i.e.]

^{19a}If the minimum period of time (40 days) set forth in this paragraph and in paragraph (b) were to be adopted, it should probably be regarded as "mandatory", unlike the rest of this article.

²⁰The words "or another uneven number of" are placed between square brackets in order to invite discussion by the Working Group on whether it might not be sufficient to deal, in the model law, only with the case of three (and not more) arbitrators and, then either to include a "*mutatis mutandis*"-provision for cases with more than three arbitrators or to leave it to the States adopting the model law whether or not to deal with questions of such big panels.

more than half of all appointed arbitrators [, provided that all arbitrators had the opportunity to take part in the deliberations leading to the award or decision].

(2) However, in the case of questions of procedure, when there is no majority or when the arbitral tribunal so authorizes, a presiding arbitrator may decide on his own, subject to revision, if any, by the arbitral tribunal.

Article XXI

(1) If, during the arbitration proceedings, the parties agree on a settlement of the dispute, the arbitral tribunal shall either terminate the arbitration proceedings or, if requested by the parties and accepted by the tribunal, record the settlement in the form of an arbitral award on agreed terms.

(2) An award on agreed terms shall be made in accordance with the provisions of article XXII and shall state that it is an award. Such an award has the same status and executory force as any other award on the merits of the case.²¹

Article XXII

(1) An award shall be made in writing and shall be signed by the arbitrator or arbitrators. In arbitration proceedings with more than one arbitrator [, if the signature of one or more arbitrators cannot be obtained,] the signatures of more than half of all appointed arbitrators shall suffice, provided that the fact and the reason for the missing signature or signatures are stated.²²

(2) The arbitral tribunal shall state the reasons upon which the award is based, unless the parties have agreed that no reasons are to be given or the award is an award on agreed terms under article XXI.

(3) An award shall state the place of arbitration [as referred to in article XVI]. The award shall be deemed [irrebuttably] to have been made at that place and on [the] [any] date indicated therein.

(4) After an award is made, a copy thereof signed by the arbitrators in accordance with paragraph (1) of this article shall be communicated to each party.

I. DURATION OF MANDATE OF ARBITRAL TRIBUNAL²³

Article XXIII

Alternative A:

The [making] [delivery] of the final award, which constitutes or completes the disposition of all claims

²¹The last sentence might later have to be modified in order to qualify this statement as regards reasons for recourse against such award or its enforcement (a subject-matter to be dealt with in WP.42).

²²The idea mentioned in footnote 20 might be considered here, too.

²³The draft articles included here might later be combined (and harmonized) with any draft provisions on termination of arbitration proceedings (to be dealt with in WP.41).

submitted to arbitration, terminates the mandate of the arbitral tribunal, subject to the provisions of article XXIV.²⁴

Alternative B:

Where the arbitral tribunal makes an award which [is not intended to] [does not] constitute a final disposition of the substance of the dispute, the making of such an award (for example, an interim, interlocutory, or partial award) does not terminate the mandate of the arbitral tribunal.

Article XXIV

(1) Within thirty days after the receipt of the award, [unless another period of time has been agreed upon by the parties,] a party, with notice to the other party, may request the arbitral tribunal

(a) To correct in the award any errors in computation, any clerical or typographical errors or any errors of similar nature; the arbitral tribunal may, within thirty days after the communication of the award, make such corrections on its own initiative; and

(b) To give, within forty-five days, an interpretation of a specific point or part of the award [; such interpretation shall form part of the award].

(2) Unless otherwise agreed by the parties, a party, with notice to the other party, may request the arbitral tribunal, within thirty days after the receipt of the award, to make an additional award as to claims presented in the arbitration proceedings but omitted from the award; if the arbitral tribunal considers such request to be justified and that the omission can be rectified without any further hearings or evidence, it shall complete its award within sixty days after the receipt of the request.

(3) The provisions of article XXII shall apply to a correction or interpretation of the award or to an additional award.

²⁴In addition to the extension of the mandate under article XXIV, another case of "extension" which might be regulated in the model law is where the final award is later set aside.

J. RECOGNITION AND ENFORCEMENT OF AWARD²⁵

Article XXV

An arbitral award made in the territory of this State shall be recognized as binding and enforced in accordance with the following procedure [unless recognition and enforcement of such awards are granted under less onerous conditions]:

An application shall be made in writing to the [competent court] [Court specified in article V], accompanied by the duly authenticated original award, or a duly certified copy thereof, and the original arbitration agreement referred to in article II, or a duly certified copy thereof.

Article XXVI²⁶

An arbitral award made outside the territory of this State shall be recognized as binding and enforced in accordance with the following procedure, subject to any multilateral or bilateral agreement entered into by this State:

An application shall be made in writing to the [competent court] [Court specified in article V], accompanied by the duly authenticated original award, or a duly certified copy thereof, and the original arbitration agreement referred to in article II, or a duly certified copy thereof. If the said award or agreement is not made in an official language of this State, the party applying for recognition and enforcement of the award shall supply a translation of these documents into such language, certified by an official or sworn translator or by a diplomatic or consular agent.

²⁵Under this heading, further provisions, still to be drafted, may be included such as provisions on objections against recognition and enforcement (to be dealt with in WP.42). A final chapter ("K. Recourse against arbitral award") would then cover the provisions on setting aside of awards (also to be dealt with in WP.42).

²⁶It should be noted that this article on foreign awards, like article XXV on domestic awards, deals merely with some procedural aspects of recognition and enforcement. Important qualifications and restrictions will be contained in future draft provisions, in particular those on objections against leave for enforcement (to be dealt with in WP.42).

2. NOTE BY THE SECRETARIAT: MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION: POSSIBLE FURTHER FEATURES AND DRAFT ARTICLES OF A MODEL LAW (A/CN.9/WG.II/WP.41)^a

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Introductory note

1. This working paper deals with subjects on which the Working Group on International Contract Practices requested further studies and with additional features which were suggested for inclusion in the model law by the Working Group. A note under each heading makes reference to the relevant discussion or conclusion of the Working Group at its third and fourth sessions (A/CN.9/216^b and A/CN.9/232^c). Draft provisions are also suggested under each subject in order to facilitate discussion at the Working Group.

A. ADAPTATION OF CONTRACTS AND FILLING OF GAPS IN CONTRACTS¹

2. Questions pertaining to adaptation of contracts and filling of gaps in contracts most often arise in transactions which are to be performed over a long period of time. In such transactions the parties, at the time of the conclusion of the contract, may not be able to foresee future events or may not have sufficient information on some of the current factors which may affect the performance of the contractual obligations. This makes it difficult to prepare in advance comprehensive contracts which would cope adequately with all contingent events occurring after the conclusion of the contract.

3. In this respect, two examples may be given:

(a) There may be events occurring after the conclusion of the contract that would significantly

change the basis under which the parties concluded the contract. The result of such a change may be that a party requests the other party to adapt their contract to the new circumstances;

(b) The parties may have, at the time of the conclusion of the contract, intentionally left a gap in their contract by postponing to agree on some aspects of the contract to a later date (e.g. mode or time of delivery, specification of quality or quantity) because they did not have sufficient information upon which to base their agreement. The parties expected such gaps to be filled by later negotiation.

4. In both cases, the parties may not be able to agree on how to adapt or supplement the contract. However, the parties may agree to refer disputes on adaptation or supplementation of contracts to a third person or to an arbitral tribunal for decision.

5. In this context, the following questions may be considered in regard to such agreements in the framework of the model law:

(a) Whether adaptation or supplementation of contracts can be regarded to fall within the domain of arbitration;

(b) If the answer to (a) is in the positive, whether the mandate to adapt or supplement a contract is presumed or should it be expressly conferred upon the arbitral tribunal; and

(c) What is the legal nature of the decision in which a contract is adapted or supplemented.

6. In regard to question (a) above, a possible objection to the possibility of calling upon the arbitral tribunal to adapt or supplement a contract may be based on the special character of decisions on adaptation or supplementation of contracts as contrasted to

^a12 January 1983. Referred to in Report, para. 87 (part one, A).

^bYearbook ... 1982, part two, III, A.

^cReproduced in this volume, part two, III, A.

¹As to the previous discussion at the Working Group, see A/CN.9/216, paras. 32 and 33.

decisions on claims arising from breach or non-performance of contractual or legal duties. Normally, in arbitration practice only cases of claims arising from breach or non-performance of contractual or legal duties are dealt with. In deciding such cases substantive legal rules are applied. However, in cases of adaptation or supplementation no breach or non-performance of a contractual or legal duty is alleged. Moreover, since there are no substantive legal rules on how to adapt or supplement contracts, the arbitral tribunal would have to base its decision on a fair and discretionary assessment of all the circumstances. The objection may be that the arbitral tribunal should not be able to adapt or supplement contracts since courts in many countries cannot do so and arbitration is a substitute for justice through a court.

7. However, it might be said in response that, unlike the competence of state courts, the principle of the supremacy of the will of the parties is the core of the competence of arbitration and this speaks for respecting an agreement by the parties to entrust an arbitral tribunal to adapt or supplement their contract. There may also be policy reasons against a court creating new contractual terms, whereas such policies may not apply to arbitrators who come to the aid of the parties if the parties so wish. The courts may be well equipped to decide on legal disputes but often lack special expertise to formulate new contractual obligations on the basis of an assessment of economic factors. The parties may trust the arbitrators' ability to appraise the economic relations between the parties and for this reason the parties may give them the mandate to adapt or supplement their contract.

8. With regard to question (b) in paragraph (5), the decisive factor may be the generally recognized principle that a contract is binding on a party only if he agreed to it. By adapting or supplementing a contract the arbitral tribunal creates new contractual obligations for the parties and, therefore, such contractual obligations can become binding only when the parties have agreed to be bound. The parties may demonstrate their agreement to be bound by expressly conferring such a mandate on the arbitral tribunal. Thus, the usual arbitration clauses may be interpreted as being limited to the mandate to adjudicate legal disputes arising from breach or non-performance of contracts.

9. With regard to question (c) in paragraph 5, one approach may be to consider that the decision has created new contract terms with the same juridical character as those in the original contract. The other approach may be to consider the decision as an arbitral award. However, since the arbitral tribunal in its decision creates obligations for the parties to be observed in the future and no contract obligation has been breached or not performed, there would be nothing in the decision to be enforced even if it is regarded as an arbitral award. If a party breaches a new obligation created by the arbitral tribunal, the other party would have to bring a claim to the court or to the arbitral tribunal to obtain a judgment or award for enforcement.

10. If the contract approach is adopted, the validity of the new terms determined by the arbitral tribunal may be challenged in judicial proceedings on the same grounds as the terms in any ordinary contract, such as that they contravene public policy. Challenging the validity of such a decision may be subject to the same limitation periods which are applicable to contracts in general. On the other hand, the arbitration award approach may indicate that an action for setting aside of the decision is only possible on exhaustively enumerated grounds and within the time-limit for such an action. The time-limit for actions for setting aside an award may be different from the limitation periods applicable to actions for annulment or rescission of a contract.

11. The following draft provisions may form a basis for discussion:

Article A

(1) If expressly authorized by the parties, the arbitral tribunal has the power to adapt the contract [to changed circumstances] or to supplement the contract by formulating provisions on points not settled by the parties.

Alternative A

(2) The [contents of the] decision by the arbitral tribunal on the adaptation or supplementation of the contract has the same effect as a contract between the parties.

Alternative B

(2) The arbitral tribunal decides on the adaptation or supplementation of the contract in an arbitral award.²

B. COMMENCEMENT OF ARBITRAL PROCEEDINGS AND CESSATION OF RUNNING OF LIMITATION PERIOD³

12. In many international transactions arbitration is a substitute for judicial proceedings as the means of settling disputes. It might, therefore, be desirable that the commencement of arbitral proceedings should affect the running of limitation periods in the same manner as the commencement of judicial proceedings. This approach is accepted in many legal systems. However, the moment of the cessation of the running of a limitation period is not necessarily uniform.

13. Divergent answers with regard to the decisive moment for the cessation of the running of the limitation period mainly stem from the fact that

²If alternative A were to be adopted, the Working Group may wish to consider whether it is necessary to make it clear that the decision by the arbitral tribunal may also be challenged on some of the grounds for challenging ordinary arbitral awards. If alternative B were to be adopted, it may become necessary to consider whether all the provisions of the model law on the arbitral award should be applicable to awards adapting or supplementing a contract.

³The decision to consider this subject was adopted at the third session of the Working Group; see A/CN.9/216, para. 72.

national laws often leave the manner of commencing arbitral proceedings to the agreement of parties. The arbitration rules which parties have adopted may provide, for example, that arbitral proceedings commence by a request for the appointment of arbitrators, by a request to submit the claim to arbitration, by seizing the arbitrator designated in the arbitration agreement, or by serving the statement of claim. No comparable divergency arises in relation to the commencement of judicial proceedings as there is normally a standard procedure in every jurisdiction for commencing judicial proceedings and the actual step which is relevant for the cessation of the running of limitation periods is clearly settled as a matter of procedural law. It is submitted that the model law should also respect the freedom of the parties to agree on the manner for commencing arbitral proceedings and provide supplementary rules for cases where the parties failed to agree.

14. The validity of this approach has been recognized by the Convention on the Limitation Period in the International Sale of Goods (New York, 1974) (hereinafter referred to as Prescription Convention). Paragraph 1 of Article 14 reads:

"Where the parties have agreed to submit to arbitration, the limitation period shall cease to run when either party commences arbitral proceedings in the manner provided for in the arbitration agreement or by the law applicable to such proceedings."

15. Furthermore, with regard to the question as to how the model law should provide a supplementary rule for cases where the parties have failed to make provision for the manner of commencing arbitral proceedings, paragraph 2 of Article 14 of the Prescription Convention suggests an approach:

"In the absence of any such provision, arbitral proceedings shall be deemed to commence on the date on which a request that the claim in dispute be referred to arbitration is delivered at the habitual residence or place of business of the other party or, if he has no such residence or place of business, then at his last known residence or place of business."

16. This provision may also be regarded as an indication of a preferred approach for arbitration rules. Thus, Article 3 of the UNCITRAL Arbitration Rules adopts a similar approach but in a more elaborated manner. The apparent difference in the degree of detail in the provision between paragraph 2 of Article 14 of the Prescription Convention^d and Article 3 of the UNCITRAL Arbitration Rules may be partly due to the fact that the former is a rule of general applicability to all arbitral proceedings while the latter is a part of a concrete set of rules which will be applied to a particular arbitration by the agreement of parties.

17. The following draft provisions may form a basis for discussion:

^dYearbook ... 1974, part three, I, B (A/CONF. 63/15).

Article B

(1) The limitation period in respect of a claim submitted to arbitration shall cease to run when any party commences arbitral proceedings in the manner provided for in the arbitration agreement.

(2) In the absence of any such agreement, the arbitral proceedings shall be deemed to commence on the date on which a request that the claim in dispute be referred to arbitration is delivered at the habitual residence or place of business of the other party or, if he has no such residence or place of business, then at his last known residence or place of business [provided that such a request sufficiently identifies the claim]⁴

18. In this context, the Working Group may wish to consider the appropriateness of regulating in the model law the minimum contents of a request of a party to the other party that the claim in dispute be referred to arbitration.⁵ This question is, in some respects, connected with the next item to be discussed, i.e. minimum contents of the statement of claim and the statement of defence.

C. MINIMUM CONTENTS OF STATEMENTS OF CLAIM AND DEFENCE⁶

19. Whether and in what form the model law should deal with the minimum contents of the statement of claim and the statement of defence, would primarily depend on the purpose of such provisions. The Working Group may, thus, wish to consider the following two approaches and accordingly request the secretariat to prepare draft provisions.

20. One approach could be to establish a mandatory requirement in order to ensure certainty about the scope of the submission, in particular what claims (and counter-claims) are submitted to arbitration. Such a rule would apply in all types of arbitration, for example, in a system which distinguishes between notice and statement of claim (e.g. UNCITRAL Arbitration Rules, articles 3 and 18) and a system which combines both in one request for arbitration (e.g., ICC Rules, article 3). Therefore, it may be necessary to omit any reference to procedural details or the varying names of such communications and merely provide, for example: "The claimant must state the relief or remedy sought and the facts supporting his claim", while the respondent may be obliged to respond to these particulars.

⁴The reference to the residence or places of business could be left out if a general rule on delivery of notices, notifications, communications or proposals were included in the model law.

⁵E.g., (a) A reference to the arbitration agreement that is invoked, (b) A reference to the contract out of or in relation to which the dispute arises, and (c) The general nature of the claim and the relief sought. Cf. UNCITRAL Arbitration Rules, Art. 3, para. 3 (Yearbook ... 1976, part one, II, A, paras. 56-57).

⁶The decision to consider this subject was adopted at the third session of the Working Group; see A/CN.9/216, para. 72.

21. The other approach could be to include supplementary rules merely to take care of those cases where the parties have not themselves made any provision. Such rules, which could be modelled on articles 18 to 20 of the UNCITRAL Arbitration Rules, could be part of a larger set of rules providing a mechanism for getting arbitration started and going even where parties have not agreed on procedural rules.

D. LANGUAGE IN ARBITRAL PROCEEDINGS⁷

22. The language to be used in international arbitral proceedings is of great practical importance because the parties, their representatives, arbitrators and witnesses often have different language backgrounds. The Working Group may therefore wish to consider what principle should be adopted in regard to languages.

23. The first principle may be that the parties should be free to agree on the language to be used in arbitral proceedings either in the arbitral agreement or at some time before or even after the commencement of arbitral proceedings. The second principle may be that, in the absence of an agreement by the parties, the arbitral tribunal should have the power to determine the language or languages to be used in the proceedings, taking into account the exigencies of the arbitration.

24. Other relevant questions which may be considered are:

(a) Whether the model law should require that the language so determined shall be used at all oral hearings and in all written statements and communications (see Article 17, paragraph 1 of the UNCITRAL Arbitration Rules), and

(b) Whether it should be expressly provided that the arbitral tribunal may order that any documents or exhibits submitted in the course of the proceedings, delivered in their original language, shall be accompanied by a translation into the language of the proceedings (see Article 17, paragraph 2, of the UNCITRAL Arbitration Rules).

25. The Working Group may also wish to consider the usefulness of a "best efforts" rule for the agreement on the language of the proceedings. Such a rule may be accompanied by a supplementary rule for cases when no agreement could be reached.⁸

⁷The decision to consider this subject was adopted at the third session of the Working Group; see A/CN.9/216, para. 72.

⁸Such is the approach in the 1977 Optional Arbitration Clause for use in Contracts in USA-USSR Trade, which reads:

"8. The parties will use their best efforts to agree on a single language for the arbitration proceedings, in order to save time and reduce costs. However, if the parties do not agree on a single language:

"8.1 Each party shall present its statement of claim or statement of defence, and any further written statements in both English and Russian.

"8.2 Any other documents and exhibits shall be translated only if arbitrators so determine.

"8.3 There shall be interpretation into Russian and English at all oral hearings.

"8.4 The award, and the reasons supporting it, shall be written in both Russian and English."

26. The following draft provisions may form a basis for discussion:

Article D

The parties are free to determine the language or languages to be used in the proceedings. [They shall use their best efforts to agree on a single language.] Failing agreement by the parties, the arbitral tribunal shall determine the language or languages to be used in the proceedings [having regard to the circumstances of the case].

E. COURT ASSISTANCE IN TAKING EVIDENCE⁹

27. Because of the lack of power of an arbitral tribunal to compel a person to testify or to produce a document or because the tribunal may not be able to enforce its decision to inspect goods or premises, the arbitral proceedings may be blocked. For this reason, some national laws expressly provide that the arbitral tribunal may request from the court assistance in taking evidence. There was general agreement in the Working Group that such court assistance could contribute to the proper and efficient functioning of international commercial arbitration. Under one view it should be possible to draft appropriate provisions to this effect, while according to another view such provisions were not feasible in view of certain difficulties and concerns.¹⁰

28. One difficulty indicated in the Working Group was that the procedures of such court assistance formed an integral part of the procedural law of the legal system concerned, and that the relevant procedural laws varied considerably from one legal system to another. This difficulty, however, may be lessened if the model law minimized its impact on the existing national rules of procedure. The model law could contain basic provisions only on the contents of the request for court assistance, on the method of taking evidence and on the conditions for refusing the requested assistance. The model law could also provide that court assistance in taking evidence would be given in accordance with the domestic rules which were applicable for similar assistance among the courts.

29. Another difficulty arises where the court assistance is required in a country other than the one where the arbitration takes place, because the model law, by its nature, may not be able to secure court assistance abroad. The arbitral tribunal could only avail itself of existing procedures for obtaining evidence abroad, if such existed.

30. However, the model law could provide for court assistance to foreign arbitral tribunals. For example, the model law may require a court to treat a request for assistance from a foreign arbitral tribunal in the same way as the court treats a similar request from foreign

⁹As to the previous discussion at the Working Group, see A/CN.9/216, paras. 61 and 62.

¹⁰*Ibid.*, para. 61

courts. Thus, a State which is bound by bilateral or multilateral treaties to execute such requests from courts in other contracting States would also become obliged to execute such requests from arbitral tribunals in those States. If this approach were followed, the establishment of a set of detailed procedural rules for court assistance to foreign arbitral tribunals may become unnecessary. The existing rules for assistance to foreign courts could be applied to court assistance to foreign arbitral tribunals.

31. A more ambitious approach to court assistance might be to provide for an obligation of States which adopted the model law to execute requests from foreign arbitral tribunals regardless of the extent of the obligation of the States to give such assistance to foreign courts. Such an approach would contribute considerably to the facilitation of taking evidence in international commercial arbitration. However, a State may be reluctant to accept the obligation to provide assistance to all foreign arbitral tribunals particularly if the State is not prepared to provide assistance to courts of all States. The State may also be reluctant to accept such an obligation if a request comes from an arbitral tribunal of a State whose courts are not prepared to give assistance to arbitral tribunals of the first State. This reluctance may be overcome if the obligation were subject to reciprocity, although it should be recognized that the principle of reciprocity has many difficulties in application.

32. If the model law were to provide for court assistance, a further question arises whether court assistance should be provided only upon request by the arbitral tribunal. This restriction may be useful to minimize the possibility of abuse of the court process. In most cases, arbitral tribunals would not have an interest in deliberately abusing court assistance. The parties who are not permitted to request court assistance directly could seek for such assistance through the arbitral tribunal.

33. A further restriction may be imposed by providing in the model law that the court may refuse to give assistance (a) if the interests of the State would thereby be prejudiced, (b) if the reason for which evidence is requested does not justify the assistance, or (c) if the arbitral tribunal or the party has other reasonable means of obtaining the evidence.

34. If, however, the Working Group decides that the parties should also be permitted to submit a request for assistance directly to the court, some supervision by the court may become necessary to prevent abuses. The court could effectively prevent abuses if it examined the usefulness and relevance of evidence in regard to the dispute.

35. With regard to the method in which court assistance is provided, there are two approaches in practice. In some legal systems the assisting court actually hears witnesses or inspects goods or premises or procures documents. In other legal systems, the court merely provides the element of compulsion which

is absent in the arbitral tribunal. Under the latter systems the court orders a witness to appear before the arbitral tribunal or orders a person to submit evidence to the arbitral tribunal. Another approach may also be envisaged where the arbitral tribunal has the choice between the two methods.

36. In this connection, it may also be noted that an arbitral tribunal may occasionally wish to obtain assistance of a court to avoid costs or inconvenience of travel. The Working Group may, therefore, wish to consider whether the model law should also provide for court assistance even for such a situation.

37. The following draft provisions may form a basis for discussion:

Article E1

Alternative A

(1) Where the arbitration takes place in this State [, or under the law of this State] the arbitral tribunal [or a party] may request the court¹¹ to order [a] [the other] party or a third person to give evidence to the arbitral tribunal [if the arbitral tribunal or the party is not able to obtain the evidence].

(2) The court shall execute such a request and apply the appropriate measures of compulsion in accordance with the rules for taking evidence before that court.

(3) The court may refuse to order a party or a third person to give evidence:

(a) If the interests of the State would thereby be prejudiced;

(b) If the reason for which the assistance of the court is requested does not justify the assistance; or

[(c) If the arbitral tribunal or the party has other reasonable means of obtaining the evidence.]

Alternative B

(1) Where the arbitration takes place in this State [, or under the law of this State.] the arbitral tribunal [or a party] may request the court to take evidence [if the arbitral tribunal or the party is not able to obtain the evidence].

(2) The court shall execute such a request in accordance with the rules for the execution of similar requests made by other courts of this State.

[(3) [If it is specified in the request,] the court shall inform the arbitral tribunal and the parties of the place and the time of the proceedings of taking evidence in order that the arbitrators and the parties may be present.]

¹¹The Working Group may wish to consider whether this court should be the Court specified in article V (in A/CN.9/WG.II/WP.40) or whether it should be another competent court.

[(4) The court shall comply with a special request by the arbitral tribunal that in taking evidence a special method or procedure be followed, unless the court considers such a method to be improper or that it would cause practical difficulties.]

(5) The court may refuse to provide evidence:

(a) If the interests of the State would thereby be prejudiced;

(b) If the reason for which the assistance of the court is requested does not justify the assistance; or

[(c) If the arbitral tribunal or the party has other reasonable means of obtaining the evidence.]

Article E2

(1) A request for assistance by the arbitral tribunal [or by a party] to the court shall include:

(a) The names and addresses of the arbitrators and the parties;

(b) The reason for which the assistance is required;

(c) A reference to the arbitration agreement under which the arbitration is conducted;

(d) The general nature of the claim, the relief sought and an indication of the amount involved, if any;

(e) The points at issue in regard to which the assistance is required, giving all necessary information thereto; and

(f) Where appropriate,

(i) The names and address of [the party or] the third person to be examined;

(ii) The questions to be put to [the party or] the third person to be examined or a statement of the subject-matter about which he is to be examined;

(iii) The description of documents, goods or other exhibits to be inspected.

(2) The request shall be in the language of the court.

Article E3

(1) A foreign arbitral tribunal [or a party to a foreign arbitration] may request the court of this State for assistance in taking evidence.

(2) The court shall execute such a request in accordance with the rules for the execution of similar requests from foreign courts. However, the court may refuse to give the assistance if:

[(a) The courts of the State in which [, or under the law of which,] the arbitration takes place do not have a right to request similar court assistance in this State; or]

(b) The courts of that State are not required to give similar assistance to arbitrations of this State.

F. TERMINATION OF ARBITRAL PROCEEDINGS¹²

38. The Working Group may wish to consider whether it would be appropriate to include in the model law a provision on termination of arbitral proceedings. In this respect, two approaches may be considered.

39. One approach is to enumerate various circumstances which would cause automatic termination of arbitral proceedings or empower the arbitral tribunal or the court to terminate the proceedings. If this approach were to be taken it may be advisable to enumerate those circumstances after all other provisions on arbitral proceedings have been established.

40. The other approach is to limit the termination of arbitral proceedings to those cases only when the continuation of proceedings is either impossible or unnecessary (e.g., the rendering of an award on the merits of the case, the agreement by the parties to terminate the proceedings, the withdrawal of the claim, or the lapse of jurisdiction or mandate of the arbitral tribunal). Under this approach there would be no termination of arbitral proceedings when various circumstances merely obstruct the normal course of proceedings without, however, making the continuation of proceedings impossible (e.g., difficulties or delays in appointing the presiding arbitrator, failure of action on the part of arbitrators, or unreasonable delay in rendering the award). In those cases appropriate measures may still be taken to make the continuation of the proceedings possible. If this approach is taken, a special rule on termination of arbitral proceedings may be regarded as superfluous because it would cover the cases when termination is a self-evident consequence. However, there may be some merit in such a rule in cases when the arbitral tribunal considers the continuation of the proceedings unnecessary and a party has a justified objection to the termination (e.g. the parties are inactive for a long time and the arbitral tribunal considers terminating the proceedings).

41. The following draft provisions may form a basis for discussion:

Article F

(1) [The arbitral proceedings shall be terminated] [The arbitral tribunal shall issue an order for the termination of the arbitral proceedings] in the following cases:

(a) When the parties agree that the arbitral proceedings are to be terminated; and

(b) In all other cases where the continuation of the arbitral proceedings becomes unnecessary or impossible.

(2) When the arbitral proceedings are to be terminated without an award on the merits of

¹²The decision to consider this subject was adopted at the third session of the Working Group; see A/CN.9/216, para. 72.

the claim, the arbitral tribunal shall inform the parties of its intention to issue an order for the termination of the proceedings. The arbitral tribunal shall have the power to issue such an order unless a party raises justifiable grounds for objection.¹³

G. PERIOD FOR ENFORCEMENT OF ARBITRAL AWARDS¹⁴

42. The Working Group may wish to consider a provision for possible inclusion in the model law on the period during which an arbitral award may be enforced. Such a provision exists in a number of legal systems. It has been suggested that the establishment of such a period in the model law would contribute to certainty in international commerce.¹⁵

43. If the Working Group decides that such a provision would be useful, two approaches may be envisaged. One possible approach may be to provide a limitation period for the enforcement of arbitral awards. In connection with this approach it may be considered whether a request to a court for enforcement in any State should cause the cessation of the running of the limitation period or whether the cessation is to be confined only to the State where the request for enforcement is made.

44. Another approach may be to provide a period with a fixed time-limit (of probably longer duration than the limitation period) which would run continuously without a possibility of a cessation or extending of its running. While this approach might enhance certainty it may have some disadvantages. For example, it may happen that the requesting party tries to enforce the

award within the time-limit but is unsuccessful because of reasons on the part of the other party (e.g. current lack of assets in the State where the enforcement is sought). It may appear unjustified if at a later stage, when the enforcement could be successful, the requesting party could not enforce his claim because it is time-barred.

45. The following draft provisions may form a basis for discussion:

Article G

Alternative A

(1) The limitation period for enforcement of the arbitral award shall be [five] years from the date when the award was received by the party requesting the enforcement. The limitation period shall cease to run when that party requests a court in any State that the arbitral award be enforced, provided that he has taken all reasonable steps to ensure that the other party is informed of the request for enforcement.¹⁶

(2) Where enforcement proceedings have ended without success for reasons other than the merits of the request for enforcement, the limitation period shall be deemed to have continued to run. If, at the time such enforcement proceedings ended, the limitation period has expired or has less than one year to run, the party requesting enforcement shall be entitled to a period of one year from the date on which the enforcement proceedings ended.¹⁷

Alternative B

Enforcement of the arbitral award may not be requested after [ten] years from the date when the award was received by the party requesting the enforcement.

¹³The second paragraph is modelled on article 34, para. 2 of the UNCITRAL Arbitration Rules.

¹⁴The decision to consider this subject was adopted at the fourth session of the Working Group; see A/CN.9/232, para. 23.

¹⁵S. Lebedev, "How long does a foreign award stay enforceable?", in *The Art of Arbitration*, V. C. Schultz and A. J. van den Berg, eds., *liber amicorum Pieter Sanders* 12 September 1912-1982 (Deventer, Kluwer, 1982) pp. 213-231.

¹⁶The provision on international effect of the cessation of the running of the limitation period is modelled on article 30 of the Prescription Convention.

¹⁷This provision is modelled on article 17 of the Prescription Convention.

3. NOTE BY THE SECRETARIAT: MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION: DRAFT ARTICLES 37 TO 41 ON RECOGNITION AND ENFORCEMENT OF AWARD AND RECOURSE AGAINST AWARD (A/CN.9/WG.II/WP.42)^a

Introductory note

1. This working paper contains draft articles on recognition and enforcement of award and on recourse against arbitral award. Since these draft articles are tentative ones to be considered by the Working Group in first reading, they are numbered and presented here as a continuation of tentative draft articles 1 to 36, as set forth in documents A/CN.9/WG.II/WP.37 and

38^b. After consideration by the Working Group, they will be revised and re-numbered as a continuation of revised draft articles I to XXVI, as set forth in document A/CN.9/WG.II/WP.40^c.

2. The draft articles submitted in this working paper have been prepared in the light of the relevant

^bReproduced in this volume, part two, III, B, 1 and 2 respectively.

^cReproduced in this volume, part two, III, D, 1.

^a25 January 1983. Referred to in Report, para. 87 (part one, A).

discussions by the Working Group at its third and fourth sessions.¹

3. As regards the subject of recognition and enforcement of arbitral awards, the draft articles follow the approach adopted by the Working Group with regard to the draft article on executory force and enforcement of award (previous draft article 36, revised draft articles XXV and XXVI), i.e. to treat separately awards rendered in the State where the model law is in force and awards rendered outside that State. Nevertheless, an attempt is made to suggest similar solutions in substance in order to come closer to the ideal of uniform treatment of "international" awards irrespective of their place of origin.

4. The above mentioned "territorial" demarcation line also means that no distinction is made according to which procedural law applies. Thus, for example, the provision on enforcement of foreign awards would apply to an award rendered abroad even if made under the law of the State where enforcement is sought (i.e. under the model law). It may be noted that such cases of awards made under a law of a State other than the country of origin involve questions of policy which come up in a number of contexts (e.g. refusal of recognition because of violation of procedural law, draft article 38 (1) (d); competence of court to set aside an award, draft article 40; and recognition of such setting aside as reason against enforcement, draft article 38 (1) (e)). While the answer to these questions may vary from one context to another, it is submitted that the individual decisions are necessarily of a tentative nature and that at a later stage an overall review of the policy would be desirable, possibly in connection with the consideration of questions of conflicts of procedural laws.

Draft articles 37 to 41 of a model law on international commercial arbitration

RECOGNITION AND ENFORCEMENT OF AWARD (continued)²

Article 37³

(1) Recognition and enforcement of an arbitral award made in the territory of this State may be refused, at the request of the party against whom it is invoked, only if that party furnishes proof that:

(a) A party to the arbitration agreement referred to in article II was, under the law applicable to him, under

some incapacity, or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of this State; or

(b) The party against whom the award is invoked was not given proper notice of the appointment of the arbitrator(s) or of the arbitration proceedings or was otherwise unable to present his case; or

(c) The award [deals with] [decides on] a dispute or matter [not submitted to arbitration] [outside the scope of the arbitration agreement or not referred to the arbitral tribunal];⁴ however, if any decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration may be recognized and enforced; or

(d) The composition of the arbitral tribunal or the arbitral procedure was not in accordance with the mandatory provisions of this Law,⁵ or the agreement by the parties, unless in conflict with any mandatory provision of this Law, or, failing such agreement, the non-mandatory provisions of this Law [, provided that, if the parties have agreed on the application of the law of another State, the provisions of that law are relevant];⁶ or

(e) The award [has not yet become binding on the parties] [is still open to appeal before a higher instance arbitral tribunal]⁷ or has been set aside [or suspended]⁸ by a court of this State [or, if the award was made under the law of another country, by a competent authority of that country]⁹.

⁴While the first alternative may be regarded as sufficient for all practical purposes, the second alternative attempts to indicate more clearly that the question of the arbitrators' exceeding their authority has to be answered by using two standards: the arbitration agreement (in particular an arbitration clause) and the often narrower mandate given to the arbitrators by way of reference, submission of statement of claim.

⁵It may be noted that most commentators interpret article V, paragraph (1) (d) of the 1958 New York Convention as giving absolute priority to the agreement of the parties, i.e. irrespective of whether such agreement is in conflict with a mandatory provision of the "applicable" procedural law (see, e.g., Fouchard, *L'arbitrage commercial international*, vol. II (Paris 1965), p.332; Sanders, *The New York Convention*, in *International Commercial Arbitration*, vol. II (The Hague, 1960), p. 317; Schlosser, *Das Recht der internationalen privaten Schiedsgerichtsbarkeit*, vol. I (Tübingen 1975), p.420; van den Berg, *The New York Arbitration Convention* (The Hague/Deventer, 1982), p. 325-330). This view leads to the dilemma that, in the case of such a conflict and if the procedure complied with the agreement, enforcement of the award would not be refused under sub-paragraph (d) but, since the award may be set aside, enforcement may be effectively refused under sub-paragraph (e). However, it is clear that this rule and its reasoning does not apply to the enforcement of non-foreign awards as governed by this draft article (see also footnote 14).

⁶See also introductory note above, para. 4.

⁷The first alternative presents the wording used in article V, paragraph (1) (e) of the 1958 New York Convention which is commonly interpreted as meaning "still open to ordinary means of recourse". Since the model law does not envisage any such ordinary appeal to courts but should not preclude appeal within the arbitration system, as known particularly in commodity arbitrations, the second alternative, which would make that point clearer, is submitted for consideration.

⁸The words "or suspended", as used in the 1958 New York Convention, might be omitted in the model law since this law does not envisage such suspension of an award, i.e. of its enforcement.

⁹See also introductory note above, para. 4.

¹Report of the Working Group on International Contract Practices on the work of its third session (A/CN.9/216) (Yearbook ... 1982, part two, III, A), paras. 103-104, 106-109, and of its fourth session (A/CN.9/232) (reproduced in this volume, part two, III, A), paras. 14-22.

²Preceding draft articles under this heading are the revised draft articles XXV and XXVI set forth in WP.40.

³This draft article is modelled on article V of the 1958 New York Convention (United Nations, *Treaty Series*, vol. 330, No. 4739 (1959), p. 38), with some suggested modifications for the sake of clarification or to adjust it to non-foreign awards.

(2) Recognition and enforcement of an award may also be refused if the court finds that the recognition or enforcement would be contrary to the [international]¹⁰ public policy of this State [, including any public policy rule on the arbitrability of the subject matter of the dispute].¹¹

Article 38¹²

(1) Subject to any multilateral or bilateral agreement entered into by this State, recognition and enforcement of an arbitral award made outside the territory of this State may be refused, at the request of the party against whom it is invoked, only if that party furnishes proof that:

(a) A party to the arbitration agreement referred to in article II was, under the law applicable to him, under some incapacity, or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of this State; or

(b) The party against whom the award is invoked was not given proper notice of the appointment of the arbitrator(s) or of the arbitration proceedings or was otherwise unable to present his case; or

(c) The award [deals with] [decides on] a dispute or matter [not submitted to arbitration] [outside the scope of the arbitration agreement or not referred to the arbitral tribunal];¹³ however, if any decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration may be recognized and enforced; or

(d) The composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties,¹⁴ or, failing such agreement, was not in accordance with the law of the country where the arbitration took place [, provided that, if the

parties have agreed on the application of the law of another State, the provisions of that law are relevant];¹⁵ or

(e) The award [has not yet become binding on the parties] [is still open to appeal or other ordinary recourse]¹⁶ or has been set aside [for one of the reasons set forth in sub-paragraphs (a) to (d) or in paragraph (2) of this article],¹⁷ or suspended, by a competent authority of the country in which [, or under the law of which,]¹⁸ that award was made.

(2) Recognition and enforcement may also be refused if the court [from which recognition and enforcement is sought]¹⁹ finds that:

(a) The subject matter of the dispute is not capable of settlement by arbitration under the law of this State; or

(b) The recognition or enforcement of the award would be contrary to the [international] public policy of this State.

Article 39²⁰

If an application for the setting aside or suspension of an award has been made to a competent authority referred to in article 37, paragraph (1) (e) or 38, paragraph (1) (e), the authority before which the award is sought to be relied upon may, if it considers it proper, adjourn the decision on the enforcement of the award and may also, on the application of the party claiming enforcement of the award, order the other party to give suitable security.²¹

RECOURSE AGAINST ARBITRAL AWARD

Article 40

No recourse against an arbitral award made under this Law [, whether or not rendered in the territory of

¹⁵See also introductory note above, para. 4.

¹⁶While the first alternative presents the wording used in article V (1) (e) of the 1958 New York Convention, the second alternative, reflecting the common interpretation thereof, is submitted for consideration as a possibly clearer rule.

¹⁷The words in square brackets are intended to serve the same purpose as article IX of the 1961 Geneva Convention (United Nations, *Treaty Series*, vol. 484, No. 7041 (1963-1964), p. 364), i.e. to recognize, for purposes of enforcement, as reasons for setting aside only those reasons on which recognition and enforcement may be refused. Such a rule, by disregarding certain unexpected local particularities, would meet the concerns underlying a proposal made by the International Chamber of Commerce some time ago (cf. A/CN.9/169, para. 9; A/CN.9/168, para. 43).

¹⁸See also introductory note above, para. 4.

¹⁹The words in square brackets might be regarded as self-evident and superfluous.

²⁰This draft article is modelled on article VI of the 1958 New York Convention.

²¹As regards non-foreign awards, this draft article may be redundant or in need of modification, if the Working Group would be in favour of stream-lining the recourse system along the lines suggested in WP.35, paras. 28-30. A provision on adjournment would, for example, not be necessary under a system such as the one adopted in article 1504 of the French law according to which an action for setting aside implies *ipso iure* an appeal against any enforcement order of the enforcement judge or disavowal of that judge. Another point in need of clarification arises with regard to those States not requiring an *exequatur* for enforcement of awards made in their territory.

¹⁰The word "international" might be retained, for the sake of uniform treatment of all "international" awards, if (and only if) it were also adopted in the context of foreign awards (see draft article 38 (2)).

¹¹The words in square brackets are based on the common view that article V (2) (a) of the 1958 New York Convention presents, in substance, a sub-category of the general reason set forth in sub-paragraph (b) of that paragraph.

¹²This draft article is modelled on article V of the 1958 New York Convention.

¹³See note 4.

¹⁴The Working Group may wish to consider the appropriateness of aligning this provision with draft article 37 (1) (d), i.e. to accord priority to the mandatory provisions of the applicable procedural law. Although this would constitute a deviation from the prevailing interpretation of this provision in the 1958 New York Convention, it would help to avoid the dilemma mentioned in footnote 5. It may be added here that the dilemma, while probably not frequent, is a real one for the conscientious arbitrator who wants to render an award that can be enforced if necessary. There is a further consideration which casts some doubt on the above interpretation of this provision: where parties have expressly subjected their agreement to mandatory law provisions, e.g. by using the UNCITRAL Arbitration Rules (Yearbook ... 1976, part one, II, A), see article I (2), it would be difficult to maintain the view that the agreement on the point at issue has priority; however, if then priority is given to the conflicting mandatory provision, a rule such as article I (2) of the UNCITRAL Rules would have legal effect which goes far beyond what the drafters had in mind.

this State,]²² may be made to a court except an action for setting aside in accordance with the provisions of article 41.

Article 41

(1) An action for setting aside [an arbitral award referred to in article 40]²³ may be brought [before the Court specified in article V]²⁴ within four months from the date on which the party bringing that action has received the award in accordance with article XXII (4).²⁵

(2) An arbitral award may be set aside only on one of the grounds on which recognition or enforcement may

²²The words in square brackets are added for the mere purpose of clarification, i.e. to prevent, in particular, the otherwise possible mis-interpretation that only awards rendered in the State of the model law are covered. Such interpretation might be based on the principle that usually only the courts of the country of origin are competent to set aside awards. While it is conceivable to adopt such "territorial" approach as a strict and clear-cut rule, the solution suggested in draft article 40 is more in line with article V (1) (e) of the 1958 New York Convention and with the principle that parties, while probably not often doing so, may agree on the application of the procedural law of a State other than the one where the arbitration takes place; in this connection, see also introductory note above, para. 4.

²³The words in square brackets might not be necessary in view of the close proximity with the preceding article. If, however, such a reference seems desirable, one might also consider using here the same words as in article 40, i.e. "an arbitral award made under this Law".

²⁴The reference is to revised draft article V as set forth in WP.40. The final decision on whether this Court or another court should be competent for setting aside would depend on a later review of the exact functions of that special Court specified in article V (see also note 9 in WP.40).

²⁵The reference is to revised draft article XXII as set forth in WP.40. The Working Group may wish to consider whether it is necessary to deal with cases of appeal within the arbitration system and expressly to state that the time-limit would then run from the date on which the award is no longer subject to appeal before arbitrators or, if such appeal was made, from the date of the receipt of the decision on the appeal.

²⁶The reference to subparagraph (d) is of particular relevance since the general reason of non-compliance of the arbitral procedure with the applicable procedural laws or rules comprises many particular grounds often set out in detail in national law provisions on setting aside (e.g. award does not comply with form requirements, including statement of reasons; award rendered *ex aequo et bono* without authorization by parties; party not notified in advance about hearing; award rendered after expiry of time-limit fixed by parties). As the last example indicates, even an issue not dealt with in the procedural law (here: the model law) may become relevant in the context of setting aside if it is regulated in the agreement of the parties (and not complied with).

It should also be noted that the generality of the above ground, if interpreted literally, would lead to setting aside in cases of procedural mistakes or defects where such legal consequence may be regarded as unjustified. The Working Group may, thus, wish to consider the appropriateness of somehow qualifying the reason under subparagraph (d) by one of the various approaches found in national laws. One possible way is to use the idea of estoppel or implied waiver and to preclude reliance on a ground which the party had knowledge of during the arbitration proceedings and did not invoke then; it may be added that the same idea might be incorporated in a provision on the arbitral procedure as such (as, e.g., article 30 of the UNCITRAL Arbitration Rules) and not merely as a restriction of the grounds for setting aside. Another possible way would be to qualify the procedural defect (e.g. "serious" or "gross" violation, non-compliance with mandatory provision). Yet another way, also used in some national laws, could be to qualify the causal connection between the procedural mistake and the award (e.g. non-compliance affected the award or is likely to have influenced the decision).

be refused under article 37, paragraph (1) (a), (b), (c), (d)²⁶ or (2)²⁷ [or on which an arbitrator may be challenged under article IX (2)].²⁸

(3) The court may, where appropriate,²⁹ set aside only a part of the award, provided that this part can be separated from the other parts of the award.

(4) If the court sets aside the award, [it may order that the arbitration proceedings continue for re-trial of the case] [a party may within three months request re-institution of the arbitration proceedings], unless such measure is incompatible with a ground on which the award is set aside.³⁰

(5) Any decision by the court on an action for setting aside is subject to appeal within three months.³¹

²⁷Draft article 41 (2) implements the view prevailing at the fourth session of the Working Group that the grounds for setting aside should be restricted to those listed in article V, paragraphs (1) (a-d) and (2) (b) of the 1958 New York Convention (see A/CN.9/232, para. 15, reproduced in this volume, part two, III, A). However, since some doubt was expressed as to whether the reasons should be thus restricted, the Working Group may wish to consider the appropriateness of adding one or more of the following grounds as found in a number of national laws:

(a) "*Infra petita*" (as, e.g. included in the 1966 Strasbourg Uniform Law, article 25 (2) (e): "if the arbitral tribunal has omitted to make an award in respect of one or more points of the dispute and if the points omitted cannot be separated from the points in respect of which an award has been made"); in considering the need for such a rule, account should be taken of draft article XXIV (2) on additional award (set forth in WP.40) and of the possibility of widening the scope of that provision (e.g. by including even those cases where further hearings or evidence are necessary);

(b) "Award contains conflicting decisions"; in considering the need for such ground, which probably occurs only rarely, account should be taken of revised draft article XXIV (1) (b) on interpretation of award (set forth in WP.40). At any rate this ground seems to be more acceptable than the sometimes found wider ground "decisions in award are in conflict with reasons stated therefor" since this would open the door to an undesirable review of the merits of the case;

(c) "Relevant facts or evidence discovered or become known only after award"; this ground is found in many national laws (though in varied versions and sometimes limited to evidence "withheld by the other party" or "which the claimant was unable to present") and its adoption may be considered as furthering justice. However, for practical purposes, it would be necessary (as done in most national laws) to provide for a much longer time-period than the one envisaged under article 41 (1); yet, if a time-limit of, e.g., five years were adopted (as in article 28 (3) of the 1966 Strasbourg Uniform Law) (*European Treaty Series*, No. 56), recognition of such ground for setting aside would run counter to the idea of a speedy and final settlement of the dispute for the sake of peace;

(d) "Award improperly procured by other party (e.g. by fraud, bribery, forgery or other criminal act)"; to this possible ground for setting aside similar considerations apply as the ones set forth under (c); in addition, it is submitted that most if not all instances of this kind would be covered by the grounds set forth in article 37 (1) (b) or (2), i.e. violation of due process or public policy.

²⁸The decision on whether the words in square brackets are to be retained depends on the final decision of the Working Group on court review of a challenge (see revised draft article X in WP.40).

²⁹The main case envisaged here (and possibly to be expressed in the provision itself) is where the ground for setting aside affected only a part of the decision.

³⁰The main case envisaged here is the ground under article 37 (1) (a), i.e. lack of valid arbitration agreement.

³¹In view of revised draft article V (2) (b), set forth in WP.40, it would seem necessary to state expressly that appeal is allowed (provided this idea is adopted by the Working Group), if the Court specified in article V would be entrusted with the setting aside of awards (see also note 26).

IV. NEW INTERNATIONAL ECONOMIC ORDER^a

A. Report of the Working Group on the New International Economic Order on the work of its fourth session (Vienna, 16-20 May 1983) (A/CN.9/234)^b

Introduction

1. At its eleventh session the United Nations Commission on International Trade Law decided to include in its work programme a topic entitled "The legal implications of the new international economic order" and established a Working Group to deal with this subject.¹ At its twelfth session the Commission designated member States of the Working Group.² At its thirteenth session the Commission decided that the Working Group should be composed of all States members of the Commission.³

2. At its first session the Working Group recommended to the Commission for possible inclusion in its programme, inter alia, the harmonization, unification and review of contractual provisions commonly occurring in international contracts in the field of industrial development (A/CN.9/176, para. 31).^c The Commission at its thirteenth session agreed to accord priority to work related to these contracts and requested the Secretary-General to undertake a study concerning contracts on supply and construction of large industrial works.⁴

3. The study (A/CN.9/WG.V/WP.4 and Add.1-8)^d was submitted to the second session of the Working Group and examined by it (A/CN.9/198, paras. 11-88).^e At that session, the Working Group requested the secretariat to prepare a further study covering topics

noted but which had not been analyzed in that study (A/CN.9/WG.V/WP.4, para. 36) and also to include a number of other topics as the secretariat deemed appropriate in the light of the discussion at that session (A/CN.9/198, paras. 90 and 91).

4. The further study (A/CN.9/WG.V/WP.7 and Add. 1-6)^f was submitted to the third session of the Working Group (A/CN.9/217, para. 11).^g At that session the Working Group concluded its consideration of the complete study (A/CN.9/217, paras. 13-129) and requested the secretariat, pursuant to a decision of the Commission at its fourteenth session,⁵ to commence the drafting of a legal guide on contractual provisions relating to contracts for the supply and construction of large industrial works (A/CN.9/217, para. 130). The legal guide is to identify the legal issues involved in such contracts and to suggest possible solutions to assist parties, in particular from developing countries, in their negotiations.⁶

5. The Working Group at its third session requested the secretariat to submit to the Working Group at its fourth session a few sample draft chapters and an outline of the structure of the legal guide (A/CN.9/217, para. 132).

6. The Working Group held its fourth session at Vienna from 16 to 20 May 1983. All the members of the Working Group were represented, with the exception of Burundi, Chile, Colombia, Cuba, Cyprus, Ghana, Hungary, Indonesia, Nigeria, Senegal, Sierra Leone, Singapore, Trinidad and Tobago, Uganda, and United Republic of Tanzania.

7. The session was attended by observers of the following States: Argentina, Brazil, Bulgaria, Canada, China, Democratic People's Republic of Korea, Ecuador, Greece, Holy See, Malaysia, Mexico, Netherlands, Norway, Poland, Republic of Korea, Sweden, Switzerland, and Thailand.

^aYearbook ... 1982, part two, IV, B.

^bYearbook ... 1982, part two, IV, A.

^cReport of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 84 (Yearbook ... 1981, part one, A).

^dReport of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 84.

^aFor consideration by the Commission see Report, chapter V (part one, A).

^b25 May 1983. Referred to in Report, para. 90 (part one, A).

^cYearbook ... 1980, part two, V, A.

^dYearbook ... 1981, part two, IV, B, 1.

^eYearbook ... 1981, part two, IV, A.

¹Report of the United Nations Commission on International Trade Law on the work of its eleventh session, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17* (A/33/17), para. 71 (Yearbook ... 1978, part one, II, A).

²Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 100 (Yearbook ... 1979, part one, II, A).

³Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17* (A/35/17), para. 143 (Yearbook ... 1980, part one, II, A).

⁴Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17* (A/35/17), para. 143.

8. The session was attended by observers from the following United Nations organs: United Nations Industrial Development Organization and United Nations Institute for Training and Research.

9. The session was also attended by observers from the following international governmental and non-governmental organizations: Commission of European Communities, Hague Conference on Private International Law, International Federation of Consulting Engineers, International Progress Organization, Organization of American States, and World Bank.

10. The Working Group elected the following officers:

Chairman: Mr. Leif Sevón (Finland)

Rapporteur: Mr. Stephen K. Muchui (Kenya)

11. The Working Group had before it the report of the Secretary-General entitled "Draft legal guide on drawing up contracts for construction of industrial works: sample chapters" (A/CN.9/WG.V/WP.9 and Add. 1-5).^h

12. The Working Group adopted the following agenda:

- (a) Election of officers
- (b) Adoption of the agenda
- (c) Consideration of draft structure and sample draft chapters of the legal guide for drawing up contracts for the construction of industrial works
- (d) Other business
- (e) Adoption of the report.

I. Structure of the legal guide

13. The Working Group began its deliberations with a discussion of the draft outline of the structure of the guide (A/CN.9/WG.V/WP.9/Add.1). There was general agreement in the Working Group that the draft outline was acceptable on the whole. It was generally recognized that as the work progressed some rearrangement of the chapters might become necessary. The Working Group agreed to give the secretariat a discretion with respect to the arrangement of chapters taking into account the views expressed by delegations.

14. It was agreed that in the title of the Guide the term "international" should be used to describe the term "contracts". It was suggested that the title of the Guide should be "Legal guide on drawing up contracts for supply and construction of industrial works", instead of the one suggested in A/CN.9/WG.V/WP.9. There was agreement that the term "large" should not be used in connection with the term "industrial works".

15. There were several suggestions with regard to the method of presentation which would facilitate the use of the Guide. There was wide support for the proposal to include an index, summaries and check lists as

appropriate. It was pointed out that definition of certain terms would be needed in the Guide. There was general agreement that the Guide should include a glossary in accordance with the decision taken at the third session of the Working Group (A/CN.9/217, para. 59). There was support for the inclusion of model clauses, including alternative model clauses, whenever appropriate. Such clauses would assist parties in drafting.

16. It was suggested that the introduction be expanded to include the question of participation of banks and other lending agencies in projects. It was also suggested that some general issues relating to the applicable law might be mentioned in the introduction while the issues connected with the choice of the applicable law might be dealt with in chapter XXXIX as suggested in the draft outline of the structure.

17. It was suggested that certain important issues, such as legal aspects of feasibility studies, pre-contractual obligations of the parties, interest to be paid, the language of the contract, selection of persons to be trained, general conditions to be applied, keeping of books and records, and total and partial failure to perform, should not be omitted from the draft structure.

18. It was suggested that the issue of licence should be listed as a separate chapter in the outline of the structure of the Guide.

19. There were several suggestions relating to the order in which the chapters were to be presented. It was suggested to place chapter XXXIII (Liquidated damages and penalty clauses) after chapter XXXI (Damages). It was also suggested that chapter XXV (Transfer of property) be placed in another location in the Guide, and that chapter XXXIV (Hardship clauses) be placed immediately after chapter XXXII (Exemptions).

20. There was agreement to delete chapter XLI (Coming into force of contract) and to deal with the subject of this chapter in chapter V (Procedure for concluding contract).

21. In connection with the discussion of chapter IV (Invitation to tender and negotiation process) in the draft outline of the Structure, the Secretary of the Commission stated that this chapter would not be prepared until all other chapters of the Guide had been drafted. He noted that since contracts for the construction of industrial works were frequently concluded on the basis of public tenders, the drafting of procurement regulations would be a promising project for the Commission to undertake (see A/CN.9/WG.V/WP.7, para. 22). Work on such a project could usefully proceed concurrently with the preparation of the chapter of the Guide dealing with legal issues involved in tender procedures.

22. In connection with chapter III (Selection of contractors) the Secretary of the Commission noted that as already suggested at the last session (A/CN.9/217, para. 65), the Working Group might deal in future with legal issues concerning joint ventures and consortia

^hReproduced in this volume, part two, IV, B.

apart from questions of corporate law. The work of the Working Group in the field of industrial contracts, together with its possible work in the areas of procurement regulations and joint ventures, could usefully serve as a basis for the Commission to provide expertise on legal issues in the field of deep-sea mining, if it is called upon to do so by the forum in the United Nations dealing with this subject.

23. In connection with chapter XXII (Transfer of technology), the Secretary of the Commission noted that the secretariat had been keeping itself informed of developments in other organizations working in the field of transfer of technology and that this work would be adequately reflected in the preparation of the draft chapters of the Guide by the secretariat.

24. It was stressed that in preparing the Guide the secretariat should bear in mind the objectives of this undertaking in the context of the new international economic order. It should be of particular benefit to purchasers from developing countries. However, it was noted that the Guide would also be useful to parties from developed countries in negotiating and drafting industrial works contracts.

25. It was stressed that the introduction should clearly emphasize the guidelines to be followed and objectives to be attained in the formulation of the Guide. It was further stressed that the Guide should carry out the basic principles laid down by the General Assembly at its sixth special session on the establishment of a new international economic order and should be in accordance with the principles of equality, mutual benefit, equity and reasonableness. In addition, it was stressed that the objectives of the Legal Guide should be to support and assist developing countries in establishing and developing their independent national economies and to promote international economic co-operation.

26. Various views were expressed concerning the way in which the Guide should be drafted. One view suggested that the Guide should not be too voluminous. There was wide support for the idea that issues to be settled were complex, and the comprehensiveness of the Guide, rather than its length, should be the primary consideration. There was agreement that it would not be advisable to predetermine the length of the Guide. Preparation of a synopsis was also suggested.

27. It was agreed that the Guide should be drafted so as to be of practical value for various categories of persons involved in negotiating and drafting industrial works contracts, such as administrators and businessmen, as well as for lawyers.

28. While model clauses would be appropriate to be recommended for use in contracts in various situations it was pointed out that illustrative clauses might assist in the discussion of certain issues dealt with in some chapters. It was noted, however, that an industrial works contract must be adapted to specific situations and that illustrative clauses to be contained in the

Guide might not necessarily be appropriate for all contracts. The clauses should therefore be included merely to illustrate legal issues discussed in the Guide. It was suggested that the Guide should nevertheless include illustrative clauses whenever appropriate.

29. It was stressed that the Guide should as far as possible indicate the advantages and disadvantages of alternative approaches to the solution of issues dealt with in the Guide, with special reference to the interests of the purchaser.

II. Choice of contract types

30. The Working Group discussed the draft sample chapter on choice of contract types (A/CN.9/WG.V/ WP.9/Add.2).ⁱ

31. According to one view it was difficult in practice to distinguish among some types of works contracts discussed in this sample draft chapter, in particular, between the semi-turnkey contract and the partial turnkey contract. Another view suggested that the types of contracts discussed in the sample draft chapter were not defined in any legal system; according to this view it was preferable to distinguish among different negotiation approaches, rather than types of contracts. Accordingly, it was advisable firstly to distinguish between an approach involving separate contracts and an approach involving a single (turnkey) contract. Thereafter, possible variations in contractual arrangements involving a turnkey contract could be examined. In this connection one should refer to the possibility of a joint venture. In examining the different arrangements, attention should be paid to the functions of each type of arrangement.

32. According to another view, however, it was useful for the Guide to employ working definitions of various types of contracts in order to facilitate the presentation of issues which arose in connection with each type.

33. There was general agreement that the issue of transfer of technology was very important for purchasers from developing countries, and even for those from developed countries. Transfer of technology was important in order to enable purchasers to operate the works when they were completed, and to build similar works on their own. The Guide should assist purchasers in negotiating contracts appropriate to their needs in technology.

34. Views were exchanged with respect to the footnotes used in the draft sample chapter. One view suggested that footnotes should be eliminated or reduced in number; in particular, the footnotes referring to documents issued by other bodies should be eliminated. Another view was that the footnotes were sometimes useful (e.g. to indicate cross-references), and did not detract from the Guide.

ⁱReproduced in this volume, part two, IV, B.

35. The view was expressed that the Guide should be drafted from a functional and practical viewpoint, that is, it should focus on various interests, objectives and concerns of the purchaser (e.g. transfer of technology, scheduling and project management considerations, and the risks involved), and assist parties, and especially the purchaser, in the negotiation of a contract which accommodates these factors in the choice of a contractual arrangement appropriate to meet the needs of the purchaser.

36. The Working Group requested the secretariat to redraft this chapter in light of the views expressed.

III. Exemptions

37. The Working Group discussed the draft sample chapter on exemptions (A/CN.9/WG.V/WP.9/Add.3).^j There was general agreement that the chapter was on the whole acceptable.

38. The Working Group stressed the importance of drawing the attention of parties to rules of applicable law, particularly mandatory provisions which might restrict the freedom of the parties in the drafting of an exemption clause. It was suggested that some examples of mandatory rules of applicable law should be included in the chapter. However, it was pointed out that this might not be advisable as such rules might be changed after the publication of the Guide, and readers might not be aware of such changes.

39. It was agreed that the Guide should recommend a narrow scope of exemptions. It was noted that it would be useful to have illustrative or model clauses showing the various methods of drafting an exemption clause. Under one view, the exhaustive approach should not be recommended as it was too restrictive. According to another view, the exhaustive approach might have advantages in some cases and make clear that there was in reality more possibility for the contractor to apply exemption clauses. The view was expressed that the exempting impediment must be unforeseeable, unavoidable and irremediable.

40. It was observed that the advantages and disadvantages of the various approaches to exemption clauses should be set out.

41. It was pointed out that a cross-reference should be made to the chapter on insurance, as the extent of insurance cover taken out by a party would influence the extent of risks, as reflected in an exemption clause, which that party was prepared to undertake.

42. The view was expressed that an exemption clause should exempt a party not only from damages but also from liability under a liquidated damages or penalty clause, and from liability to perform the obligation which is prevented by the exemption. However, under

another view an exempting impediment should only exempt a party from liability to pay damages.

43. There was a suggestion that in addition to the legal effects mentioned in part E of the chapter, parties should be advised that an obligation to renegotiate the contract might be appropriate in certain circumstances.

44. It was suggested that the title of the chapter should be amended to read "Exempting impediments" rather than "Exemptions", as this title would reflect more clearly the content of the chapter.

45. There were suggestions on the contents and drafting of particular paragraphs of the chapter, which were noted by the secretariat, and were to be taken into account in finalizing the draft chapter.

IV. Hardship clauses

46. The Working Group discussed the draft chapter on hardship clauses (A/CN.9/WG.V/WP.9/Add.4).^k

47. The Working Group considered whether the Guide should contain a chapter on hardship clauses. According to one view, such a chapter should not be included, because such clauses usually benefited the contractor rather than the purchaser, who is normally from a developing country, creating inequality between the parties. Moreover, the notion of hardship is not established universally and is unknown in some legal systems. According to another view, the Guide should contain a chapter on hardship clauses in order to make the parties aware of the problems which such clauses create. After deliberation the Working Group agreed that a chapter on hardship clauses should be included, but the chapter should recommend that the definition of hardship circumstances be drafted narrowly. An exhaustive list of circumstances which should be considered as cases of hardship should be mentioned. While the Guide should indicate both the advantages and disadvantages of hardship clauses, it should strongly warn the parties about their dangers and substantial disadvantages, in particular for the purchaser. There was considerable support for the idea that the chapter should indicate that its inclusion in the Guide is not to be taken as an endorsement by the Commission of the desirability of hardship clauses.

48. It was suggested that the distinction between hardship clauses and exemption clauses should be further clarified, and that some illustrations should be given to demonstrate the two notions.

49. It was suggested that the chapter on hardship clauses should be combined with the chapter on price revision, as the two types of clauses were of a similar nature. Under another view, such a relocation was inappropriate because of the wider ambit of hardship clauses, that is, to re-establish the balance of contractual

^jReproduced in this volume, part two, IV, B.

^kReproduced in this volume, part two, IV, B.

obligations envisaged by the parties. It was suggested that currency clauses should be mentioned in that chapter. Reservations were expressed concerning the appropriateness of the word "hardship" to describe the subject matter of the chapter.

50. There were suggestions concerning the contents and drafting of particular paragraphs of the chapter, which were noted by the secretariat to be taken into account in finalizing the draft chapter.

V. Other business and future work

51. The Working Group noted that the secretariat had now acquired the expertise needed to carry out its new task in a complex area of work. The Working Group expressed its appreciation for the high quality of the work of the secretariat on the sample chapters submitted, which formed a useful basis for the discussions.

52. Concern was expressed that the work should not be delayed. There was general agreement in the Working Group that the Guide should be completed expeditiously. In this connection, the Secretary of the Commission made a statement in which he observed that, as forecast at an earlier stage in the deliberations of the Working Group, half of the available secretariat resources were already devoted to this project. Because of the experience gained in preparing the draft chapters currently before the Working Group, and because of the comments made by the Working Group at this session, the secretariat could to some extent accelerate

its work. However, because of the complexity of the work and the need to maintain a high standard, it would be realistic to predict that two to three years would be needed under present conditions for the completion of the project.

53. The Secretary of the Commission also noted that by January of 1984 the secretariat expected to produce sufficient draft chapters to justify the holding of a two week session of the Working Group. It would therefore be possible to hold the fifth session of the Working Group in New York at the end of January 1984. If this were done, the sixth session could be held towards the end of 1984 in Vienna. Such a course would also expedite the work. After deliberation, the Working Group decided that the date and length of the next session of the Working Group should be fixed by the Commission, as decisions to be taken by the Commission as to the agenda for its sixteenth session were relevant to these matters.

54. At the close of the session, the Working Group expressed its appreciation to its Chairman, Mr. Leif Sevón, for the able manner in which he had conducted the proceedings in this extremely complex field. This had enabled the Working Group to proceed with its work in an efficient and productive manner. It was noted that Finland would cease to be a member of the Commission as from the commencement of the sixteenth session of the Commission, and would accordingly also cease to be a member of the Working Group. The view was expressed that it would be highly desirable if means could be found for Mr. Sevón, despite this fact, to continue to associate himself with the work of the Working Group.

B. Report of the Secretary-General: draft legal guide on drawing up contracts for construction of industrial works: sample chapters^a (A/CN.9/WG.V/WP.9 and Add. 1-5)^b

[A/CN.9/WG.V/WP.9]^c

1. At its second session the UNCITRAL Working Group on the New International Economic Order decided to entrust the secretariat with the drafting of a legal guide on contracts for the supply and construction of large industrial works (hereinafter referred to as "works contracts") (A/CN.9/198, para. 92).^d The Commission at its fourteenth session approved this decision by the Working Group and authorized the secretariat to draft the legal guide, which should identify the legal issues involved in works contracts and

suggest possible solutions to assist parties, in particular from developing countries, in their negotiations.¹

2. After having completed at its second² and third³ sessions the consideration of a study submitted by the secretariat of clauses used in contracts for the supply and construction of large industrial works (A/CN.9/WG.V/WP.4 and Add. 1-8⁴ and A/CN.9/WG.V/WP.7 and Add. 1-6⁵), the Working Group suggested that at

^aYearbook ... 1982, part two, I, A.

^bYearbook ... 1981, part two, IV, B, 1.

^cYearbook ... 1982, part two, IV, B.

^dThe draft chapters prepared at the end of the period covered by the present volume are: chapter II: Choice of contract types (Add.2); chapter XXXII: Exemptions (Add.3); chapter XXXIV: Hardship clauses (Add.4); chapter XXXVIII: Termination (Add.5).

¹Referred to in Report, para. 90 (part one, A).

²13 April 1983.

³Yearbook ... 1981, part two, IV, A.

⁴Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth session, Supplement No. 17* (A/36/17, para. 84) (Yearbook ... 1981, part one, A).

⁵Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh session, Supplement No. 17* (A/37/17, para. 93) (Yearbook ... 1982, part one, A).

its fourth session the draft outline of the structure of the Guide and the approach to be adopted in its drafting should be discussed, and the secretariat was requested to prepare a few sample draft chapters and an outline of the structure of the guide and submit them to the Working Group (A/CN.9/217, paras. 132-133). This decision was approved by the Commission. The present document is submitted in compliance with that request.

3. The secretariat is submitting for consideration by the Working Group a draft and outline of the structure (A/CN.9/WG.V/WP.9/Add.1), and draft sample chapters on choice of contract types (A/CN.9/WG.V/WP.9/Add.2), exemptions (A/CN.9/WG.V/WP.9/Add.3), hardship (A/CN.9/WG.V/WP.9/Add.4) and termination (A/CN.9/WG.V/WP.9/Add.5).

4. In drafting these sample chapters the secretariat has taken into account a broad range of relevant documents, contract forms, books and articles. In addition, the secretariat has benefitted from the comments of the *Ad Hoc* Expert Group, which met at Vienna from 14 to 18 February 1983.

5. In the sample chapters reference has occasionally been made to the text of the United Nations Convention on Contract for the International Sale of Goods⁴. Such reference is made solely for the purpose of attaining consistency in approach, whenever appropriate, with the legal text emanating from the work of the Commission.

6. The sample chapters and the draft outline of the structure use the same terminology as that employed in the two studies by the secretariat on clauses related to contracts for the supply and construction of large industrial works (A/CN.9/WG.V/WP.4 and Add. 1-8 and A/CN.9/WG.V/WP.7 and Add. 1-6). It is proposed that in its final form the Guide will have an introduction which will explain the terminology used. It may be advisable to decide on some of the more special terminology at a later stage when considering the draft chapters in which such terminology occurs. The terms "purchaser" and "contractor" as well as the term "works contract" have been provisionally retained in the sample chapters and the draft outline of the structure. In the title of the Guide the term "contract for construction" has been used instead of "contract for supply and construction" and the term "large industrial works" has been replaced by "industrial works". The latter change has been made because the borderline between large and small industrial works may be vague, and the treatment of most issues will be the same regardless of the size of the works.

7. It is possible for certain parts of the Guide to include model clauses which may be recommended for use in certain circumstances. The secretariat, therefore, intends to provide such clauses, whenever appropriate, when the basic approach in these sample chapters is accepted by the Working Group.

[A/CN.9/WG.V/WP.9/Add.1]^a

DRAFT OUTLINE OF THE STRUCTURE

Paragraphs

Introduction 1-4
Draft outline of the structure

Introduction

1. The secretariat has been requested by the Working Group to submit a draft outline of the structure of the Legal Guide for consideration by the Working Group at its fourth session.^b The purpose of this outline is to enable the Working Group to decide on the overall contents of the Guide and its structure.

2. In the draft outline, the subject matters dealt with are grouped under two parts. Under part one are grouped subject matters relating to the preparation for contracting, including invitation to tender, negotiation and issues connected with the procedure for the conclusion of contracts. Under part two are grouped subject matters connected with the drawing up of works contracts. The chapters included in that part will indicate the issues that should be settled in works contracts, and suggest possible alternatives for their solution.

3. The order of the subject matters adopted in part two of the draft outline tries to follow, to the extent possible, that found in most work contracts. Furthermore, subject matters concerning the construction phase (chapters IX-XVII) are separated from subject matters concerning the post-construction phase (chapters XVIII-XXI). Subject matters which are common to both these phases are dealt with in chapters XXII-XLI.

4. The most appropriate structure of the Guide, and in particular the most appropriate arrangement of the chapters and their contents, may finally emerge only after an analysis of the issues relating to the various subject matters. The Working Group may, therefore, wish to consider the draft outline as provisional and to give the secretariat a discretion to modify the structure if the need arises.

DRAFT OUTLINE OF STRUCTURE OF LEGAL GUIDE ON DRAWING UP CONTRACTS FOR CONSTRUCTION OF INDUSTRIAL WORKS

Introduction

(Background, lack of experience of contract negotiating and drafting by purchasers from developing countries, context of NIEO-scope and purpose of legal guide, system of and definitions in legal guide, concluding remarks on using legal guide)

PART ONE

PREPARATION FOR CONTRACTING

- | | |
|------------|---|
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| | A. Purpose of feasibility studies |
| | B. Responsibility for errors in feasibility studies |

^a14 April 1983. Referred to in Report, para. 90 (part one, A).

^bA/CN.9/234, reproduced in this volume, part two, V, A.

^hYearbook ... 1980, part three, I, B (A/CONF. 97/18, annex I).

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	2. Principal elements characterizing nature of contracts to be chosen			2. Drawings and descriptive documents to be provided by contractor
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	(b) Co-ordination			4. Drawings and descriptive documents to be agreed by parties after conclusion of contract
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	[A/CN.9/WG.V/WP.9/Add.2] ^a				
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^a13 April 1983. Referred to in Report, para. 90 (part one, A).

A. Introduction

1. General remarks

1. The purchaser who wishes to construct industrial works may proceed in various ways. He may enter into several contracts dealing with various aspects of the project, such as contracts for design, civil engineering, sales contracts for the supply of equipment and materials, contracts for erection of the plant, consulting contracts and licensing contracts.¹ Alternatively, the purchaser may conclude works contracts, i.e. contracts of a more comprehensive nature, comprising many or all aspects of the construction such as design, delivery of equipment and materials, erection of plant, civil engineering, building construction and transfer of technology.

2. Where the purchaser chooses to use a works contract he may use a single contract in which only one contractor is responsible for all the necessary steps of the works construction. Alternatively, the responsibility for construction can be divided among various contractors under two or more works contracts, to which may be added one or more contracts of the types mentioned in paragraph 1, above. Co-operation by the purchaser and his participation in the construction is usually required under all types of works contracts. He is usually expected to provide a site for the construction, he often supplies the contractor with power and water needed for the construction and he is usually obligated to procure all permits and authorizations needed for the construction under the law of the place of construction.

3. A works contract can be expected to contain, as a basic minimum, two composite elements of varying degrees of value and importance, i.e. erection at the site (often involving the supply of materials), and supply of equipment, manufactured elsewhere prior to delivery and erection at the site. In some cases the manufacture contemplated may use relatively common technology, which is available from a number of competing sources and may even be designed by the purchaser's personnel or consultants. Where highly complex technology is to be used, there may be an element of specialization or exclusiveness involved, which may require a much higher degree of control over the construction by the contractor, balanced by an assumption on his part of considerable design and performance obligations if the purchaser is to receive proper protection of his interest. In addition, a contractor may assume post-completion obligations relating for example to the provision of spare parts, technical maintenance and repairs of works.

2. Principal elements characterizing nature of contract to be chosen

4. A purchaser contemplating a project for industrial works should, as a matter of broad principle, first make a

careful analysis of his own needs and of the project's various constituent parts with a view to determining the best contractual arrangements for three essential elements of the works contract: the design of the works, co-ordination of the construction process and the price.

(a) Design for plant and erection

5. One of the most important issues to be settled in connection with the choice of contract type relates to determining what contractual arrangements should be made for the design. On the one hand, a single contractor may be employed to design and construct the whole project, or a number of contractors employed under separate contracts, in which some or all of the contractors may be required to assume the responsibility for the design and suitability for the intended purpose of their own work or equipment. On the other hand, the purchaser may employ independent design professionals, or use his own technical employees, with the contractor or contractors being responsible only for performance in strict accordance with the purchaser's or his professionals' designs and specifications and not (in the absence of poor workmanship or materials) for the subsequent performance or suitability of the works or equipment after completion.

6. The contractual arrangements concerning the design are particularly relevant in connection with the allocation of the responsibility for the proper functioning of the works. Only in cases where the construction is to be executed by a single contractor on the basis of a design supplied by him is the responsibility not allocated between two or more contractors or suppliers. Even in cases where the plant is to be delivered and erected by a single person but under a design supplied by a different party it may be difficult for the purchaser to prove whether the designer or the contractor is liable for the failure of the works to operate (see paragraph 13, below).

7. In regard to some types of works, a class of design professionals may not be available to design the plant, and both the design and equipment will, as a commercial reality, have to be obtained from a contractor. Thus, the equipment for a power station or a hydro-electric dam, or the entire layout and equipment of a cement plant or sugar-mill or factory, is likely to be both designed and supplied by an experienced industrial manufacturer. In such a case the purchaser is compelled to rely on the contractor for the design of his product, and it will be of the essence of the contractor's responsibility that he will in such a situation (independently of any question of fault on his part) be responsible for the product's suitability for its required purpose. Even when such a contractor is employed, his design competence may not extend to some parts of the plant or equipment (e.g. lifts) and separate design professionals may be needed to design such parts of the plant or equipment.

8. In the field of erection, experienced design professionals may be available. Their skill might lie in evolving the best design to meet the limitations of a particular site and the special need of the purchaser. However, it may be noted that even if the erection is to be designed by a design professional, there may be other parts of the project which may be outside the expertise of such a professional and may need to be designed elsewhere. This erection design can either be provided by sub-consultant professionals working in collaboration with the principal design professional (where such a class of specialist sub-professionals exist, as, for example, in heating and ventilation) or else under separate contracts by contractors responsible for the design and performance of the equipment delivered by them.

¹The Guide does not deal with the contents of these various types (see introduction to the Guide). However, identification and settlement of some issues connected with these various types of contract may be found in the chapters of the Guide dealing with these issues in the context of works contracts. For negotiating and drafting these special types of contracts other guides and manuals elaborated by certain United Nations organs or specialized agencies can be used, such as *Manual on the Use of Consultants in Developing Countries* (United Nations publication, Sales No. 72.II.B.10), *Guide for Use in Drawing up Contracts Relating to the International Transfer of Know-how in the Engineering Industry* (United Nations publication, Sales No. 70.II.E.15), *Guide for Drawing up International Contracts on Consulting Engineering Including Some Related Aspects of Technical Assistance* (United Nations publication, Sales No. E.83.II.E.3) and *Licensing Guide for Developing Countries* (WIPO publication No. 620(E)).

(b) *Co-ordination*

9. Another issue to be settled is the arrangement to be made for the co-ordination of the various elements of the construction process, and determining who is to be responsible for such co-ordination. Co-ordination may be entrusted to one comprehensive contractor (with or without selected subcontractors or suppliers) or the project may be subdivided into separate contracts concluded by the purchaser, with the purchaser undertaking necessary co-ordination.

(c) *Price*

10. The purchaser, having determined the best arrangements for design and the co-ordination of responsibilities, should deal with the issue of the arrangements to be made for the price. The settlement adopted on the issues of design and co-ordination will strongly affect the pricing arrangements to be adopted (see paragraph 75, below). The amount of the price is influenced by the extent of risk to be borne by the contractor. The greater the risk that he must bear the higher the price will be, since the contractor must pay to insure against such risks or provide financial reserves to cover them. For these reasons the price for the same scope of construction is usually higher in the turnkey approach than in the semi-turnkey approach, and in the semi-turnkey approach than in the separate contracts approach.

B. Main types of works contracts

11. Various types of works contracts are used in international trade practice. The two most important methods of classifying them are on the basis of the allocation of responsibilities for the construction and on the pricing method used by the parties.

12. The main types or approaches to works contracts based on the allocation of responsibility are "separate contracts", "turnkey contracts" and "semi-turnkey contracts". Under separate contracts the construction obligations are allocated to two or more contractors and each of them is responsible only for supplies of equipment, materials and services entrusted to him under the terms of the contract. The design would usually be supplied by a design professional. The purchaser bears the principal responsibility for co-ordinating the contents and execution of the separate contracts (see paragraphs 18-27, below). Under a turnkey contract in principle a single contractor undertakes the responsibility for the entire construction of the works including the design and assumes the responsibility for co-ordinating all aspects of the construction process as to enable the works to be completed in time and to be able to operate in accordance with the contract (see paragraphs 28-40, below). Under semi-turnkey contracts the semi-turnkey contractor, although he does not undertake the entire construction, is responsible for putting the whole works into operation in the same way as a turnkey contractor. However, he can avoid liability for any failure of the works by proving that such a failure is due to a failure relating to the part of the construction not covered by the semi-turnkey contract. Such part may be entrusted to another contractor or undertaken by the purchaser himself (see paragraphs 49-53, below).

13. Some elements of both the separate contracts approach and turnkey contract approach may be found in a comprehensive works contract under which a single contractor undertakes to construct the whole works in accordance with a design supplied by another party. Under such a contract the co-ordination liability for construction is assumed by the contractor as in a turnkey contract, but in contrast thereto the responsibility for a failure of the works to operate is allocated

between the comprehensive contractor and the designer. If the works are incapable of operating as foreseen, it may be difficult for the purchaser to prove whether this failure has been caused by an error in the design or by a defect in the equipment or its installation (see paragraph 26, below).

14. The main types of works contracts classified on the basis of the pricing method used by the parties are "lump-sum contracts", "cost-reimbursable contracts" and "unit-price contracts". The term "lump-sum contracts" (or "fixed-price contracts") is usually used for contracts in which the agreed price is not subject to any price revision if there is an increase or decrease, after the contract is made, in the costs of construction (due to a change in the price of construction materials, or in the quantities of work to be done over the estimates made at the time of contracting), unless there is a price revision clause in the contract. Under "cost-reimbursable contracts" the contractor is entitled to be paid whatever the execution of the contract costs him, and in addition to claim a fee. Under "unit-price contracts" a determined price is to be paid for a defined unit of work and the price to be paid will vary with the quantities of work performed.

15. The denomination of various types of works contracts is, however, not uniform and different terminology is used in practice. In addition, only exceptionally is a single pricing method used in a contract, and in many contracts various pricing methods are combined, although one of them is usually dominant.

16. Choosing an appropriate type of works contract is a complex and difficult undertaking. The parties should, accordingly, consider the types of contract described below, and the allocation of responsibilities and the pricing methods that they involve. While parties are free to modify these types to meet their particular needs, care should be taken that such modifications do not create inconsistencies in the rights and obligations of the parties. Furthermore, if a certain type of contract is used, it may be advisable to settle certain issues (e.g. passing of risks, insurance, payment conditions) in a particular way. In any event, the contract should be very clear in the stipulation of the rights and obligations of the parties. If the parties expressly denominate a contract (e.g. "turnkey contract") but are unclear as to the stipulation of the rights and obligations of the parties, this denomination may be relevant in interpreting its effect.

17. The following is a brief description of the major types of works contracts classified above. Certain aspects of these types of contracts are dealt with in detail in other chapters of the Guide.

*1. Contract types classified by allocation of responsibilities**(a) Separate contracts approach*

18. Construction obligations may be allocated to two or more contractors on the basis of separate contracts concluded by the purchaser with them.² The purchaser may himself undertake part of the construction.

²The term "separate contracts" is now widely used. However, in contrast to the terms "turnkey contract" and "semi-turnkey contract", it gives no indication of the nature of the contractor's responsibility. In the typical form of the separate contracts approach considered in this section, the responsibility for construction is allocated among several contractors. The use of a partial turnkey contract (see paragraph 41) or a semi-turnkey contract (see paragraph 49), may also involve separate contracting, but in these cases the responsibility for construction rests mainly on the partial turnkey or semi-turnkey contractor.

19. Each of these contractors is responsible only for supplies of equipment, materials and services entrusted to him under the terms of the contract. The contract only requires that the equipment, materials or services to be supplied by each contractor conform with specifications in his contract; it does not impose a liability on the contractor if the purchaser fails to attain a construction target anticipated by the purchaser in using the equipment, materials or services. The purchaser will thus have to bear the financial consequences of a failure to achieve a construction target unless he proves that the failure was caused by a non-conformity of a contractor with his contractual obligations. Since the construction is divided among two or more contracts, the purchaser bears the principal responsibility of co-ordinating the contents and execution of these contracts in order to achieve the construction target.

20. The ways in which the works construction is to be divided among various contractors and the purchaser may depend in particular on the nature and size of the works and on financial considerations. Separate contracts are sometimes concluded for the supply and erection of various parts of equipment on the one hand, and for the building and civil engineering on the other hand.³ The erection of the equipment is, however, in many cases effected by the purchaser's personnel or by a local enterprise and the foreign contractor only supervises the erection.

21. Under the separate contracts approach, the design on the one hand, and construction and deliveries of equipment on the other, are often separated. The purchaser may employ a specialized design office or a consulting engineer or a construction manager to carry out the design, or it may be done by the purchaser's staff. The separate contracts approach may be advisable where different design sources have to be used for different parts of the project (see paragraphs 4-8, above). This approach may also be appropriate where no single principal contractor can be found having the expertise to undertake all parts of the project, or to supervise parts of the construction entrusted to subcontractors.

22. The main disadvantage of the separate contracts approach for the purchaser is that he assumes the risks connected with a failure to co-ordinate the construction of the works, such as a delay in the works construction as a whole (for example, postponement of erection of the equipment to be effected by one contractor due to a failure to complete building construction in time by another contractor), and a failure to achieve construction targets. If the works fail to operate, the purchaser must prove which contractor is responsible for the works' failure. Since there are complex and interrelated performances by several contractors, this may be extremely difficult.

23. If a failure to perform by one contractor has repercussions on the work of the others, the purchaser may be liable to pay damages for any resulting loss to the others provided that they have performed or were ready to perform their contractual obligations. The purchaser may, however, be entitled to penalties or liquidated damages or to be indemnified for these damages by the contractor who was responsible for the failure. The possibility of legal action against the contractor who has failed to perform his obligation to recover damages paid to other parties, may, however, be limited by the contract or the applicable law. Even when there is a special clause providing such a right to the purchaser, damages may be limited in the contract to an agreed sum and

this may result in the purchaser having to bear some portion of the damages which other contractors have recovered from him.⁴

24. Under the separate contracts approach, the purchaser usually retains control over the construction and has more flexibility in making changes in the scope and manner of the construction than when all construction obligations are integrated within a single contract and only one contractor bears responsibility for the work. In general, the smaller the size of the works the easier it is for the construction to be divided into a small number of separate contracts and for the purchaser to co-ordinate their contents and execution. The risks connected with co-ordination increase when a large number of contractors or other parties participate in the construction. In respect of major works or projects involving a complex technology the separate contracts approach should be used only if the purchaser has a well-established engineering department which is experienced in such co-ordination or if he can employ a reliable consulting engineer⁵ or other consultant for the purpose of co-ordinating and controlling the construction process.

25. The risks borne by the purchaser in connection with the co-ordination of the contents and execution of separate contracts may be reduced by employing a construction manager, sometimes called a managing contractor. The construction manager may be the designer of the works. Whether or not he is the designer his responsibility need not be limited to giving advice, but may include integrated construction management, i.e. planning, inviting tenders and negotiating separate contracts for the various sections of the works, concluding such contracts for and on behalf of the purchaser, co-ordination of all site activities and supervision of the construction. If the design is undertaken by other parties, the purchaser may wish to employ as construction manager a firm with design capabilities, and to give it the responsibility to check the design and to discover errors therein, and to specify the standard of testing which the firm has to exercise. The scope of the obligations of a construction manager is broader than that of a consulting engineer or a consultant; but it is more limited than that of a turnkey contractor (see paragraphs 28-29, below), since the construction manager concludes contracts with various contractors participating in the construction only for and on behalf of the purchaser. The construction manager may, however, be responsible under the contract for the appropriate selection of these contractors. A fixed fee is usually paid for the services of a construction manager, which is usually higher than the fee of a consulting engineer or consultant because of the broader scope of the construction manager's obligations. The parties may agree that the fee is to be reduced if the works are completed late or if the cost of the construction is higher than envisaged, and increased if the works are completed early or the cost is less than envisaged.⁶

26. Employing an independent professional for design has the advantage of enabling such a designer to supervise the works construction and to check whether the construction technique meets the design requirements and specifications. On the other hand, if the works are found to be incapable of operating as intended, it may be difficult for the purchaser to prove that this failure was due to an error in the design and not to a defect in the equipment or its erection, or vice versa. This risk of the purchaser may be reduced by stipulating in the contract that the contractor is obliged to inform the

⁴*Ibid.*, para. 14.

⁵See chapter "Consulting engineer".

⁶See chapter "Co-operation and liaison agents", section E "Construction manager".

³See *Guide on Drawing up Contracts for Large Industrial Works* (United Nations publication, Sales No. E.73.II.E.13), para. 4.

purchaser of evident errors in the design of equipment to be supplied by the contractor. A disadvantage of employing an independent professional for design is that he may be unable to achieve manufacturing and construction economies which a contractor undertaking both design and supply could achieve (see paragraph 35, below).

27. Purchasers from developing countries are generally interested in the employment of their nationals as contractors to the greatest extent possible. The purchaser may attempt to employ local contractors for the construction of some parts of the works under the technical direction and control of experienced foreign contractors employed for another part of the construction. This approach may save foreign exchange and transfer technical and managerial skills to local firms in the purchaser's country. The respective responsibilities of the local contractors and of the foreign contractor should be clearly stipulated in the contracts concluded by the purchaser in order to avoid disputes and difficulties later.

(b) *Turnkey contracts*

(i) *Pure turnkey contracts*

28. Under the pure form of a turnkey contract (sometimes called "total turnkey contract") a single contractor takes responsibility for the entire construction of the works, and his obligations normally cover the design, the supply of drawings and other documentation, the supply of equipment and materials to be incorporated in the works, civil engineering, building construction, transfer of technology, putting the works into operation and handing over to the purchaser the works capable of operation in accordance with the contract terms. In short, the contractor's responsibility covers the design and all other steps of the construction up to the "turning of the key" by the purchaser to start the operation of the works.⁷

29. Under pure turnkey contract terms all items of work needed for the completion and appropriate operation of the works in accordance with the contract, even if not expressly provided in the contract specifications of equipment or services, must be supplied by the contractor and are considered to be covered by the scope of the contract. If the turnkey contractor fails to perform his obligation to complete the works and put it into operation, he can avoid liability to pay damages only by proving that his failure was caused by a failure on the part of the purchaser to perform a contract obligation, or by exempting impediments.⁸

30. The integration of the works construction under a single turnkey contract means that there is only one contractor responsible for the completion and putting into operation of the works in accordance with the contract. In most cases, however, a turnkey contractor will be unable to supply all equipment, materials and services himself and will have to employ subcontractors. However, his liability will not be reduced by employing such subcontractors and he will be responsible not only for his own failure to perform but also for failures of his subcontractors.⁹

31. The contractor assumes *vis-à-vis* the purchaser the responsibility for co-ordinating all deliveries and work needed to complete the construction in time and without any defects, and he bears the consequences of any discrepancy between his responsibility arising from the turnkey contract and the

separate responsibilities he has placed on his subcontractors. Thus, with a turnkey contract the purchaser passes on to the contractor the duty to co-ordinate and the risks arising therefrom which are borne by the purchaser under the separate contracts approach.

32. Depending on the character of the works to be constructed either the owner of the technology or the main supplier is frequently selected as the turnkey contractor. Such persons usually have experience of works construction and the problems of co-ordination.

33. The main advantage of the pure turnkey contract approach is that, if the works fail to operate as stipulated in the contract, the purchaser will not be concerned to discover whether the failure is due to defective design on the one hand or defective equipment, installation or materials, on the other. In addition, in case of an inadequacy of the design the financial resources of a turnkey contractor available to meet the purchaser's claim will in many cases be greater than those of a professional designer.

34. The turnkey contract approach is advisable if the purchaser does not have the management resources needed to adopt successfully the separate contracts approach (see paragraphs 22-25, above). The turnkey contract approach may be useful in developing countries in the early stages of industrialization when local technological capabilities are limited and when it is therefore important to ensure that total responsibility for setting up the works and putting them into operation is entrusted to a contractor having the needed experience in the field involved. In particular, specialized high technology and manufacturing process projects may dictate the use of the turnkey approach, due to the absence of any available class of consultant to provide the essential design.

35. As a turnkey contract can be awarded after competitive bidding, the turnkey approach enables the purchaser to obtain the benefit of competition in respect of the project design which under the separate contracts approach is usually carried out by a design office or consultant or the purchaser's staff. The separate designer may tend to overdesign and his construction may become, therefore, more expensive. In addition, the design produced by a turnkey contractor is likely to reflect potential manufacturing or construction economies which are specifically known only to the turnkey contractor. Such a design can be arrived at taking full account of construction problems, and it should offer both saving in costs and speedier construction. The possibility of design economy may vary with the nature of the works to be constructed.

36. However, in addition to having to pay a high price to the contractor to compensate him for bearing the risks mentioned above, there are a number of other possible problems connected with the turnkey approach.

37. There can be little check on the reasonableness of the turnkey price as it is difficult to make any genuine assessment or comparison of prices between contractors where their designs differ. If, for example, a project is put to tender with the purchaser's outline requirements specified, the result may be a competition in under-design, with considerations of long-term life and quality, and simplicity of maintenance, sacrificed to offering an apparently attractive price. If a thorough checking of the turnkey contractor's design is attempted by employing independent professionals, the costs may substantially increase and the design economy of the turnkey contract approach may be lost. In addition, if the purchaser wishes to use the turnkey contract approach under competitive

⁷See UNIDO, "Features and issues in turnkey contracts in developing countries" (ID/WG.337/5), para. 7.

⁸See chapter "Exemptions".

⁹*Ibid.*

tendering procedures, the cost of tendering is increased since all contractors will have to engage design or consultant personnel to prepare and submit the competing designs, and the design costs of the unsuccessful tenders will, in the long term, need to be recoverable in the prices of their successful tenders.

38. By concluding a turnkey contract the purchaser places himself entirely in the hands of the turnkey contractor. Accordingly, an appropriate selection of the contractor is of vital importance for the purchaser, and he may often need professional advice on the technical qualifications and financial ability of the turnkey contractor under consideration.

39. The turnkey contractor may insist on the right to select subcontractors since he will be liable for their failures of performance (see paragraph 30, above). However, it should be noted that in some countries the supply of certain equipment, civil engineering or various services may be reserved for firms in these countries if the works are to be constructed there.

40. By placing the construction responsibility upon one contractor the purchaser loses, at least to some extent, control over detailed engineering, since the contractor usually wishes to be given authority to make decisions on the methods of construction. The purchaser faces the risk that the turnkey contractor, who is paid a lump sum, will be guided in his decisions on detailed design, selection of subcontractors and construction methods only by the desire to reduce his costs, and that he may not take into account factors such as the long-term life and reliability of the works which would guide a consulting engineer.

(ii) *Partial turnkey contracts*

41. The parties may limit the scope of the turnkey contract to the construction of the main technological process for which special knowledge is needed and exclude from it ancillary buildings (such as administrative buildings or other facilities) or even a technological unit not forming an integral part of the main technological process. This kind of turnkey contract is sometimes called a "partial turnkey contract" and is often used in cases when the turnkey contractor is a foreign enterprise and the ancillary buildings or technological units not forming an integral part of the main technological process can be constructed by local contractors. The separate contracts approach may be adopted for the parts of the construction excluded from the turnkey contract.

42. The partial turnkey contractor is responsible for the construction of the main technological process covered by his contract to the same extent that a pure turnkey contractor is responsible for the construction and putting into operation of the works as a whole. The distinction between the two types lies, therefore, in the scope of the respective contracts and not in the nature of the contractor's responsibility. In using a partial turnkey contract the purchaser must undertake some co-ordination, as when he uses the separate contracts approach (see paragraph 19, above), but only to a very limited extent. If he fails to co-ordinate the work, and, for example, construction under the partial turnkey contract is completed before the completion of the ancillary facilities, he may be obligated to bear unnecessary expenses in paying a bonus price for an earlier date of completion without being able to start the operation of the works at that earlier date. In principle, the partial turnkey contract has, in respect of the portion of the construction covered thereby, the same advantages and disadvantages as the pure turnkey contract has in respect of the entire works construction.

(iii) *Product-in-hand contracts*

43. The product-in-hand contract is usually considered to be a kind of turnkey contract. Its use in practice has been limited. Under the product-in-hand contract (the French term "*produit en main*" contract is often used in practice) the contractor has all the responsibilities of the turnkey contractor, but also has additional responsibilities after the stage of start-up of the works for a specified period of initial operation of the works.

44. The product-in-hand contract entails the widest responsibility of the turnkey contractor, since he must not only complete the works so that they are capable of producing products of the quality and quantity stipulated in the contract, but he must also enable the purchaser to operate the works and achieve the production targets with the purchaser's own staff. The contractor is obligated to direct production and management of the works during an agreed test period, and the final take-over of the works occurs only after the works have been successfully operated during such a test period with the purchaser's own staff and by using raw materials and other materials which the purchaser would use.

45. In the pure turnkey contract the contractor's responsibility does not extend to the successful functioning of the works after the test acceptance has been completed, and even if the contractor guarantees performance the guarantee is limited only to the curing of technical defects in the works arising during the guarantee period. The pure turnkey contractor does not guarantee the successful operation of the works by the purchaser's staff. This legal situation is basically the same even when the contractor is obligated to train the purchaser's staff, for, while he is liable to give appropriate training, he does not guarantee the acquisition of the knowledge needed to operate the works.

46. The purchaser's staff to be employed in operating the works must be trained and placed on the job under the product-in-hand contract by the contractor who is responsible for the results of his training. In addition to training, the contractor is responsible also for testing and placement of the purchaser's staff within the works, and organization of their activities, and for continuous on-the-job training according to the agreed schedules. The product-in-hand contract, therefore, requires some transfer to the purchaser of management skills needed for the operation of the works.

47. In the product-in-hand contract the purchaser is protected to the maximum possible extent, since all the risks of the failure of the works to operate successfully during the agreed period of time are borne by the contractor. If the works' output target is not achieved the contractor is relieved from liability to pay damages only by proving that the failure was due to exempting impediments.¹⁰ The price in a product-in-hand contract may, therefore, be considerably higher than in a pure turnkey contract.

48. In general, the product-in-hand contract has all the advantages and disadvantages of the pure turnkey contract. In addition, the purchaser is assured of being able to operate the works himself. On the other hand, the ability of the purchaser to select personnel for the works may be limited as the contractor may insist on his own choice of suitable persons to be trained.

(c) *Semi-turnkey contracts*

49. In practice a type of contract (sometimes called "semi-turnkey contract") is used which can be considered an

¹⁰*Ibid.*

intermediate step between the separate contracts approach and a turnkey contract. Under this approach, the purchaser concludes a contract with a supplier of design, equipment, materials, technology and services (the semi-turnkey contractor) for the major part of such supplies needed for the works construction, and separate contracts with other parties for supplying the equipment, materials or services not included in the semi-turnkey contract. Like the turnkey contractor, the semi-turnkey contractor is responsible for putting the whole works into operation and handing over to the purchaser the works capable of operation in accordance with the contract terms. The semi-turnkey contractor can, however, avoid liability for any failure of the works by proving that such failure is due to failure to perform the separate contracts relating to that part of the construction excluded from the scope of the semi-turnkey contract.¹¹

50. This approach may be useful in cases where the functioning of the part of the technological system to be excluded from the scope of the works contract with the main contractor is closely linked with the functioning of the rest of the system to be constructed by the main contractor (for example, the semi-turnkey contractor to supply and erect a power station, and the other contractors to supply the valves and tubing for the power station). Since the design of the works would be the responsibility of the semi-turnkey contractor he would be obligated to inform the purchaser of the specifications of the equipment, materials or services to be supplied under the separate contracts. A purchaser who wishes to obtain still greater security may obligate the semi-turnkey contractor to check that the performance of the separate contractors is in accordance with specifications or with a time schedule provided by the semi-turnkey contractor.

51. Like the partial turnkey contractor, the semi-turnkey contractor undertakes only part of the construction. However, while the partial turnkey contractor only assumes responsibility for the part of the construction which he undertakes, the semi-turnkey contractor assumes responsibility for the whole construction, subject to his power to avoid liability in the circumstances noted (see paragraph 49, above). In respect of the part of the construction which he undertakes the partial turnkey contractor is solely responsible and cannot place responsibility on other contractors (see paragraph 41, above).

52. The semi-turnkey contract may in some cases offer advantages over both the turnkey contract approach and separate contracts approach. Where the purchaser uses the separate contracts approach, and a failure of the works occurs, he may have difficulty in establishing which contractor's default caused the failure. Under the semi-turnkey approach, the purchaser will in the first instance hold the semi-turnkey contractor responsible for all failures of the works; if the semi-turnkey contractor avoids liability in the manner indicated above, the purchaser will have the evidence which may be used to establish the responsibility of one or more of the separate contractors.

53. Another advantage for the purchaser in a semi-turnkey contract over the separate contracts approach is that the design of the works and supplies of main equipment are usually integrated in one person which could result in manufacturing and construction economies. Further advantages are that the purchaser maintains complete freedom to select suppliers of parts not covered by the semi-turnkey contract, and that the responsibility for co-ordination imposed on the purchaser is of a limited extent (cf. paragraph 19, above). The main

advantage for the semi-turnkey contractor is that, while he is responsible for construction and for putting the works into operation, his responsibility (in comparison with the pure turnkey contractor) is limited by his ability to prove that the failure of the works to achieve performance objectives was due to defects in parts of the works not covered by the semi-turnkey contract.

2. Contract types classified by pricing method

(a) Lump-sum contracts

54. A lump-sum contract is a contract whereby the contractor agrees for a price fixed in a lump sum to perform the obligation set forth in the contract, which may sometimes consist of the entire construction of the works. The term lump-sum contract is also used where the various obligations to be performed are divided in the contract and a separate sum is fixed as the price for each set of obligations. The lump sum is the aggregate of the separate sums.¹² Sometimes the term "fixed-price contract" is used for this kind of contract.

55. In a lump-sum contract the contractor takes the risk of being able to perform for the specified amount and he cannot obtain any price revision if there is an increase in the costs of performance after the conclusion of the contract unless there is a price revision clause in the contract.

56. The contractor may, however, be entitled under the contract or applicable law to an equitable adjustment of the price in the event that his costs are increased by changes required by the purchaser after the conclusion of the contract or by a necessary modification needed to the scope of the work, provided the contractor is not responsible for the circumstances making the modification necessary.¹³ The precise extent of work which the contractor must do for the lump sum should be defined in the contract.

57. The lump-sum or fixed-price method is often used in pure turnkey contracts, but it may also be used in other types of contracts (i.e. separate contracts or semi-turnkey contracts), in particular in fixing the price for the supply of equipment and materials, the granting of licences and know-how, civil engineering, procurement services and inspection services.¹⁴

58. The contractor's profit, if any, is realized by the difference between the fixed price agreed upon in the contract and the cost of construction incurred by him. In calculating the fixed price the contractor usually includes an amount additional to estimated costs and profits in order to cover the risk of an increase in costs.

59. As the fixed price is, in general, to remain firm even if the performance entails more costs for the contractor than he anticipated at the time he concluded the contract, the fixed price method is usually provided in cases where significant changes in the scope of the works are not envisaged.

(b) Cost-reimbursable contracts

60. Cost-reimbursable contracts are sometimes also described as cost contracts, cost-plus contracts, prime-cost

¹²For this approach see "UNIDO model form of turnkey lump-sum contract for the construction of a fertilizer plant" (UNIDO/PC. 25), art. 20.

¹³See chapter on "Scope and quality of works".

¹⁴Under the "UNIDO model form of cost-reimbursable contract for the construction of a fertilizer plant" (UNIDO/PC. 26), art. 20, a fixed price is to be stipulated for licences and know-how, procurement, inspection and expediting services and for providing training and training facilities.

¹¹See "First draft of the UNIDO model form of the semi-turnkey contract for the construction of a fertilizer plant" (ID/WG. 318/2), art. 4.1.

contracts or fee contracts. In a cost-reimbursable contract, the price is not a fixed amount, but rather the actual cost of executing the contract incurred by the contractor. The contractor is obliged to perform his obligation efficiently and economically, but subject to these conditions he is entitled to be paid whatever the execution of the contract costs him. In addition he is entitled to claim an additional payment (usually denominated as "fee") to cover his overheads and to bring him a profit. The fee may be agreed upon in the form of a fixed amount, but it is sometimes determined as a percentage of the costs incurred in performing the contract (the so called "cost-plus-percentage-cost-contract").

61. The main disadvantages of a cost-reimbursement pricing method are that the incentives to economy or speed of construction are greatly reduced. While the contractor is obliged to work efficiently and economically and not to waste resources or expenditure, in practice it is difficult to enforce this obligation. Furthermore, the contract must be carefully drafted to define what costs are reimbursable and what the payment arrangements are for subcontractors or suppliers.¹⁵ In addition, if the purchaser is to be properly protected, a cost-reimbursable contract requires detailed day-to-day supervision in checking the contractor's claims for payment, and supervisory services may be expensive. Cost-reimbursable contracts are therefore advisable only for purchasers who have some experience in the industry involved and who can check the appropriateness of the contractor's price claims at a reasonable cost.

62. Cost-reimbursable contracts may sometimes be used when the extent of work needed for the construction of the works cannot be accurately determined in advance, or where the major part of the construction is to be done by subcontractors and their charges are unknown at the time of conclusion of the contract. Since the total amount of the cost of the works is not determined at the conclusion of the contract, the purchaser will have to exercise control over expenditures during construction.

63. The uncertainty of the purchaser as to the total amount payable inherent in the reimbursable price method may be mitigated by the parties agreeing on an estimated cost. However, the effect of such an estimate should be clearly specified. The contractor might guarantee the estimate in which case he may be precluded under the contract from claiming any higher price. Alternatively, he may be entitled to claim only a percentage of the excess over the estimated cost. Where such limitations are imposed an increment is usually included in fixing the fee to be paid to him in order to cover the risks connected with the increase of costs.¹⁶

64. The purchaser may find it advantageous to agree upon a method of determining the fee which gives an incentive to the contractor to reduce construction costs. In some works contracts (often called "incentive contracts") a target cost of construction is fixed, and the contractor shares in any saving below such cost.¹⁷ On the other hand, it is not advisable to determine the fee by a percentage of the costs incurred by the contractor performing the contract, since he may be interested in increasing the cost of construction in order to obtain a higher fee. Since under a cost-reimbursable contract the purchaser pays the actual costs incurred by the contractor for the equipment, materials and services used in the construction, the purchaser usually has the right to select or approve suppliers or subcontractors. It is therefore possible for him to

choose the optimum design and specifications for equipment and materials, and subcontractors offering the most competitive prices.

(c) Unit-price contracts

65. Under unit-price contracts (also called "remeasurement contracts"), the work to be done shown in the drawings and specifications is divided into recognizable work processes, capable of being individually priced. A unit price is then fixed for each work process (for example, per cubic meter of dredging, per cubic meter of reinforced concrete, per hour of work of electrical technician). It would be possible to make an estimate of the quantities of work to be done on the basis of the drawings and specifications, and, accordingly, on the basis of the rates quoted for the various units, an approximate price for the construction can be determined. However, a price for the construction as a whole is not specified in the contract, and the final price payable is dependent on the final measurement of quantities of work done or materials used in the construction and the number of hours spent by the contractor's personnel in constructing the works.

66. This type of contract is advisable if the quantities of work to be done or materials to be used cannot be determined accurately in advance (for example, the quantities of work requiring removal when the foundations are excavated cannot be determined in advance). The risks connected with pricing are divided between the contractor and the purchaser. Since the price per work unit is firm¹⁸ the contractor bears the risk of increases in costs of materials and labour. The purchaser assumes the risk of an increase of price due to an increase in quantities of work or materials or amount of labour needed for the completion of the works over the estimate at the time of concluding the contract.

67. When entering into a unit-price contract, therefore, a purchaser should ensure that his estimate of quantities of work to be done is reasonably accurate, as otherwise he may be faced with a high degree of uncertainty as to the price payable. Furthermore, as the price payable depends on measurement of units of work done, parties should agree on clear rules as to how particular units are to be measured, or quantities ascertained. The purchaser will also incur some expenses in employing professionals to check the quantities of work done and their measurement.

68. While in a lump-sum contract a contractor will need to include a contingent element in the price to cover possible underestimates of the work to be done or the quantities of material needed, the unit-price method may eliminate this need. Accordingly, the price for the same quantity of work or material may be less in a unit-price contract than in a lump-sum contract. A unit-price contract will also be advantageous to a purchaser if there is a real possibility that the work to be done will turn out to be less than the estimated quantity of work.

C. Other factors to be taken into account in choosing contract type

69. In addition to the factors relating to design, co-ordination, allocation of responsibilities and price, the purchaser may also wish to consider the following factors.

¹⁵See chapter "Price".

¹⁶*Ibid.*

¹⁷See UNIDO, "Features and issues ...", para. 30.

¹⁸Contract clauses are, however, sometimes used under which the price per work unit may be varied if the quantities of work done differ significantly upon final measurement from the estimated quantities of work.

1. Taxation

70. Parties should take into account the impact of tax liability on different types of contracts. Under some tax legislations the profit relating to a turnkey contract may be taxed at a higher rate than in the case of separate contracts. Under other legislations a turnkey contract may be considered as a sale of works, and the turnkey price taxed accordingly.¹⁹

2. Selection of subcontractors

71. The purchaser may wish to select or to at least have an influence on the selection of subcontractors employed for the works construction. In developing countries it may be advisable to employ local enterprises in order to develop their technological capabilities and to conserve foreign exchange. However, a turnkey contractor may insist on choosing his own subcontractors since this contractor will be responsible for the subcontractors. A contractor under a lump-sum contract may also insist on selecting subcontractors in order to be able to control the cost of subcontracting so that he can make a profit within the fixed amount agreed upon in the contract.

3. Transfer of technology

72. In developing countries, works contracts are frequently intended to be a means of acquiring not only the physical works themselves but also technology. This transfer of technology always includes a transfer of information needed to use and operate the works. However, it often has a wider scope, covering technical and other knowledge, training and rights relating to patents, trademarks, design, copyrights and know-how. The scope of transfer of technology may depend on detailed contractual terms agreed upon by the parties, but can also be influenced by the contract type chosen by the parties. The minimum extent of the transfer of technology is mainly dependent upon the degree of the contractor's responsibility to ensure the operation of the works; the transfer of technology is broader in a turnkey contract than in a semi-turnkey contract, and it is most limited under separate contracting. On the other hand, under separate contracting, in participating in the construction the purchaser's personnel may acquire some experience and skill, in particular at handling the equipment.

73. There may be other aspects to be taken into consideration in selecting the contract type, such as the degree of the technical complexity of the construction processes to be used, the size of the works, performance specifications, the need for flexibility in changing the scope of the works (see paragraph 24, above), and requirements of a bank or organization financing construction.

D. Combination of contract types

74. In works contracts a combination of pricing methods for various suppliers is frequently used. In such cases the contract is denominated in accordance with the pricing method which is dominant. On the other hand, it is very difficult to combine the various contract types characterized by the allocation of parties' responsibilities.

75. The parties may theoretically agree on various pricing methods in any type of contract characterized by the allocation of responsibility.²⁰ In practice, however, the turnkey contract is usually combined with a lump-sum price.²¹ The use

of the cost reimbursable pricing method may cause some difficulties in the types of contracts in which the contractor is responsible for achieving an agreed production capacity of the works, particularly in the turnkey contract. The application of the cost reimbursable method of pricing presupposes basically the purchaser's right to approve the subcontractors chosen by the contractor or at least to approve the prices required by such subcontractors, thus permitting the purchaser to select them indirectly. However, the contractor may hesitate to assume total responsibility for the production capacity of the works without having the right to select his subcontractors. The unit-price method cannot be adopted as the main pricing method in a turnkey contract for a number of reasons. The nature of the work to be done does not lend itself to division into well recognized pricing units of a repetitive character. Furthermore, in regard to highly specialized manufacturing processes used in the contractor's own factories which will often be a major part of the project, it will be very difficult for the purchaser's personnel to verify or fix costs. The latter difficulty may also arise if the cost reimbursable pricing method applies.

76. What has been said in the previous paragraph in respect of the turnkey contract equally applies to the semi-turnkey contract. Under the separate contracts approach any pricing method can be used, although in particular circumstances one method may be more advantageous than others.²²

²²See chapter on "Price".

[A/CN.9/WG.V/WP.9/Add.3]^a

CHAPTER XXXII. EXEMPTIONS¹

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^a8 April 1983. Referred to in Report, para. 90 (part one, A).

¹This term is also used in article 79 of the United Nations Convention on Contracts for the International Sale of Goods (A/CONF. 97/18, annex I) (Yearbook ... 1980, part three, I, B).

¹⁹See chapter on "Customs duties and taxes".

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A. General remarks

1. Impediments may occur which prevent the performance by a party of his contractual obligations. These impediments may be of a physical nature such as a natural disaster, or they may be of a legal nature (for example, after the conclusion of the contract the law on environment protection in the purchaser's country is amended to prevent the use of the equipment specified in the contract). The impediments may prevent performance permanently or for a limited period, or they may prevent performance on time.

2. This chapter deals with the question of what impediments can exempt a party from liability to compensate the other party for loss suffered by the failure to perform an obligation. Other issues which parties should deal with are considered in other chapters. For instance, a change which may be required in the scope of construction together with a consequent change in the price, is dealt with in the chapter "Changes in scope and quality of works". Modifications which may be required of other contractual terms are dealt with in the chapter "Variation". The issue of who is to pay the costs incurred in a reconstruction of plant damaged as a result of such impediments is dealt with in the chapter "Passing of risks". The effects of exemptions on a penalty or liquidated damages clause are discussed in the chapter "Liquidated damages and penalty clauses". The chapter "Suspension" discusses the situations when an exempting impediment causing a delay justifies the suspension of a contract and the legal effects of such suspension. If the impediments are permanent or of a long-term nature and cannot be overcome by a modification of the scope of the contract or variation of its terms, it may become necessary to terminate the contract. This issue is discussed in the chapter "Termination of contract".

3. The grounds for exemption should be settled by the parties after taking into account the nature of a works contract. Performance of a works contract extends over a long period of time, and the contract is generally of a comprehensive and complex nature. Accordingly, clauses intended to be applied to various types of contracts may not always be appropriate. Parties may in addition wish to note that giving a wide scope to an exemption clause creates uncertainty as to the obligations imposed under the contract, as parties are excused from performance in a wide range of circumstances. Furthermore, the effect of the operation of an exemption is to place the loss caused by the exempted failure of performance on the party not invoking the exemption, thereby creating an exception to the normal rule that a party who fails to perform must bear the loss caused by such failure. Considering the heavy losses which may be caused by a failure of performance in a works contract, it may be desirable to limit the scope of the exemption clause. Additionally, a narrow scope of exemption may encourage careful planning by the parties to avoid failures of performance which may be costly to both of them. It is recommended that, as a minimum, a party should only be exempted if an impediment is of a physical or legal nature that prevents the performance by him of an obligation, and that such party could not by reasonable efforts overcome or avoid the impediment or its consequences. However,

circumstances which only make the performance more onerous or cause economic hardship, should not be treated as exempting.² The scope of exemption has, however, ultimately to be determined in the light of the special circumstances attending the contract in question, and such circumstances may require a narrower or wider scope of exemption than that indicated above. Because of the nature of the performances to be executed by the parties it is evident that in most cases exempting impediments would prevent performance by the contractor. A wide definition of exempting impediments may therefore increase the purchaser's risk of loss.

4. Both parties should be able to invoke the exemption clause as in some situations the purchaser may also need to be exempt from failure to perform some of his obligations (for example, to provide the site in time or to supply water or power needed for construction).

B. Exemption clause and applicable law

5. The parties may find it advisable to include in their contract clauses which define the conditions under which the parties are exempt from liability to pay damages for loss caused by either party's failure to perform his obligation. Alternatively, they may wish to leave the issue of liability for damages to be settled under the rules of the applicable law. However, institutions financing the construction of industrial works frequently insist on such a clause in the contract as it is of great importance for determining the risks connected with financing the construction.

6. If parties do wish to refer the issue of exemptions solely to the applicable law, it would be advisable to provide expressly for this in their contract. In deciding whether the settlement of the issue by the applicable law is preferable, parties should examine the relevant rules of that law to determine whether they are appropriate to settle the special problems that may arise when performance of a works contract is prevented, or whether the rules need to be supplemented or modified by exemption clauses in the contract.

7. Where parties desire both the rules of the applicable law and the exemption clauses in the contract to regulate the issue of exemptions, the contract should clearly so provide. In most cases, however, it is not advisable to permit the contract to be regulated both by exempting impediments on the basis of the applicable law and also by the exemption clauses, as the combination of the two approaches to a situation may be inconsistent and may unduly widen the scope of exemptions.

8. At the same time, where parties wish to settle the issue of exemptions by express provisions in their contract, they should carefully consider the extent to which the mandatory rules of the applicable law would limit their power to do so. In drafting an exemption clause, parties may use the terminology of the applicable law, provided that they do not intend to modify the meaning given to that terminology under that law. Otherwise, terminology (such as force majeure, frustration, fault or recklessness) which may have a special meaning in some legal systems should be avoided.

C. Methods of drafting

9. In drafting an exemption provision, parties may adopt one of the following approaches:

- (i) Providing a general definition of exempting impediments;

²See chapter "Hardship clauses".

- (ii) Combining a general definition with a list of impediments;
- (iii) Providing a list of exempting impediments. The list may be exhaustive or non-exhaustive.

and may also wish to consider the following issues:

- (iv) Exclusion of certain impediments from the scope of exemption;
- (v) The scope of exemption when failure of performance is caused by a third person employed by a party.

1. General definition of exempting impediments

10. Parties frequently include in the contract a definition qualifying the impediments in general terms. Such a definition avoids the danger of overlooking some impediments which parties might have considered as exempting (see paragraph 24, below) and problems of interpretation resulting from the mere listing of exempting impediments without the necessary criteria determining when the impediments are exempting (see paragraphs 22-29, below). On the other hand such a general definition, if not followed by an illustrative list (see paragraph 18, below), may sometimes give rise to difficulties in determining whether or not a particular impediment is covered by the definition. Parties should consider the inclusion of the following elements in a general definition.

(a) *That the physical or legal impediment must unavoidably prevent performance*

11. This element embraces two interrelated requirements. As a first requirement, parties may wish to stipulate that the physical or legal impediment must, permanently or temporarily, prevent performance of an obligation, and not, for instance, only make performance inconvenient or more expensive. As a second requirement parties may wish to stipulate that an impediment would exempt a party only if it were beyond his control. In addition, to determine whether performance is prevented by an impediment it will be relevant to consider what measures might have been taken to overcome or avoid the impediment or its consequences. Therefore the exemption clause should stipulate the standard of conduct a party would be expected to observe for this purpose. As regards the standard to be expected, it would unduly restrict the scope of the exemption to require that a party is exempt only if he proves that the impediment or its consequences could not have been overcome or avoided by the taking of every conceivable measure. On the other hand, not to require the party to take measures to overcome or avoid it or its consequences, may encourage a party to seek to rely on impediments to evade performance of his obligations. However, it would not be advisable to require a party to take measures which promise only a very slight chance of success with a high degree of risk (for example, to run a military blockade). Accordingly, it may be advisable to stipulate that a party is exempted only if he proves that a physical or legal impediment or its consequences prevented his performance and that he could not reasonably have been expected to overcome or avoid it or its consequences.³

³This approach is based to some extent on article 79 (1) of the United Nations Convention on Contracts for the International Sale of Goods (A/CONF. 89/13, annex I) (Yearbook ... 1978, part three, I, B) which reads as follows:

"(1) A party is not liable for a failure to perform any of his obligations if he proves that the failure was due to an impediment beyond his control and that he could not reasonably be expected to have taken the impediment into account at the time of the conclusion of the contract or to have avoided or overcome it or its consequences."

12. It may not be desirable to stipulate that the impediment could not have been reasonably avoided by both parties. The party invoking an impediment should be exempted even if the impediment could be averted by the other party.

13. It is suggested that inclusion of this requirement (i.e. that the impediment must unavoidably prevent performance) is necessary if a general definition is to be acceptable. However, parties may also wish to consider the additional elements set out below.

(b) *That the impediment was unforeseeable*

14. Parties may wish to provide as a necessary condition for the exemption of a party that he could not reasonably foresee an impediment at the time of the conclusion of the contract. A party may, however, foresee an impediment but not its effects on the performance of his obligation. Parties may therefore wish to provide that a party is exempted if he could not reasonably be expected to take into account at the time of the conclusion of the contract the effect of an impediment upon his ability to perform.

(c) *That the impediments must intervene after conclusion of the contract*

15. Parties may wish further to narrow the scope of the exemption clause by providing that only impediments intervening after the conclusion of the contract are to have an exempting effect. This approach may be justified on the ground that impediments existing at the time of the conclusion of a contract should be known to a party and taken into account by him when entering into a contract. This element may be combined with element (a) noted above (i.e. a party is exempted if impediments beyond his control intervening after the conclusion of the contract unavoidably prevent performance) or with elements (a) and (b) (i.e. a party is exempted if impediments intervene after the conclusion of the contract and are unavoidable and unforeseeable).

(d) *That the impediment must be of an extraordinary nature*

16. Parties may wish to stipulate that the impediments must be of an extraordinary nature if they are to be exempting. If they so stipulate, impediments which normally occur (for example, the normal freezing of rivers in winter) would not exempt. This element may be combined with element (a) or element (c) noted above. Since in most cases an extraordinary impediment will not be reasonably foreseeable, it is usually used only as a substitute for, but not in combination with, element (b) noted above. However, there may be some cases where an impediment could not reasonably be foreseen at the time of the conclusion of the contract by a party in the same position as the failing party, but where the impediment could not be considered as extraordinary. Accordingly, the inclusion of the element that the impediment must be of an extraordinary nature may narrow the scope of the exemption.

2. Definition followed by a list of exempting impediments

17. A general definition of exempting impediments followed by a list of exempting impediments could combine flexibility with certainty. The following approaches may be considered by the parties.

(a) *Definition followed by an illustrative list*

18. Under this approach, a general definition is followed by a list of impediments which, if they satisfy the conditions in

the general definition, would have an exemptive effect. Care should be taken to indicate that the list of impediments is not exhaustive. Parties should include in the list impediments which they clearly desire should have an exemptive effect, but which might possibly be regarded as falling outside the general definition. The examples might also be chosen so as to clarify the scope of the general definition.

(b) *Definition followed by an exhaustive list*

19. Parties may prefer an exemption clause in which the list of impediments, however wide or narrow, is exhaustive. The listed impediments must satisfy the elements set out in the general definition to have an exemptive effect. Under this approach, impediments which are not in the list, even though they may fall within the scope of the general definition, do not exempt. Accordingly, parties should use this approach only if they are certain that they can foresee and list all the impediments which they wish to be exempting.

(c) *Definition followed by an additional list of exempting impediments outside the scope of the definition*

20. Under this approach, parties may lay down a general definition of exempting impediments, and in addition include a list of specific impediments which are exempting whether or not they fall within the definition given. For example, the definition may include the element of unforeseeability, but the specific impediments in the list would be exempting, whether they were foreseeable or not. As these impediments have an independent exempting effect, the observations made in paragraph 22 would equally apply here.

21. This approach may be useful where parties have chosen a narrow general definition but may wish, nonetheless, that certain impediments which do not fall within the scope of the definition that they have adopted should be exempting.

3. *List of impediments: non-exhaustive or exhaustive*

22. Some exemption clauses in practice simply provide a list of impediments either non-exhaustive or exhaustive, without any general definition. These clauses often do not provide any set of criteria to determine when the impediments are exempting, which is unsatisfactory. If, however, the parties do not wish to have a general definition but only a list of exempting impediments, they must decide whether the list is to be non-exhaustive or exhaustive. In preparing the list (whether non-exhaustive or exhaustive) care should be taken to set out the criteria and qualifications under which a particular impediment would be considered exempting, since there is no general definition which can be resorted to. It is not sufficient simply to include "war" or "military activity" within a particular list; parties should go further and state that the war or military activity is such as prevents the performance of the obligations (see paragraph 27, below). As another example, the mere mention of "explosions" as an exempting impediment would raise questions such as whether an explosion would exempt a party even if it were caused by the negligence of that party, and what effect the explosion must have on the performance due from that party before it would have an exempting effect.

23. A non-exhaustive list is intended to provide some examples of exempting impediments. If the parties have agreed that the issue of exemption would not be governed by the applicable law, there may be difficulty in determining what impediments other than those listed are exempting. The list itself may provide no guidance as to what impediments

other than those listed the parties intended to be exempting. If, in addition to the list the applicable law regulates the issue of exemptions, that law will determine what impediments other than those listed will exempt.

24. An exhaustive list of impediments may be unsatisfactory because parties may overlook certain impediments which they intend to have an exemptive effect. As the list is exhaustive, the applicable law, except its mandatory rules, is excluded and cannot remedy such an oversight.

25. Natural disasters (such as earthquakes, floods, cyclones, sandstorms) are often listed as exempting impediments. If the parties decide to include such impediments in the list, the contract should provide that the party failing to perform is exempted only to the extent to which and during the time when the consequences of such a natural disaster prevent him from performing, and only if such consequences thereof cannot be avoided or overcome. Storms, cyclones, floods or sandstorms may in fact be the normal weather conditions at a particular time of the year at the place where the construction is carried out and should be taken into consideration by the contractor in agreeing to a time-schedule for the construction and they should not exempt the contractor if their consequences can be avoided or overcome by him.

26. Unexpected site conditions may render the contract physically impossible of performance in accordance with the contract. They may arise from latent physical conditions differing materially from those indicated in the contract, in the feasibility study or from those ordinarily encountered. The contractor should not be exempted if such conditions could have been discovered or foreseen by him and if he was obliged to do so. If the contractor assumes all risks relating to site conditions he should not be exempt even if unexpected site conditions could not have been discovered or foreseen.

27. War (whether declared or not) or other military activity is usually considered to be an exempting impediment. One difficulty is to determine when a war or a particular military activity can be considered as preventing performance of an obligation and therefore exempting a party. For instance, frequent air-raids near the construction site may create a high risk to the safety of the contractor's employees without preventing them directly from continuing the construction. Parties may therefore wish to specify very clearly when a war or other military activity is considered to prevent performance.

28. Strikes, boycotts, go-slows and occupation of factories or premises by workers should not be considered as exempting impediments if they are caused by the personnel of the contractor, as the liability of a party to perform should not be reduced because of the conduct of his own employees. In addition it may be difficult to determine whether strikes by the contractor's personnel and other labour disputes are avoidable or not. A strike by the purchaser's personnel may be regarded as an exempting impediment for the contractor, if the employment of such personnel is required under the contract for the execution of the performance by the contractor (for example, for supervision of erection).

29. Shortages of raw materials needed for the construction should not usually be considered as an exempting impediment. The contractor should be obliged to procure such materials in time and he should be responsible if he fails to do so. If his supplier fails to supply such materials to the contractor in time, the contractor can normally claim damages.

4. Exclusion of impediments

30. Whichever approach is adopted, parties may wish further to clarify the scope of an exemption clause by expressly excluding some impediments which might otherwise conceivably come within the scope of such a clause, for example, the financial position of a party which prevents him from performing. Parties may also wish to consider excluding impediments which occur after a breach of contract by a party and which, but for the breach, would not have prevented performance by that party.

31. The exemption clause should, in principle, include as exempting impediments any legal impediments which prevent performance of an obligation (for example, any new legislation preventing performance).

32. Parties may however wish to exclude certain acts of State organs from being regarded as exempting impediments. A contract usually imposes an obligation on a party to secure a licence or other official approval which may be required in his country for the performance of certain of his obligations. If such a licence or approval is refused by a State organ, or if it is later withdrawn, parties may wish to agree that the party who does not secure or loses the licence or approval cannot rely on the act of the State organ as an exempting impediment in respect of the failure to perform resulting from the absence of the licence or approval. If parties do not so agree, a party who does not wish to proceed with the contract might be tempted not to take all necessary measures to obtain the needed licence or approval. It may be extremely difficult for the other party to determine whether the measures taken to obtain the licence or approval are adequate. Parties may also consider that it is fairer that the loss caused by the failure to perform resulting from the absence of the licence or approval should be borne by the party who had the duty to secure it.

33. Parties may also wish to consider the position where, apart from the refusal or withdrawal of a licence or approval, the performance of a party is prohibited by an act of a State organ (for example, prohibiting the export of a certain kind of technology). Enforcement of the performance prohibited by a legal system would usually be contrary to the public policy under such legal system and the performance prohibited in the country of the party who is to perform may be considered as legally impossible, even if another legal system is to apply to the contract. Under some legal systems, however, parties may be permitted to include in the contract a provision under which a party whose performance is prohibited should compensate the other party for the loss caused by the failure of performance due to such prohibition.

5. Failure caused by third person

34. It is common in a works contract for a party to employ third persons (e.g. subcontractors) to perform his obligations under the contract. Where the party fails to perform due to the failure by a third person whom the party has engaged to perform the whole part of the contract, the question arises whether and to what extent the party is exempt from liability.

35. In addressing this question, parties may wish to note that in general the liability of a party for failure of performance should not be reduced because he employs third persons to execute performance. Parties may therefore find it advisable to provide only a limited exemption to a party who seeks to excuse himself on the ground that his failure was caused by a failure by such third persons. A possible

approach may be to provide that a party is exempted in such circumstances only if two conditions are satisfied: firstly, that the party is exempted under the exemption clause in the construction contract; and secondly, that the third person would be exempted if the exemption clause in the works contract were contained in the contract between the party and the third person.⁴ The extent of liability of the contractor for a performance of a subcontractor may, however, depend upon whether the subcontractor has been chosen by the contractor or the purchaser.⁵

36. An alternative approach would be to exempt the contractor employing a third person if he proves that he took reasonable care in selecting the third person. However, this approach, may give insufficient protection to the purchaser. The contractor employing the third person would in this case have little incentive to continue to supervise the third person after the latter is selected, or to pursue remedies against him for his failure of performance. Furthermore, by exercising care at the moment of selection, the selecting party can effectively divest himself of the responsibilities for performance which he had assumed.

37. It has been suggested that, where performance by a party has been prevented by an impediment, the party should only be exempted if by taking reasonable measures he could not have overcome or avoided the impediment or its consequences. Accordingly, when a third person employed by a party fails to perform, the party should seek to overcome the impediment by employing another person. When, however, a subcontractor is designated in the contract by agreement of the parties, or is chosen by the purchaser, the contractor cannot employ another subcontractor without a variation of the contract or a new approval by the purchaser, or a choice of another subcontractor by the purchaser. In such cases the contractor may be exempted upon his proving that the subcontractor's failure to perform resulted from an exempting impediment as defined in the contract between the parties. Parties may wish to specify the steps which a contractor should take when a third person fails to perform in these special cases (for example, that the contractor should propose to the purchaser the name of another person who may be employed).

D. Notification of impediments

1. Obligation to notify

38. A party who invokes an impediment should be obligated under the contract to notify the other party of the impediment which prevented or is likely to prevent the performance of any of his obligations, and of the cessation of the impediment. This notification may facilitate the taking of measures by the other party to mitigate the loss caused or which is likely to be caused by the failure of performance.

39. The parties should consider the form, means of communication and contents of the notice, and the period of

⁴This approach is based on article 79 (2) of the United Nations Convention on Contracts for the International Sale of Goods, which reads:

"(2) If the party's failure is due to the failure by a third person whom he has engaged to perform the whole or a part of the contract, that party is exempt from liability only if:

"(a) He is exempt under the preceding paragraph; and

"(b) The person whom he has so engaged would be so exempt if the provisions of that paragraph were applied to him."

⁵See chapter "Third parties employed in execution of contract".

time within which it should be given. The form of the notice may depend on the circumstances in question. Generally, notice in writing should be required. The means of communication may be cable or telex (when such means of communication are available), confirmed by registered air-mail. Parties should also specify when a notification takes effect (for example, at the time of despatch, or receipt).

40. The notice should specify details concerning the impediment together with evidence that the performance is thereby prevented, and if possible the anticipated period of its duration. The party invoking the exemption may also be required to continue to keep the other party informed of all circumstances which may be relevant for an appraisal of the impediment and its effects.

41. As exemptions have serious consequences on the legal position of the parties, verification of the events relied on as exempting impediments may be required when feasible (for example, by a public authority, notary public, a consulate or chamber of commerce in the country where the impediment occurred). Parties should consider the evidentiary effect to be given to such verification.

42. The parties may require the notice to be given immediately, or without undue delay, or within a time-limit agreed to in the contract, after the party invoking the exemptions learned or could be reasonably expected to learn of the occurrence or likelihood of the occurrence of the impediment. When a party knows in advance that an impediment will occur, he should not be permitted to postpone the notification until the date when the obligation is to be performed, as the prevention or the mitigation by the other party of the loss which will be caused by the failure to perform requires the information to be given as soon as possible. If the parties require that the notification is to be given immediately or within an agreed time-limit, they should also take into consideration the fact that such notification may sometimes be impossible (for example, in case of natural disasters) and should therefore enable an adequate extension of time in these cases.

43. The party invoking an exemption should also be required to notify the other party, within an agreed time-limit, of the cessation of the impediment or its effects. This period should start running after the notifying party has learned or could reasonably be expected to learn of the cessation of the impediment or its effects.

44. The parties may further wish to provide that, upon notification of the exempting impediments, they should deliberate on what measures to take in order to prevent or limit the effects of impediments, and to prevent or mitigate any damage which may be caused by them. A modification of the scope of construction or the specification of equipment or a variation of some contractual terms may be needed.⁶

2. Legal effects of failure to notify

45. Express provision should be made for the consequences of failure to notify the other party of an exempting impediment. Even if parties decide that no legal effects should flow from the failure to notify, this should be expressly stated. However, such instances should be limited to cases where there is no probability of loss being caused by such failure.

46. In some cases the parties may consider a timely notification of the impediments to be so important that the party failing to notify in time should thereby lose his right to invoke the exemption. If this legal effect is intended, it should be clearly provided for in the contract. In most cases, however, the failure to notify in time should not entail loss of the right to rely on the exemption.

47. The parties may wish to provide that a party can rely on an impediment from the time it occurred even if he has failed to notify in time, but that in such a case he is liable to compensate the other part for damage resulting from the delay in notification.⁷

48. A compromise approach may be to combine the effects mentioned in paragraphs 47 and 48. Parties may provide that an exemption is effective from the time the impediment occurs only if notice is given in time. If the party fails to notify in time, the exemption would become effective only from the time of notification. The party failing to notify in time is liable to compensate for damage resulting from the delay in notification.

E. Legal effects of exemptions

49. The main legal effect of an exemption clause should be to relieve the party, whose performance is prevented by the exempting impediment, from liability to pay damages for loss caused by the failure to perform.⁸ If an impediment prevents performance by a party of only part of an obligation, the exemption should apply only in respect of that part. If an impediment prevents a party from performing his obligation only temporarily, the exemption should be effective only for the period during which performance is prevented by an exempting impediment or its consequences. For example, if a flood prevents construction, the exemption should be effective only for the duration of the flood if construction can recommence immediately after the flood subsides. If, however, construction cannot recommence until the consequences of the flood are remedied, the exemption should continue until the remedy is completed (for instance, until the mud and stones are removed).

50. The other possible legal effects, which have been noted in paragraph 2 above, should also be considered by the parties. Other rights and remedies may or may not be affected by the exempting impediments. For example, while the failing party may be relieved from damages, he may still be liable for penalties or liquidated damages under a penalty or liquidated damages clause. If the parties wish to exempt the party invoking an exempting impediment from other remedies, they should expressly so provide in the respective contract clauses relating to such remedies.

⁷This approach is based on article 79 (4) of the United Nations Convention on Contracts for the International Sale of Goods, which reads:

"(4) The party who fails to perform must give notice to the other party of the impediment and its effect on his ability to perform. If the notice is not received by the other party within a reasonable time after the party who fails to perform knew or ought to have known of the impediment, he is liable for damages resulting from such non-receipt."

⁸This effect is stipulated in article 79 (5) of the United Nations Convention on Contracts for the International Sale of Goods, which reads:

"(5) Nothing in this article prevents either party from exercising any right other than to claim damages under this Convention."

⁶See chapter "Changes in scope and quality of works" and chapter "Variation".

[A/CN.9/WG.V/WP.9/Add.4]^a

CHAPTER XXXIV. HARDSHIP CLAUSES

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A. General remarks

1. "Hardship" is not a legal concept; it has been employed in some clauses in international contracts to describe situations where economic, financial, legal, political or technological factors have changed causing serious economic consequences to a party in a contract. Most hardship clauses provide for the renegotiation of contracts in order to adapt them to new situations. However, some hardship clauses in practice provide for termination without first resorting to renegotiation. This should, however, be discouraged.

2. Attention is directed to two main aspects of a typical hardship clause: first, what constitutes hardship and, secondly, the adaptation of the contract to the new situation through the mechanism of renegotiation. The legal effect of a hardship clause may differ under different legal systems. Also, the adaptation of a contract, due to changed circumstances, may be recognized under some legal systems and not in others (see paragraphs 36-38, below). Parties contemplating a hardship clause should consider whether the applicable law makes provision for changed circumstances affecting the economics of the contract. If it does, the parties may wish to consider whether it is suitable or adequate for their purpose. If the applicable law is not suitable or adequate, but is mandatory, parties may wish to choose another applicable law. If the applicable law is not mandatory parties may modify it (see paragraph 6, below).

3. The Guide draws a distinction between hardship clauses and exemption clauses in that in a hardship situation the contract is not incapable of performance whereas an exempting impediment must render a contract incapable of performance, whether temporarily or permanently.¹

4. Hardship clauses should be distinguished from other similar clauses (e.g. index clauses) which deal with situations concerning the economics of the contract. Such clauses, for example those dealing with currency fluctuations, are usually well-defined as the changed circumstances are predictable and hence the precise consequences can be provided for; no renegotiations are needed unlike in a hardship clause (see paragraph 9, below). Thus, for example, a predetermined formula may apply automatically in the event of a currency fluctuation to realign the contract to changed circumstances.

B. Factors to be considered as to whether to include a hardship clause

5. Although the advantages and disadvantages of a hardship clause will depend on the way it is drafted (e.g. a widely formulated hardship clause will have adverse effects on the stability of the contract and will tend to lean in favour of the contractor), nonetheless, certain advantages and disadvantages may be discerned.

6. Advantages of a hardship clause:

(a) Some legal systems may recognize the adaptation of contracts in the event of changed circumstances disrupting the initial equilibrium of the parties. However, the law may be too flexible or too restrictive (e.g. leading only to termination, or only permitting adaptation of contracts by courts). In such situations, a hardship clause can be usefully drafted to modify the applicable law, if it is not mandatory (see paragraph 2, above);

(b) Since industrial works contracts are of a long-term nature and cannot be easily terminated, renegotiation of such contracts to adapt them to new situations may be acceptable;

(c) In the absence of a hardship clause, a party, say, the contractor may decide to terminate the contract even though he would be liable for breach, provided the legal system permits. Under some legal systems, however, the party may not be able to terminate the contract. Where a hardship clause exists the contract may be saved through renegotiations, perhaps to the ultimate benefit of both parties. Although there is nothing to prevent parties from renegotiating in the absence of a renegotiation clause, nonetheless, an express provision for renegotiations can take into consideration certain factors to ensure greater predictability and a fair determination of the outcome (see paragraphs 28-33, below). The rights and obligations of the parties during renegotiations can also be regulated (see paragraphs 46-47, below).

7. Despite the above-mentioned advantages there are serious disadvantages which may outweigh the advantages:

(a) A hardship clause with the mechanism for readaptation renders the contract uncertain and unstable;

(b) However carefully drafted, a general hardship clause could prove imprecise and vague because of the nature of hardship itself. Moreover, hardship clauses are of recent origin and their validity has seldom, if ever, been tested in the courts or the arbitral tribunals in some legal systems;

(c) The mechanism for renegotiation may protract the time for the performance of obligations under the contract;

^a22 March 1983. Referred to in Report, para. 90 (part one, A).

¹See chapter "Exemptions".

(d) A hardship clause may open the door to spurious claims of hardship situations as an excuse for suspending performance of the contract.

8. In determining the question whether or not to have a hardship clause parties should, apart from considering the advantages or disadvantages, also consider which party is more likely to invoke such a clause, and the impact it might have on the performance of the contract (see paragraph 7, above). Hardship clauses generally tend to favour the contractor more than the purchaser, for he has more reason to invoke a hardship situation as when he finds that the costs of executing the contract are higher than he anticipated. Moreover, hardship clauses may tend to encourage contractors to offer a low price in order to secure the contract, if they think that they might subsequently be able to rely on a hardship clause to renegotiate the contract. In so far as the purchaser is concerned, his position is such that there will be fewer occasions when he would need to rely on a hardship clause. Changed circumstances affecting his position can generally be dealt with within the framework of the contract.²

9. Instead of using a hardship clause, which does not deal with the exact consequences of a hardship situation but leaves the matter for renegotiations, it is better to have specific clauses (e.g. currency fluctuation or index clauses) to deal with particular situations affecting the economics of the contract and where well-defined formulae can be used for an automatic economic adjustment. However, a particular formula may turn out to be unworkable or certain specific clauses may not be recognized under a legal system. In such situations, a hardship clause could be useful.

C. Approach to drafting a hardship clause: general definition followed by exhaustive list

10. As a matter of policy, hardship clauses, if they are to be included in a contract, should be circumscribed and confined to exceptional circumstances. Also, in view of the doubtful legal effect of hardship clauses under some legal systems, extreme care should be taken in their drafting, if parties wish to insert such a clause in their contract. A hardship clause which simply sets out in general terms open-ended and vague criteria for its application (e.g. "changed circumstances", "upsetting the initial equilibrium of the parties", and "causing serious economic consequences") should be avoided. Equally unsatisfactory is an approach which merely provides a list of hardship situations which is not intended to be exhaustive. Even if the general definition were to be accompanied by an illustrative list, the approach is still too flexible, and the scope may still be vague.³

11. An approach which might be acceptable from a legal and policy viewpoint, is a general definition followed by an exhaustive list of hardship situations. Such an approach ensures that parties have to be specific and will know the scope of the hardship clause in advance. However, because of the nature of hardship, the clause may still turn out to be imprecise. Nevertheless, this approach has the advantages that, firstly, doubts as to what specific circumstances come under the general definition are avoided. Secondly, it reduces the uncertainties created by a mere list of situations which is not clear as to when such situations are to be regarded as hardship situations.

²See, for example, chapters on "Scope of contract" and "Termination" (termination for convenience).

³See chapter "Exemptions" where these various approaches are considered.

1. General definition

12. The scope of the general definition should be narrow and should at least include the following elements: change of circumstances, nature of change in circumstances (unforeseeable and beyond the control of the party invoking the hardship clause), and consequences of change in circumstances (serious economic consequences).

(a) Changed circumstances

13. The hardship clause should cover situations in which the circumstances which existed at the time the contract was concluded have undergone a change. Such a change in circumstances should not lead to an application of the clause unless it produces serious economic consequences. In some hardship clauses the change itself is qualified, that is, it is required to be "substantial", "fundamental" or "serious". It is suggested, however, that the seriousness of the consequences of the change, rather than that of the change itself, should be the focus of the definition of hardship circumstances (see paragraphs 19-21, below).

14. Instead of relying on a general formulation of a "change in circumstances", the parties should delimit the change in circumstances more specifically by reference to particular areas in which a change of circumstances might be relevant for the particular contract concerned. For example, the clause should specify that the change must be due to economic, financial, legal, political or technological circumstances.

15. It is preferable to require that the change in circumstances must occur after the conclusion of the contract. The parties should be deemed to have taken into account circumstances which have occurred up to the time when the contract was concluded.

(b) Unavoidable, unforeseeable or extraordinary nature of the change

16. It is advisable to provide in all cases that a party may invoke the clause only if the change in circumstances was not caused by him. The contract may also require that the party could not reasonably have been expected to avoid the change or overcome its consequences. The considerations in this regard in connection with exempting impediments also apply here.⁴

17. The scope of the hardship clause may be narrowed further by requiring the change in circumstances to be unforeseeable. If this requirement is adopted, it should be formulated in an objective manner so that it would not be sufficient for the party to show merely that he did not foresee the change; the change should not be reasonably foreseeable.⁵

18. In some cases the requirement that the change in circumstances be unforeseeable may be replaced by a requirement that the change be extraordinary. This requirement is more objective than the "unforeseeable" requirement (even according to the formulation suggested in paragraph 17), since the "extraordinary" requirement takes even less account of the foresight of the party invoking the clause.

(c) Serious economic consequences

19. A change in the circumstances existing at the time the contract was concluded should not be enough to justify an application of the hardship clause. It should also be required that the change in circumstances must result in serious economic consequences for the party invoking the clause.

⁴See chapter "Exemptions".

⁵*Ibid.*

20. It is advisable to quantify the consequences resulting from the change in circumstances so that the contract will not be subject to renegotiation upon the occurrence of economic effects which are within the risk that a party should bear. This may be done in a general way, by using a term such as "substantial financial burden". The use of such a term, however, could give rise to difficulties of interpretation and application in concrete situations. Similar difficulties could arise if the parties were to add to or substitute for such a term equally vague concepts of equity or fairness (e.g. "undue hardship" or "unfair prejudice"). If possible, the parties should attempt to quantify the seriousness of the consequences more concretely (for example, by requiring cost increases to exceed a specified amount or percentage of the price).

21. The parties should consider the degree of likelihood of serious economic consequences to a party as a result of the change in circumstances which should be required before a clause can be invoked. In some situations it might be sufficient to require that the party invoking the clause must establish that these consequences are very likely to occur, or even that the risk of their occurrence has substantially increased. In other situations it might be advisable to require the party to establish that the consequences will occur beyond any doubt.

2. *The exhaustive list*

22. Due to the very broad range of circumstances which may change after the conclusion of the contract the parties may wish to limit the scope of the application of the clause by having an exhaustive list of hardship situations.

23. Under the approach suggested (general definition followed by a exhaustive list), the list of hardship situations must also satisfy the criteria set out in the definition. Owing to the imprecise nature of hardship it is advisable to tighten the scope of a hardship clause further by including a list of situations to be excluded which might otherwise be included under the list read in conjunction with the general definition. The parties may, for example, exclude circumstances arising from a weakening of the financial position of a party or a change in the economic situation of the country. They may also exclude circumstances occurring after the party invoking the clause is in breach of the obligation in respect of which the hardship is claimed.

24. The application of the clause may also be restricted by preventing the clause from being invoked within a certain period of time after the conclusion of the contract. Furthermore, the parties may agree to restrict the number of times or the frequency with which a party may invoke the clause. Such provisions are aimed at reducing the element of uncertainty and instability which a hardship clause introduces into the contract.

D. Renegotiations

25. The parties may wish to decide whether the renegotiation provision should carry with it only an obligation to participate in the renegotiations, or whether it should go further by requiring an agreement as to the adaptation of the contract. The purpose of the former approach is only to give an opportunity to the party suggesting the renegotiations to put up his proposals, but the other party has the option whether or not to accept them. In such a situation parties may not wish to authorize a court, an arbitrator or a third party to modify the contract on their behalf. However, they may agree upon a third person who could assist them in an independent and impartial manner in their attempt to reach an agreement

on a reasonable modification of the contract terms.⁶ In the event of a failure to reach any agreement the parties may intend that the contract is to continue according to its original terms. This should be clearly stated in the contract. Provided the parties participate in the renegotiations there is no obligation to reach an agreement. Hence, there is no breach if parties fail to reach an agreement.

26. The decision as to which obligation should be imposed upon the parties (i.e. participate in the renegotiations, or renegotiate and reach an agreement) will depend to some extent upon the consequences which the parties intend in the event that renegotiations are not successful. Three types of consequences are possible if the parties fail to agree upon an adaptation of the contract: continuation of the contract according to its original terms; adaptation of the contract by a court, an arbitrator or a third party; or termination of the contract. However, if it is provided that parties must come to some agreement, the party who is entitled to invoke the renegotiation clause should have the right to resort to a court, an arbitrator or a third party to adapt the contract on behalf of the parties in case no agreement is reached (see paragraphs 36-44, below). If the parties intend the contract to continue according to its original terms, then it will be sufficient to obligate the parties only to participate in the renegotiations. If they fail to reach an agreement, neither party will be in breach for the failure to agree, and the original contract can continue. On the other hand, if the parties intend the contract to be adapted by a court or an arbitrator or by a third party in the event of a failure to agree to an adaptation parties should make express provision to this effect (see paragraph 38, below).

27. Whichever obligation is imposed, the parties should be careful to co-ordinate this aspect of the hardship clause with the provisions of a termination clause.⁷ For example, a termination clause may make a contract terminable only upon a serious breach by a party. If the parties do not intend a breach of an obligation to renegotiate or to adapt the contract as justifying termination (see paragraph 45, below) such a breach should be excluded from the termination clause.

I. *Procedure for renegotiations*

(a) *Notification*

28. Upon the occurrence of a hardship situation the party invoking the clause should be obligated to notify the other party of it and of his intention to invoke the clause. The notification should be required to be made without undue delay after the invoking party becomes aware of it. The notification should not be postponed even if the extent or character of the adaptation sought cannot be determined at the time of notification.

29. The contract should require the notification to be in writing, and to set forth relevant details concerning the change in circumstances and its consequences as to enable the other party to evaluate the situation. The contract may also require that, if possible, the notice should indicate the nature of the adaptation sought.

30. Upon receipt of the notification, the other party should be obligated to confirm the subject, the ground, the date and the place of renegotiations, without undue delay. If he is silent he should be deemed under the contract to have refused either to participate in the renegotiations or to renegotiate. If he

⁶See chapter "Settlement of disputes".

⁷See chapter "Termination".

should consider that the grounds set out are not sufficient to justify renegotiations, he should indicate the reasons for his conclusion. The contract may provide for the obligation of the party to participate in the renegotiations without his thereby conceding that there are grounds for the renegotiations or that the grounds alleged by the other party are sufficient for the adaptation sought. If the place or the date of the renegotiations proposed by one party are not acceptable to the other party he should make a counter-proposal within a specified time-limit set out in the contract, giving reasons why they are unacceptable.

31. The parties may wish to agree on one of the following consequences if the party entitled to invoke the hardship clause fails to give the required notice, or fails to give it on time:

(a) The party may lose his right to invoke the hardship clause. This approach may avoid the situation in which a party initially chooses not to seek an adaptation of the contract, but later tries to use the hardship circumstances to reduce or escape his obligations for reasons not related to those circumstances;

(b) If the party does not give the required notification within the time specified in the contract, he might remain entitled to invoke the clause, but be liable to compensate the other party for losses resulting from the delay.

(b) Guidelines for renegotiations

32. Parties may wish to facilitate the application of a hardship clause by following some guidelines which should be aimed at assisting parties in coming to a fair solution. They may, for example, only limit the restoration of their initial balance to the extent that it has become burdened by the hardship situation and that other terms of the original contract should, as far as possible, be followed. Other guidelines may include the following: that the principle of good faith in the execution of the contract should apply; that renegotiations should aim at the attainment of performance; that there should be no undue prejudice to either party arising from the adaptation or that the interests of the parties must be maintained proportionately.

(c) Time-limit for renegotiations

33. If the parties wish to confer some right upon one party in case of a failure to agree to the adaptation of the contract (e.g. to initiate judicial or arbitral proceedings) they should stipulate a time-limit within which the renegotiations should be concluded, whether successfully or unsuccessfully, as otherwise it would be difficult to determine when the parties fail to adapt the contract.

2. Failure to agree

(a) When failure to agree occurs

34. The contract should stipulate the time when failure to participate in the renegotiations or failure to agree to the adaptation of the contract would deem to occur. It may stipulate that failure occurs when the party who has been requested to participate in the renegotiations refuses to do so, or if he does not express his readiness to do so within a time-limit, or if the parties do not reach an agreement within a certain period of time after renegotiations have commenced (see paragraphs 30 and 33, above).

(b) Effect of failure to agree

35. It has been noted (see paragraphs 25-27, above) that parties may adopt one of the two approaches in drafting a

renegotiation provision (i.e. participate in the renegotiations only, or renegotiate and reach an agreement). If they follow the latter approach, they may wish to provide for some of the following legal consequences in the event that they fail to agree on the proposals of a party for adaptation.

(i) Adaptation of the contract in judicial or arbitral proceedings

36. In the event of a failure to agree, the party entitled to invoke the renegotiations should be able to resort to judicial or arbitral proceedings to adapt the contract. In so far as the court or the arbitrator is concerned it should be noted that in some legal systems the jurisdiction of the court or the arbitrator is limited to a determination of the rights and duties of the parties arising from the contract. As such they may not have the competence to adapt a contract as this may be considered as creating new contractual rights and obligations for the parties and which may be outside their normal function.

37. Parties should choose a court or place of arbitration where the law applicable to the judicial or arbitral proceedings recognizes the competence of the court or arbitral tribunal to adapt the contract. In choosing the applicable law of the contract, the parties may wish to consider a legal system which does not prevent a court or an arbitrator from adapting contracts.

38. In addition, parties should empower the court or the arbitrator to adapt the contract on behalf of the parties. The following may be suggested as specific powers which the parties should confer on the tribunal: determination as to whether or not there are grounds for renegotiation; adaption of the contract (e.g., to readjust the contract as far as reasonable in the interests of the parties); termination (in whole or in part) in the event where the contract cannot be adapted; determination of the legal effects of termination (the guidelines suggested in paragraph 32, above, should also apply here). However, in deciding whether to empower a court to adapt the contract parties should consider whether there are mandatory limitations on the competence of the court to adapt contracts.

39. On the other hand, arbitral proceedings are, generally speaking, less formal and more flexible, and there are less mandatory limitations in regard to their competence than in regard to that of the courts. Therefore, it may be preferable to resort to arbitration for the adaption of contracts. Moreover, arbitrators may be chosen for their expertise in construction law and practice and hence may be better equipped for adapting the contract to the satisfaction of both parties. As such, parties may prefer arbitration as the appropriate form of dispute settlement where parties fail to agree. If arbitral proceedings are contemplated, parties may find it advisable to include special provisions for the adaptation of contracts (see paragraph 38, above) either in a general arbitration clause dealing with other disputes (if such a clause is contemplated), or in a special arbitration clause dealing with adaption.

40. The contract should provide for the effect of the court decision or the arbitral award: the adapted terms should be considered as new contractual terms to be substituted for the original ones and be incorporated in the original contract. The parties should be obligated to comply with the new terms.

41. In the usual type of court decision or arbitral award, the tribunal decides on the rights and obligations of the parties under the contract and the decision or award can be

enforced. However, when a court or an arbitral tribunal adapts a contract, the decision or award simply creates new contractual terms to be substituted for or added to the original ones. This decision or the award is therefore not immediately enforceable, although the new contractual terms contained in the decision or award are binding on the parties. If a party breaches a new contractual term and judicial or arbitral proceedings are initiated for the breach, the judge or the arbitrator has to consider the question of the recognition of the decision or the award which adapted the contract. The recognition of the new contractual terms may encounter difficulties if the court or arbitrator asked to recognize the decision or the award adapting the contract cannot under the law applicable to such judicial or arbitral proceedings recognize such a decision or an award.

42. A method of avoiding the above-mentioned difficulties is to resort to a court or an arbitral tribunal in the same country both for the adaptation of the contract, and for breach of the new contractual terms created by the adaptation.

(ii) *Adaptation of the contract other than by court or arbitrator - a third party*

43. Another possible approach in overcoming the difficulties posed by the lack of jurisdiction of a court or an arbitrator to adapt a contract is to appoint a third party (not to be regarded as an arbitrator) to do it. The third party is to be empowered by the parties to modify the contract (see paragraph 38, above). The advantage of this approach over resort to court or arbitration is that the jurisdictional limitations (noted above) placed upon a court or an arbitrator may not be applicable to a third party, who is acting on the basis of authority granted by the parties.

44. This approach may, however, have some disadvantages. While almost all legal systems contain special legal rules on arbitration which ensure that arbitration proceedings are conducted fairly and lead to an arbitral award, many legal systems do not have special rules regulating the conduct of third persons, who are not arbitrators, deciding on such matters as the adaptation of contract, and in particular do not have rules to ensure the giving of decisions by third persons. Decisions of such third persons will be open to challenge on the basis of general rules of the applicable law such as those relating to the abuse of authority by a person to whom parties to a contract have granted authority. Such general rules, however, may not resolve all the problems which may arise under this procedure. The parties may, therefore, have to rely heavily on the good faith and competence of the third party.

(iii) *Termination*

45. The parties may wish to limit the possibility of terminating the contract only to exceptional cases where other solutions in respect of the failure to agree upon the adaptation of the contract are inadequate.⁸ In principle the right to terminate the contract should be exercised only if the adaptation of the contract in judicial or arbitral proceedings or by a third party has failed or is impossible. Termination should not generally be permitted before an attempt at renegotiation has been made and has failed. Even in cases where the only possible solution to the situation would be the termination of the contract it is advisable to authorize a court or an arbitrator or a third party to terminate the contract rather than allow a party to do so himself. In this way the ground for the termination may be verified and a settlement of complex problems concerning the consequences of the termination may be effected.

⁸*Ibid.*

3. *Status of the contract during renegotiations*

46. The parties should spell out the position of the contract during the renegotiations. The parties should consider whether the execution of the contract should continue during the renegotiations or whether the performance is to be suspended during this period. Generally, an interruption in the construction can cause serious prejudice to either party and it would, therefore, be preferable for both parties to continue to fulfil their obligations during the renegotiations. The mere fact that higher costs would be incurred by the contractor and that this is the subject to be resolved by the renegotiations should not justify suspension of performance of the contract.⁹

4. *Normalization of circumstances*

47. As renegotiation is required only upon a change of circumstances, provision should be made as to what should happen if circumstances return to normal. A problem arises when the situation is not exactly back to its original position. Here, to the extent possible, the original terms and conditions of the contract should be restored to take account of the extent of normalization of circumstances. The parties may therefore agree upon a procedure for renegotiating the consequences of a return to normality.

⁹See chapter "Suspension".

[A/CN.9/WG.V/WP.9/Add.5]^a

CHAPTER XXXVIII. TERMINATION OF CONTRACT

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^a16 March 1983. Referred to in Report, para. 90 (part one, A).

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A. General remarks

1. Termination of an industrial works contract, particularly during the construction phase (see paragraph 11, below), will cause significant difficulties for both parties. Both parties will have made substantial investments of finances, resources and time in the project. Upon termination, the contractor will have to stop his work, remove his personnel and equipment from the site, and discharge himself from a frequently complex web of contractual relationships with subcontractors and suppliers (see paragraph 76, below). The purchaser will have to find and engage another contractor to complete the project (see paragraph 72, below), and the work is likely to be delayed for a significant amount of time. The financial costs of terminating an industrial works contract are high.¹ For these reasons, the remedy of termination is infrequently used by parties to industrial works contracts, and is usually invoked only as a last resort.

2. However, no matter how much planning and foresight the parties might exercise at the pre-contractual stage, and despite the parties' good faith and the expectations of full performance with which they enter into the contract, circumstances may arise which make it prudent or necessary to terminate the contract before it has been completely executed. Therefore, parties negotiating an industrial works contract should devote serious consideration to the subject of termination, and should include a clearly-drafted termination provision in the contract in order to provide for an orderly and equitable termination in the event such circumstances arise.

¹The apportionment of these costs between the parties is discussed in section E, 6.

3. When drafting a provision on termination the parties should take account of any mandatory rules of the applicable law on the subject. In certain legal systems rules may exist which restrict the freedom of the parties to agree upon termination provisions, or which otherwise regulate the termination of a contract. Moreover, the parties should be aware of any non-mandatory rules of applicable law relative to termination, and should consider whether these rules are sufficient and appropriate to regulate termination of the contract being negotiated. Very often, general legal rules on termination are ill-suited to the termination of long-term and complex industrial works contracts.

4. The parties should consider termination in relation to other remedies under the contract or applicable law for a failure of performance, such as requiring performance in accordance with the contract, requiring defects in performance to be remedied, renegotiating and varying contractual provisions, and damages. These remedies are discussed in other sections of this Guide. The parties may wish to reserve the remedy of termination, in particular when construction is in progress (see paragraph 11, below), for situations in which such other remedies are not available or are inadequate by themselves.

5. Under most legal systems it is possible for the parties to a contract to agree to terminate the contract. While some legal systems specify the form which such an agreement must take, it is advisable for the contract to specify that an agreement to terminate it must be in writing. A detailed discussion of the drafting and contents of an agreement to terminate is beyond the scope of this Guide.

B. Extent of termination

6. The word "termination" is used in this Guide in preference to other terms (such as "cancellation", "recession" or "annulment") which may be closely linked with particular legal systems and which may be thought to carry with them certain legal rules and consequences which exist in those systems. As conceived in this Guide termination does not refer to a complete abrogation of the contract from its beginning or in its entirety. Rather, termination refers to a cessation of the obligations of both parties to perform (e.g. the obligations of the contractor to do the work and the obligations of the purchaser to pay the price) as of the time of termination.² The contract will not be able to be terminated in respect of obligations which have already been performed, since this would require each party to return what he has received from the other. This is not possible in an industrial works contract because the purchaser will not be able to return to the contractor the portion of the works which have been constructed on the purchaser's land.

7. Moreover, the concept of termination as used in this Guide does not imply that all rights and obligations under the contract cease to be effective upon termination. The parties will wish certain of these rights and obligations to remain in effect even after termination, such as those which regulate the termination itself (see section E, below), certain rights and obligations in respect of performance which has occurred prior to termination (e.g. damages for breaches occurring prior to termination, and guarantees in respect of work which has been done), and other obligations (e.g. confidentiality and the settlement of disputes). In order to ensure that such rights and obligations remain in force, it is advisable for the contract expressly to provide that they are to survive the termination (see paragraph 92, below).

²See paras. 58-62 concerning the time of termination.

8. In many cases a contractor may fail or be prevented by an impediment from performing only a portion of his remaining obligations under the contract. The parties should consider whether, in such cases, the purchaser should have the option of terminating the balance of the contract in its entirety or only the portion which the contractor failed or was unable to perform. The following paragraphs consider this question.

9. If the contractor fails to perform a portion of the work, it might be possible for the purchaser to bring in another contractor to complete or remedy that portion, keeping the original contractor bound to complete the balance of the work. In very many cases, however, this will not be feasible, as, for example, when the work in question involves a unique design or construction techniques with which a new contractor would not be familiar, or if a new contractor would not find it profitable to equip and prepare himself to perform only that portion of the work. Moreover, a new contractor will often be unwilling to enter the site and perform work while the original contractor is still present. In addition, in some types of contracts, particularly turnkey or product-in-hand contracts, the various functions which the contractor is obliged to perform may be so interlinked that it is not possible to terminate only a portion of the contract. In these cases termination of the entire balance of the contract may be the only feasible remedy.

10. In some situations the purchaser may not wish to terminate the entire balance of the contract, even if he is entitled to do so, for a particular failure or inability of the contractor to perform. Such situations might be dealt with by other mechanisms, such as the recovery of damages, or variation of the work (see chapter "Variations"). If the purchaser wishes to bring in a new contractor to perform only the portion of the work which the original contractor did not perform, he may do so by a variation deleting that portion from the work to be performed by the original contractor, or by terminating the contract only in respect of that portion.

C. Grounds for termination

11. Due to the extreme consequences for both parties of the termination of an industrial works contract, termination should be chosen as a remedy (particularly during the construction phase) only in serious situations and used only as a last resort when continuation of the contract is likely to cause still greater loss to the terminating party, and when other means of relieving the circumstances giving rise to the termination have failed or are ineffective.

12. However, in a contract in which the contractor is to perform services after the works have been constructed (e.g. supplying spare parts, transferring technology, or performing maintenance services), the parties may consider whether the purchaser should have greater flexibility to terminate the contract after construction has been completed than he has during the construction phase. Circumstances and issues which pertain to obligations which are to be performed after construction has been completed differ from those which pertain to the construction phase. For example, when the works have been constructed, the purchaser will receive a completed plant and the contractor will be entitled to be paid for the work done. The hardship resulting from termination in such cases is not comparable with that which occurs when one party or the other is burdened with a partially completed industrial plant which is of no use.

13. The following paragraphs suggest various grounds for termination which parties involved in contract negotiations should consider for inclusion in their contracts.

1. *Unilateral termination by the purchaser*

(a) *Breach of contractual obligation by the contractor*

14. Serious contractual breaches by the contractor should justify termination by the purchaser. Not every breach should be considered serious enough to warrant termination. During construction work breaches frequently occur which are either trivial, or can be easily remedied, or which will not affect the progress or quality of the completed work. Breaches of this nature should not justify termination.

15. In order to ensure that the remedy of termination is available only for breaches which entail serious consequences, the termination clause should require that the breaches be of such a character. The following framework might be used in order to achieve this. First, the termination clause could enumerate certain breaches which will always be considered sufficiently serious to justify termination, such as abandonment of the contract by the contractor. Second, the clause could enumerate certain additional breaches which would justify termination if they are likely to produce serious consequences (e.g. delay in completion or work of defective or inferior quality). Examples of such breaches are discussed in the following paragraphs. To avoid the hazard of precluding certain grounds from justifying termination by inadvertently excluding them from the enumeration, the enumeration might be coupled with a general residuary provision to the effect that any other breach which has not been specifically mentioned can justify termination if it produces serious consequences for the purchaser. However, such a residuary provision suffers from the fact that its vagueness opens the clause to abuse and is likely to lead to disputes over whether termination is permissible in particular cases. A preferable approach may be to provide that any other breach by the contractor will justify termination by the purchaser if the contractor does not remedy it within a specified period of time after having been notified to do so by the purchaser. Some industrial works contracts permit the purchaser to terminate for any breach by the contractor if it is "persistent or flagrant". Thus, although an individual breach may not be serious, persistence in committing such a breach may itself substantially prejudice the performance of the work, or may portend chronic problems with performance by the contractor, and would therefore warrant termination.

(i) *Abandonment of contract: delay in construction*

16. A failure by the contractor to commence construction at all, or his express abandonment of the construction, should entitle the purchaser to terminate the contract, as should an interruption of construction which evidences the contractor's intention to abandon the construction.

17. In certain circumstances delays during construction may also justify termination by the purchaser. It should be noted, however, that delays in the construction of complex industrial works are virtually inevitable. In many cases the contractor will be able to hire labour or take other measures to perform the balance of his work more expeditiously, and make up the time lost during the delay, so that the work can be completed on time. The parties may conclude that delays which do not prevent the contractor from meeting the completion date¹ should not justify termination by the purchaser.

¹In considering this issue the parties should take into account any ability of the contractor to obtain an extension of the completion date.

18. Works contracts often provide for a construction schedule or programme which, when several contractors are involved, will serve to co-ordinate various phases of the construction work (such as the supply of equipment and materials and the performance of work by other contractors). A failure by a contractor to meet intermediate time limits specified in the schedule may not prevent the final completion date from being met, but may result in the liability of the purchaser to other contractors on the project who suffer financial loss because of the failure in co-ordination (e.g. other contractors who incur overhead costs while having to wait to commence their work as a result of the contractor's delay). Such circumstances may be more satisfactorily dealt with by the payment of damages, liquidated and actual, by the contractor to the purchaser, than by termination.

19. On the other hand, a failure by the contractor to make satisfactory progress with his work may prevent the completion date from being met. The parties may consider it appropriate to permit the purchaser to terminate the contract in such cases. There are several ways in which such a provision could be formulated. First, the termination clause could provide that the purchaser may terminate after the accumulation of a specified amount of unexcused⁴ delay by the contractor.⁵ Second, when delays by the contractor oblige him to pay liquidated damages to the purchaser, termination may be permitted after a specified amount of liquidated damages has accumulated.⁶

20. Third, the clause may be phrased more generally, and permit the purchaser to terminate if the contractor fails to proceed with "due diligence", (perhaps coupled with the condition that the failure makes it unlikely that the contractor will be able to meet the completion date or that date as extended). Such a generalized formulation suffers from vagueness and therefore might be considered to be less preferable than the first two approaches. On the other hand, if the contractor is subject to a construction schedule, the schedule might be used as one indication (although not conclusive evidence) of the diligence with which the contractor has proceeded.

21. A termination provision based upon failure to proceed with due diligence may be conditioned upon notification being given by the purchaser to the contractor. The purchaser would have the right to terminate upon failure by the contractor to restore a satisfactory rate of progress within a specified period of time after the notice. Purchasers should be aware, however, of the possibility that with this type of provision the contractor may be able to improve his progress temporarily in order to forestall the termination, and then retard his progress once again, requiring a new notice by the purchaser, followed by a repetition of this pattern. To avoid this situation, the purchaser might be permitted to terminate upon a new delay by the contractor after the first notice, without further notification.

22. Whichever approach is adopted, it would be desirable for an engineer or project manager to certify the existence and

duration of each delay, in order to minimize the possibility of disputes as to these matters. This is particularly true in the case of a failure of the contractor to proceed with due diligence, because of the vagueness of this approach and its susceptibility to disputes.

(ii) Defects in performance

23. The purchaser should be able to terminate the contract if the work performed by the contractor is seriously defective (e.g. if the works are not of the agreed quality or do not function in accordance with contractual stipulations), and if the contractor fails to remedy these defects within a specified period of time after having been notified of the defects by the purchaser. In this connection the parties should bear in mind the obligations of the contractor under guarantee provisions of the contract (see chapter "Guarantees"). The contract should be as specific as possible in enumerating the defects which will justify termination.

(iii) Failure to obey proper instructions of the engineer

24. In those contracts which provide for an engineer to play a supervisory role (see chapter "Engineer") the parties may wish to permit the purchaser to terminate the contract if the contractor fails to obey proper instructions of the engineer concerning matters of significance to the progress or outcome of the work. The parties may also consider it appropriate to permit the purchaser to terminate if the contractor persistently fails to obey even minor instructions of the engineer. In either case, notification by the purchaser and a failure by the contractor to remedy his behaviour should be pre-requisites to termination.

(iv) Breach of obligations concerning the assignment of contracts and subcontracting

25. As discussed in the chapter "Assignment", under the contract the contractor usually may not, without the purchaser's consent, assign the contract so as to substitute another party for itself. The parties may well regard an unauthorized attempt to assign by the contractor to a serious matter, comparable to abandonment of the contract, and permit the purchaser to terminate in such an event.

26. Subcontracting, on the other hand, is very common in the construction of industrial works. In general, the contractor may subcontract unless he is prohibited from doing so under the contract. However, as discussed in the chapter on "Third parties employed in execution of the contract", some subcontracting may be subject to conditions or restrictions.

27. If the contract contains no express restrictions on subcontracting, the fact that the contractor has subcontracted should in itself provide no grounds for termination.

28. Any violation of contractual provisions restricting or conditioning the contractor's ability to subcontract might be considered to be serious enough to justify termination by the purchaser. Alternatively, the parties may choose to differentiate between restrictions the breach of which would significantly prejudice the purchaser and restrictions which are not so serious. For example, a contract may permit the contractor to subcontract only with subcontractors who have been approved by the purchaser. Subcontracting by the contractor without such approval might be considered serious enough to permit the purchaser to terminate. On the other hand, if the contract merely requires the contractor to advise the purchaser of the identity of subcontractors, without allowing the purchaser to influence the choice of subcontractors, a violation of this provision may be thought not to be so serious as to justify termination. A breach by the contractor of a provision

⁴See chapter "Exemptions".

⁵Termination might also be permitted if the contractor has, without justification, stopped work for a single period of time of a specified length. This approach suffers from the defect that a contractor could avoid termination by recommencing work shortly before the expiration of the period, and could continue this pattern several times. It would therefore be preferable to base the right to terminate upon the accumulated time of delay.

⁶Under both of these approaches due account should be taken of the fact that work in some phases of a project may be seasonal, due to climatic or other conditions.

prohibiting him from subcontracting the entire construction should normally justify termination by the purchaser.

29. The parties may wish to permit the purchaser to terminate only after he has notified the contractor, and the contractor has failed to terminate the subcontract within a specified time period after notice. On the other hand, termination might be permitted immediately if the contractor improperly assigns the contract (see paragraph 25, above).

(v) *Breach of other obligations*

30. In a particular contract there may be other contractual obligations the breach of which may produce consequences which are serious enough to justify termination by the purchaser. If so they should be precisely identified in the contract.

(b) *Bankruptcy or insolvency of the contractor*

31. In most legal systems the contract and its performance will be subject to mandatory legal rules in the event of the bankruptcy of a party. The parties should take account of the relevant bankruptcy laws in drafting termination provisions. In particular, under some bankruptcy laws, even if the parties wish to continue with performance of a contract after bankruptcy, their ability to do so may be severely restricted.

32. The bankruptcy or insolvency of the contractor will seriously threaten the carrying out of the construction. Under most legal systems, the assets of the bankrupt, including his rights and obligations under the contract, will pass to the control of a trustee in bankruptcy or comparable officer. This officer will usually cease carrying on the business of the bankrupt in the ordinary course, except to the extent necessitated by the bankruptcy proceedings. In addition, at least during the pendency of the bankruptcy proceedings, the contractor will be severely restricted in his ability to subcontract or to purchase from third parties equipment or supplies needed to carry out the work, or to make current payments for them. The bankruptcy of the contractor, therefore, should be a ground for terminating the contract.

33. The purchaser should have the right to terminate immediately upon the bankruptcy of the contractor so as to enable him to take necessary actions to protect his position, particularly *vis-à-vis* other creditors of the contractor. Furthermore, the possibility of immediate termination might be important to enable the purchaser to prevent the contractor from incurring additional obligations to third parties for which the purchaser would be responsible.

34. The parties should consider providing that not only an adjudication of bankruptcy, but also the commencement of bankruptcy proceedings by or against the contractor, constitutes a ground for termination. Under most legal systems the institution of such proceedings can seriously disrupt the carrying out of the work by the contractor.

35. The parties should designate as a ground for termination not only bankruptcy, but also similar or related proceedings to which the contractor may be subject, and which would significantly interfere with his performance of the contract (e.g. liquidation, insolvency, assignment of assets and comparable proceedings under relevant law).

36. When the contract requires the contractor to furnish a performance guarantee, the parties may wish to consider permitting the purchaser to terminate if the guarantor becomes subject to the proceedings or adjudications described above, and the contractor fails to provide a new performance guarantee within a stipulated time.

(c) *Termination for convenience*⁷

37. Some industrial works contracts permit the purchaser to terminate the contract at its convenience. A termination for convenience need not be justified by any particular circumstances; the purchaser is permitted to terminate whenever he wishes to do so. In practice this right is confined to purchasers who are Governments or government entities.

38. The right to terminate for convenience may be coupled with other specific grounds. If a purchaser purports to terminate under one of those specific grounds and if it is subsequently determined that termination under that ground was improper, the termination might, under the contract, nevertheless be justifiable as a termination for convenience. However, the rights and obligations of the parties may differ according to whether termination is based upon a serious ground or is for the convenience of the purchaser. The contract should make it clear that the parties are subject only to the rights and obligations which are appropriate to the grounds under which the termination properly occurred.

(d) *Other grounds*

39. The grounds discussed in the foregoing paragraphs which might justify termination by the purchaser are intended to be illustrative only. In a particular contract there may exist other grounds which the parties consider enough to justify termination.

2. *Unilateral termination by the contractor*

(a) *Breach of contractual obligation by the purchaser*

40. As was the case with termination of the contract by the purchaser upon a breach by the contractor, the contractor should be entitled to terminate in the event of a breach of a contractual provision by the purchaser if the breach entails serious consequences for the contractor.

41. The purchaser's principal obligation under the contract is to pay the agreed price. A breach of this obligation by the purchaser should entitle the contractor to terminate the contract in some situations, as will be discussed below.

42. The purchaser will also have obligations which are related to the contractor's right to payment, such as providing a bank guarantee, and obligations which affect this right, such as those relating to interim performance tests, the issuance of interim completion of payment certificates or the acceptance of completed work. A breach by the purchaser of such obligations might entail serious consequences for the contractor, for example if he finances his work in part with the interim payments and cannot proceed with the work in the absence of these payments. The purchaser will have other obligations under the contract, such as making the site available to the contractor, and in the case of a partial-turnkey contract, obligations to perform or to provide for the performance of some of the work. The ability of the contractor to terminate for breaches of such obligations is discussed in the following paragraphs.

(i) *Non-payment*

43. Non-payment by the purchaser of sums due to the contractor should be regarded as a serious breach and should entitle the contractor to terminate the contract. In many contracts payments become due upon certification by an engineer, and the breach of the purchaser will occur upon his non-payment within the time allowed of the amount certified. Of course, termination should be possible only if the

⁷See paras. 89-90.

purchaser fails to pay the sum which is due after setting off amounts owed by the contractor to the purchaser, such as costs of repairing defective work, liquidated damages payable by the contractor, and authorized direct payment made by the purchaser to subcontractors.

44. The parties may wish to consider the advisability of giving the contractor the option to suspend the work as an additional and less extreme measure for dealing with non-payment (see chapter "Suspension").

45. It is advisable to condition the right of the contractor to suspend or terminate for non-payment upon his giving notice to the purchaser and the purchaser's failure to make payment within a specified time limit after the notice.

46. The parties may wish to consider including in the contract measures to protect the contractor's right to payment which are less disruptive than suspension and less severe than termination. For example, the contract could provide for periods of escalating interest payments after which, if the purchaser still has not paid, the contractor would be entitled to suspend or terminate. Also, in the case of a dispute concerning the contractor's right to payment, the purchaser might be permitted to avoid termination or suspension by providing a bond from an appropriate financial institution guaranteeing payment if it is found to be owed.

(ii) *Breaches affecting the contractor's right to payment*

47. Certain breaches by the purchaser could affect the contractor's right to receive payment. These could include an unjustifiable interference with or failure of acceptance by the purchaser of a completed stage of work,⁸ an unjustifiable interference with the issuance of a performance or payment certificate by the engineer or other certifier or failure to issue a certificate for which the purchaser is responsible. Such breaches may be made grounds for suspension and/or termination by the contractor. Again, it is advisable to permit termination only after a failure by the purchaser to cure his breach within a specified time after notification.

(iii) *Interruption of or interference with the contractor's work*

48. Termination by the contractor might be warranted if the purchaser without justification significantly interferes with or obstructs the contractor's work, or if the contractor's work is interrupted due to a cause for which the purchaser is responsible, and the interruption persists for a certain amount of time. Obstruction could occur as a result of actions unrelated to the contract as well as by failures to act in accordance with the contract. It could occur, for example, if the purchaser fails to make the site or portions of the site available to the contractor on time. In contracts in which the purchaser has obligations with respect to the supply of materials or construction, obstruction could occur from a failure to perform these obligations. If the obstruction or interruption relates to all or substantially all of the work to be performed by the contractor, then termination would probably be warranted. Termination may also be warranted if the obstruction or interruption relates only to a portion of the work, but if completion of that portion is necessary before further work can be performed.

⁸The contract may provide that if the purchaser unjustifiably fails to accept then acceptance is deemed to occur at a particular time. (See chapter "Take-over and acceptance"). If the contract so provides, there will be no need to permit the contractor to terminate upon such a failure by the purchaser.

(b) *Bankruptcy or insolvency of the purchaser*

49. The contractor should be able to terminate the contract if the purchaser becomes bankrupt or insolvent. Considerations similar to those discussed in paragraphs 31-35, above, concerning the bankruptcy or insolvency of the contractor, are applicable here.

3. *Prevention of performance due to an exempting impediment*

50. During the course of an industrial works project events can occur which physically or legally⁹ prevent the contractor from performing his obligations under the contract. The contractor will be exempt from liability for failure to perform if the events are covered by the exemption clause (in this Guide these events are called "exempting impediments"; see chapter "Exemptions").¹⁰ The contract should be terminable if the inability to perform will be permanent or if it will persist for an excessive period of time. The following paragraphs consider ways in which this may be accomplished.

51. When the contractor encounters an exempting impediment which prevents him from performing, he should be obliged to notify the purchaser immediately or within a reasonable time thereafter. The contract could then obligate the parties to meet in order to consider the likely extent and duration of the impediment and its effects, and to decide upon how to deal with them.¹¹ If the inability of the contractor to perform is not expected to persist for an excessive amount of time, the parties could agree simply to suspend the contract until the work can be resumed. If it will be permanent, or last for an excessive amount of time, the parties could consider whether the scope of construction or specification of equipment could be modified so as to avoid the impediment (see chapters "Change in scope and quality of works" and "Variations"). The contract might be made terminable only if the impediment or its effects cannot otherwise be avoided or overcome.

52. Alternatively, the termination clause could provide that an inability of the contractor to perform due to an exempting impediment would, upon notice, permit suspension of the contract, and that if the suspension persists for a period of time specified in the clause, the contract would be terminable.

53. In extreme cases, when it is clear from the onset of the impediment that the inability of the contractor to perform will be permanent or will persist for an excessive period of time, the contract might be terminable without requiring a delay. However, even in such extreme cases it would seem that nothing would be lost by requiring the parties to meet and explore whether the impediment or its effects can be avoided or overcome, before permitting termination.

54. The parties should consider which party should be able to suspend or terminate in the event of an exempting impediment. Often, an exempting impediment is beyond the control of both parties; in such a case either party should be able to suspend or terminate. However, an impediment may exempt the party who is prevented from performing his

⁹The question of termination because of economic difficulties is discussed in the chapter "Hardship".

¹⁰A failure to perform due to events which do not exempt the contractor constitutes a breach of contract, and termination for such a failure will be governed by the provision of the termination clause pertaining to breaches (see section C, 1).

¹¹For a discussion of issues and practices concerning renegotiation in general, see chapter "Exemptions".

obligations, but be within the responsibility¹² of the other party. It might be considered that the latter party should not be permitted to suspend or terminate, but that only the exempted party should be permitted to do so.

55. Performance by a party can be prevented by actions taken by a State.¹³ For example, the Government might requisition land needed for construction of the works, refuse or rescind import or export licenses, or prohibit performance of the contract by the party. Parties negotiating an industrial works contract should consider whether actions taken by a Government which prevent performance of the contract should justify termination, and if so, to what extent.

56. The question of whether such governmental restrictions should exempt a party from failure to perform is dealt with in the chapter "Exemptions". It would be reasonable to conclude that a governmental restriction which exempts a party from liability for the failure to perform should justify termination of the contract to the same extent as do other exempting impediments (see paragraphs 50-54, above).

57. Certain governmental restrictions might not under the contract exempt a party. In such cases the party who cannot perform is liable for breach of the contract. One approach which the parties might consider to deal with these restrictions is to treat them in the same manner as other breaches (see section C, 1 above, and note 10). In such cases a party would not be able to terminate if his performance were impeded by a non-exempting government restriction. On the other hand, the parties may consider that such government restrictions should be treated differently from other impediments, in that even if they are not considered to be exempting impediments, a party should not be compelled to risk violating a law or other governmental restriction by requiring him to perform; rather, the party should be able to choose to terminate the contract and pay damages to the other party. However, in order to avoid abuse of this right to terminate, its use might be limited to situations in which the duration of the restriction is unlimited, or, if the duration is fixed, it will persist for an excessive amount of time.

D. Procedure for termination

1. Time for termination

58. The contract should specify the time when a party becomes entitled to terminate the contract. Various approaches may be adopted in this regard. These include permitting a party to terminate immediately upon the occurrence of grounds for termination, or only after the lapse of a period of time following notice of such grounds.

59. As indicated in the sections of this chapter dealing with the various grounds of termination, it is usually desirable to require notification and the lapse of a period of time prior to termination, particularly when the ground for termination is a situation which can be remedied, avoided or overcome.¹⁴

¹²In this chapter, termination due to circumstances within the responsibility of a party means termination due to a breach of contract by that party, termination due to non-exempting impediments preventing the performance of contractual obligations by that party, and bankruptcy or related proceedings to which that party is subject.

¹³The validity of the purported exercise of jurisdiction by a State over a party is beyond the scope of this Guide.

¹⁴See, however, para. 33. In addition, if the right of termination is based upon the accumulation of unexcused delay by the contractor in the progress of his work (see para. 19), it will probably be unnecessary to require the purchaser to wait an additional period of time after the amount of accumulated delay giving rise to the right to terminate has been reached.

60. It will usually be preferable for the termination clause to set forth a specific time period, rather than merely requiring the terminating party to wait a "reasonable time". A specific time period avoids uncertainty as to whether in a given case the time was reasonable. The appropriate length of time will vary depending upon the grounds invoked for termination; but this can be taken into account by setting forth different time periods for different grounds.

61. If it is the intention of the parties that performance may be suspended during the time period, then this should be expressly set forth in the contract. Otherwise the parties may be obligated to proceed with performance during this period.

62. The parties should consider whether a party should lose its rights to terminate if it does not exercise its right when it becomes entitled to do so (i.e. immediately upon the occurrence of a ground for termination or upon the lapse of a period of time). Four possible approaches exist in this regard. First, the termination clause could provide that the party loses its right to terminate if it does not do so immediately upon entitlement. (This will not usually be a desirable approach). Second, the clause could provide that the party loses its right if it does not terminate within a specified time period or within a reasonable time after entitlement (see paragraph 58, above). Third, the clause could permit a party to exercise a right to terminate at any time but provide that a delay of an excessive amount of time in doing so will require the terminating party to compensate the terminated party for any damages suffered as a result of the delay. Fourth, the clause could provide that a failure to terminate upon entitlement will result in a loss of the right in respect of certain grounds (perhaps, for example, the breach of an obligation concerning subcontracting (see paragraph 28, above)), but not others.

2. Notice

63. The contract should expressly require any notice to be given by one party to another to be in writing. It may also set forth requirements as to the contents of the notice, such as the requirement that the notice clearly specify the grounds for termination, and perhaps the measures which the non-terminating party must take in order to cure the grounds and the time period within which such measures must be taken. If an initial notice requires a non-performing party to perform or remedy a defect within a specified time period, the notice should state whether the termination will take place (upon a failure of the party to perform or remedy) automatically upon the expiration of the time period, or whether an additional notice of termination will be given at that time.

64. The contract should specify the method for delivering the notice to the non-terminating party, such as registered mail, telegram, telex or delivery by hand, and the time when the notice takes effect (e.g. upon receipt, or despatch). It should also specify the addresses of the parties to which all notices are to be sent.

3. Establishment of grounds

65. The parties should consider whether a party may terminate the contract upon its own assessment that grounds for termination exist, or whether the existence of grounds for termination must be verified by some third party. In contracts in which an engineer plays a supervisory role, certification of grounds by the engineer would help to avoid disputes as to the existence of such grounds. A determination or certification

by a third party of the existence of grounds for termination should not restrict the ability of a court or arbitral tribunal to determine the existence of such grounds.

66. In some legal systems a contract can be terminated only by judicial consent unless the contract expressly authorizes a party to terminate without such consent. Therefore, unless the parties desire termination to be subject to judicial authorization, it is advisable for the termination clause to specify that the contract may be terminated without requiring the consent of any court.

E. Rights and obligations of the parties upon termination

67. Difficulties connected with the termination of a works contract relate not only to the physical operations of winding up the works by the contractor and withdrawing from the site, but also to the reconciling of financial accounts between the parties, and the allocation of their rights and obligations.

68. As discussed below, some consequences of termination may differ depending upon whether or not the contract is terminated because of circumstances within the responsibility of a party (see note 12).

1. Cessation of work by the contractor

69. Upon termination by either party the obligation of the contractor with respect to construction should cease. While this might seem to be self-evident, it is nevertheless worthwhile for the termination clause to contain an express provision to that effect. Furthermore, it would be advantageous to specify that the contractor must cease issuing purchase orders, subcontracting or incurring other obligations to third parties in respect of the work.

70. In many instances it will not be feasible or advisable for the contractor simply to "lay down his tools" and leave the site at the moment termination takes effect. Certain operations in progress may have to be completed, and measures may have to be taken to protect or secure various elements of the partially completed works. It is therefore advisable for the contract to allow the contractor to take such measures as are necessary in connection with the stoppage of work, even after the termination date. The contract might go further and obligate the contractor to take such measures.

71. The contract should also expressly require the contractor and persons or firms employed by him to vacate the site without delay once all work has finally stopped, or when ordered to do so by the purchaser.

2. Completion of work by the purchaser

72. In most cases, when the purchaser terminates a works contract he will wish to make other arrangements to have the work completed. Often, the purchaser will wish to employ another contractor to complete the work. As discussed below (see paragraph 83), the costs of completing the work will in some cases be chargeable to the terminated contractor. The parties may therefore wish to consider having in the contract set forth requirements concerning the selection of a new contractor directed toward keeping these costs at a reasonable level. The contract could stipulate the extent to which the purchaser must mitigate or minimize the cost of completing the work.

3. Use and disposition of contractor's equipment and materials

73. In the construction of some works it might be important for a purchaser or the new contractor to be able to use plant, equipment and materials belonging to the original contractor in order to continue the work. If so, the termination clause should expressly authorize this. The parties should also consider whether the purchaser should be charged a rental for this use, and the extent of the purchaser's responsibility for the contractor's equipment. One factor which may be relevant to these issues is whether the termination is due to circumstances within the responsibility of one party or the other (see note 12). The parties should also consider what the position should be if termination is due to exempting impediments (see chapter "Exemptions").

74. The contract should also provide for the disposition of the contractor's plant and construction equipment when the contractor stops work, or, if the purchaser is to use them, when the work is completed. In particular, if the plant and equipment are not to be used in continuing the construction or if the purchaser is not otherwise given rights in respect of them, it is important for the contractor to remove them from the site so as not to interfere with the completion of the work.

75. A number of arrangements are possible with respect to the disposition of the contractor's plant and equipment when they are not to be used by the purchaser. For example, the contractor may be obligated to remove them from the site within a certain period of time. If he fails to do so, the purchaser could be empowered to have them removed at the contractor's expense, or sell them through appropriate means and apply the proceeds toward sums owed to the purchaser by the contractor.¹⁵ Alternatively, if the contractor fails to remove his plant and equipment, ownership of them could be deemed to pass to the purchaser in the nature of a contribution towards sums owed to the purchaser. The purchaser could also be given a right to retain the plant and equipment as security against sums due to him from the contractor, or to purchase them at a price to be agreed by the parties or established by an independent valuer, or at its market value. Parties should be aware, however, that these approaches may be subject to or restricted by mandatory rules of applicable law; parties should therefore take such rules into account in drafting provisions such as these.

4. Assignment of third-party contracts and assumption of liability

76. Very often when termination occurs there will exist outstanding contracts which the contractor has entered into in his own name with subcontractors and suppliers. If the work is to be completed by the purchaser or by another contractor, the purchaser may wish to take over some of these contracts. Alternatively, he or the new contractor may wish to enter into new contracts with these subcontractors or suppliers. This may be the case if the original contract was not assignable, or if the purchaser or new contractor does not wish to take over all of the obligations due from the terminated contractor to the subcontractors or suppliers by taking an assignment of the contracts. The conclusion of such new contracts will be practicable only if the subcontractors or suppliers are released from their contracts with the contractor. Therefore parties should consider obligating the contractor to assign such contracts, if assignment is possible, or to terminate them, in accordance with the instruction of the purchaser.

¹⁵See United Nations Convention on Contracts for the International Sale of Goods (A/CONF.97/18, annex 1, art. 88) (Yearbook ... 1980, part three, I, B).

77. When assignment of a contract or a new contract with a subcontractor or supplier is contemplated, difficulties may arise because of sums owed to such third parties by the contractor. The third party may not wish to continue his participation in the project unless past sums owed to him by the original contractor are paid. Furthermore, the third party may refuse to deliver items which were contracted for prior to termination but for which payment has not yet been made, or even take back materials which have already been delivered. The purchaser may therefore want the authority to pay the third party directly for past-due sums owed by the original contractor, and charge these payments against the original contractor. If the purchaser accepts an assignment of the third party contract, he will under most legal systems be obligated to pay these past-due sums. The contract should expressly authorize such direct payments and permit them to be charged against the contractor.

78. The contractor could incur penalties or other expenses as a consequence of terminating his contracts with third parties. In addition, the purchaser may have contracted with other contractors or suppliers, and these contracts will have to be terminated if it is impossible to complete the work, possibly resulting in penalties or expenses. The parties should consider who is to bear these expenses. If termination was due to circumstances within the responsibility of one party or the other, one way to resolve this question is to have the responsible party bear the expenses. If termination was due to a situation not within the responsibility of either party, each party could bear his own expenses, or they could be shared by the parties.

5. *Drawings and descriptive documents*

79. If the purchaser intends to complete the work left unfinished by the terminated contractor it will be important for the purchaser to have the drawings, designs, calculations, descriptions, documentation for know-how and engineering and other materials relating to the work which has been completed by the contractor, as well as for work yet to be completed. The contract should therefore obligate the contractor upon termination to deliver to the purchaser such of these materials as are in the possession of the contractor. The purchaser might be required to compensate the contractor for materials relating to work in respect of which the contractor has not been or will not be paid.

6. *Payments to be made by one party to the other*

80. The contract should establish the financial rights and obligations of each party upon termination. In principle this will usually depend upon whether termination is due to circumstances within the responsibility of one party or the other.

81. The termination clause should provide that upon termination by either party the purchaser should make no further payments to the contractor—even payments which are then outstanding for work which has been completed. These sums should be credited to the contractor in the final reckoning.

(a) *Termination arising from circumstances within the responsibility of the contractor*

82. If the contract is terminated for grounds within the responsibility (see note 12) of the contractor he should not be entitled to payment for work which he has not yet performed.

However, it will usually be considered appropriate for him to receive some payment for work which he performed satisfactorily prior to termination. Such payment would include the costs incurred by the contractor in performing this work, as well as the cost of materials which have been paid for by the contractor and delivered to the site but not yet incorporated in the works, constructional or temporary works which will remain on the site and continue to be of use in completing the works and reimbursement for obligations reasonably incurred by the contractor prior to termination (such as materials ordered). The parties should consider whether and in what circumstances the contractor should also be entitled to an amount over and above his costs in respect of the work performed, in the nature of a fee or profit. If the work performed by the contractor is not of use or value to the purchaser, the parties may consider that the purchaser should not be obligated to pay any sum for that work.

83. On the purchaser's side, he may incur expenses in connection with the termination which he would not have incurred had the contract not been terminated and had the work been completed by the contractor. For example, the purchaser may have to have temporary work done to secure or protect the partially completed works until construction can resume, or, if it is impossible to complete the works, he may incur penalties or expenses in connection with the termination of contracts with other contractors or suppliers. In addition, the cost of completing the work not performed by the terminated contractor could very likely exceed the amount which under the contract would have been due to the contractor in respect of that work. If termination is due to circumstances within the responsibility of the contractor, the parties may consider it reasonable for the contractor to be obligated to the purchaser for these costs.

84. The purchaser could suffer other losses in connection with the termination. For example, the process of selecting and employing a new contractor to complete the work could delay its completion. So too could the time required for the new contractor to integrate himself in the project and continue from where the terminated contractor left off. The parties might consider that these and other losses suffered by the purchaser in connection with the termination should be compensated by the contractor. In addition, any damages owed by the contractor to the purchaser should be taken account of in the final reckoning (see chapter "Damages").

85. The costs which the purchaser incurs to complete the work will not be known until the work is in fact completed. Moreover, damages owed by the contractor for defects in work performed may not be finally determined until the expiration of the guarantee period. For these reasons, the parties might agree that the final reckoning, and the payment of any sum due to the contractor from the purchaser, should not occur until the work has been completed, the guarantee period has expired, and all expenses and damages can be calculated.

(b) *Termination arising from circumstances within the responsibility of the purchaser*

86. If the termination occurs due to circumstances within the responsibility of the purchaser, the contractor should receive his costs and a fee for the work which he has satisfactorily completed, and reimbursement for obligations reasonably incurred in anticipation of completing the works (as for materials ordered). The parties may consider that he should also be reimbursed for his extra expenses occasioned by the termination. These could include, for example, the costs of any measures required to be taken or requested by the purchaser to secure or protect the works, the cost of

repatriating his personnel and equipment¹⁶ and damages for terminating contracts with subcontractors or other third parties.

87. The contractor should be entitled to compensation for other losses, such as the profit he would have earned if he were able to complete the entire contract. The amount of such compensation could be delimited, such as by restricting the contractor's entitlement to the contract price less the costs saved to the contractor by not having to perform the rest of the contract, or to a liquidated sum.

(c) *Termination arising from circumstances not within the responsibility of either party*

88. If the contract is terminated for reasons outside the responsibility of either party the contractor should normally be entitled to his costs and a fee in respect of the work satisfactorily completed, and reimbursement for obligations reasonably incurred in the expectation of completing the contract. The parties should consider, however, the most equitable way to deal with their respective expenses occasioned by the termination. One possibility is to share these expenses equally or in accordance with an agreed formula. Another possibility is for each party to bear his own expenses. The purchaser should not be required to compensate the contractor for profit lost by being unable to complete the contract.

(d) *Termination for convenience*

89. Contracts permitting a purchaser to terminate at his convenience generally require him to compensate the contractor fully for work performed prior to the termination, including reasonable profit for that work, as well as for costs incurred by the contractor incidental to the termination, such as the costs of repatriating his equipment and personnel (to the extent that such costs are not already included in the

price), the costs of terminating his contracts with subcontractors and suppliers, and the cost of items in the process of manufacture or delivered to the site but not yet paid for. On the other hand, the contractor is usually not entitled to be compensated for lost profit on the portion of the contract remaining to be performed.

90. Under some contracts at the time when the contract is terminated for convenience the purchaser may have received the design for the works from the contractor, but this may not yet have been adequately reflected in the price which would be due to the contractor if this price were based upon the work which the contractor had performed. In cases in which this might be a problem, the contract could specify that the purchaser must compensate the contractor for the design insofar as such compensation is not otherwise reflected in the price due to the contractor.

7. *Parties' rights to damages and other remedies*

91. The parties should carefully consider the relationship between remedies under the contract and remedies under the applicable law (see paragraph 3, above). The contract should state clearly whether a party is entitled to remedies both under the contract and the applicable law, or only to remedies under the contract.

92. In some legal systems termination of the contract might be interpreted as bringing to an end all contractual provisions, including those which the parties might wish to survive, such as the rights and obligations of the parties upon termination, guarantees for work performed, and provisions such as those concerning settlement of disputes and the preservation of confidentiality. The parties should take care to ensure that rights, obligations and remedies which they wish to survive do not lapse upon termination. To do so, the parties should specify in the contract those provisions which will survive and continue to bind the parties even after termination (see paragraph 7, above).

¹⁶To the extent that this has not already been included in the price.

V. CO-ORDINATION OF WORK^a

A. Report of the Secretary-General: co-ordination of work in general (A/CN.9/239)^b

Introduction

1. In its resolution on the report of the Commission on the work of its fifteenth session, the General Assembly reaffirmed the mandate of the Commission to co-ordinate legal activities in the field of international trade law in order to avoid duplication of efforts and to promote efficiency, consistency and coherence in the unification and harmonization of international trade law (resolution 37/106 of 16 December 1982, paragraph 7). The main activities undertaken for the purpose of co-ordination since the fifteenth session of the Commission are set forth below.

Co-ordination of work

2. There was a strong response by international organizations requested to provide information for the report of the Secretary-General on current activities of international organizations related to the harmonization and unification of international trade law (A/CN.9/237 and Add. 1 to 3).^c This is a further indication of the recognition that the Commission is the core legal body for the unification and harmonization of international trade law.

3. At the invitation of the Swiss Government a diplomatic conference was held at Geneva from 31 January to 17 February 1983 and the Convention on Agency in the International Sale of Goods was adopted on the basis of a draft text prepared by the Committee of Governmental Experts of the International Institute for the Unification of Private Law (UNIDROIT), which met at Rome from 2 to 13 November 1981. At the invitation of UNIDROIT, States members of UNCITRAL that are not members of UNIDROIT attended that meeting to consider the draft (see A/CN.9/237/Add.2).

4. The meeting of the Special Commission of the Hague Conference on Private International Law, held from 6 to 15 December 1982 at The Hague to consider the revision of the 1955 Convention on the Law Applicable to International Sale of Goods, was attended by representatives of 25 Hague Conference members and 11 States members of UNCITRAL which are not members of the Conference. Representatives of the

UNCITRAL secretariat, the Council of Europe and the International Chamber of Commerce (ICC) were also in attendance. The States elected as new members of UNCITRAL will be invited to attend the next meeting of the Special Commission from 7 to 18 November 1983, along with the States members of UNCITRAL which participated in the previous meeting (see A/CN.9/237/Add.1, paragraphs 1 to 4).

5. The UNCITRAL draft model law on international commercial arbitration^d will be the main theme at the Interim Congress of the International Council for Commercial Arbitration (ICCA) to be held at Lausanne in 1984. In order to ensure that, to the greatest extent possible, the draft model law reflects the concerns and needs of international commercial arbitration practice, an informal consultation will be held at Lausanne on 7 May 1983 with members of ICCA.

6. There has been a favourable response to the "Recommendations to assist arbitral institutions and other interested bodies with regard to arbitrations under the UNCITRAL Arbitration Rules", which were adopted at the fifteenth session of the Commission. A number of arbitral institutions have written asking for comments or advice on their intended procedures, to which the secretariat has responded.

7. The International Law Association, at its 60th Conference held at Montreal from 29 August to 4 September 1982, on the recommendation of its Committee on International Commercial Arbitration adopted a resolution supporting the efforts to promote commercial arbitration as a method of settling business disputes in developing countries, and especially the efforts at present being undertaken by national legislatures and UNCITRAL to achieve the necessary adaptations of national laws.

8. The European Committee on Legal Co-operation of the Council of Europe, at its 28th session held at Strasbourg from 29 November to 3 December 1982, decided, after hearing a statement from the Secretary of UNCITRAL, to await the outcome of the work in UNCITRAL on the draft Convention on International Bills of Exchange and International Promissory Notes^e and the draft Convention on International Cheques^f

^aFor consideration by the Commission see Report, chapter VI (part one, A).

^b27 April 1983. Referred to in Report, para. 94 (part one, A).

^cReproduced in this volume, part two, V, B.

^dA/CN.9/246 (6 March 1984) which will be reproduced in Yearbook ... 1984.

^eYearbook ... 1982, part two, II, A, 3 (A/CN.9/211).

^fYearbook ... 1982, part two, II, A, 5 (A/CN.9/212 and Corr. 1) (Spanish only).

before it considers further the desirability of revising the 1930 Geneva Convention providing a Uniform Law for Bills of Exchange and Promissory Notes and the 1931 Geneva Convention providing a Uniform Law for Cheques. It was noted that many of the problems encountered with the Geneva Conventions were treated by the UNCITRAL draft texts.

9. Co-ordination continued with ICC on the revision of the ICC Uniform Customs and Practice for Documentary Credits. On 16 August 1982 the UNCITRAL secretariat sent a note verbale to all Governments enclosing the then current draft of the revision with a request for comments. The comments received were forwarded to the ICC for its consideration. The UNCITRAL secretariat has been represented at the meetings of the ICC Commission on Banking Technique and Practice at which the revision is being considered. A final draft has been circulated to members of the ICC Commission and to the ICC National Committees in the expectation that it can be submitted to the ICC Council for adoption in June 1983 with an effective date of 1 October 1984.

10. The International Law Association, at its 60th Conference held at Montreal from 29 August to 4 September 1982, on the recommendation of its Committee on International Monetary Law, welcomed the decision of UNCITRAL taken at its fifteenth session to adopt a preferred universal unit of account based on the special drawing right (SDR), particularly for conventions of global application, and two alternative provisions for the adjustment of the limit of liability in transport and liability conventions.

11. Several international organizations, including the Bank for International Settlements (BIS) and the International Monetary Fund (IMF), have been co-operating with the UNCITRAL secretariat in the work on electronic funds transfers. The UNCITRAL secretariat was invited to a meeting of legal advisors of the central banks of the Group of Ten and Switzerland held by BIS at Basle on 20 and 21 October 1982 to discuss the project.

12. A working group of the ICC Commission on International Contract Practices is preparing a commentary on the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980)⁸ aimed at giving practical advice to parties involved in negotiating and drafting international sales contracts in the context of the Convention. This is based on an anticipation that the Convention will enter into force in the near future.

13. The Working Party on Facilitation of International Trade Procedures, sponsored by the Economic Commission for Europe (ECE) and UNCTAD, transmitted to UNCITRAL through the Executive Secretary of ECE a study on legal aspects of automatic trade data interchange. The Working Party concluded that, since the problems primarily concerned international trade

law, UNCITRAL would appear to be the central forum to establish rules regarding legal acceptance of trade data transmitted by telecommunications. The study and the letter from the Executive Secretary of ECE are reproduced in A/CN.9/238.⁹

14. At the Expert Group meeting at Vienna from 14 to 18 February 1983 to consider the secretariat drafts of sample chapters of the draft legal guide on drawing up contracts for the construction of industrial works,¹ representatives of the United Nations Industrial Development Organization (UNIDO), the Centre for Transnational Corporations (CTC), the Economic and Social Commission for Asia and the Pacific (ESCAP), the World Bank, the Asian Development Bank and the International Federation of Consulting Engineers (FIDIC) participated as observers.

15. The UNCITRAL secretariat was represented at a meeting organized by UNIDO and the International Centre for Public Enterprises in Developing Countries (ICPE) held at Ljubljana, Yugoslavia from 11 to 15 April 1983, on guarantees in contracts for the transfer of technology. The ICPE is a joint institution of developing countries devoted to the cause of public enterprise in those countries. It has at present a membership of 33 countries. It is planned to collaborate with ICPE in areas of common interest in the legal field.

16. The UNCITRAL secretariat was represented at a meeting of the ECE Expert Group on International Contract Practices in Industry, held at Geneva from 13 to 15 December 1982, at which the Expert Group decided to prepare a legal guide for drawing up international contracts on services relating to maintenance, repair and management of industrial works. The Expert Group noted that, although these items would also be dealt with in the UNCITRAL legal guide in connection with construction contracts, these services were often supplied by consulting engineers or other parties independently of a construction contract. Nevertheless, the view was held that, because of the close connection between the two projects, it would be advisable to co-ordinate work between the Expert Group and UNCITRAL.

17. The draft agenda for the Third Inter-American Specialized Conference on Private International Law (CIDIP-III), which will be held at Washington, D.C. at the end of 1983 or during the first months of 1984, includes an item on international maritime transportation. In the resolution of the Permanent Council of the Organization of American States which adopted the draft agenda (CP/Res. 376 (510/82) of 10 November 1982) it was stated that:

"In regard to the topic on international maritime transportation, due consideration was given to the United Nations Conference on the Carriage of Goods by Sea, held on March 6

⁸Yearbook ... 1980, part three, I, B (A/CONF.97/18, annex I).

⁹Reproduced in this volume, part two, V, D.

¹Reproduced in this volume, part two, V, B.

through March 31, 1978, which approved the 'United Nations Convention on Carriage of Goods by Sea' and at which 14 member states of the Organization of American States were represented, some of which have already signed, ratified or acceded to the Convention."

18. In General Assembly resolution 37/103 of 16 December 1982 the Commission was requested to continue to submit relevant information to, and to co-operate fully with, the United Nations Institute for Training and Research (UNITAR) in its study on

^aYearbook ... 1978, part three, I, B (A/CONF.89/13, annex 1).

progressive development of the principles and norms of international law relating to the new international economic order. Information on relevant activities of the Commission was supplied by the secretariat to UNITAR for use in its study.

19. Further, besides collaboration envisaged with other international organizations in the field of training and assistance (see A/CN.9/240),^k the UNCITRAL secretariat has been in contact with these organizations with a view to ascertaining possibilities for further co-ordination in other areas of common interest.

^kReproduced in this volume, part two, VII.

B. Report of the Secretary-General: current activities of international organizations related to the harmonization and unification of international trade law (A/CN.9/237 and Add.1-3)^a

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^aReferred to in Report, para. 105 (part one, A).

^b28 April 1983.

^c13 April 1983.

^d27 April 1983.

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[A/CN.9/237]^a

Introduction

1. The General Assembly in resolution 34/142 of 17 December 1979, requested the Secretary-General to place before the United Nations Commission on International Trade Law, at each of its sessions, a report on the legal activities of international organizations in the field of international trade law together with recommendations as to the steps to be taken by the Commission to fulfil its mandate of co-ordinating the activities of other organizations in the field.

2. At its fourteenth session in 1981, a detailed report on current activities of other organizations related to the harmonization and unification of international trade law was submitted (A/CN.9/202 and Add. 1 to 4)^b in response to the General Assembly resolution mentioned above. At that session the Commission was in agreement that the co-ordination of work in international trade law depended upon an exchange of information, and that the report was useful for this purpose.^c

^aYearbook ... 1981, part two, V, A.

^bReport of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17 (A/36/17)*, para. 100 (Yearbook ... 1981, part one, A).

3. At the fifteenth session, the Commission repeated its desire that such a report be submitted at regular intervals. The Commission was informed that the report was of particular interest to government ministries, especially those in developing countries. Some Governments circulated the report to their ministries and the information contained therein enabled the Governments to co-ordinate their approach in different fora.²

4. Accordingly, this report has been prepared to update and supplement the report submitted at the fourteenth session. The report is based on information received from international and other organizations concerning their current activities. Such information appears in addenda 1 to 3 of this report.

5. The work of the following organizations is described in the present report:

(a) *United Nations bodies and specialized agencies*

CTC	Centre on Transnational Corporations A/CN.9/237/Add.1, paras. 61, 67-70
CTN	Commission on Transnational Corporations A/CN.9/237/Add.1, paras. 63-65, 69-72
ECA	Economic Commission for Africa A/CN.9/237/Add.2, para. 139
ECE	Economic Commission for Europe A/CN.9/237/Add.1, paras. 13-15, 24-28, 48-49 A/CN.9/237/Add.2, paras. 17-19, 40-41, 120-124, 139-152, 154
ECLA	Economic Commission for Latin America A/CN.9/237/Add.2, paras. 41, 120-124, 137
ESCAP	Economic and Social Commission for Asia and the Pacific A/CN.9/237/Add.1, para. 19 A/CN.9/237/Add.2, paras. 28-30, 84-86
FAO	Food and Agriculture Organization A/CN.9/237/Add.1, paras. 41-42, 61-62 A/CN.9/237/Add.2, para. 153
GATT	General Agreement on Tariffs and Trade A/CN.9/237/Add.2, paras. 110-112, 137

IAEA	International Atomic Energy Agency A/CN.9/237/Add.2, para. 108
ILO	International Labour Organisation A/CN.9/237/Add.1, paras. 55, 66, 77, 90 A/CN.9/237/Add.2, paras. 22, 107-108
IMO	International Maritime Organization A/CN.9/237/Add.2, paras. 9, 14-18, 38, 146
UNCITRAL	United Nations Commission on International Trade Law A/CN.9/237/Add.1, paras. 2-4, 26 A/CN.9/237/Add.2, paras. 37, 55
UNCTAD	United Nations Conference on Trade and Development A/CN.9/237/Add.1, paras. 33-40, 52, 73-75, 77-78 A/CN.9/237/Add.2, paras. 1, 3-5, 7, 10, 21, 36-38, 84-86, 89, 103-106, 140-149, 152
UNDP	United Nations Development Programme A/CN.9/237/Add.2, para. 29
UNEP	United Nations Environment Programme A/CN.9/237/Add.2, paras. 76-80
UNESCO	United Nations Educational, Scientific and Cultural Organization A/CN.9/237/Add.1, paras. 90, 95-99 A/CN.9/237/Add.2, paras. 68-71, 113
UNIDO	United Nations Industrial Development Organization A/CN.9/237/Add.1, paras. 43-44, 50-54, 72, 80
UNSO	United Nations Sudano-Sahelian Office A/CN.9/237/Add.2, para. 128
WHO	World Health Organization A/CN.9/237/Add.2, paras. 82-83
WIPO	World Intellectual Property Organization A/CN.9/237/Add.1, paras. 76, 79, 81-94, 96-97

²Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17 (A/37/17)*, para. 107 (Yearbook ... 1982, part one, A).

(b) Other intergovernmental Organizations

AALCC	Asian-African Legal Consultative Committee A/CN.9/237/Add.1, paras. 16-18, 45
CARICOM	Caribbean Community A/CN.9/237/Add.1, para. 100 A/CN.9/237/Add.2, paras. 2, 32, 64-65, 137
CCC	Customs Co-operation Council A/CN.9/237/Add.2, paras. 41, 124-139, 146
CE	Council of Europe A/CN.9/237/Add.1, para. 3 A/CN.9/237/Add.2, paras. 50-51, 59-62, 72-75, 81
CEAO	Communauté économique de l'Afrique de l'Ouest (West African Economic Community) A/CN.9/237/Add.2, paras. 126, 137
CEC	Commission of the European Communities A/CN.9/237/Add.1, para. 31 A/CN.9/237/Add.2, paras. 6, 59, 124, 137 A/CN.9/237/Add.3
CMEA	Council for Mutual Economic Assistance A/CN.9/237/Add.1, paras. 20-23, 46-47, 59-60, 107-108 A/CN.9/237/Add.2, paras. 39, 48, 109, 114-115
ECOWAS	Economic Community of West African States A/CN.9/237/Add.2, para. 137
EFTA	European Free Trade Association A/CN.9/237/Add.1, para. 56 A/CN.9/237/Add.2, para. 137
LAIA	Latin American Integration Association A/CN.9/237/Add.2, para. 124
SOEC	Statistical Office of the European Communities A/CN.9/237/Add.2, para. 128
The Hague Conference	The Hague Conference on Private International Law A/CN.9/237/Add.1, paras. 1-4, 76 A/CN.9/237/Add.2, paras. 53, 63
UNIDROIT	International Institute for the Unification of Private Law A/CN.9/237/Add.1, paras. 5-12

A/CN.9/237/Add.2,
paras. 19-20, 23-26, 35, 52,
54-57, 66-71,
90-102

(c) Non-governmental organizations

FIATA	Fédération internationale des associations de transitaires et assimilés (International Federation of Freight Forwarders Associations) A/CN.9/237/Add.2, paras. 8, 146
FIDIC	Fédération internationale des ingénieurs conseils (International Federation of Consulting Engineers) A/CN.9/237/Add.1, para. 71
IATA	International Air Transport Association A/CN.9/237/Add.2, para. 146
ICC	International Chamber of Commerce A/CN.9/237/Add.1, paras. 3, 29-30, 57-58, 101-106 A/CN.9/237/Add.2, paras. 11-12, 42-45, 47, 58, 87-88, 116-117
ICCA	International Council for Commercial Arbitration A/CN.9/237/Add.2, paras. 48-49
ICS	International Chamber of Shipping A/CN.9/237/Add.2, para. 146
Institute of International Business Law and Practice	A/CN.9/237/Add.1, para. 30 A/CN.9/237/Add.2, para. 45
IRU	International Road Transport Union A/CN.9/237/Add.2, paras. 124, 126
ISO	International Organization for Standardization A/CN.9/237/Add.2, paras. 38, 140-143, 146
UIC	Union internationale des chemins de fer (International Union of Railways) A/CN.9/237/Add.2, para. 146
UNICE	Union des industries de la Communauté européenne (Union of the Industries of the European Communities) A/CN.9/237/Add.2, para. 137

[A/CN.9/237/Add.1]^a

1. *International contracts*

A. INTERNATIONAL SALES OF GOODS

1. At its fourteenth session in October 1980, the Hague Conference on Private International Law decided to include in its agenda the revision of the 1955 Convention on the Law Applicable to International Sales of Goods.^b The Secretary General of the Conference convened a Special Commission in June 1981 to determine the best way of bringing about participation in this work by States which are not members of the Conference. That Commission decided that the preparatory work should be done by Special Commissions in which all States members of UNCITRAL which are not members of the Conference would be invited to participate along with Conference members, and that the final text of the revised Convention should be established at a diplomatic conference to be held at The Hague with all States invited to participate.

2. The decision taken by the Special Commission of June 1981 was communicated to the secretariat of UNCITRAL, and UNCITRAL in the Report on the work of its fourteenth session (19-26 June 1981) welcomed the Conference's initiative and encouraged States members of UNCITRAL to participate in this work.

3. Invitations were sent out to all Conference members and all UNCITRAL States members in July 1982 for a first Special Commission meeting, to be held from 6 to 15 December 1982, at The Hague. At that meeting representatives of 25 Hague Conference members and of 11 UNCITRAL States members which are not members of the Conference were in attendance. Representatives of the following organizations attended as observers: the UNCITRAL secretariat, the Council of Europe and ICC.

4. The next meeting of the Special Commission will be held from 7 to 18 November 1983. The new States members elected to UNCITRAL will also be invited to participate, along with the States members of UNCITRAL which have already participated. It is expected that, if a viable draft is produced by the end of the second Special Commission meeting, a diplomatic conference will be called to meet at The Hague in October 1985 to prepare the final text of the revised Convention.

B. PROGRESSIVE CODIFICATION OF INTERNATIONAL TRADE LAW

5. At its first session, held at Rome from 10 to 14 September 1979, the UNIDROIT Study Group on the Progressive Codification of International Trade Law focused its attention principally on the drafts on

formation and interpretation which, it was decided, the secretariat should revise in the light of the proposals for amendment and of the new suggestions made. The Group also agreed that it was opportune to deal in the next chapter of the Code with the problem of validity of contracts in general, in which connection it was considered that the work already carried out by the Institute in this field could serve as a starting point and that, in the future draft, specific rules on the validity of general conditions and standard forms of contracts should be added. As to the proposed chapters on performance and non-performance of contracts, the Group requested the President of UNIDROIT to set up special subcommittees for their preparation in view of their extreme complexity.

6. Two informal meetings of the Working Group were subsequently held, the first at Copenhagen on 31 March and 1 April 1980 and the second at Hamburg from 23 to 25 February 1981. The Copenhagen meeting was essentially of an exploratory character while at Hamburg the Group considered two preparatory studies. The first of these aimed at the clarification and completion of the existing UNIDROIT draft of a law for the unification of certain rules relating to validity of contracts of international sale of goods of 1972, so as to adapt it to the requirements of international commercial contracts in general while the second investigated the possibility of dealing with the problem of illegality of international commercial contracts in the framework of the future Code.

7. The draft rules included a number of new provisions as compared with the 1972 UNIDROIT draft in order to cover important questions such as unequal bargaining power, gross unfairness and the right of adaptation, while in addition the remaining part of that draft was revised in the light of recent developments in international legislation and case-law. As to the draft rules on prohibition and licences requirements, these constitute the first attempt to deal with the problem in a general and systematic manner at international level.

8. The revised texts of the draft sets of rules were considered by the Study Group at its second session, held at Rome from 5 to 9 April 1982.

9. As to the first draft, the attention of the Study Group was mainly concentrated on the new provisions on abuse of unequal bargaining power, gross unfairness and the right of adaptation. While all the participants agreed on the necessity of the future Code dealing with these questions, different views were expressed as to the content of some of the provisions contained in the draft. After an exhaustive discussion the Group reached substantial agreement on the amendments which should be incorporated in the final version in order to make it generally acceptable.

10. Some members expressed doubts as to whether the future Code should contain provisions on the so-called public prohibitions and permission requirements relating to international commercial contracts, although

^a13 April 1983.

^bUnited Nations, Treaty Series, vol. 510, No. 7411 (1964), p. 149.

the great majority was of the opinion that the various problems which in practice arise in connection with State prohibitions and permission requirements relating to international contracts were too important to be totally disregarded by the Code. As to the draft which had been submitted to the Group, proposals were submitted for amending or at least clarifying the text of several articles while attention was also drawn to the need for better co-ordination between the general approach adopted in the draft on public prohibitions and permission requirements and some of the provisions contained in the other draft on the substantive validity of international contracts.

11. At the end of the session the Study Group decided that on the basis of its discussions a revised text of the two drafts of chapter III (validity) of the Code should be prepared by the informal Working Group and that this text, together with those of chapters I (formation) and II (interpretation) could be submitted to it for final approval at its next session.

12. The informal Working Group will also be seized of a collection of materials relating to performance and non-performance which contains some 40 international Conventions and uniform laws, as well as general conditions and standard forms of contract relating to international contracts in general and the various kinds of contracts of sale, including contracts for the supply and construction of large industrial plant and machinery, which have been assembled by the secretariat.

C. COUNTER-TRADE PRACTICES

13. At its thirty-first session held in December 1982, the ECE Committee on the Development of Trade devoted attention to developments in the field of compensation trade. The basis for discussion was the report of the *Ad Hoc* Meeting on Compensation Trade (TRADE/AC.18/2) held at Geneva from 9 to 13 November 1981 and on 30 November 1981; and a note by the secretariat containing updated information relevant to compensation trade in the ECE region. Compensation agreements were generally considered to be an increasingly prevalent element in east-west trade. Analysing the impact of compensation transactions on the development of east-west trade, a number of delegations referred to the problems raised by the increasing frequency of this type of transaction and stressed that such problems were particularly acute in the case of small and medium-sized enterprises since they did not have the same absorptive capacities as large enterprises. Other delegations stressed that these agreements, particularly those of a long-term and a large-scale nature, had exerted a beneficial impact on the development of trade between interested countries.

14. The Committee decided to convene a special experts' meeting on compensation trade in 1983 and to revert, at its thirty-second session (in December 1983), to discussion of the problem of compensation transactions in all their forms.

15. The ECE secretariat prepared a series of studies dealing with reciprocal trading arrangements in east-west trade: (i) "Large-scale and long-term compensation agreements in east-west trade" (TRADE/AC.18/R.1); (ii) "Short and medium-term linked transactions in east-west trade" (TRADE/AC.18/R.3); (iii) "Reciprocal trading arrangements at the western enterprise level, with special reference to east-west trade" (TRADE/AC.18/R.2); (iv) "East-west co-operation in the automotive sector and reciprocal trading arrangements"; and (v) "Reciprocal trading arrangements in the chemicals industry: the experience of selected western chemicals producers and plant contractors in east-west trade" (in *Economic Bulletin for Europe*, Vol. 34, No. 2). Information contained in the latter publication was updated in a note by the secretariat submitted to the thirty-first session of the Committee on the Development of Trade (TRADE/R.444).

D. CONTRACT FORMS AND GENERAL CONDITIONS

1. *Standard form contracts*

16. In 1976 a Special Meeting of Experts on Standard Contracts was convened, in conjunction with the AALCC annual session, to prepare the standard form of the F.O.B. contract for sale transactions in certain types of commodities (for example, grain, rubber, oil, coconut products, spices) and the standard form of the F.A.S. contract for sale transactions in regard to the same type of commodities. These forms were approved at the annual session of AALCC in 1978 and have been widely circulated.

17. In 1979 a standard form for sale transactions in light machinery and durable goods (C.I.F.) as well as the general conditions for transactions for the purchase of the same items (C.I.F. maritime) was also prepared by the Special Meeting of Experts on Standard Contracts. AALCC approved the form and the general conditions at its session in 1980.

18. The AALCC Subcommittee on International Trade Law Matters at its meeting at Colombo (Sri Lanka) in May 1981 considered the draft of a standard form of the C and F contract intended to be used for sale transactions in light machinery and durable consumer goods prepared by the AALCC secretariat in response to a direction given by the Subcommittee at the Jakarta session held in April 1980. At that session, the Subcommittee had also directed that the secretariat, in so doing, should maintain the basic approach of the C.I.F. contract which it had adopted at that session. Keeping in view the above direction, the secretariat had maintained intact all the provisions of the C.I.F. contract in the draft contract except the provisions concerning marine insurance. The Subcommittee requested the secretariat to carry out further studies so as to reflect the current developments in the field of international trade and transport law, and that the matter could be taken up at a future session of the Committee.

2. *Contract form for pepper*

19. A consultant was recruited by the ESCAP secretariat in mid-1981 to draw up a draft contract form after examining various existing forms and holding discussions with exporters and relevant government agencies involved in the pepper trade in the International Pepper Community (IPC) member countries in the ESCAP region, namely, India, Indonesia and Malaysia. The report of the study was completed and submitted to the Seventh Technical Panel of IPC held in London in May 1982. Comments on the draft contract form have been received. The consultant visited the major pepper consuming countries during October and November 1982, and is expected to complete the second part of the study in March 1983. The report of the study will be considered by the ESCAP/IPC Meeting of Representatives of Spice/Pepper Exporters Association at Bangkok in May 1983.

3. *General conditions governing delivery of goods*

20. Since 1980 work has been continuing within the framework of the CMEA Conference on Legal Matters with a view to the study and wider application of the General Conditions Governing Delivery (GCD) of Goods Among Organizations of CMEA Member Countries (GCD CMEA 1968/1975, 1979 version). Work is being carried out on the settling of questions arising in connection with the liability of organizations for failure to comply or for inadequate compliance with their contractual obligations and on ways of dealing with complaints concerning the quality and quantity of the goods delivered. At present this research is focused on the task of improving the GCD CMEA with a view, in particular, to enhancing the buyer's rights in cases where the goods delivered fail to meet the required standards.

21. It is intended that, as in the past, proposals for the amendment and extension of the GCD CMEA will be incorporated in their final form in the above-mentioned General Conditions by decision of the CMEA Standing Commission on Foreign Trade and enforced by the member countries on the basis of a recommendation of the Commission and in accordance with each country's legislation.

4. *General conditions governing the technical standards of maintenance of machines, equipment and other goods*

22. By its decision of 21 January 1982 the CMEA Executive Committee approved the proposals prepared by the CMEA Standing Committee on Foreign Trade for the Improvement of the General Conditions Governing the Technical Standards of Maintenance of Machines, Equipment and Other Goods Delivered Among Organizations of the Member Countries of CMEA Empowered to Conduct Foreign Trade Operations (GCTS CMEA 1973). These amendments and additions, which in particular concern the question of the liability of

parties, were incorporated in these General Conditions, and are now referred to as GCTS CMEA 1973 in the 1982 version.

23. The CMEA Executive Committee recommended that the CMEA member countries bring the above-mentioned amendments and additions into force as of 1 July 1982, the intention being that the texts of the GCTS CMEA 1973 in the 1982 version should apply to all contracts drawn up between organizations of the CMEA member countries as from 1 July 1982.

5. *General conditions of sale of milk*

24. The ECE Committee on Agricultural Problems (Working Party on Standardization of Perishable Produce) is engaged in a project for the establishment of standard documents for general conditions of sale for milk and milk products with emphasis on current trade practices in Europe but with regard to potential usefulness in other regions. Technical regulations and rules on safety of products and surveillance will be included; and reference will be made to INCOTERMS. Legal issues concern, *inter alia*, responsibility of contracting parties, products liability, payments, trade documents, claims and arbitration. All these relate to private international law. The project is being implemented in co-operation with the International Dairy Federation (IDF). The general conditions will be available for use by the trade and will have the legal force of a recommendation. The general conditions have not yet been adopted; the first revised draft is currently being circulated for comments.

E. INTERNATIONAL TRADE TERMS

PAYTERMS—abbreviations for terms of payment

25. Abbreviations for terms of payment are contained in recommendation No. 17 adopted by the ECE Working Party on Facilitation of International Trade Procedures (1980 and 1982).

26. An important part of a contract of sale is the conditions under which the buyer extinguishes his debt to the seller: the terms of payment. Lack of precision in terms of payment and different interpretations of such terms are known to give rise to disputes between trade partners. For this reason, the ECE Working Party on Facilitation of International Trade Procedures, when discussing its initial comprehensive programme of work in 1972, considered that there was a need for standardization in the field of terms of payment, and agreed to initiate work in this area by preparing an inventory including definitions of the most frequently used terms relating to payments in international trade. The delegations of Austria, Belgium and Romania, later joined by that of France, agreed to act as rapporteurs for the project. Their proposal was presented to the twelfth session of the Working Party in September 1980 and was adopted at that session. Following consideration by

interested delegations and the secretariats of ECE and UNCITRAL which took place in 1981, a few drafting changes were made; these changes were endorsed by the Working Party at its fifteenth session in March 1982, and are reflected in the list of common terms annexed to the recommendation in document ECE/TRADE/142.

27. In the recommendation, the Working Party noted that no world-wide international forum for trade law had yet established standard terms of payment for international trade and drew attention to the list of PAYTERMS in the recommendation "corresponding to those conditions of payment which are the most frequently used in international trade, which can be employed when the contract of sale to which they relate makes this appropriate". The Working Party recommended that the abbreviations shown in the list of PAYTERMS be used in such contracts.

28. The Working Party requested the ECE secretariat to make the necessary arrangements for bringing up to date the list of terms of payment, when required—i.e. to review the list in order to make the terms, their descriptions and abbreviations compatible with any harmonized standard terms of payment in international trade that might be developed in the future under the auspices of a world-wide forum for international trade law.

F. MODEL CLAUSES

Force majeure and hardship clauses

29. The ICC Commission on International Commercial Practice is drafting a model clause on *force majeure* and one to cover the hardship situation, together with an explanatory introduction on the use of the clauses. It is intended that the clause may be incorporated by simple reference in an international contract.

G. TRADE USAGES

30. The Institute of International Business Law and Practice has undertaken a project on the interpretation and application of international trade usages. After scrutinizing decisions from various countries concerning international trade usages, ICC will, if necessary, propose appropriate action to be taken by ICC or other organizations. A first report has already been published by the Institute (publication number 374). The final report will be available in 1984.

H. Commodities

A. COMMODITY AGREEMENTS

31. By 1 February 1983, the Agreement establishing the Common Fund for Commodities had been signed by 93 States and the European Economic Community.

Of these States, 41 had deposited instruments of ratification, acceptance or approval. The Agreement will enter into force when it is signed and ratified, accepted or approved by at least 90 States, whose total subscriptions of shares of directly contributed capital comprise not less than two-thirds of the total allocated to the States listed in schedule A of the Agreement. The period for the fulfilment of the requirements for entry into force of the Agreement was extended until 30 September 1983.

32. Preparations are being made for bringing the Common Fund into operation. For this purpose a Preparatory Commission has been established to prepare proposals concerning matters including an outline of a model association agreement between the Fund and international commodity organizations.

33. The following commodity agreements, adopted at various United Nations Conferences under the auspices of UNCTAD, have come into force. These agreements were prepared pursuant to the objectives adopted by UNCTAD in its resolutions 93 (IV) and 124 (V) on the Integrated Programme for Commodities:

(a) International Natural Rubber Agreement, 1979 (TD/Rubber/15/Rev. 1). The Agreement entered into force provisionally on 23 October 1980 and definitively on 15 April 1982. It should remain in force until 22 October 1985, unless terminated before that date or extended for a period of not more than two years;

(b) International Cocoa Agreement, 1980 (TD/Cocoa/6/7), replacing the 1975 Agreement. It entered into force provisionally on 1 August 1981 and should remain in force until 30 September 1983, unless terminated before that date or extended for a period not exceeding two years;

(c) International Tin Agreement, 1981 (TD/Tin/6/14), replacing the 1975 Agreement. It entered into force provisionally on 1 July 1982 and should remain in force until 30 June 1987, unless terminated earlier or extended for a period not exceeding two years.

34. The above-mentioned agreements aim at the stabilization of conditions in the international trade of the commodities concerned and, hence, establish pricing and supply arrangements.

35. The International Agreement on Jute and Jute Products, 1982 (TD/Jute/11), was adopted by a United Nations conference in October 1982. The objectives of the Agreement are the improvement of structural conditions in the jute market, the enhancement of the competitiveness of jute and jute products, maintenance, and enlargement of existing markets as well as the development of new markets for jute and jute products.

36. The International Agreement on Tropical Timber was adopted by a United Nations conference in March 1983. The objectives of this Agreement are aimed at research and development, improved market intelligence, re-forestation and increased processing.

37. The United Nations Sugar Conference will be convened under the auspices of UNCTAD from 2 to 20 May 1983 to negotiate a new international sugar agreement to replace the International Sugar Agreement of 1977.

38. A United Nations conference is expected to be convened in 1983 or 1984 to negotiate an international agreement on tea. Preparatory work on other international commodity agreements pursuant to conference resolutions 93 (IV) and 124 (V) on the Integrated Programme for Commodities is continuing on the following commodities: cotton, hard fibres, manganese, bauxite, iron ore, bananas, meat, copper, phosphates, vegetable oils and seeds.

B. COMPLEMENTARY FACILITY FOR COMMODITY-RELATED SHORTFALLS IN EXPORT EARNINGS

39. The stabilization of commodity export earnings and avoidance of excessive price fluctuations with a view to maintaining price levels which would be remunerative to both producers and consumers, was envisaged as one of the principal aims of the UNCTAD Integrated Programme for Commodities (IPC), as set out in conference resolution 93 (IV). The complementary facility would be designed to achieve overall stability in the commodity sector to the extent that it responds to the residual fluctuations in earnings deriving from variations in export volumes as well as the overall earning instability of commodities that are not amenable to price stabilization through buffer stocking arrangements. This will be one of the main subjects to be considered at UNCTAD VI scheduled to be held at Belgrade in June 1983.

40. Among the recent studies made by UNCTAD are "Complementary facility for commodity related shortfalls in export earnings" (TD/B/C.1/221, TD/B/C.1/222, TD/B/C.1/234); "Review of Stabex and Sysmin" (TD/B/C.1/237); "Review of the operation of the compensatory financing facility of the International Monetary Fund" (TD/B/C.1/243).

C. INFORMAL COMMODITY ARRANGEMENTS AND GUIDELINES

1. *Informal price arrangements on hard fibres*

41. During its subsequent reviews of the informal price arrangements in March 1981 and June 1982, the FAO Intergovernmental Group on Hard Fibres decided not to change the indicative prices for sisal and abaca and agreed that the operation of the export quota system for sisal and of the trigger mechanism for automatic consultations for abaca should remain suspended.

2. *Informal price arrangements on jute, kenaf and allied fibres*

42. Although market prices of jute had remained far below the floor of the agreed price range since early 1980, the FAO Intergovernmental Group on Jute agreed in June 1981 to retain the indicative price for jute for the 1981/1982 season at its previous level. It also agreed on an indicative price range for Thai kenaf. At its session in September-October 1982, it retained the indicative price for jute and for Thai kenaf at the current level for the 1982/1983 season. It decided, however, that for jute the quotation should be expressed in metric tons and on cash terms basis; previously quotations had been in long tons and on 90 days sight terms.

III. Industrialization¹

A. UNIDO—MODEL CONTRACTS FOR THE FERTILIZER INDUSTRY

43. A UNIDO International Group of Experts met at Vienna from 23 February to 6 March 1981 to finalize the UNIDO model forms for the construction of a fertilizer plant² for (a) turnkey lump-sum and (b) cost-reimbursable contracts. It recommended to UNIDO that a further expert group meeting was required to complete discussions on a few pending articles. Accordingly, a meeting was convened at Vienna from 4 to 6 May 1981 that completed the text of both model forms of contracts, which appeared as documents: "UNIDO model form of turnkey lump sum contract for the construction of a fertilizer plant" (UNIDO/PC.25) and "UNIDO model form of cost-reimbursable contract for the construction of a fertilizer plant" (UNIDO/PC.26).

44. UNIDO has also prepared guidelines to the above model contracts to provide some guidance for their use by purchasers in developing countries. These guidelines which were finalized in 1982, were issued as "Guidelines on the UNIDO model form of turnkey lump-sum contract for the construction of a fertilizer plant" (UNIDO/PC.40) and "Guidelines on the UNIDO model form of cost-reimbursable contract for the construction of a fertilizer plant (UNIDO/PC.41)".

B. DRAFT OF A MODEL AGREEMENT FOR PROMOTION, ENCOURAGEMENT AND RECIPROCAL PROTECTION OF INVESTMENTS

45. The AALCC Sub-Committee on International Trade Law Matters at its meeting at Colombo (Sri Lanka) in May 1981 examined the draft of a model agreement for promotion, encouragement and reciprocal protection of investments which the secretariat had

¹See also paras. 63-80 below and A/CN.9/237/Add.2, chap. XII, sections L, P and Q.

²These forms were considered by the UNCITRAL Working Group on the New International Economic Order in study I (A/CN.9/WG.V/WP.4 and Add. 1-8) (Yearbook ... 1981, part two, IV, B, 1), and study II (A/CN.9/WP.V/WP.7 and Add. 1-7) (Yearbook ... 1982, part two, IV, B).

prepared pursuant to the recommendations of the Ministerial Meeting on Industries held at Kuala Lumpur in December 1980 which had envisaged bilateral investment protection agreements between the countries of the Asian-African region in the context of providing encouragement for greater economic co-operation between the countries of the region. The draft will be revised on the basis of comments and suggestions by Governments.

C. SCIENTIFIC AND TECHNICAL CO-OPERATION

46. In 1981 the CMEA Conference on Legal Matters drafted and approved model rules concerning the liability of organizations with regard to agreements on scientific and technical co-operation. These model rules are designed to be used at the discretion of the parties in concluding civil law agreements concerning scientific and technical co-operation among organizations of the CMEA member countries and Yugoslavia. In particular, they apply to the performance of commissioned research, design, structural and experimental work, the establishment of a provisional international scientific and technical group; the establishment of a joint laboratory (department); and licences and other agreements concerning the transfer of scientific and technical results. The CMEA secretariat has sent these model rules to the appropriate organs and organizations of the CMEA member countries and Yugoslavia for use at their discretion.

47. In 1982 the CMEA Conference on Legal Matters drafted and approved a model agreement on the performance of commissioned research, design, structural and experimental work. The purpose of this model agreement is to improve contractual practice in matters of scientific and technical co-operation. The CMEA secretariat has submitted this model agreement to the CMEA member countries and Yugoslavia for use by the relevant bodies and organizations of those countries at their discretion.

D. GUIDE FOR DRAWING UP INTERNATIONAL CONTRACTS ON CONSULTING ENGINEERING, INCLUDING SOME RELATED ASPECTS OF TECHNICAL ASSISTANCE

48. The work on this project, which was started in 1979, was successfully completed in December 1982: the guide, drawn up under the auspices of the ECE Committee on the Development of Trade, was drafted by the Group of Experts on International Contract Practices in Industry and approved at its twenty-first session. The guide deals with consulting engineering and some aspects of technical assistance by means of a checklist and sections relating to the main contract provisions. It may usefully be read in conjunction with the numerous general conditions, model forms, guides, manuals, standards of professional conduct, and codes of ethics which have been drawn up and adopted by professional associations of consulting engineers and by other international organizations.

E. DRAFT GUIDE ON THE SUBJECT OF DRAWING UP INTERNATIONAL CONTRACTS ON SERVICES PROVIDED ON CONCLUSION OF A PROJECT, INCLUDING OPERATION, MAINTENANCE AND REPAIR

49. At its twenty-first session held from 13 to 15 December 1982, the ECE Group of Experts on International Contract Practices in Industry (under the auspices of the Committee on the Development of Trade) decided to prepare a new guide on contracts for services which are provided once a project has been completed, such as maintenance, repair, etc. The Chairman and Vice-Chairman, in co-operation with the secretariat, will prepare an annotated outline of the future guide for consideration by the Group of Experts at its twenty-second session in 1983. At that session, the Group of Experts will decide which elements of the newly-selected topic will be covered by the new guide, to what extent, and on its precise title.

F. GUIDELINES FOR THE ESTABLISHMENT OF INDUSTRIAL JOINT VENTURES IN DEVELOPING COUNTRIES

50. The above guidelines 1982 (UNIDO/IS.361) appeared as an advance edition of a UNIDO publication (it will subsequently appear in the Development and *Transfer of Technology* series). The guidelines include the following topics: incorporation of a company and its international guidelines, negotiating management and control in a joint-venture company, negotiating the capital structure of the joint-venture company, negotiating the transfer of know-how and technology-related services (in the context of joint-ventures).

G. THE UNIDO SYSTEM OF CONSULTATIONS

51. The UNIDO System of Consultations is an instrument through which UNIDO is to serve as a forum for developed and developing countries in their contacts and consultation directed towards the industrialization of developing countries. It is intended to help in identifying problems associated with the industrialization, and to contribute to closer industrial co-operation among States members, in accordance with the Lima Declaration and Plan of Action.

52. In accordance with the recommendations adopted by consensus and further elaborated by competent expert groups, UNIDO is evolving, in this context, a set of legal materials, including model contracts, model clauses, guidelines and checklists for contractual arrangements according to the requirements of each individual sector. This work constitutes a continuing process interlinked with other issues related to policy, economic, financial, social and technical matters pertaining to the different sectors. In the course of 1983, it is intended, in the framework of the scheduled consultation meetings and expert group meetings, to further advance work *inter alia* in the following fields:

(a) In the leather and leather-products industry—elaboration of a checklist for contractual arrangements; similar checklists have been made for the tanning and leather-goods industries;

(b) In the pharmaceutical industry—preparation of several documents regarding contractual arrangements, notably for the manufacture of drugs and intermediates;

(c) In the petrochemical sector—finalization of the "Second draft of UNIDO model form of agreement for the licensing of patents and know-how including annexures, an integrated commentary and alternative texts of some clauses" (recently revised) (UNIDO/PC.50);

(d) In the sector of agricultural machinery—preparation of a first checklist of main elements to be included in several types of contracts (import, training, manufacture, licensing etc.) which will be submitted to the second consultation meeting on that sector to be held in October 1983.

53. In addition, as a follow-up to the *Ad Hoc* UNCTAD/UNIDO Group of Experts on Trade and Trade-related Aspects of Industrial Collaboration Arrangements, UNIDO will further analyse the present practice and future outlook for such co-operation at the enterprise level, including the legal framework.

54. UNIDO's programme within the System of Consultations covers 13 industrial sectors, monitoring the world situation in each sector, identifying the industrialization problems and opportunities in developing countries and providing a new framework for industrial co-operation between developed and developing countries.

H. SOCIAL ASPECTS OF INDUSTRIALIZATION

55. At its 69th session in June 1983 the ILO International Labour Conference will undertake a general discussion on the social aspects of industrialization, with the objective of updating ILO policies and programmes concerning industrialization.

I. STUDIES AND TRAINING

1. *Commentary on Yugoslav legislation concerning industrial co-operation*

56. The group of legal experts under the Joint EFTA-Yugoslavia Committee concluded its work in July 1982 by finalizing its report containing a commentary on the Yugoslav legislation concerning three types of industrial co-operation (long-term production co-operation, licensing and joint venture). The report is being published by the EFTA secretariat.

2. *Cost-reimbursable contracts*

57. An ICC working group has been set up to study cost-reimbursable contracts. The group is composed of

employers, contractors, financing agencies and representatives of international organizations. Its objective is to publish recommendations on the best use of cost-reimbursable contracts, with practical examples from various countries.

58. A research group on the subject of cost-reimbursable contracts was set up by the Institute of International Business Law and Practice, which met on 22 November 1982. Among the topics researched into were concept and types of cost-reimbursable contracts, allowable costs, contractor's fee, liability for delay and defects, choice of and liability for subcontractors and suppliers, employer's influence on scope and specification of the permanent works and on the contractor's working methods, and conversion of cost-reimbursable contracts into fixed-price contracts.

3. *Some legal aspects of economic, scientific and technical co-operation among CMEA member countries*

59. In 1982 work commenced within the framework of the CMEA Conference on Legal Matters on the study of questions relating to the elaboration of new and the improvement of existing legal standards governing foreign trade relations between economic organizations of the CMEA member countries together with the elaboration of an improved set of measures to guarantee compliance with mutual obligations arising from international agreements (protocols) concerning trade turnover, payments and other agreements in the sphere of economic, scientific and technical co-operation. During 1983 and 1984 it is planned to prepare proposals regarding the substance of these questions and also practical ways and means of resolving them.

60. During 1980, 1981 and 1982 a comparative study was undertaken within the framework of the CMEA Conference on Legal Matters regarding the national legal standards of CMEA member countries applicable subsidiarily to contracts in relation to which the General Conditions adopted within the framework of the CMEA were operative. In particular, this comparative study focused on standards relating to the conclusion of contracts and fulfilment of obligations and also an analysis of conflict rules applicable to economic, scientific and technical co-operation. It is planned to prepare the basic results of this comparative study of standards for publication in 1984.

4. *Joint ventures in fisheries: training on negotiation*

61. FAO, through its Fisheries Department and Legal Office (Legislation Branch), has been co-operating with CTC over a number of years in the holding of a series of regional training workshops on the negotiation of joint ventures and other commercial arrangements in fisheries. The workshops have been aimed at middle level government lawyers, fisheries administrators and other government personnel responsible for negotiating agreements with transnational corporations. The objec-

tives are to make them more aware of the policy options open to coastal states, the main issues and problems they will be faced with in negotiating agreements and the techniques of negotiation that can be used. A workshop has been held at Lima in November 1981 concentrating on the member countries of the Sistema Económico Latino Americano (SELA). A further workshop in the series is scheduled to be held in West Africa in 1983 with a repeat workshop envisaged for the South Pacific in 1984.

62. A FAO manual on the negotiation of joint ventures in fisheries is scheduled for publication in 1983 to replace the study produced under the auspices of the Indian Ocean Programme in 1975 (James Crutchfield, *et al.*, *Joint Ventures in Fisheries*, IOFC/DEV/75/37, FAO, Rome, 1975).

IV. Transnational corporations

A. DRAFT CODE OF CONDUCT ON TRANSNATIONAL CORPORATIONS

63. The Intergovernmental Working Group on a Code of Conduct on Transnational Corporations (established by CTN) submitted its final report (E/C.10/1982/6), containing the draft Code of Conduct on Transnational Corporations, to CTN at its eighth session from 30 August to 10 September 1982.

64. Although the draft Code of Conduct contains definitive formulations in substantial areas of the document, the entire Code was not finalized. On the recommendation of CTN at its eighth session, ECOSOC, in its resolution 1982/68 of 27 October 1982, decided that CTN should hold a special session open to the participation of all States early in 1983 for the purpose of completing the Code of Conduct.

65. The draft Code of Conduct consists of six main parts (chapters) (see E/C.10/1982/6). The first part, which has not yet been drafted, is to contain a preamble and a statement of objectives. The second part consists of a set of provisions on definitions and the scope of application of the Code. The third part deals with the activities of transnational corporations (TNCs). It contains provisions addressed to TNCs specifying the kinds of conduct that are deemed permissible and proper by the Governments that will eventually adopt the Code. A first set of paragraphs covers general and political matters; a second set deals with more specific economic, financial and social issues; and a third set contains a series of provisions on disclosure of information by TNCs. The fourth part of the Code deals with the treatment that TNCs are to receive from the Governments of the countries in which they operate and the questions of nationalization and compensation and of jurisdiction. The fifth part of the Code addresses the necessary co-operation among Governments for the application of the Code, while the sixth part deals more specifically with the action needed at the national and international levels for the implementation of the Code.

B. PRINCIPLES CONCERNING MULTINATIONAL ENTERPRISES

66. The ILO follow-up procedures for the Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy are being implemented. Governments have been asked to supply their second reports on the effect given to the Declaration by 31 March 1983, and these reports will be examined by the Committee on Multinational Enterprises at the November 1983 session of the Governing Body.

C. PUBLICATION AND RESEARCH

67. CTC, in continuing its work on national legislation and regulations relating to transnational corporations, which was first published in 1978 (ST/CTC/6) and supplemented in 1980 (ST/CTC/6/Add.1), completed a survey of national laws and regulations relating to TNCs in 20 countries in 1981 (ST/CTC/26). In 1982, a similar study was completed for a further 20 countries (ST/CTC/35). A study on an additional 10 countries is scheduled for completion by June 1983. The issues which are reviewed in these reports include: main investment legislation, screening and monitoring investors, ownership control and divestment, foreign exchange control regulations, technology transfer and restrictive business practices, fiscal incentives and taxation, export processing zones, disclosure requirements under corporate laws, investment guarantees and governing law and dispute settlement. The 50 countries reviewed in the past three years under these series of reports are: Algeria, Argentina, Australia, Bolivia, Botswana, Brazil, Canada, Chile, Colombia, Costa Rica, Egypt, Germany, Federal Republic of, France, Ghana, Guyana, India, Indonesia, Iraq, Israel, Italy, Ivory Coast, Kenya, Kuwait, Liberia, Libya, Malaysia, Mexico, Morocco, Nigeria, Pakistan, Panama, Papua New Guinea, Peru, Philippines, Portugal, Republic of Korea, Romania, Saudi Arabia, Singapore, Sudan, Thailand, Trinidad and Tobago, Tunisia, Turkey, United Kingdom of Great Britain and Northern Ireland, United Republic of Tanzania, Venezuela, Yugoslavia, Zaire, Zambia.

68. In addition to the above, CTC has also undertaken a survey of taxation of resource-based industries in six selected countries. This survey covers corporate tax issues relating to TNCs in the agricultural sector including forestry and fishing, as well as in the mining and petroleum areas. The six countries covered are Australia, Botswana, Brazil, Indonesia, Nigeria and Venezuela.

69. CTC, in response to CTN, is also updating the report on "International codes and regional arrangements relating to TNCs" (E/C.10/9/Add.1). In updating this report the earlier survey will be amplified and critical analysis will be given to bilateral, regional and multilateral arrangements on matters related to TNCs. This study will be presented to CTN in 1984.

70. With regard to contracts and agreements a draft report is being finalized, which deals with the analysis of approximately 80 engineering and manufacturing consultancy contracts between TNCs and developing countries as well as analysis of model or standard engineering consultancy contracts used by various international organizations. The report is entitled "Analysis of engineering and industrial consultancy contracts" and the key issues analyzed include duties and responsibilities of project owner and the consultant, standard of performance required under contractual provisions, transfer of technology and proprietary information, aspects of insurance, financial provisions, validity of contract, and settlement of disputes.

71. In 1982, at the eighth session of CTN, two reports dealing with contracts and agreements were submitted: "TNCs and contractual relations in world uranium industry" (ST/CTC/37) and "Analysis of equipment leasing contract" (ST/CTC/36). The uranium report analyses approximately 17 production contracts as well as approximately 30 uranium (yellowcake) sales contracts. The equipment-leasing report analyses approximately 25 contracts including standard draft contracts recommended by FIDIC. It also traces the rising trend of equipment leasing contracts both in developed and developing countries and the role of IFC in this regard.

72. Three other reports dealing with contracts and agreements have been completed and should be published as sales publications in 1983. These are "Management contracts in developing countries: an analysis of their substantive provisions" (ST/CTC/27), "Features and issues in turnkey contracts in developing countries" (ST/CTC/28) and "Main features and trends in petroleum and mining agreements" (ST/CTC/29). The first study analyses the key provisions in approximately 35 management contracts made between TNCs and developing countries. These contracts are found mainly in the tourist industry and services sector, manufacturing and processing and in the petroleum and mining sectors. The turnkey report reviews approximately 15 contracts including the UNIDO draft model turnkey contract for the fertilizer industry. The third report discusses the contractual changes which have taken place, in particular since 1973, and analyses the changes which have taken place in petroleum and mining contracts in the past decade as well as contractual provisions which are mandatory in national legislation. It concludes with a projection of the trend for the next decade.

V. *Transfer of technology*

A. INTERNATIONAL CODE OF CONDUCT ON THE TRANSFER OF TECHNOLOGY

73. The General Assembly, by resolution 32/188, convened the United Nations Conference on an International Code of Conduct on the Transfer of Technology to negotiate and adopt an international code of conduct on the transfer of technology. This

Conference has held four sessions since October 1978. The substantive provisions of the present text of the proposed code (TD/CODE/TOT/33) fall into two broad groups: those concerning the regulation of transfer of technology transactions and of the conduct of the parties to them; and those relating to steps to be taken by Governments to meet their commitments to the code.

74. By resolution 36/140, the General Assembly established an interim committee of the Conference which in its session held in 1982 formulated proposals on the outstanding issues for the consideration of the Conference (TD/CODE/TOT/35). The main issues are: definitions and scope of application (meaning of an international transfer of technology transaction, application of the code to agreements between States for development purposes); applicable law and settlement of disputes; international institutional machinery (nature of the institutional machinery, mandate and timing of a conference to review the code). The General Assembly in its resolution 37/210 decided that the fifth session of the Conference should be convened in the second half of 1983.

B. THE INDUSTRIAL PROPERTY SYSTEM

75. UNCTAD continues to examine the economic, commercial and development aspects of the industrial property system, patents and trade marks, and to contribute to the current revision of the Paris Convention for the Protection of Industrial Property. This subject was considered by expert groups convened in September 1975 (TD/B/C.6/8), August 1977 (TD/B/C.6/24) and February 1982 (TD/B/C.6/76), and also at the fourth and fifth sessions of the Conference (resolutions 88 (IV) and 101 (V)). At its fourth session in December 1982 the Committee on Transfer of Technology, by resolution 21 (IV), requested UNCTAD to convene another meeting of the governmental experts to continue the examination of the economic, commercial and developmental aspects of industrial property in the transfer of technology to developing countries and to report its findings and recommendations to the fifth session of the Committee to be held in 1984.

C. TRANSFER OF TECHNOLOGY: APPLICABLE LAW

76. At its fourteenth session in October 1980, the Hague Conference on Private International Law decided to continue to study the possible preparation of a convention on the law applicable to licensing agreements and know-how, in liaison with the international organizations concerned, in particular the World Intellectual Property Organization (WIPO).

D. TRANSFER OF TECHNOLOGY: ECONOMIC CO-OPERATION

77. At the International Labour Conference in June 1983, one of the topics to be considered will be

international economic co-operation and employment, including questions of technology transfer.

E. STUDIES, GUIDES AND MANUALS

78. The UNCTAD secretariat has issued several studies on patents and trade marks, including: "The role of the patent system in the transfer of technology to developing countries", 1975 (TD/B/AC.11/19/Rev. 1), "The role of trade marks in developing countries", 1979 (TD/B/C.6/AC.3/3/Rev.1), "The international patent system: the revision of the Paris Convention for the Protection of Industrial Property", 1981 (TD/B/C.6/AC.3/2), "Review of recent trends in patents in developing countries" (TD/B/C.6/AC.5/3) and "Trade marks and generic names of pharmaceuticals and consumer protection", 1982 (TD/B/C.6/AC.6/4).

79. In response to Trade and Development Board resolution 240 (XXIII) the UNCTAD secretariat prepared a report entitled "Common approaches to laws and regulations on the transfer and acquisition of technology", 1982 (TD/B/C.6/91). Having considered this report, the Committee on Transfer of Technology, in its resolution 20 (IV), requested the secretariat to prepare a manual reviewing policies and instruments on the promotion and encouragement of technological innovation in order to assist developing countries in formulating policies in this area. The Committee also invited the secretariat to complete the empirical analysis of the effects of the implementation of transfer of technology regulations; the secretariat has already done two studies on this subject: "The implementation of transfer of technology regulations: a preliminary analysis of the experience of Latin America, India and the Philippines", 1980 (TD/B/C.6/55); and "Transfer of technology regulations in the Philippines", 1980 (UNCTAD/TT/32).

80. The WIPO guide on the organization of industrial property activities of enterprises in developing countries, at present under preparation, and the study entitled "The role of industrial property in the protection of consumers", published in June 1982, contain chapters dealing with the acquisition and transfer of technology.

81. UNIDO has issued Guidelines for Evaluation of Transfer of Technology Agreements (No. 12 of the Development and Transfer of Technology series) (ID/233).

VI. Industrial and intellectual property law

A. WORK OF THE WORLD INTELLECTUAL PROPERTY ORGANIZATION

1. Industrial property and patent information

(a) Industrial property and patent information activities of particular interest to developing countries

82. Legal-technical assistance continues to be given to a number of developing countries in the form of

advice by the staff of the International Bureau of WIPO through specialists on the adoption of modern legislation and the strengthening of the administration of the industrial property system.

83. The WIPO *Guide for Developing Countries on the Examination of Patent Applications* was published in October 1982. A guide on the organization of industrial property activities of enterprises in developing countries is under preparation and will be published in 1983.

(b) Revision of the Paris Convention

84. Three sessions of the Diplomatic Conference on the Revision of the Paris Convention have been held so far: in February/March 1980 at Geneva, in October 1981 at Nairobi and in October/November 1982 at Geneva. The fourth session is scheduled for 27 February-24 March 1984 at Geneva.

(c) Promotion of industrial property protection through new international arrangements

85. A committee of experts to consider a draft treaty for the protection of computer software, prepared by the International Bureau of WIPO, will meet in June 1983.

(d) Promotion of industrial property protection outside treaties

86. A committee of experts on joint inventive activity will meet in May 1983. A special issue of the periodical *Industrial Property* dealing with anti-piracy measures (concerning the manufacture, importation and distribution of goods which are marketed with false indications as to their origin or under unauthorized commercial names or trademarks) was published in November 1982. Another special issue of that periodical dealing with the professional liability of industrial property agents was published in April 1982. A study entitled "The role of industrial property in the protection of consumers" was published in June 1982.

(e) Maintenance of general industrial property information services

87. The industrial property statistics for the year 1980 were published by WIPO in February 1982. The detailed tables of statistics for 1981 were published in November 1982.

2. Copyright and neighbouring rights activities

(a) Copyright and neighbouring rights activities

88. In this field WIPO is giving priority treatment to developing countries in training specialists; creating or modernizing domestic legislation; stimulating creative activity; and facilitating access to foreign works protected by copyright owned by foreigners.

89. Pursuant to the above objective, WIPO awards fellowships for trainees from developing countries, organizes training courses in various countries, and provides legal-technical assistance to developing countries in the form of advice on the adoption of new laws

and regulations and the administration of copyright. (See also paragraphs 97-98, below.)

(b) *Promotion of the acceptance of copyright and neighbouring rights treaties*

90. The objective is to ensure that more countries become party to the treaties dealing with the international protection of copyright and neighbouring rights. Those treaties are: the Berne Convention for the Protection of Literary and Artistic Works; the International Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organizations; the Convention for the Protection of Producers of Phonograms against Unauthorized Duplication of their Phonograms; the Convention Relating to the Distribution of Programme-Carrying Signals Transmitted by Satellite; the Multilateral Convention for the Avoidance of Double Taxation of Copyright Royalties and Additional Protocol; and the Vienna Agreement for the Publication of Type Faces and their International Deposit and Protocol.

(c) *Promotion of the practical application of laws and treaties in the fields of copyright and neighbouring rights*

91. During 1982, committees of experts or working groups were convened, jointly with UNESCO, to study (i) the problems arising from the use of computers for access to or the creation of works; (ii) the intellectual aspects of the protection of expressions of folklore; (iii) the "domaine public payant"; (iv) the question of copyright ownership and its consequences for the relations between employers and employed or salaried authors (a meeting convened jointly also with the ILO); (v) the access by the visually and auditory handicapped to material reproducing works protected by copyright; and (vi) the formulation of guidelines in the system of translation and reproduction licenses for developing countries under the copyright conventions. A committee of governmental experts, convened, jointly, by WIPO with UNESCO and ILO, also met in 1982 to examine the copyright and neighbouring rights problems raised by cable television.

92. Special issues of the periodical *Copyright* were published in 1982 dealing with the subject of private copying of recordings and private recording of broadcasts and with the subject of private copying of printed matter. A world-wide forum on the piracy of sound and audiovisual recordings was organized by WIPO in March 1981 and another, on the piracy of broadcasts and of the printed word, in March 1983.

(d) *Maintenance of information services in the fields of copyright and neighbouring rights*

93. WIPO continues to keep up to date its collection of the texts of laws, regulations and treaties dealing with copyright and neighbouring rights. Basic texts are published in the monthly periodicals *Copyright* and *Le droit d'auteur*.

94. WIPO continues to publish in various languages the *Guide to the Berne Convention*, the *Guide to the*

Phonograms Convention and the *WIPO Glossary of Terms on the Law of Copyright and Neighbouring Rights*.

(e) *Executive Committee of the Berne Union*

95. The Executive Committee of the Berne Union met in extraordinary session in 1981. It reviewed the work undertaken by the International Bureau of WIPO and by various committees of experts and working groups on the current problems in the field of copyright and neighbouring rights and took decisions concerning the continuation of that work.

B. WORK OF UNITED NATIONS EDUCATIONAL, SCIENTIFIC AND CULTURAL ORGANIZATION

Copyright and neighbouring rights

96. The activities of the United Nations Educational, Scientific and Cultural Organization (UNESCO) in the field of copyright and neighbouring rights comprise, *inter alia*, the application and promotion of the international instruments on copyright and on the protection of performers, producers of phonograms and broadcasting organizations concluded under the sponsorship of UNESCO and the extension of the geographical field of their application. Among these, the most recent one is the Multilateral Convention for the Avoidance of Double Taxation of Copyright Royalties. A brief account of that convention and of other relevant activities in the above-mentioned fields is set out below.

(a) *Joint International UNESCO-WIPO Service for Access by Developing Countries to Works Protected by Copyright*

97. In view of the fact that since 1976 some of the activities in the permanent programme of WIPO concerned fields covered by the activity of the already existing International Copyright Information Centre of UNESCO, particularly with regard to access to works of foreign origin in pursuance of resolution 5/01 adopted by the General Conference of UNESCO at its twenty-first session, the Director-General of UNESCO entered into negotiations with the Director-General of WIPO which culminated in the establishment of the Joint International UNESCO-WIPO Service for Access by Developing Countries to Works Protected by Copyright with effect from 1 January 1981. In order to advise the Directors-General of those two organizations on the preparation and implementation of the activities of the joint service, a joint UNESCO-WIPO consultative committee was also set up. In November 1982 UNESCO and WIPO convened a joint meeting of a working group on model contracts concerning co-publishing and commissioned works.

98. The Joint UNESCO-WIPO Consultative Committee held its first ordinary session at UNESCO headquarters from 2 to 4 September 1981 and considered the "Plan of Action for 1981/1982 of the Joint International UNESCO-WIPO Service for Access by Developing Countries to Works Protected by Copyright" which included: (i) collection and dissemination

of data; (ii) establishment of recommended standards; (iii) arrangements and machinery designed to operate realistic economic conditions; (iv) procedures for settling disputes between users of works in developing countries and foreign copyright owners; and (v) intellectual, technical and financial assistance to developing countries.

(b) *Creation of the Committee for International Copyright Funds (COFIDA)*

99. The International Fund for the Promotion of Culture, an autonomous financial body under UNESCO, adopted at the April 1981 session of its Administrative Council the rules of procedure of the Committee for International Copyright Funds (COFIDA). COFIDA is a subsidiary organ of the Fund and provides, *inter alia*, total or partial financing for copyright royalties when a developing country encounters difficulties in paying for the reproduction, translation, adaptation, broadcast or communication to the public by any other means of works of foreign origins of an educational, scientific, technical, technological or cultural nature. The operations of COFIDA may take various forms, such as loans, intellectual and technical assistance to developing countries for purposes related to access to protected works of foreign origin. A brochure entitled "Committee for International Copyright Funds—COFIDA" explaining the aims, object, constitution and operation of the Funds was published by UNESCO in 1981.

Model contracts concerning the cession of copyright in printed and audio-visual works

100. In the context of its overall activities in the field of facilitating access of developing countries to protected works and to serve as a link between publishers and copyright holders in various countries, both developed and developing, the International Copyright Information Centre of UNESCO has established the following model contracts accompanied by comments, and guidelines, for use by interested parties in the fields of publication and granting of rights:

- (a) Model Contract for the Publication of a Reproduction of an Edition of a Work;
- (b) Model Contract for the Publication of the Translation of a Work;
- (c) Model Contract for the Licensing of Rights in a Work for the purpose of Sound Recording;
- (d) Model Contract for the Licensing of Motion Picture Rights;
- (e) Guidelines for the Preparation of Contracts for Translation, Reproduction and other Rights required by Developing Countries.

C. WORK OF THE STATES OF THE CARIBBEAN COMMUNITY

101. The proposals of the secretariat of the Caribbean Community (CARICOM) for legislation relating to intellectual property were circulated to the Governments of CARICOM States in 1978 for examination and comment, in particular the proposals for the

protection of copyright and neighbouring rights (performers' rights). Active consideration is being given by the Governments of CARICOM States to the preparation of the legislation necessary to provide better protection for the creative works of writers, dramatists, composers and performers. The Government of Barbados has recently enacted a number of laws dealing with intellectual property, for example, the Copyright Act 1981, the Industrial Designs Act 1981, the Trade Marks Act 1981 and the Patents Act 1981.

D. WORK OF THE COMMISSION OF THE EUROPEAN COMMUNITIES^c

Trade marks

101a. The proposal of the Commission of the European Communities (CEC) for a first CEC Council directive to approximate the law of the States members relating to trade marks aims to create a common market in trade-marked goods, removing the barriers to the free movement of trade-marked goods and services by instituting arrangements which ensure that competition within the common market is not distorted and by creating legal conditions under which firms can adapt their activities to the scale of the Community. It creates Community arrangements for trade marks whereby undertakings can by means of one system of procedure obtain Community trade marks to which uniform protection is given and which produce their effects throughout the entire area of the Community. The proposal has since June 1981 been the subject of discussions in the Council by a group of government experts.

101b. CEC's proposal for a Council regulation on Community trade marks seeks to remove disparities in the trade mark laws of States members which may impede the free movement of goods and freedom to provide services, or may distort competition within the common market and may therefore directly affect the establishment and functioning of the market. It harmonizes those provisions of trade-mark law which at present have the strongest and most direct influence on the establishment and functioning of the common market in trade-marked goods, particularly the rules governing the scope of the protection afforded to trade marks, use of trade marks, amicable settlement of conflicts and the relative and absolute grounds for the refusal of registration or invalidation of trade marks. The proposal has since June 1981 been the subject of discussions in the Council by a group of government experts.

VII. *International payments*

A. DOCUMENTARY CREDITS

102. Documentary credit operations throughout the world are made subject to the ICC Uniform Customs and Practice for Documentary Credits (UCP) (1974

^cA/CN.9/237/Add.3, paras. 1 and 2.

version). The Commission on Banking Technique and Practice of ICC is revising the UCP with the intention of bringing the rules into line with the most current modern practices. In particular, the articles dealing with transport of shipping documents are being updated. More detailed guidance will be added on a number of procedural aspects, and specific reference will be made to stand-by letters of credit. It is anticipated that the work will be completed in the course of 1983.

103. Following the adoption of the revised rules, ICC standard forms for issuing documentary credits, and forms for use by credit applicants together with a guide to documentary credit operations will also be updated.

B. RULES FOR FOREIGN EXCHANGE CONTRACTS

104. The ICC Commission on Banking Technique and Practice in collaboration with representatives of the "Group of Ten" banks is continuing its work on rules governing forward foreign exchange contracts. The rules deal with the formalities on conclusion of foreign exchange contract, and the consequences between the parties when the contract cannot be carried out.

105. The objective of the above rules is to establish internationally accepted standards applicable to the liquidation of such contracts in cases when one of the parties is unable to perform its contractual obligations. It is intended that these rules be adopted by banks as contractual terms in their foreign exchange contracts.

C. COLLECTIONS

106. The ICC Commission on Banking Technique and Practice is continuing its work on standard forms for use by banks carrying out collection operations subject to the ICC Uniform Rules for Collections. The aim is to facilitate procedures between banks by providing a standard format. An accompanying explanatory brochure is also in the course of preparation.

107. The Commission is also authorized to establish draft forms and explanatory brochures for approval by the ICC Council. The information provided will be used for instructing banks responsible for carrying out collection operations.

D. STANDARDIZATION OF FOREIGN TRADE INSTRUMENTS

108. In June 1980, as part of its continuing work on the standardization of foreign trade instruments, the CMEA Standing Commission on Foreign Trade approved a recommendation entitled "Standardized forms" for the bank documents "Order-register" and "List of payment demands" and recommended that CMEA member countries should take the appropriate measures in line with their established systems to bring these forms into effect as of 1 January 1981.

109. The "Order-register" and the "List of payment demands" are consolidated documents used in clearing operations between banks of CMEA member countries through the International Bank for Economic Co-operation. These operations involve the use of payment orders and are carried out by means of collection with subsequent acceptance. The aim of the recommendation is to standardize these foreign trade documents. The recommendation of the Commission was approved by the delegations of the CMEA member countries without reserve.

[A/CN.9/237/Add.2]^a

VIII. International transport

A. TRANSPORT BY SEA AND RELATED ISSUES

1. International shipping legislation

1. In response to resolution 43 (S-III), adopted by the UNCTAD Committee on Shipping at its third special session, in June 1981, and resolutions 49 (X) adopted at its tenth session, in June 1982, the UNCTAD secretariat is preparing model maritime legislation, dealing in particular with the commercial aspects of maritime transport, for use by developing countries in the formulation of their national legislation. An outline of the proposed model legislation is found in the secretariat report "International maritime legislation: future work" (TD/B/C.4/244).

2. A technical committee, established by the Secretary General of CARICOM completed its examination of the draft Maritime Code for the CARICOM States and is in the process of revising the draft legislation in the light of its deliberations and recommendations. It is intended that the revised shipping legislation will, in due course, be circulated to the Governments of the CARICOM States for consideration and will eventually replace the United Kingdom Merchant Shipping Act 1894, which still applies to the CARICOM States.

2. Marine insurance

3. For the work of UNCTAD, see "Report of the Secretary-General: some recent developments in the field of international transport of goods" (A/CN.9/236)^b paragraphs 5 and 6.

3. Open registry shipping

4. The UNCTAD Committee on Shipping, by resolution 43 (S-III) adopted at its third special session, in June 1981 (TD/B/C.4/S-III/Misc.2, annex I), established

^a27 April 1983.

^bReproduced in this volume, part two, V, C.

the Intergovernmental Preparatory Group on Conditions for Registration of Ships which it entrusted with the task of formulating proposals for a set of basic principles concerning the conditions upon which vessels should be accepted on national shipping registers, with a view to their consideration and adoption as an international agreement by a United Nations conference. The Group met in April 1982 (TD/B/904) and in November 1982 (TD/B/935). In accordance with General Assembly resolution 37/209, a United Nations conference on the registration of ships will be convened in early 1984. A preparatory committee is scheduled to meet in late 1983.

5. The UNCTAD secretariat has prepared several studies on open registry shipping including "Beneficial ownership of open-registry fleets" (TD/222/Supp.1), "Open-registry fleets", 1981 (TD/B/C.4/220) and "Beneficial ownership of open-registry fleets—1981" (TD/B/C.4/223).

4. *Convention on a Code of Conduct for Liner Conferences*

6. This Convention will enter into force six months after the date on which not less than 24 States, with a combined tonnage of at least 25 per cent of world liner tonnage, have become parties to it. By February 1983, 56 States with a combined tonnage of 20.81 per cent had become parties to the Convention. The Council of Ministers of CEC, by regulation 954/79 of 15 May 1979, decided that the States members of the Community should become parties to the Convention. Finland, Japan, Norway, Spain and Sweden also have announced their intention of becoming parties to the Convention (TD/B/C.4(X)/Misc. 4).

5. *Treatment of foreign merchant vessels in ports*

7. The UNCTAD Committee on Shipping has requested the secretariat to monitor developments in this field, and in the light of this information, the Committee will decide at its eleventh session, to be held in 1984, what further work is necessary on this subject.

6. *Freight forwarding*

8. For the work of FIATA, see A/CN.9/236, paragraph 13; for the work of UNCTAD, see *ibid.*, paragraph 14.

7. *Maritime fraud*

9. At its twelfth regular session in November 1981 the Assembly of the International Maritime Organization (IMO) adopted resolution A. 504 (XII) relating to barratry, unlawful seizure of ships and their cargoes and other forms of maritime fraud. This resolution was adopted following a study undertaken by an *ad hoc* working group appointed by the IMO Council to

examine the matter on the basis of information provided by Governments and interested organizations, and to submit proposals aimed at promoting concerted action by all relevant parties and interests for the prevention and suppression of fraudulent acts which gravely endanger the international sea-borne trade.

10. The UNCTAD Committee on Shipping by resolution 49 (X) established an intergovernmental group to examine, with the assistance of a report to be prepared by the secretariat, maritime fraud connected with bills of lading, charter parties, marine insurance and general average, and submit recommendations on means of combating such fraud to the Trade and Development Board (TD/B/C.4/254). This group is expected to meet in October 1983.

11. ICC prepared a *Guide to the Prevention of Maritime Fraud*, which was published in October 1980 as ICC publication No. 370. The *Guide* discusses the general characteristics of current fraud situations and gives examples of recent frauds. It addresses itself to the ways fraud can be prevented by Chambers of Commerce, buyers and sellers, foreign forwarders, banks, vessel owners and charterers, and insurers. It also deals with the question of what to do when a vessel does not arrive as scheduled.

12. The work of ICC in the prevention of maritime fraud culminated with the establishment of the International Maritime Bureau (IMB) in London on 1 January 1981. The objectives of IMB are to act as a clearing house for information on fraudulent and suspect practices; to suggest procedures and remedies to those involved in a transaction which they suspect to be fraudulent; to provide advice in setting up or improving operational and commercial systems to reduce their vulnerability to fraud; and to provide educational services for fraud prevention.

13. IMB provides full investigation services in cases of maritime fraud or malpractice. IMB also offers one- or two-day seminars throughout the world, at the request of interested parties, based on the *Guide to the Prevention of Maritime Fraud*.

8. *Carriage of noxious and hazardous substances by sea: draft Convention on liability and compensation*

14. The Legal Committee of IMO continued its work on the preparation of a draft convention on liability and compensation in connection with the carriage of noxious and hazardous substances at sea. The Committee completed its work on the draft articles at the beginning of 1982. It is expected that a diplomatic conference will be convened by IMO in 1984 to consider the adoption of the convention.

9. *Salvage: legal questions ("Amoco Cadiz" disaster)*

15. The Legal Committee of IMO has agreed to consider at an early date a draft convention on salvage

and assistance at sea designed to revise and replace the 1910 Convention for the Unification of Certain Rules of Law with Respect to Assistance and Salvage at Sea. The Council of IMO has expressed the view that top priority should be accorded to this new convention. It is therefore envisaged that the Legal Committee will give priority attention to that subject after completion of work on the subjects for the 1984 diplomatic conference.

10. *Conventions on civil liability for oil pollution damage*

16. The Legal Committee of IMO has undertaken a review of the limits of liability contained in the International Convention on Civil Liability for Oil Pollution Damage, 1969 and the International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1971. The results of this review, in the form of two protocols to amend the 1969 and 1971 Conventions, are expected to be considered at the diplomatic conference scheduled to be held in 1984.

11. *Facilitation of international maritime traffic*

17. The Facilitation Committee of IMO established the *Ad Hoc* Working Group on Automatic Data Processing with the mandate to scrutinize the 1965 Convention on Facilitation of International Maritime Traffic with a view to proposing measures to remove unnecessary obstacles to the use of teletransmitted data in maritime transport. The Group has emphasized the desirability of moving away from the concept of a "document" as being necessarily "a piece of paper". It has made a number of suggestions for a more flexible approach in this regard. One of these suggestions was to insert the following definitions (elaborated by ECE) in section 1 A of the annex to the 1965 Convention:

"Document"—data carrier with data entries

"Data carrier"—medium designed to carry records of data entries

(See also "Note by the secretariat: legal aspects of automatic data processing" (A/CN.9/238)).^c

18. The proposals of the *Ad Hoc* Working Group to remove obstacles to automatic data processing in the Convention are contained in annex 3 to document FAL/7, and have been approved (with the exception of a few) by the Facilitation Committee. (See also "Report of the Secretary-General: international transport documents" (A/CN.9/225)^d paragraphs 31-32; and A/CN.9/238).

12. *Carriage of goods by inland waterway*

19. Following communications from the President of the Central Commission for the Navigation of the

Rhine and of the Chairman of the UNIDROIT Committee of Governmental Experts recommending that the work on the draft Convention on the Contract for the Carriage of Goods by Inland Waterway of the Committee be resumed, as well as a request to the same effect from ECE, the Governing Council of UNIDROIT gave consideration to a possible resumption of work on the draft Convention. At its sixty-first session (April 1982) it decided that only in the event of prior agreement being reached regarding the exoneration of the carrier for fault in the navigation of the vessel should the secretariat proceed to the convening of a fourth session of the Committee of Governmental Experts for the revisions of the draft Convention. If, however, the necessary condition for holding the meeting were to be met, then the Committee should be empowered to proceed to a total revision of the draft Convention.

20. Since the session of the Governing Council the secretariat has been informed of the failure of the Rhine States to reach agreement on the problem of the carrier's exoneration for fault in the navigation of the vessel and in these circumstances it would propose the deletion of this item from the work programme.

13. *Other subjects*

21. The UNCTAD Committee on Shipping at its tenth session in June 1982 reviewed the work programme which it established in 1969 for its Working Group, and decided by resolution 49 (X) that the Working Group should, in addition to general average, examine maritime liens and mortgages, arrest of vessels, and the registration of rights in vessels under construction. The consideration of these subjects will call for the examination of several international legal instruments, i.e. the 1926 Convention and the 1967 Convention for the Unification of certain Rules relating to Maritime Liens and Mortgages, and the 1952 International Convention for the Unification of certain Rules relating to the Arrest of Sea-Going Ships (TD/B/C.4/254). The same resolution requests the secretariat to update its earlier report "Terms of shipment" (TD/B/C.4/36/Rev. 1).

22. A maritime session of the ILO International Labour Conference is due to be held before the end of the decade. Preparatory work will begin with a session of the Joint Maritime Commission in 1984 whose agenda includes the following items which may form the subject of new standards at the planned maritime session: social security and employment conditions of seafarers serving in ships flying flags other than those of their own country (including flags of convenience); medical care on board ships; review and possible revision of recommendation No. 109 on wages, hours of work and manning (sea), 1958; revision of the Conventions on the Placing of Seamen (No. 9, 1920) and on the Repatriation of Seamen (No. 23, 1926); and of recommendation No. 27 on repatriation (ship masters and apprentices), 1926.

^cReproduced in this volume, part two, V, D.

^dYearbook ... 1982, part two, VI, B.

B. TRANSPORT OVER LAND AND RELATED ISSUES

1. *Civil liability for damage caused by hazardous cargoes*

23. The UNIDROIT Committee of Governmental Experts for the Preparation of Uniform Rules Relating to Liability and Compensation for Damage Caused During the Carriage Over Land of Hazardous Substances held two sessions at the headquarters of the Institute at Rome from 16 to 19 March 1981, and from 1 to 4 February 1982.

24. The Committee has decided to restrict the sphere of application of the future uniform rules to liability for damage caused during the carriage of hazardous substances by road, rail and inland waterway and in consequence it rejected a suggestion to cover also transmission of hazardous substances by pipelines. It has also agreed for the time being not to endorse a proposal to broaden its terms of reference to cover liability for damage resulting from the carrying out of dangerous activities in general.

25. The first session of the Committee was devoted to consideration of a list of questions prepared by the secretariat intended to focus discussion on a number of points of special importance and on the basis of these discussions a preliminary set of draft articles was prepared for a convention on liability and compensation for damage caused during the carriage over land of hazardous substances (study LV—Doc. 8). The Committee also agreed at its first session that a list of substances to which the future convention should apply should be annexed to it together with a series of questions, permitting the appropriate technical bodies of the United Nations to give advice on the lists of substances.

26. At its second session the Committee began its consideration of the draft articles and although some comments of a general character were made on those provisions, the Committee concentrated its attention on a number of key areas such as scope of application, the person or persons to be held liable under the future conventions (sole carrier liability or joint carrier-shipper liability), the nature of the liability regime, limitation of liability, compulsory insurance, claims and actions and definitions. While the work continues, a strong trend in favour of establishing a scheme of compulsory insurance is also emerging.

2. *Rail/road transport contract: alignment of documents*

27. A draft contract of the International Union of Combined Rail/Road Transport Enterprises, Union international de transport rail-route (UIRR) has been drawn up by the Union's Data Processing Commission on the basis of the new International Convention Concerning the Carriage of Goods by Rail (CIM) consignment note. UIRR had noted that many of the elements contained in the CIM consignment note linking

enterprises in the Union and railways were identical to the elements contained in the UIRR contract linking road transporters and enterprises in UIRR. UIRR has therefore prepared a contract based on the CIM consignment note; this avoids the repetition of certain information and prevents discrepancies between the documents. The draft contract has not yet been finalized.

3. *Formation of the railway co-operation group within ESCAP*

28. The establishment of an Asian railway union was first discussed at the fifth meeting of Top Railway Executives in Asia and the Middle East, in 1979, and considered by the ESCAP Committee on Shipping, and Transport and Communications at its third session. Since then, this proposal has been examined in depth and considered at various ESCAP and allied forums. Eventually, a consensus was reached at the sixth meeting of Top Railway Executives of Asia and the Middle East, in October 1981, which urged the Executive Secretary of ESCAP, *inter alia*, to take appropriate measures for the secretariat to service a railway co-operation group in lieu of an Asian railway union.

29. The Committee on Shipping, and Transport and Communications, at its fifth session, endorsed this recommendation, which was also endorsed by the Commission at its thirty-eighth session. It urged the secretariat to take all appropriate measures in that regard and requested UNDP and interested countries to provide ESCAP with the necessary resources. The proposed railway co-operation group is expected to provide a regional framework for closer co-operation and collaboration arrangements among railways of the region and for fostering collective self-reliance among them.

30. In pursuance of the mandate of ESCAP, the ESCAP secretariat has drawn up a work plan for the implementation of a project on the formulation of the railway co-operation group (RCG). The secretariat has also prepared a draft memorandum of understanding for adoption and acceptance at the Meeting of Ministers Responsible for Railways and Preparatory Meeting of Senior Officials, held at Bangkok, 24 February to 2 March 1983. The RCG will be established after the adoption of the memorandum of understanding, and its first meeting will be convened as soon as possible for the formulation of its rules of procedures and work programme.

31. For the work of the Central Office for International Railway Transport, see A/CN.9/225.

C. TRANSPORT BY AIR AND OTHER RELATED MATTERS

1. *Civil aviation legislation*

32. The CARICOM secretariat prepared harmonized up-to-date civil aviation legislation for the CARICOM

member States which was circulated to the Governments of member States in December 1981 for examination and comments. The draft legislation, when enacted, will replace the application to the CARICOM States of the United Kingdom civil aviation legislation, for example, the Civil Aviation Act 1949, and will also give the force of law in the CARICOM States of international conventions on civil aviation to which they are parties, for example, the Tokyo Convention 1967, the Montreal Convention 1971 and the Convention for the Suppression of Unlawful Seizure of Aircraft 1970 (the Hijacking Convention). Some CARICOM States already have legislation in force in their territories on some of the matters provided for in the draft legislation prepared by the CARICOM secretariat.

2. International standards and recommended practices

33. The eighth edition of the International Standards and Recommended Practices (annex 9 to the Convention on International Civil Aviation) incorporates, *inter alia*, provisions arising from recommendations of the ninth session of the Facilitation Division (Montreal, April-May 1979) which again resulted in a comprehensive expansion and amendment of annex 9. This edition became effective on 15 July 1980, and applicable on 15 October 1980.

34. The Standards and Recommended Practices on Facilitation are the outcome of article 37 of the Convention, which provides, *inter alia*, that the "International Civil Aviation Organization shall adopt and amend from time to time, as may be necessary, international standards and recommended practices and procedures dealing with ... customs and immigration procedures ... and such other matters concerned with the safety, regularity and efficiency of air navigation as may from time to time appear appropriate". The policy with respect to the implementation by States of the Standards and Recommended Practices on Facilitation is strengthened by article 22 of the Convention, which expresses the obligation accepted by each Contracting State "to adopt all practicable measures, through the issuance of special regulations or otherwise, to facilitate and expedite navigation by aircraft between the territories of Contracting States, and to prevent unnecessary delays to aircraft, crews, passengers, and cargo, especially in the administration of the laws relating to immigration, quarantine, customs and clearance", and by article 23 of the Convention, which expresses the undertaking of each Contracting State "so far as it may find practicable, to establish customs and immigration procedures affecting international air navigation in accordance with the practices which may be established or recommended from time to time pursuant to this Convention".

D. LIABILITY OF INTERNATIONAL TERMINAL OPERATORS

35. For the work of UNIDROIT on the liability of international terminal operators (the warehousing contract) see A/CN.9/236, paragraphs 15-18 and 33-39.^e

^eReproduced in this volume, part two, V, C.

E. UNITED NATIONS CONVENTION ON INTERNATIONAL MULTIMODAL TRANSPORT OF GOODS^f

36. The United Nations Conference on International Multimodal Transport, in May 1980, adopted by consensus the United Nations Convention on International Multimodal Transport of Goods (TD/MT/CONF/17). The Convention establishes an international legal regime for the contract for the international multimodal transport of goods.

37. The Convention will enter into force 12 months after 30 States become parties to it. By 1 February 1983, two States had become parties to the Convention and four States had signed it subject to ratification. The entry into force of this Convention, however, is linked to the entry into force of the United Nations Convention on the Carriage of Goods by Sea,^g adopted in March 1978, which was prepared by UNCITRAL at the initiative of UNCTAD. By 7 April 1983, the latter Convention had been ratified or acceded to by nine States (signature only—25 States).

F. TRANSPORT BY CONTAINER

38. For the work of UNCTAD in this field, see A/CN.9/236, paragraphs 7-8; for the work of ISO, see *ibid.*, paragraphs 9-10; for the work of IMO, see *ibid.*, paragraphs 11-12.

G. CARRIAGE OF HEAVY AND BULKY NUCLEAR POWER EQUIPMENT IN INTERNATIONAL TRANSIT

39. On 11 March 1982 the CMEA Agreement on Provision for the Carriage of Particularly Heavy and Bulky Nuclear Power Equipment in International Transit came into force. The aim of the Agreement is to promote the more efficient use of all types of transport (rail, road, river and sea) with a view to providing for the international carriage of goods and speeding up the delivery of particularly heavy and bulky nuclear power equipment. The parties to the Agreement are the Governments of Bulgaria, Czechoslovakia, German Democratic Republic, Hungary, Poland, Romania and Union of Soviet Socialist Republics.

H. HARMONIZATION OF FRONTIER CONTROL OF GOODS

40. For the work of ECE in this field, see paragraphs 120-122 below.

I. CUSTOMS TRANSIT

41. For the work of ECE, CCC and ECLA in this field, see paragraphs 123-124 below.

^fYearbook ... 1978, part three, I, B (A/CONF.89/13, annex I).

^gSee also A/CN.9/225, paragraphs 11 and 18-20.

IX. International arbitration

A. ACTIVITIES CONCERNING SPECIALIZED TYPES OF ARBITRATION

1. Arbitration in the field of international contracts of building construction

42. In 1982, the Commission on International Arbitration of ICC adopted a report outlining suggested principles to be followed in the settlement of disputes involving building construction contracts. The report has been forwarded to the ICC Court of Arbitration for implementation. A final report is expected to be issued by the ICC Court of Arbitration before the end of 1983.

2. Arbitration and competition law

43. The Ad Hoc Arbitration and Competition Law Working Party, set up jointly by the Commission on International Arbitration of ICC, and the Commission on Law and Practices affecting Competition, has been working since 1978 on the elaboration of a study aimed at developing rules for arbitration in accordance with economic policies designed to ensure free competition. The arbitrability of disputes involving anti-trust law in national and community laws is being analysed, particularly in the light of recent court decisions.

3. Arbitral referee proceedings

44. The ICC continues its work on this project which is intended to promulgate rules for referee procedures in the field of arbitration, which would enable interim or preliminary decisions to be taken at an early stage in the arbitration proceedings.

4. Arbitration and State enterprises

45. The Institute of International Business Law and Practice has undertaken a study on the special problems of arbitration involving State enterprises which are increasingly involved in international trade, as it was thought that rules governing commercial disputes differ for State enterprises from those applicable in the private sector. The study, which will be published in 1983, will analyse the complications this implies for arbitration, as the most widely used technique for settling international commercial disputes.

B. PUBLICATION, RESEARCH AND OTHER DEVELOPMENTS²

46. The *Guide to Arbitration Law in Europe* was published by ICC in June 1981 (ICC publication 353).

The book features a series of standardized articles summarizing the principal features of arbitration law in 17 European countries. In September 1982, the ICC published a *Guide to Multi-party Arbitration* (ICC publication No. 404).

47. In 1982 the CMEA Conference on Legal Matters embarked upon a study of the practical application of the Convention on Settlement by Arbitration of Civil Law Disputes arising from Economic, Scientific and Technical Co-operation (26 May 1972), and also of the application by CMEA member countries of the Uniform Rules for Arbitration Tribunals (1974) on the basis of which the CMEA member countries approved national regulations for arbitration tribunals attached to their chambers of commerce. It is planned to prepare a report based on this work for examination in the CMEA member countries and to co-ordinate future work in this area.

48. ICCA continues to publish its *Yearbook: Commercial Arbitration*. Volume seven, published in 1982, contains national reports on arbitration law and practice, up-dating of national reports, national court decisions on the application of the New York Convention 1958³ and extracts of arbitral awards from arbitral institutions and *ad hoc* arbitrations.

49. Under the auspices of ICCA, the VIIth International Arbitration Congress (Hamburg, 7-11 June 1982) dealt with new trends in the development of international commercial arbitration and the role of arbitral and other institutions. The following topics were discussed in various working groups: (a) contributions which conventions, treaties and agreements can make to the development of arbitration; (b) resolving disputes involving commodities and raw materials; (c) new methods for resolving international commercial disputes; (d) developments in maritime arbitration. The reports and resolutions of that Congress will be published in May 1983.

X. Products liability

50. The Council of Europe has prepared the European Convention on Products Liability in Regard to Personal Injury and Death. This Convention was opened to signature in 1977, and has not yet come into force.

51. The Convention grants a supplementary right of action for damage causing death or personal injury where a product, by not providing the safety a person is entitled to expect, is considered to be defective.

52. For the work of UNIDROIT on the preparation of a convention on the civil liability for damage caused by hazardous cargoes, see paragraphs 23-26 above.

²With regard to other developments in the field of international commercial arbitration, see "Report of the Secretary-General: co-ordination of work in general" (A/CN.9/239) and "Report of the Secretary-General: training and assistance" (A/CN.9/240), both reproduced in this volume, part two, V, A and VII, respectively.

³United Nations, Treaty Series, vol. 330, No. 4739 (1959), p. 38.

XI. Private international law

A. WORK OF THE HAGUE CONFERENCE ON PRIVATE INTERNATIONAL LAW

53. At its fourteenth session in October 1980, the Hague Conference on Private International Law decided that a feasibility study should be undertaken on the law applicable to contractual obligations, to see whether a convention on this subject should be prepared. A report on this point is to be submitted at the Conference's fifteenth session, in October 1984. (See also A/CN.9/237/Add.1.).

B. WORK OF UNIDROIT

54. For the work of UNIDROIT, see A/CN.9/237/Add.1, I; see also paragraphs 55-56 and 66-71, below.

C. WORK OF CEC^h

54a. The CEC Convention on the Law Applicable to Contractual Obligations was signed in 1980. It is a complement to the Convention on Jurisdiction and Enforcement of Judgments in Civil and Commercial Matters, 1968, and is designed to facilitate the determination of the law applicable and to ensure that all the courts of the member States apply the same law to identical cases between the same parties.

XII. Other topics of international trade law

A. AGENCY

1. *Convention on Agency in the International Sale of Goods*

55. At the invitation of the Swiss Government a diplomatic conference was convened from 31 January to 17 February 1983 at Geneva, and the Convention on Agency in the International Sale of Goods was adopted on the basis of a draft text prepared by UNIDROIT's Committee of Governmental Experts held at Rome from 2 to 13 November 1981. At the invitation of UNIDROIT, States members of UNCITRAL that are not members of UNIDROIT attended this meeting to consider the draft.

56. Since the Convention does not cover rules relating to the internal relations between agents and principals involved in the international sale of goods, and because of some concerns expressed by some members of the Governing Council of UNIDROIT, this question may be considered at some future session of the Governing Council.

2. Powers of attorney

57. UNIDROIT has undertaken the preparation of uniform rules governing the validity of powers of attorney to be exercised abroad and, if possible, of a uniform form of power along the lines of the uniform international will established by the Washington Convention of 1973. At its sixtieth session, held in April 1981, the Governing Council decided that the preliminary comparative law study (study LXIII—doc. 1) should be circulated, with a questionnaire, to the interested circles. On the basis of the replies, a decision will be taken by the Council of UNIDROIT at its sixty-second session in May 1983 regarding the next steps to be taken in this connection.

3. Commercial agency

58. The Commission on International Commercial Practice of ICC is updating its existing Guide relating to commercial agency contracts. The Guide will serve as a check-list for agents and principals in the drafting and negotiating of contracts. It is anticipated that work on this project will be completed in the course of 1983.

58a.ⁱ CEC has proposed a Council Directive to co-ordinate the laws of the CEC member States relating to commercial agents. The aim of this proposal is to harmonize the laws of the member States governing relations between traders and their (self-employed) commercial agents, thereby removing the cost differences between the prices that traders have to pay. In some member States agents already enjoy protection; in others this protection is much less advanced. As a result the cost of employing agents varies from one member State to another.

B. BANKRUPTCY

59. At the end of 1980 a meeting was held jointly by CEC and CE to exchange information on the reforms in respect of bankruptcy which were contemplated by member States. As CEC had drawn up a draft Convention on Bankruptcy, it was thought useful that a committee of experts of CE should examine not only what was being done nationally in the way of reform in Europe, but also what supplementary action should be taken in this field of law which could be of interest to the 21 member States of CE. The Committee of Ministers of CE therefore decided to set up a committee of experts to deal with that question.

60. The Committee of Experts on Bankruptcy Law, a committee responsible to the European Committee on Legal Co-operation of CE, has been given the following terms of reference by the Committee of Ministers:

“Examination of the following items with a view to drawing up appropriate international

^hA/CN.9/237/Add.3, para. 3.

ⁱA/CN.9/237/Add.3, para. 4.

instruments (for instance, conventions or recommendations):

- “(i) Allowing the administrator in bankruptcy, for example, liquidator, official receiver or trustee, appointed according to a procedure opened abroad (list of procedures to be established) to act on behalf of the body of creditors and to recognize, *inter alia*, the possibility of the administrator taking protection measures and instituting legal proceedings;
- “(ii) Ensuring the right of foreign creditors to prove their claims in the national proceedings, and to this effect, ensure as far as possible the provision of adequate information and further to provide for the introduction of a standard form for the submission of claims by foreign creditors.

“Exchange of views and information:

- “(i) On reforms in the field of bankruptcy;
- “(ii) On measures intended to facilitate co-operation among member States in this field, such as the setting-up of a system of information concerning national bankruptcy proceedings likely to have effects abroad.”

61. The Committee of Experts on Bankruptcy Law, at its third meeting in December 1982 gave a first examination to a draft convention which, *inter alia*, would establish the right of the receiver to exercise abroad exclusive rights over the goods of a debtor if he was recognized as possessing those rights under the law of the State in which the voluntary bankruptcy proceedings were opened. The fourth meeting of the Committee of Experts will take place in June 1983.

C. BEARER SECURITIES

62. The Convention on Stops on Bearer Securities in International Circulation came into force in 1979 between Austria, Belgium, France and Luxembourg. The Office national des valeurs mobilières at Brussels has been designated by the Committee of Ministers of CE as the central office responsible for performing the functions prescribed by the Convention. Lists of bearer securities deemed to be in international circulation are published by the Secretary General of the Council of Europe.

D. BUSINESS TRUSTS

63. The subject of business trusts, as well as trust deeds and indentures used for securing the payment of indebtedness has been included in the programme of work of the Hague Conference on Private International Law. The decision to include these topics was made at the first meeting of the Special Commission, in June 1982.

E. COMPANY LAW

64. The CARICOM Working Party on Off-Shore Companies completed its deliberations after holding four meetings, and circulated its report to the Governments of member States of CARICOM in January 1982. The report recommends a number of legislative and administrative measures for the better regulation of off-shore companies operating within CARICOM.

65. Revised up-to-date company legislation was enacted by the Parliament of Barbados in 1982—The Companies Act 1982. The legislation adopts substantially recommendations for company law reform contained in the report of the CARICOM Working Party on the Harmonization of Company Law in the Caribbean Community. Proposals for company law reform adopting some of the recommendations of the Working Party have been published by the Government of Trinidad and Tobago for public comment.

65a.^j CEC issued a third Council Directive (78/855/EEC) concerning mergers of public limited liability companies which was implemented on 12 October 1981. The Directive contains specific provisions to safeguard the interests of shareholders of merging companies, those of employees and creditors in general, including debenture holders, and persons having other claims on the merging companies. Safeguards include, notably, supplementary disclosure requirements and the *ipso jure* transfer to the acquiring company of all assets and liabilities of the company being acquired, which ceases to exist. Similar safeguards are included in a supplementary directive on scissions or divisions of public companies governed by the law of the same member State. Division can be described as an operation in which the assets and liabilities of a company are divided between more than one successor company.

65b.^j CEC issued a fourth Council Directive (78/660/EEC) on the annual accounts of certain types of companies which was implemented on 31 July 1980. (This Directive has been implemented in some Member States and remains to be implemented in others.) This Directive, which has as its aim the protection of creditor, regulates in detail the form and content of the annual accounts of individual companies.

65c.^j CEC proposed a fifth Directive on the structure of public limited liability companies and the powers and obligations of their organs. This proposal concerns the board structure of public companies and the issue of employee participation in that structure.

65d.^k CEC issued the sixth Council Directive (82/891/EEC) concerning divisions of public limited liability companies which was adopted on 17 December 1982 and will be implemented on 1 January 1986. Similar to the third Directive, its aim is to safeguard the interests of shareholders, employees and creditors.

^jA/CN.9/237/Add.3, paras. 6, 7 and 8 respectively.

^kA/CN.9/237/Add.3, paras. 9, 10, 11 and 12 respectively.

65e.^k An amended proposal (proposed seventh Directive) on group accounts is being discussed in the Council and could be adopted during 1983. It is intended to regulate the form and content of consolidated accounts.

65f.^k CEC's proposal for a Council regulation on the statute for European companies seeks to establish a legal structure, available throughout the Community, which would permit undertakings to establish themselves or reorganize their businesses at a European level (by merger, creation of holding companies or joint subsidiaries) rather than to continue to rely on different national systems operating side by side. The first reading of the proposal has been nearly completed by an *ad hoc* group in Council. Only titles V (employee representation), VI (annual accounts) and VII (groups) still remain to be examined.

65g.^k The CEC draft Convention on the International Mergers of Public Limited Liability Companies aims to make mergers between companies established under the laws of different states possible.

F. PROTECTION OF THE ACQUISITION IN GOOD FAITH OF CORPOREAL MOVABLES

66. Following the completion by the UNIDROIT Committee of Governmental Experts of its work on the draft Uniform Law on the Protection of the Acquisition in Good Faith of Corporeal Movable, the UNIDROIT secretariat engaged in consultations for the convening of a diplomatic conference for its adoption.

67. The draft Uniform Law was the subject of detailed discussion by the Governing Council of UNIDROIT at its sixty-first session (April 1982) on which occasion differing opinions were expressed. In the view of some members of the Council, the draft touched upon extremely delicate problems relating to third party rights which experience had shown to be a less fruitful terrain for unification than was the case with contractual relations. There was in addition considerable doubt in their minds as to whether solutions could be found which would satisfy a sufficiently large number of States, given the wide divergencies at present existing between the various national laws in this field. The question was also raised as to whether the scope of application of the draft, which laid down the same rules for cultural property as for industrial goods and agricultural products, was not too ambitious.

68. A majority of members of the Council however expressed continuing interest in the draft and while admitting that some of the solutions contained in it might not be suited to all types of property, they considered that a resumption of work on it should be contemplated at some time in the future. Attention was in particular drawn to the work currently in progress in UNESCO on the return of cultural property and to the fact that the responsible committee had shown interest in UNIDROIT's draft.

69. In these circumstances the Council agreed that enquiries should be conducted with the appropriate officials in UNESCO into the possibility of co-operation between UNESCO and UNIDROIT in this regard and that the secretariat should report back to the Council at its next session on the outcome of consultations and on the prospects of collaboration between the two organizations on the basis of the draft Uniform Law on the Acquisition in Good Faith of Corporeal Movable. In the light of this information a decision could then be taken by the Council as to the form which any future work on the draft might assume.

70. In accordance with these instructions the secretariat contacted the secretariat of UNESCO's Cultural Heritage Division and the possibility was discussed of the Uniform Law on the Acquisition in Good Faith of Corporeal Movable being revised either as a separate instrument or in the form of a Protocol to the 1970 UNESCO Convention on the Means of Prohibiting and Preventing the Illicit Import, Export and Transfer of Ownership of Cultural Property, in respect of which Convention considerable difficulties had been encountered in connection with the interpretation of the terms "innocent purchaser" and "person who has valid title to the property" (article 7, paragraph (b) (ii)).

71. It was agreed that the two secretariats would raise the question of including this item on the work programmes of their respective organizations with the competent bodies for the preparation of those programmes as soon as possible and that in the meantime thought might be given to the form which co-operation between the two organizations could assume.

G. RIGHTS OF CREDITORS

72. The CE Committee of Experts on the Rights of Creditors has completed its work and adopted a draft Convention and explanatory report on simple reservation of title. These texts will be submitted to the Committee of Experts at its next meeting which is to be held from 27 June to 1 July 1983 and then sent to the Committee of Ministers of CE for adoption. This draft Convention was prepared by CE in close co-operation with CEC.

73. After noting the difficulty in harmonizing all the different types of creditors' rights the Committee of Experts decided to limit the Convention to simple reservation of title which was one of the most widespread means of guaranteeing creditors rights.

74. This draft lays down the conditions for recognition and enforcement of simple reservation of title, and aims at safeguarding the rights of creditors internationally, thus facilitating commercial relations in Europe. It also aims at setting up a relatively simple recognition system to meet practical needs.

75. The most important provision in the draft concerns the scope of the Convention (ships and aircraft being excluded); the definition of "reservation

of title"; the goods subject to this reservation; the time and conditions of transfer of title; the formal conditions governing the reservation which must be in writing; and the effects of the Convention, which allow goods to be recovered even in case of bankruptcy.

H. CONSUMER PROTECTION

76. By decision 10/24, the Governing Council of UNEP at its tenth session (Nairobi, 31 May 1982) authorized the Executive Director to convene in 1983/84, after consultations with Governments and the international agencies concerned, a meeting of government experts to consider guidelines or principles on the exchange of information relating to trade in, and use and handling of potentially harmful chemicals, in particular pesticides. Decision 10/24 was based on the recommendations of the *Ad Hoc* Meeting of Senior Government Officials Expert in Environmental Law (Montevideo, 28 October to 6 November 1981), the report of which was approved by the Governing Council of UNEP in decision 10/21. The programme for the development and periodic review of environmental law, as adopted by this decision, includes as an objective "to control international trade in hazardous or inadequately tested chemicals, particularly where the sale of such substances has already been banned or restricted in the producing country". The strategy for this objective includes the "preparation of guidelines at the global level as a first step towards a global convention; development and implementation of internationally harmonized practices, in particular for the gathering and dissemination of information".

77. The Montevideo programme suggested the following first steps in this subject area:

"UNEP should consider convening an inter-governmental meeting of experts for the development of principles or guidelines on the exchange of information in relation to the trade in potentially harmful chemicals, drawing upon, *inter alia*, the results of the discussions on the subject, in the General Assembly".

78. The General Assembly, by resolution 34/173 (17 December 1979), had urged States members to exchange information on hazardous chemicals and unsafe pharmaceutical products that had been banned in their territories and to discourage, in consultation with importing countries, the exportation of such products to other countries. The General Assembly further specified the action to be taken by States members and by the United Nations Secretariat in resolutions 35/186 (15 December 1980); 36/166 (16 December 1981); and 37/137 (17 December 1982) on protection against products harmful to health and the environment.

79. It is noted that an earlier UNEP Governing Council decision (85/V of 25 May 1977) had urged Governments "to take steps to ensure that potentially

harmful chemicals, in whatever form or commodity, which are unacceptable for domestic purposes in the exporting country, are not permitted to be exported without the knowledge and consent of appropriate authorities in the importing country". The Governing Council had further specified the action to be taken by Governments and by the Executive Director in decision 6/4 (24 May 1978), which in turn was communicated to the General Assembly in the report of the Economic and Social Council on "Exchange of information on banned hazardous chemicals and unsafe pharmaceutical products" (A/36/255, 22 May 1981).

80. In order to implement decision 10/24, the Executive Director has initiated a follow-up project (FP/1002-82-02) for the preparation of *ad hoc* inter-governmental expert meetings, in consultation with the competent international organizations. Phase one of the follow-up project provides for the preparation of background and working documents by July 1983, to be reviewed by the Advisory Panel on Toxic and Dangerous Wastes and Harmful Chemicals and by specialized agencies for technical input as appropriate.

81. In 1981 the Committee of Ministers of CE adopted recommendation No. R(81)2 on the legal protection of the collective interests of consumers by consumer agencies. The principles in the recommendation deal with the provision of information and assistance to consumers, requests to suppliers, conciliation or arbitration, negotiation with trade and industry, participation in the preparation of legislation, stopping suppliers acting contrary to the law, institution or participation in proceedings and co-operation between agencies.

81a.¹ CEC's proposal for a Directive concerning liability for defective products aims to remove distortions of competition resulting from differences in national rules, as the resale prices of products are higher in those countries where the rules are stricter. It also seeks to eliminate certain barriers to the free movement of goods and to reinforce consumer protection. The proposal has, since January 1980, been the subject of discussions in the Council by a group of government experts.

I. CODE OF MARKETING FOR BREAST-MILK SUBSTITUTES

82. The WHO International Code of Marketing of Breast-Milk Substitutes was adopted as a recommendation by the thirty-fourth World Health Assembly in May 1981. The aim of this Code is to contribute to the provision of safe and adequate nutrition for infants, by the protection and promotion of breast-feeding, and by ensuring the proper use of breast-milk substitutes, when these are necessary, on the basis of adequate information and through appropriate marketing and distribution.

¹A/CN.9/237/Add.3, para. 5.

83. The Code applies to the marketing, and practices related thereto, of the following products: breast-milk substitutes, including infant formula; other milk products, foods and beverages, including bottled/complete foods, when marketed or otherwise represented to be suitable, with or without modification, for use as a partial or total replacement of breast-milk; feeding bottles and teats. It also applies to their quality and availability, and to information concerning their use.

J. MULTILATERAL AGREEMENT FOR COMBATING CUSTOMS FRAUD AND SMUGGLING

84. ESCAP, in co-operation with UNCTAD, has initiated work towards evolving a mutual co-operative arrangement among countries of the ESCAP region in combating customs fraud and smuggling which have caused a serious threat to the revenue collection and economic controls in the developing countries of the ESCAP region. In this regard, the ESCAP/UNCTAD Seminar on Anti-fraud and Anti-smuggling Measures was convened at Bangkok in April 1981 to bring about greater awareness of the problems involved in controlling customs fraud and smuggling and to consider possible solutions to those problems.

85. At the Seminar a set of recommendations for mutual administrative assistance and co-operation among customs administrations for action against customs fraud and smuggling was formulated, and the Executive Secretary of ESCAP was requested to convene a high-level expert group meeting to consider those recommendations. Based on the recommendations, the ESCAP secretariat prepared a tentative draft of a multilateral agreement on mutual administrative assistance for the prevention, investigation and repression of customs offences and presented it to the UNCTAD/ESCAP Expert Group Meeting on Arrangements for Mutual Administrative Assistance and Co-operation among Customs Administrations of ESCAP Countries for Action against Customs Fraud and Smuggling which was held at Kathmandu in January 1982, for consideration. The draft multilateral agreement was examined and finalized by the experts, and transmitted to the member and associate member countries of ESCAP, for consideration. A number of countries have expressed their intention to endorse the agreement while others have informed that they would need more time to examine it in detail before they would be able to endorse it.

86. A follow-up meeting to the UNCTAD/ESCAP Expert Group Meeting on Arrangements for Mutual Administrative Assistance and Co-operation among Customs administrations of ESCAP Countries for Action against Customs Fraud and Smuggling was held at Bangkok from 29 March to 1 April 1983, to consider the draft multilateral agreement and finalize it for possible adoption by the member and associate member countries of ESCAP.

K. CONTRACT GUARANTEES, GUIDELINES ON SIMPLE DEMAND GUARANTEES AND SURETY GUARANTEES

87. Work has recently been completed on the preparation of model forms for issuing contract guarantees subject to the ICC's Uniform Rules for Contract Guarantees.

88. The ICC's Commission on Banking Technique and Practice, and the Commission on International Commercial Practice are currently preparing a Code of Practice on simple demand guarantees. The aim of this work is to give guidance to banks and other guarantors called on to issue guarantees payable on the simple or first demand of the beneficiary without proof of loss or of default in the underlying commercial contract. In particular, the purpose is to minimize the possibilities of abuse of such guarantees, especially to the detriment of the principal.

L. EXPORT CREDIT GUARANTEE FACILITY

89. The question of establishing an international export credit guarantee facility (ECGF), to give support to developing countries' exports, has been extensively discussed within UNCTAD. At its eighth session, the UNCTAD Committee on Invisibles and Financing related to Trade (CIFT) dealt with policy and technical issues relating to the establishment of a facility. In its resolution 15 (VIII) and decision 17 (IX) the Committee requested the secretariat, in consultation with member States and international institutions and with the assistance of financial experts, to formulate detailed operational features of a facility. The secretariat prepared a study entitled "The operational characteristics of an export credit guarantee facility" (TD/B/AC.33/2 and Corr. 1) which was considered by a group of experts meeting in January 1982 (TD/B/889). The Committee on Invisibles and Financing related to Trade, at the second part of its tenth session in February/March 1983, will further consider this study as well as a recent report entitled "Evaluation of the operational features of an export credit guarantee facility" (TD/B/C.3/183/Add.1, 2 and 3).

M. INTERNATIONAL LEASING

90. The preliminary draft uniform rules on international leasing (study LIX — doc. 13 rev.) was considered by the Governing Council of UNIDROIT at its sixtieth session, held at Rome from 22 to 24 April 1981. Two decisions were taken in its regard on that occasion. First, the Council endorsed the recommendation of the UNIDROIT Study Group that, given the novelty of leasing, it would be preferable to delay the eventual transmission of the text to a committee of governmental experts for the hammering out of a final text until such time as the preliminary draft has been given maximum exposure among practitioners by the organization of symposia in the different parts of the world. The Council's second decision was, pursuant to

the offer made by the Deputy Secretary General of the Hague Conference on Private International Law on the occasion of the third session of the Study Group, to agree that the assistance of the Hague Conference should be sought in revising article 2 of the preliminary draft, given its private international law ramifications.

91. Pursuant to the Council's first decision, symposia have been organized in New York (May 1981) and at Zurich (November 1981), addressed to an audience of bankers, businessmen and lawyers having expertise in international leasing.

92. Further to the Council's second decision, the UNIDROIT secretariat in April 1981 formally requested the assistance of the Hague Conference in revising article 2 of the preliminary draft. At the meeting of the Special Commission of the Conference in June 1981 this request was favourably received and the Permanent Bureau of the Conference is now looking into the problems of private international law raised by article 2 of the preliminary draft, with a view to proposing in due course a new wording of that provision.

N. INTERNATIONAL FACTORING

93. The preliminary draft uniform rules on certain aspects of international factoring (study LVIII—doc. 12) were approved by the UNIDROIT Study Group at its third session held from 19 to 21 April 1982.

94. One of the principal features of the draft rules is the affirmation of the commercial or professional character of the receivables which the supplier undertakes to assign to the factor on a continuing basis by way of sale or security. As consideration for the assignment, the factor provides certain services such as financing, the maintenance of accounts, collection of receivables and protection against credit risks. The international character of the factoring contract is based on the fact that it relates to receivables arising from a contract for the sale of goods or provision of services between parties whose places of business are situated in different States, with the rider that if a party has more than one place of business, his place of business for the purpose of the provision is that having the closest relationship to the contract of sale and its performance. Since it is the original sales contract which confers on the contract of factoring its international character, the proposed rules also apply to successive assignments between several factors, even though their places of business are situated in the same State.

95. With a view to encouraging factoring operations, the assignment of receivables by the supplier to the factor, including in certain circumstances future receivables, will be effective notwithstanding any agreement between the supplier and the debtor prohibiting such assignment. The factoring contract or any assignment made pursuant to it may validly provide for the transfer to the factor of all or any of the supplier's rights under the contract of sale, including any provision in such contracts reserving title to the supplier.

96. The factor is further protected by a provision to the effect that he shall not, by reason only of transfer of title to goods to him, incur liability to a third party for loss, injury or damage caused by the goods. On the other hand, he may be held liable if he sells or otherwise disposes of the goods to a person who is not the supplier or another factor or the debtor.

97. Another important feature of the rules is that they are intended to apply only in relation to factoring contracts pursuant to which notice of assignment of the receivables is to be given to the debtor. It is also provided that for the assignment to be effective against the debtor the notice must be given to the debtor in writing and reasonably identify the receivables which have been assigned and the person to whom the debtor is required to make payment. The notice must contain a statement that the assignment is governed by the uniform rules. Furthermore the notice is effective only in relation to a receivable arising under a contract concluded at or before the time the notice is given.

98. On the other hand, when the factor claims payment of a receivable arising under a contract of sale, the debtor may set up against the factor all defences of which the debtor could have availed himself under the contract if such claim had been made by the supplier. The debtor may also exercise against the factor any right of set-off, in respect of claims existing and available to the debtor at the time the debtor received notice of the assignment, against the supplier in whose favour the receivable arose. However, non-performance or defective or late performance of the contract of sale by the supplier does not entitle the debtor to recover money paid by the debtor to the factor except in the cases mentioned above.

99. Finally a debtor in good faith who has no reason to know of any other person's right to payment of a receivable and who pays the factor pursuant to a notice of assignment given by the supplier or by the factor with the supplier's actual or apparent authority will be discharged pro tanto of his liability even though the receivable had not been validly assigned to the factor by the supplier or the right to payment of the receivable was vested in a third party.

100. The Study Group was, in addition, of the opinion that it was not advisable at the present time to attempt to regulate the content of contracts between factors and suppliers or to lay down rules governing contracts between factors as these appeared to be areas where the contracts which are used by the practitioners and their customers seemed to give satisfaction. Nor does the draft seek to determine the validity of the factoring contract which is to be decided by the law applicable to that contract.

101. Similarly the Group ultimately abstained from providing in the rules a solution to the problem of priorities, i.e. competing claims of a factor and of a third party, both of whom have rights over the receivables assigned by the supplier, since it did not seem possible to lay down a substantive uniform rule,

given the wide differences in national law. Moreover, the search for a conflicts rule led to fairly clear solutions, but on detailed examination each of these was shown to present drawbacks.

102. The preliminary draft rules approved by the Group will now be distributed among circles interested in factoring so as to obtain the greatest number of reactions and observations. Thereafter the criticisms and suggestions made with regard to the text will be analysed and the Study Group perhaps reconvened to see whether the draft should be enlarged or amended or, if it is deemed to be sufficiently complete, pass on to a new state, such as its submission to Governments for observations or even to a committee of governmental experts for consideration.

O. MULTINATIONAL MARKETING ENTERPRISES

103. The Committee on Economic Co-operation among Developing Countries in its resolution 1 (I), establishing the UNCTAD work programme on economic co-operation among developing countries, decided that multinational marketing enterprises among developing countries would be one of the priorities for further work. In response to this resolution, the secretariat prepared studies dealing with the legal and institutional aspects of this subject, including "Juridical aspect of the establishment of multinational marketing enterprises among developing countries" (TD/B/C.7/28/Rev.1); "Individual aspects of the establishment of multinational marketing enterprises among developing countries—selection of constituent instruments of multinational enterprises compiled by the UNCTAD secretariat" (TD/B/C.7/28/Rev. 1, annex I); "Selection of juridical texts" (TD/B/C.7/28/Rev. 1, annex II); "Juridical regimes for the establishment of multinational enterprises among developing countries organized in integration and economic co-operation groupings" (TD/B/C.7/30); and "Latin American multinational enterprises: an analytical compendium" (TD/B/C.7/50).

P. RESTRICTIVE BUSINESS PRACTICES

1. *Set of multilaterally agreed equitable principles and rules for the control of restrictive business practices*

104. The Trade and Development Board of UNCTAD at its twenty-second session, in March 1981, established by resolution 228 (XXII) an Intergovernmental Group of Experts on Restrictive Business Practices to perform the functions described in section G of the Principles and Rules for the Control of Restrictive Business Practices, which form a comprehensive programme of work on the monitoring, implementation and review of the Principles and Rules. This Group at its first session, in November 1981, by resolution 1 (I) invited all countries to take appropriate steps at the national or regional levels to meet their commitments under the Principles and Rules and to communicate annually to the Secretary General of UNCTAD appropriate information in that regard (TD/B/884, annex I).

2. *Model law on restrictive business practices*

105. The UNCTAD Intergovernmental Group of Experts by the same resolution 1 (I) decided to continue its work of a model law on restrictive business practices. The Group requested the secretariat to submit to it at its second session, in October 1983, a draft of a model law or laws, in accordance with the provisions of the Principles and Rules.

106. Recent reports on restrictive business practices issued by the secretariat include: "Marketing and distribution arrangements in respect of export and import transactions: structure of international trading channels, 1981" (UNCTAD/ST/MD/25), and "Annual report, 1981, on legislative and other developments in developed and developing countries in the control of restrictive business practices" (TD/B/RBP/9).

Q. LABOUR

107. The activities of ILO pertaining to labour and its related aspects are: Collective Bargaining Convention, 1981 (No. 154); Collective Bargaining Recommendation, 1981 (No. 163); Occupational Safety and Health Convention, 1981 (No. 155); Occupational Safety and Health Recommendation, 1981 (No. 164); Workers with Family Responsibilities Convention, 1981 (No. 156); Workers with Family Responsibilities Recommendation, 1981 (No. 165); Maintenance of Social Security Rights Convention, 1982 (No. 157); Termination of Employment Convention, 1982 (No. 158); and Termination of Employment Recommendation, 1982 (No. 166).

108. ILO also prepared the following codes of practice, guides and manuals: Model Code of Safety Regulations for Industrial Establishments (revision expected to be completed during the next two biennia); Code of Practice on Safety in Haulage and Transport Operations in Mines (draft of Code completed in French and English); Code of Practice on Safety and Health in the Iron and Steel Industry (in print); Code of Practice on Radiation Protection of Workers in Mining and Milling of Radioactive Ores (part VI of ILO Manual of Industrial Radiation Protection—a joint IAEA/ILO/WHO publication. The draft, approved by the Governing Body in November 1982, will be published by IAEA); and Code of Practice for the Safe Use of Asbestos (the draft will be submitted to a meeting of experts in September 1983).

109. In 1980 the CMEA secretariat issued a model statute on the working conditions of workers in international enterprises. This model statute was approved by the CMEA Conference on Legal Matters for use by CMEA member countries and CMEA bodies at their discretion. The document is intended to apply in those cases where an international enterprise is established by international agreement and the rules governing the working conditions of its staff are approved by the parties to the agreement.

R. CUSTOMS AND TARIFFS

1. *The GATT Valuation Agreement*

110. On 1 January 1981 the Agreement on Implementation of article VII of the General Agreement on Tariffs and Trade entered into force. It is a new international customs valuation system, which resulted from the Multilateral Trade Negotiations in GATT. Most of the major trading countries of the world have already adopted or undertaken to adopt this system.

111. Under the provisions of the Agreement a Technical Committee on Customs Valuation is established, under the auspices of CCC, to be responsible for uniformity in interpretation and application of the Agreement at the technical level. This Committee is composed of representatives of the contracting parties to the Agreement; the remaining Council members, and other countries, may be represented as observers.

112. The Committee has commenced the issue of instruments to clarify the treatment of various questions arising from the Agreement. The instruments take the form of advisory opinions, commentaries, explanatory notes and case studies, and they are published by the Council in a loose-leaf compendium. The Committee may also make recommendations to a GATT Committee on Customs Valuation for amendment or modification to the Agreement. Under the Plan for the 1980's CCC is preparing a model training course on the Agreement.

2. *Agreements on abolition of customs duties on educational, scientific and cultural materials sponsored by UNESCO*

113. The following UNESCO sponsored agreements serve to free educational, scientific and cultural materials from customs duties:

(a) Agreement for Facilitating the International Circulation of Visual and Auditory Materials of an Educational, Scientific and Cultural Character (the Beirut Agreement) 10 December 1948;

(b) Agreement on the Importation of Educational, Scientific and Cultural Materials and Protocol (the Florence Agreement) 17 June 1950; this Protocol to the Florence Agreement, adopted on 26 November 1976 by the UNESCO General Conference, entered into force on 2 January 1982. It extends customs-duty exemption to various groups of materials not covered by the Florence Agreement, such as sports equipment, musical instruments, materials and machines for book production.

3. *Standardized regulations on preferential tariffs*

114. The CMEA Agreement on Standardized Regulations Governing the Origin of Goods from Developing Countries in the Awarding of Preferential Tariffs under the General System of Preferences entered into force on 24 March 1981 between Bulgaria, Czechoslovakia, Hungary, Poland and the Union of Soviet

Socialist Republics. The purpose of this Agreement is to guarantee the most favourable conditions possible for access to goods coming from developing countries and standardizing the regulations governing the origin of such goods in the awarding of preferential tariffs, while at the same time taking into account resolutions 21 and 24 of the second session of UNCTAD and resolution 96 of this Conference's fourth session.

S. TAXATION

1. *CMEA agreements on abolition of double taxation on income and property*

115. On 1 January 1979 the CMEA Agreement on the Abolition of the Double Taxation on Income and Property of Juristic Persons and the Agreement on the Abolition of the Double Taxation on Income and Property of Physical Persons entered into force between Bulgaria, Czechoslovakia, German Democratic Republic, Hungary, Mongolia, Poland, Romania and the Union of the Soviet Socialist Republics. These agreements are designed to create more favourable conditions for the development of economic, scientific and technical co-operation and cultural exchange. They are based on the principle that juristic and physical persons should not be liable at the same time to taxation on the same income and property in two or more States party to the agreements.

2. *Proposals for the resolution of international tax conflicts arising under conventions for the avoidance of double taxation*

116. The ICC Commission on Taxation is examining problems involved in the mutual agreement procedure, the principal method for the resolution of international tax conflicts at present. The Commission will consider proposing amendments which could ameliorate the mutual agreement procedure and will examine the possibility and advisability of the use of arbitration or the creation of an international fiscal jurisdiction to dispose of cases not adequately resolved under the mutual agreement procedure.

3. *Tax treatment of interest in international economic transactions*

117. The ICC Commission on Taxation is elaborating proposals for a uniform fiscal approach to the treatment of interest in international economic transactions.

T. RECOMMENDATIONS TO PROMOTE TRADE

118. At its 57th/58th session in June 1981, CCC adopted the following recommendations:

(a) *Recommendation concerning the transmission and authentication of goods declarations which are processed by computer*

This recommendation provides that customs administrations allow declarants to

use electronic or other automatic means to transmit goods declarations to customs for automatic processing and that customs authorities accept that goods declarations so transmitted can be authenticated by means other than handwritten signature.

- (b) *Recommendation concerning time tolerance in the application of interpretative note 5 to article I of the Definition of Value*

This recommendation provides that when goods are being valued on the basis of the price paid or payable, under the Brussels Definition of Value, no adjustment should be made to take account of price fluctuations occurring between the date of the contract of sale and the time of valuation, provided that the contract of sale is executed within a period consistent with normal practice in the trade concerned.

- (c) *Recommendation concerning the overriding application of interpretative note 5 to article I of the Definition of Value*

This recommendation provides that when it is possible to determine dutiable value, under the Brussels Definition, on the basis of the price paid or payable, no other method of valuation should be used.

119. At its 59th/60th sessions in June 1982, CCC adopted the following recommendations:

- (a) *Recommendation concerning the production of goods declarations by means of computer or other automatic printers*

This recommendation provides that customs administrations authorized declarants to produce their goods declarations by means of computer or other automatic printers on preprinted forms or on plain paper.

- (b) *Recommendation concerning the use of the ISO alpha-2 country code for the representation of names of countries*

This recommendation provides that customs administrations use the two-letter alphabetic code referred to in International Standard ISO 3166 as the "ISO alpha-2 country code" for the representation of names of countries in international data exchange.

- (c) *Recommendation concerning the use of a code for the representation of modes of transport*

This recommendation provides that customs administrations use the one-digit numeric code structure contained in recommendation No. 19 of the Working Party on Facilitation of International Trade (UN/ECE) for the representation of modes of transport in international data exchange.

- (d) *Recommendation concerning the establishment of links between customs transit systems*

This recommendation, which was developed in close co-operation with ECE, provides that States and customs or Economic Unions attempt to establish a link between the customs transit systems in force in their respective territories and, to this end, to conclude bilateral and multilateral agreements if required for this purpose.

XIII. Facilitation of international trade

A. HARMONIZATION AND FACILITATION OF ADMINISTRATIVE PROCEDURES RELATING TO GOODS AND DOCUMENTS

1. Harmonization of frontier control of goods

120. The ECE Inland Transport Committee adopted the International Convention on the Harmonization of Frontier Control of Goods at its thirty-third (special) session in October 1982. Article 9 of the Convention provides that the contracting parties must endeavour to further the use, between themselves and with the competent international bodies, of documents aligned on the *United Nations Layout Key for Trade Documents* (United Nations publication, Sales No. E.81.II.E.19). (See also A/CN.9/225,^m paragraphs 8-9).

121. In connection with the draft International Convention on the Harmonization of Frontier Control of Goods, ECLA took part in the forty-sixth special session of the ECE Group of Experts on Customs Questions relating to Transport, and in view of the importance of this Convention in facilitating international transport in the countries of the region, it has circulated the contents of the draft and the steps taken within ECE to negotiate the Convention.

122. At the twelfth Meeting of Ministers of Public Works and Transport of the Southern Cone countries (Asunción, 18-22 October 1982) the question of delays in passing frontiers was discussed and an agreement was adopted asking ECLA to co-operate with the countries in studying the International Convention on Harmonization of Frontier Control of Goods. ECLA will carry out this task during 1983 on the basis of information provided by ECE in connection with the final draft approved for the Convention.

2. Customs

(a) Customs transit

123. The ECE Inland Transport Committee is continuing its project involving consideration of the possibility of establishing a link between the different existing systems of customs transit. The legal issues

^mYearbook ... 1982, part two, VI, B.

involved in the project concern, *inter alia*, mutual recognition of the validity of the information contained in the transit documents, acceptance of seals, and administrative co-operation. No decision has yet been made as to the establishment of a link between customs transit systems and the form (resolution or convention) that an eventual link would take.

124. The following international organizations participated in the work on that project: CEC, CCC and IRU. CCC, having undertaken similar work in the past, resumed consideration of this question parallel with the work of ECE and adopted a resolution on the matter as did the Inland Transport Committee of ECE at its forty-fourth session in February 1983. ECLA has been promoting the application of an international customs transit system such as the TIR Convention of 1975. In November 1982 an agreement was formalized with LAIA for jointly promoting the signing of a partial agreement, under the LAIA Montevideo Treaty of 1980, for the application of an international customs transit system based on the provisions of the 1975 TIR Convention. A draft agreement has been drawn up which has been discussed with the customs authorities of Argentina, Brazil, Chile, Paraguay and Uruguay. Once the process of consultation with the different national customs authorities is completed, negotiations on the draft agreement will be conducted.

(b) *Promotion of the International Convention on the Simplification and Harmonization of Customs Procedures (Kyoto Convention)*

125. CCC has undertaken a programme to promote the widest possible adoption and implementation of the Kyoto Convention, which CCC completed in June 1980 when it adopted the last four of the annexes to the Convention. The Convention is made up of a body of rules for its implementation and 30 annexes, each dealing with a separate customs procedure. The Convention and 19 of its annexes have entered into force. Thirty-eight countries and EEC have become contracting parties to the Convention by accepting at least one of its annexes.

126. In co-operation with national customs administrations, CCC has undertaken a series of seminars to explain the Convention and its practical application. Seminars have been held at Vienna, Austria, in November 1981; at Ouagadougou, Upper Volta; with the assistance of the West African Economic Community (CEAO), in June 1982; and at Blantyre, Malawi, in December 1982. Seminars are scheduled to be held in the United States of America with the assistance of CARICOM, in April 1983, and in France on a date still to be set.

127. In addition, CCC has published the Convention in a brochure entitled "Introducing the Kyoto Convention" which sets out the benefits of the Convention and the procedure for acceding to it. The Council has also undertaken a series of detailed studies in selected areas within the Convention of which five have been completed and an additional six are being prepared for consideration by the Council at its June 1983 sessions.

3. *Commodity classification for requirements of customs, statisticians and carriers*

128. CCC's plan for the 1980's gives first priority to the completion of the Harmonized System in 1983. This will be a new and expanded international commodity description and coding system for use in customs classification, international trade statistics and transportation. There has been regular liaison on the development of the System between the CCC secretariat and the secretariats of the United Nations Statistical Office and the UN/SOEC Joint Working Group on World Level Classifications. A paper which will be submitted to the Council in June 1983 sets 1 January 1985 as the earliest date for implementation of the System.

129. In 1983, CCC will publish the first brochures setting out the essential features of the Harmonized System, its advantages and the obligations involved in joining it. In 1984, CCC and ECA will jointly organize a training course aimed at preparing eastern, central and southern African countries for the introduction of the System; and in 1985, CCC will hold a training course on the System at its headquarters at Brussels.

130. The main objective of the System is to provide simultaneously, at a developed and internationally agreed level of detail, for the major needs of authorities, statisticians, carriers and producers. To the maximum extent possible, all these interests, together with organizations involved in trade facilitation, are represented on the Harmonized System Committee (HSC) or its Working Party, charged with the development and implementation of the System. More than 50 countries, groups of countries and national or international organizations have taken part in the work of the HSC and its Working Party.

131. In preparing the System the HSC has taken into account a wide range of classification systems (including certain important systems not based on the Customs Co-operation Council Nomenclature, chosen as being representative of the requirements of customs, statisticians and carriers.

132. The complete package of proposals will be submitted to CCC in June 1983. The System, as a new Convention, will be introduced concurrently with the new version of the Customs Co-operation Council Nomenclature, and a submission to CCC in June 1983 sets 1 January 1985 as the earliest date for implementation. Following a period of transition the System will replace the Customs Co-operation Council Nomenclature.

133. From the outset it has been the intention that the System should be a multi-purpose international system. In the area of statistics, the external trade aspect was covered by terms of reference which required that the provisions of the Standard International Trade Classification (SITC, Rev.2) should, wherever possible, be respected. The need for a better correlation with production statistics was also stressed in 1973 in the report of a study group to CCC.

134. Concerning the SITC there has never been any question but that there should continue to be a correlation between the Customs Co-operation Council Nomenclature (and the subheadings of the System) and the SITC. It was, however, inevitable that the major review of the Customs Co-operation Council Nomenclature which is now nearing completion would result in the need for a third revision of the SITC. For wholly practical reasons, SITC (Rev. 3), the new Customs Co-operation Council Nomenclature and the System will enter into operation on the same date.

135. CCC will undertake its own training programmes on CCC and CCC-administered instruments, specifically the International Convention on the Simplification and Harmonization of Customs Procedures (Kyoto Convention), the GATT Valuation Code and the Harmonized System.

4. Rules of origin of goods

136. At its 59th/60th sessions in June 1982, CCC decided with regard to rules of origin of goods that, as a first step, it should identify and assist countries to remove from their systems those rules of origin which were particularly difficult to apply and to control.

137. An initial study of the subject has been completed by the secretariat with the assistance of 14 member countries and ECLA, GATT, CARICOM, Cartagena Agreement, CEAO, CEC, ECOWAS, EFTA and UNICE. The study has been circulated for comments by member countries and interested international organizations and will be considered by the CCC Permanent Technical Committee at its May 1983 meetings.

138. The question of what kind of international instrument might be developed to implement this project has not been decided. However, the CCC Policy Commission has this question and the question of further involvement of CCC in the field of rules of origin under consideration and will make recommendations to CCC for its consideration at its sessions in June 1983.

B. MEASURES DESIGNED TO FACILITATE TRANSPORTATION

139. The activities of CCC involve the following measures designed to facilitate transportation:

(a) Organization of meetings of the Administrative Committee for the Customs Convention on Containers (next meeting to be held at the end of 1983);

(b) Co-operation with ECE in the preparation of a recommendation establishing a link between transit systems (1982) and eventual development of further international instruments in this field (1983);

(c) Co-operation with ECE in the elaboration of an international Convention for facilitation of road traffic (similar to the instruments developed by IMO for maritime traffic and by ICAO for air traffic);

(d) Co-operation with the ECE in connection with the Trans-European Motorway (TEM) Programme;

(e) Participation with the ECE and ECA in the ten-year development project for road traffic in Africa.

C. FACILITATION OF INTERNATIONAL TRADE PROCEDURES

1. ECE/UNCTAD Trade Data Elements Directory and the rules for its maintenance

140. The ECE/UNCTAD Trade Data Elements Directory (TDED) was published in 1981 and at the same time the competent Technical Committee of the International Organization for Standardization proposed in "Documents and data elements in administration, commerce and industry" (ISO/TC 154) that it should become an international standard (ISO DP 7372). A number of international bodies took an active part in the preparation of the *Directory*, their members being potential users of the standardized data elements in their specific areas of application. An updated version of the *Directory* was issued in English, French and Russian at the beginning of 1983.

141. The data elements included in the *Directory* are intended for use, for example, in trade data interchange and in documents and data banks for national as well as international applications. The contents of the *Directory* is described in document TRADE/WP.4/INF.76:TD/B/FAL/INF.76, which also contains information on its distribution.

142. An organized maintenance function is required to keep the *Directory* up to date. Taking into account the decision by ISO/TC 154 that the *Directory* should be established as an ISO standard and that its maintenance should be entrusted to the ECE/UNCTAD secretariats, it was agreed that the maintenance function should be established in such a way that it could be recognized as a maintenance agency in accordance with the relevant parts of ISO directives.

143. At its sixteenth session in September 1982, the ECE Working Party on Facilitation of International Trade Procedures agreed on rules for the maintenance of the *Trade Data Elements Directory*. These rules form part of the TDED; it has been proposed that the same text should be included in ISO DP 7372. The rules have been published in document TRADE/WP.4/INF.86:TD/B/FAL/INF.86.

144. In order to keep the ECE/UNCTAD Trade Data Elements Directory up to date to meet changing or new requirements in trade, a Maintenance Agency has been established and entrusted with the maintenance of the *Directory*, as set out below.

145. The secretariats of ECE and UNCTAD jointly provide the secretariat for the Maintenance Agency through the ECE Trade and Technology Division and the UNCTAD Special Programme on Trade Facilitation (FALPRO).

146. In addition to the secretariats of ECE and UNCTAD and ISO/TC 154, and the ISO central secretariat, which will be represented in the Maintenance Agency, the following bodies have indicated their interest in being associated with the work of the Maintenance Agency, and each may appoint a participant: IMO, CCC, FIATA, IATA, ICS, IRU and UIC.

2. ECE/UNCTAD Trade Data Interchange Directory

147. The ECE/UNCTAD Working Party on Facilitation of International Trade Procedures initiated work in 1976 to develop "a set of standards for data exchange between international trade partners over data communication links and for computer exchange using various media ...". In 1979 guidelines for trade data interchange developed within the Working Party were approved, and it was agreed to issue them as part 4 of a new publication to be issued in a loose-leaf presentation in instalments: the ECE/UNCTAD *Trade Data Interchange Directory* (TDID).

148. Part I "Introduction" and part 4 "Guidelines for trade data interchange developed within the ECE" of the *Directory* were published in 1981; part 2 presenting "Rules for registration of application level protocols" for trade data interchange was agreed in 1982 and published in 1983.

149. In the "Introduction" to the *Directory* it is stated that the work on the guidelines had demonstrated that it would be unrealistic to recommend only one world standard for trade data interchange. For this reason, application level protocols fulfilling the requirements of the rules for registration will be made available to interested users through the *Directory*; in this way, it is hoped that protocols of this type may be less numerous and more harmonized than they would have been without publication of the *Directory*. The contents of part 4, i.e. the guidelines, are described in document TRADE/WP.4/INF.77: TD/B/FAL/INF.77.

150. For the work of ECE on the legal aspects of automatic trade data interchange, see A/CN.9/238.^a

151. For the work of ECE on a universal (multi-purpose) transport document, see A/CN.9/225, paragraphs 64-65.

152. A list of titles of trade documents with numeric identifiers and descriptions of their functions was adopted by the ECE Working Party on Facilitation of International Trade Procedures and published in the joint ECE/UNCTAD series of information documents (TRADE/WP.4/INF.84: TD/B/FAL/INF.84).

153. Phytosanitary certificates aligned with the United Nations Layout Key for trade documents, for use with the FAO International Plant Protection Convention as revised in 1979, were adopted in 1982.

D. NOTIFICATION OF LAWS AND REGULATIONS CONCERNING FOREIGN TRADE AND CHANGES THEREIN (MUNOSYST)

154. The ECE Committee on the Development of Trade is examining the possible scope and functioning of a multilateral system of notification of laws and regulations concerning foreign trade and changes therein (MUNOSYST) in order to assess whether its creation would be practicable and desirable. The line of action suggested in documents TRADE/R.426 (1981) and TRADE/R.427 (1981) will be followed. The questionnaire agreed upon by the Committee at its thirtieth session will be circulated to ECE member countries for completion. In 1982 the secretariat prepared an inventory of primary and secondary sources of information on the basis of information provided by Governments (TRADE/R.447). The interim results of research into potential user information, inquiry, access and retrieval requirements were presented in a secretariat note (TRADE/R.448).

^aReproduced in this volume, part two, V. D.

C. Report of the Secretary-General: some recent developments in the field of international transport of goods (A/CN.9/236)^a

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^a13 April 1983. Referred to in Report, para. 109 (part one, A).

Introduction

1. The Commission, at its eleventh session, decided to include the topic of transportation in its future work programme, and to accord priority to consideration of that subject.¹ Also at the same session the Commission requested the secretariat to prepare a study setting forth the work accomplished so far by international organizations in the fields of multimodal transport, charter parties, marine insurance, transport by container and the forwarding of goods.² The Commission would decide on the scope of further work on these subjects and their possible allocation to working groups after having examined studies prepared by the secretariat.³

2. The Commission, at its twelfth session, had before it the report which it requested at its eleventh session.⁴ After considering that report the Commission decided not to undertake work on multimodal transport or transport by container (it being noted that a draft Convention on International Multimodal Transport had been completed by an UNCTAD Intergovernmental Group⁵), on contracts for the forwarding of goods (because the need for uniform rules was not clearly established and the proposed Convention on International Multimodal Transport might resolve some of the difficulties which were experienced⁶), or on charter parties and marine insurance (which were under consideration by an UNCTAD Working Group⁷). The Commission also did not adopt a suggestion made at that session that it might undertake work on the subject of the warehousing contract.⁸ However, the Commission took note of the survey prepared by the secretariat of the work of international organizations in the field of transport, and requested the secretariat to continue to follow such work and to report developments in this field to the Commission.⁹

3. The secretariat also prepared reports for the thirteenth and fourteenth sessions of the Commission, which up-dated the activities of some of the organizations referred to in the previous report in the fields, *inter alia*, of marine insurance, container standards, and freight forwarding.¹⁰

4. The present report will update some of the activities described in the reports referred to in the previous paragraphs, particularly in light of the adoption of the United Nations Convention on International Multimodal Transport of Goods¹¹ on 24 May 1980. It will also examine more closely the work of the International Institute for the Unification of Private Law (UNIDROIT) on the liability of international terminal operators, which has now reached a final stage.¹²

I. Marine insurance¹³

5. At its ninth session, held in 1980, the UNCTAD Committee on Shipping endorsed the recommendation of the Working Group on International Shipping Legislation that a set of standard marine hull and cargo insurance clauses be drawn up for use as a non-mandatory international model.

6. The Working Group engaged in work on marine insurance clauses at its seventh (1980), eighth (1981), and ninth (1983) sessions, adopting, as to hull insurance, two composite texts, one on an "all risks minus exceptions" basis, and the other on a "named perils" basis, each presenting basic coverage clauses, including risk clauses, exclusion clauses, collision liability clauses and clauses on general average and sue and labour.¹⁴ As to cargo insurance, the Working Group adopted a composite text setting forth general coverage and exclusion clauses and it was agreed to incorporate into the report of the eighth session of the Working Group a text formulated on a general average and salvage clause.¹⁵

II. Transport by container¹⁶

7. Pursuant to a decision of the UNCTAD Trade and Development Board in 1980, the UNCTAD Committee on Shipping, at its ninth session (1980), decided to include the question of container standards for international multimodal transport in its work programme and to keep activities in this field under constant review in connection with its work on multimodal transport.

8. An intergovernmental group will be convened under the auspices of UNCTAD to recommend principles for model rules for multimodal container tariffs.

¹Report of the United Nations Commission on International Trade Law on the work of its eleventh session, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17* (A/33/17), paras. 67(c)(vii), 68 and 69 (Yearbook ... 1978, part one, II, A).

²*Ibid.*, para. 67 (c) (vii).

³*Ibid.*, para. 67 (e).

⁴A/CN.9/172 (Yearbook ... 1979, part two, V, A).

⁵Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 104 (Yearbook ... 1979, part one, II, A).

⁶*Ibid.*

⁷*Ibid.*

⁸*Ibid.*, para. 105.

⁹*Ibid.*, para. 106.

¹⁰A/CN.9/192/Add. 1 (Yearbook ... 1980, part two, VI); A/CN.9/202/Add. 2 (Yearbook ... 1981, part two, V, A). See, also, A/CN.9/225 (Yearbook ... 1982, part two, VI, B), in which the secretariat reported to the fifteenth session of the Commission on developments in regard to international transport documents.

¹¹TD/MT/CONF/16.

¹²For other current activities of organizations in the field of international transport, see A/CN.9/237/Add.2 (reproduced in this volume, part two, V, B).

¹³See A/CN.9/172, paras. 32-41; A/CN.9/192/Add.1, para. 2; and A/CN.9/202/Add.2, paras. 5-10.

¹⁴TD/B/C.4/ISL/L.69.

¹⁵TD/B/C.4/ISL/37, para. 10 and annex II.

¹⁶See A/CN.9/172, paras. 42-53; A/CN.9/192/Add.1, paras. 13-14; A/CN.9/202/Add.2, paras. 62-63.

9. The International Organization for Standardization (ISO) has informed the UNCTAD secretariat that it has continued its policy of encouraging and welcoming the participation of developing countries in the work of its Technical Committee 104, which is responsible for freight container standards, and that it has also continued the policy of maintaining a high degree of stability of container standards and avoiding frequent changes which may affect compatibility, intermodality or modularity of ISO containers. ISO has also adopted the policy that whenever proposals are put forward for revisions to the basic freight container standards which affect the compatibility, intermodality and modularity of ISO containers, there should be a wider circulation of the proposals, i.e. to include all ISO members and competent United Nations bodies, in addition to the normal circulation to members of Technical Committee 104, in order to permit the widest possible consultation.¹⁷

10. Recent revisions to ISO container standards have reduced the number of approved sizes of containers.¹⁸ Refinements and revisions to other ISO standards have been made, and additional standards have been published.¹⁹ Other revisions and additions are under consideration.²⁰

11. In 1981, the Maritime Safety Committee of IMCO (now the International Maritime Organization (IMO)) unanimously adopted proposals for the amendment of the International Convention for Safe Containers. The principal amendments allow more time for the completion of the work of plating existing containers and new containers not approved and plated at the time of manufacture. The amendments were adopted under the simple procedure included in the Convention for the amendment of its technical annexes.²¹ The Organization's Sub-Committee on Containers and Cargoes, at its twenty-third session held in 1982, considered other amendments to the Convention.

12. Recommendations on the Harmonized Interpretation and Implementation of the Convention, as amended and adopted by the Maritime Safety Committee in the spring of 1981, are to be found in document MSC XLIV/21, annex 35.

III. Freight forwarding²²

13. The International Federation of Freight Forwarders' Association (FIATA) has issued a Combined Transport Bill of Lading. This document, in its revised form, was approved in 1978 by the ICC Joint Committee on Intermodal Transport as conforming with the ICC Uniform Rules for a Combined Transport Document.

The FIATA document is therefore subject to the ICC Uniform Rules. A number of freight forwarders who act as multimodal transport operators are issuing the FIATA document.

14. In a report issued in March 1982 (TD/B/C.4/243), the UNCTAD secretariat noted that the terms and conditions for multimodal transport services provided by freight forwarders are governed by standard conditions for freight forwarding adopted by their national associations (other than those of the FIATA negotiable Combined Transport Bill of Lading). It noted that it would not be appropriate to apply the standard conditions adopted by national associations, which are designed for segmented transport arrangements, to multimodal transport in which a freight forwarder acts as a principal. The UNCTAD secretariat recommended that consultations among shippers' organizations, freight forwarders' associations, appropriate authorities and other relevant organizations should be encouraged so that standard conditions for multimodal transport services which have not been provided for in the United Nations Convention on Multimodal Transport of Goods can be elaborated.

IV. Liability of international terminal operators²³

15. A study group of UNIDROIT has drawn up a preliminary draft Convention on the Liability of International Terminal Operators²⁴ in connection with work within UNIDROIT on the subject of warehousing contracts, which has been on the general work programme of UNIDROIT since 1960.

16. The subject of warehousing contracts was accorded priority by the Governing Council of UNIDROIT at its fifty-third session, held in 1974. It occurred at a time of a growing awareness, prompted in part by the work of UNCITRAL in the area of carriage of goods by sea, of the lack of uniform rules for the liability of persons entrusted with the custody of goods before, during and after transport. The UNIDROIT Governing Council, at its fifty-sixth session (1977), set up a Study Group on the Warehousing Contract, and gave it the task of drawing up such uniform rules. In October 1981 the Study Group approved the preliminary draft Convention.²⁵

17. At its sixty-first session (1982), the Governing Council of UNIDROIT requested the UNIDROIT secretariat to co-operate with interested international organizations in the taking of initiatives for the purpose of giving wide publicity to the preliminary draft Convention. As noted in the report on international transport documents submitted to the fifteenth session of the Commission, the Council was informed by the

¹⁷TD/B/C.4/195, paras. 22 and 26; TD/B/C.4/235, para. 8.

¹⁸TD/B/C.4/235, para. 9.

¹⁹*Ibid.*, paras. 15-17.

²⁰*Ibid.*, paras. 18-23.

²¹*Ibid.*, paras. 39-44.

²²See A/CN.9/172, paras. 54-63; A/CN.9/192/Add.1, para. 15; A/CN.9/202/Add.2, para. 18; A/CN.9/225, paras. 19 and 57.

²³See A/CN.9/202/Add.2, paras. 46-58; A/CN.9/225, paras. 22-23, 30, 32 and 40.

²⁴UNIDROIT 1982, study XLIV-doc. 14.

²⁵It is expected that the Governing Council of UNIDROIT, at its next session, to be held in the first week of May 1983, will adopt the text as a draft Convention.

Secretary of the Commission of the interest of the Commission in the subject, which might perhaps at some time in the future be translated into positive action, given its close relationship with the international conventions relating to the carriage of goods and in particular the Hamburg Rules, as well as its relevance to the needs of a number of developing countries.²⁶

18. At the fifteenth session of the Commission, the observer from UNIDROIT stated that his organization was interested in co-operating with the Commission in future work leading to the preparation of a draft convention on the liability of international terminal operators.²⁷

A. SOME RELEVANT CHARACTERISTICS OF STORAGE OF GOODS IN TRANSIT²⁸ AND TERMINAL OPERATORS²⁹

19. The storage of goods is only one element of non-carriage operations which are typically performed in connection with the transport of goods in international trade. Other elements include freight forwarding, and handling operations such as loading and unloading the goods on the transport vessel or vehicle, securing the goods on the vessel or vehicle ("stowage"), and moving goods on the wharf prior to loading or after unloading ("wharfage").

20. The storage of goods in transit is sometimes performed by an enterprise as an independent activity, separate from other non-carriage operations. However, it is often performed in combination with other operations mentioned in the previous paragraph by the carrier, by a freight forwarder or by a terminal operator. Thus, a freight forwarder or, in certain modes of carriage, the carrier itself, may perform loading, stowage and unloading operations, as well as the temporary storage of goods in transit. Similarly, a terminal operator may provide loading, stowage or wharfage services ancillary to the storage of goods. Practices in this regard vary depending upon the location of the operation and the type of trade or carriage involved.

²⁶A/CN.9/225, footnote 10.

²⁷Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17(A/37/17)*, para. 105 (Yearbook ... 1982, part one, A).

²⁸This discussion deals with the storage of goods in connection with the transport of goods, rather than storage unconnected with transport. Much of the discussion is derived from the "Preliminary Report on the Warehousing Contract" prepared by D. Hill for UNIDROIT in 1976 (UNIDROIT 1976, study XLIV-doc. 2).

²⁹The UNIDROIT preliminary draft Convention on the Liability of International Terminal Operators uses the term "terminal operators" in preference to "warehousemen". The UNIDROIT Study Group believed that the latter term, with its implication of shelter, is becoming outmoded due to the development of new techniques in the storage of goods and due to the fact that such operators now perform services that the traditional warehouseman would not have provided (see para. 20). The discussion in the present document adopts this terminology, and "terminal operator" refers herein to an operator whose primary function is the safekeeping of goods, but who may also perform other non-carriage services in connection with the transport of goods. See UNIDROIT 1982, study XLIV-doc. 14, para. 22.

21. The advent of containerization has resulted in the merging of transit storage with other services in one overall operation, since the container can be stored in an area of the depot which serves as a wharf, transit warehouse, and reception and delivery area.

B. LIABILITY OF TERMINAL OPERATORS UNDER NATIONAL LEGAL SYSTEMS

22. The rules governing the liability of terminal operators under national legal systems are widely disparate, both as to the source and to the substantive content of the rules.

23. Rules governing the liability of terminal operators may be contained in civil or commercial codes or rules of common law governing the deposit or bailment of goods generally. Particular categories of operations may be governed by special laws. However, in several legal systems, the legal liability of terminal operators may be restricted or modified contractually, through the use of general conditions. The extent to which this is possible varies from one legal system to another, and this further contributes to the disparities in the liability of terminal operators.

24. The standards of liability of terminal operators as established by these different sources of rules vary substantially. Disparities also exist within some legal systems, due to the application of different standards of liability to different categories of terminal operators.

25. The standards of liability applicable under various legal systems to terminal operators in respect of the storage of goods range from strict liability (e.g. liability unless the terminal operator proves the existence of certain narrow exonerating circumstances), to negligence (e.g. failure to take reasonable care of the goods), and to the exclusion of most forms of liability (e.g. by general conditions). Moreover, although under many legal systems the burden is on the terminal operator to prove that he is not liable, in some systems the burden is on the claimant. In the latter systems, however, the claimant is often aided by a presumption that the terminal operator is liable which may be overcome if the terminal operator produces a certain quantum of evidence.

26. Disparities also exist among legal systems in respect of prescription periods and financial limits of liability. With respect to the latter, it has been observed that the financial limits of liability contained in general conditions of contract are often excessively low, with the result that even in cases where the standard of liability is relatively high, the real effect of this standard may be reduced by the low financial limits of liability.³⁰

27. The disparities in the liability of terminal operators are further complicated by the facts that terminal operators under the same legal system may be subject to different rules concerning liability depending upon

³⁰UNIDROIT 1976, study XLIV-doc. 2, p. 20.

the nature of services rendered (e.g. storage or handling), and that the same services may be performed within a given locality by different types of operators who use different conditions of contract, resulting in varying rules concerning liability in respect of such services.

C. TERMINAL OPERATORS AND INTERNATIONAL TRANSPORT CONVENTIONS

28. The transportation of goods involves operations falling within two distinct categories—the actual carriage of the goods, and the storage and handling of the goods before, during and after transit. While the rules governing the liabilities of various modes of international carriers (e.g. by sea, air, road, rail and inland waterway) have become increasingly harmonized through international conventions, the rules governing the operations of non-carrying intermediaries such as terminal operators have not. The work of UNIDROIT on the liability of international terminal operators has been based in part on the belief that an attempt should be made to unify the rules in this area in order to fill in the gaps in the liability regimes left by existing international transport conventions.³¹

29. These gaps exist in respect of the storage of goods during periods of time before, during and after transport which are not covered by the harmonized regimes established by international transport conventions. During these periods the storage will be subject to the disparate legal regimes and usually lower standards and limits of liability described in paragraphs 23 through 27, above.

30. Shippers and consignees (hereinafter referred to as "cargo interests") whose goods are stored or handled by terminal operators are directly affected by gaps in the legal regime relating to the liability of terminal operators in respect of their claims against terminal operators for loss of or damage to the goods. Carriers and others (such as freight forwarders³²) using the services of terminal operators are directly affected in respect of their recourse actions against terminal operators to recover damages for which the carriers or others are liable to cargo interests for loss of or damage to goods while in the hands of the terminal operators.

31. Recently adopted international transport conventions will, when they enter into force, reduce some of the adverse consequences to cargo interests from the existence of gaps in the legal regime relating to the liability of terminal operators. In doing so, however, they may in some cases increase the adverse consequences upon carriers. These results may occur because

the liability regimes to which a carrier³³ will be subject under the conventions will extend over periods of time when the goods may be stored, and because under these regimes the standard of the carrier's liability to the cargo interest will often be higher, and will often be subject to higher financial limits of liability, than the standards and limits of liability which would otherwise have applied to the storage. For example, under the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg Rules)³⁴, the Convention Concerning International Carriage by Rail (COTIF), and the United Nations Convention on International Multimodal Transport of Goods, a carrier will be responsible for the goods and subject to a single liability regime from the time that the goods are taken over until the time they are delivered.³⁵ Under the Hamburg Rules and the Multimodal Convention the carrier will be liable for loss of or damage to the goods caused by an occurrence taking place during his period of responsibility, unless he proves that he took all reasonable measures to avoid the occurrence and its consequences.³⁶ Moreover, the standard and limits of liability established by these conventions cannot be reduced by contractual stipulations.³⁷ Under COTIF the carrier will be liable for loss of or damage to the goods during his period of responsibility unless he could not avoid the circumstances causing the damage and prevent their consequences, or unless they result from specified perils.³⁸ The ability to derogate contractually from this standard is restricted.³⁹

32. Even under these international conventions, however, there will remain gaps which directly affect cargo interests. The periods of responsibility of carriers may not cover all times when goods may be in the hands of a terminal operator. For example, under the Hamburg Rules and the Multimodal Convention, if the consignee does not receive the goods from the carrier the responsibility of the carrier under the Conventions ends when he places them at the disposal of the consignee,⁴⁰ which in many cases will involve placing them in storage. Moreover under the Hamburg Rules the carrier's responsibility covers only the period during which the carrier is in charge of the goods at the port of loading, during the carriage and at the port of discharge.⁴¹ This Convention, therefore, will not cover transit storage outside the ports of loading or discharge.

³¹In the following discussion the word "carrier" will, when reference is made to the Multimodal Convention, include multimodal transport operators.

³²A/CONF.89/13, annex I, (*Official Records of the United Nations Conference on the Carriage of Goods by Sea*, United Nations publication, Sales No. E.80.VIII.1).

³³Hamburg Rules, art. 4 (but see art. 11); COTIF, appendix B, arts. 35 and 36; Multimodal Convention, art. 14. The Multimodal Convention also specifies that the multimodal transport operator shall be liable for the acts and omissions of persons whose services he uses for the performance of the multimodal transport contract (art. 15).

³⁴Hamburg Rules, art. 5 (1); Multimodal Convention, art. 16 (1).

³⁵Hamburg Rules, art. 23; Multimodal Convention, art. 28.

³⁶COTIF, appendix B, art. 36.

³⁷COTIF, appendix B, art. 6 (2), (3) and (4).

³⁸Hamburg Rules, art. 4 (2) (b) (ii); Multimodal Convention, art. 14 (2) (b) (ii).

³⁹Hamburg Rules, art. 4 (1).

³¹Explanatory report on the preliminary draft Convention on the Liability of International Terminal Operators (hereinafter referred to as "explanatory report") (UNIDROIT 1982, study XLIV-doc. 14), para. 9.

³²E.g. when the forwarder acts as a principal; see A/CN.9/172, paras. 59-63 (Yearbook ... 1979, part two, V, A).

D. THE UNIDROIT PRELIMINARY DRAFT CONVENTION

33. The major characteristics of the UNIDROIT preliminary draft Convention on the Liability of International Terminal Operators parallel those of the Hamburg Rules and the Multimodal Convention. Thus, the terminal operator would be liable for loss of or damage to goods from the time he takes them in charge until delivery, unless he proves that he took all measures that could reasonably be required to avoid the occurrence which caused the loss and its consequences.⁴² Liability would be limited to 2.75 units of account⁴³ per kilogram,⁴⁴ unless the loss or damage results from an act or omission of the terminal operator with the intent to cause the loss or damage, or recklessly and with knowledge that the loss or damage would probably result.⁴⁵

34. The preliminary draft Convention would require the terminal operator, at the request of the customer, to issue a dated document acknowledging receipt of the goods. The document would constitute *prima facie* evidence of the terminal operator's taking charge of the goods described therein. However, its negotiability would depend upon the agreement of the parties and applicable law.⁴⁶

35. The terminal operator would have a right of retention over and sale of the goods to satisfy his fees and other claims relating to the goods.⁴⁷ The text would also uphold contractual provisions for a general lien insofar as they are not contrary to applicable law.⁴⁸

36. Comparably to the Hamburg Rules⁴⁹ and the Multimodal Convention⁵⁰, the preliminary draft Convention provides that the obligations and responsibilities imposed on the international terminal operator would

not be able to be diminished by contractual stipulations.⁵¹ Moreover, the preliminary draft Convention would be supplementary to international transport conventions in that it would not modify the rights or duties of a carrier which arise under any such convention.⁵²

37. The rules contained in the preliminary draft Convention would in principle be of a mandatory character and would be applied by a contracting State to all international terminal operators in its territory. However, States would be able to declare that the rules will apply only to international terminal operators who agree to be bound by it.⁵³

38. During the work leading to the preliminary draft Convention questions were raised as to whether the existing disparities in the liability of terminal operators created such problems in practice as to justify an effort to unify and harmonize the law in this area. It was also noted that the magnitude of the disparities may make it difficult to unify the law in a manner which would receive wide acceptance. Moreover, terminal operators may well oppose the creation of a legal regime which imposes standards and limits of liability on them exceeding those to which they have become accustomed, and which cannot be reduced by general conditions. However, within the UNIDROIT Study Group on the Warehousing Contract views were expressed that the following features could make the preliminary draft text more acceptable: (a) realistic standards and limits of liability which, as part of national law, would not be interfered with judicially; (b) financial limits to liability which would be difficult for a claimant to break; (c) the ability of States to apply the Convention only to terminal operators which accept the regime established by it; (d) a short prescription period; (e) the right of retention over and sale of the goods by the terminal operator, which might not otherwise be available in some legal systems.

39. The preliminary draft Convention is intended to establish a minimum set of rules governing the liability of international terminal operators. It does not deal with a number of issues, such as the obligations of the customer. The UNIDROIT Study Group on the Warehousing Contract has stated that matters not covered by the preliminary draft Convention might be dealt with at a later stage, or, alternatively, might be regulated by standard conditions which might be prepared by interested commercial organizations.⁵⁴ In this connection the Comité Maritime International (CMI) informed the Study Group in 1981 that the CMI had decided to elaborate standard conditions governing operations performed by international terminal operators, on the understanding that such conditions would be fully compatible with the provisions of the draft Convention.⁵⁵

⁴²Arts. 3 (1), 6 (1); comparable to article 5 of the Hamburg Rules and article 16 of the Multimodal Convention.

⁴³The per-kilogram limit in the Hamburg Rules (art. 6 (1) (a)) is 2.5 units of account and in the Multimodal Convention (art. 18) 2.75 units of account. Under the UNIDROIT preliminary draft Convention (art. 13) the unit of account would be converted to a national currency in a manner comparable to the method in the Hamburg Rules (art. 26) and the Multimodal Convention (art. 31). The limits of liability may be revised under the preliminary draft Convention (art. 21) in a manner comparable to the revision mechanism in art. 33 of the Hamburg Rules. The UNIDROIT secretariat has been informed of the desirability to take into account General Assembly resolution 37/107 of 16 December 1982. In that resolution the General Assembly recommended that in the preparation of international conventions containing limitation of liability provisions, the unit of account provision and one of the two alternative provisions for adjustment of the limitation of liability adopted by the Commission at its fifteenth session should be used. Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17 (A/37/17)* (Yearbook ... 1982, part one, A).

⁴⁴Art. 7.

⁴⁵Art. 9 (1); comparable to art. 8 of the Hamburg Rules and art. 21 of the Multimodal Convention.

⁴⁶Art. 4.

⁴⁷Art. 5.

⁴⁸Explanatory report on the preliminary draft Convention, note 31, above, para. 57.

⁴⁹Art. 23.

⁵⁰Art. 28.

⁵¹Art. 12.

⁵²Art. 14.

⁵³Art. 18.

⁵⁴Explanatory report on the preliminary draft Convention, note 31, above, para. 18.

⁵⁵Report of the secretariat of UNIDROIT on the third session of the Study Group on the Warehousing Contract held at Rome from 19 to 21 October 1981 (UNIDROIT 1982, study XLIV-doc. 13), para. 5.

V. Conclusion

40. The Commission may wish to take note of the work of other organizations in the various fields described in this report, and request the secretariat to keep it informed of developments in these fields.

41. With respect to the liability of international terminal operators, if the Commission is favourably disposed to the harmonization of law in this field, it could, pursuant to its co-ordinating function and its position as the core legal body of the United Nations system in the field of international trade law, direct a request to UNIDROIT that UNIDROIT transmit its draft Convention to UNCITRAL for its consideration. At the same time, the Commission could request the secretariat to prepare a study of the issues involved in the topic.

42. Thereafter, there may be various ways in which the Commission could proceed. For example, after examining the draft Convention at a future session, it could prepare comments on it and perhaps recommendations which would then be communicated to UNIDROIT. The Commission could also undertake its own elaboration of a text in an appropriate form (e.g. convention, model law or general conditions), perhaps using the UNIDROIT draft as a basis. Any such work might be assigned to an UNCITRAL Working Group.

43. On the other hand, if the Commission does not consider it opportune to proceed with work on the topic at this time, it may wish to request the secretariat to keep it informed of developments in this field together with developments in other fields discussed in this report.

D. Note by the secretariat: legal aspects of automatic data processing (A/CN.9/238)^a

1. The Commission at its fifteenth session considered two reports by the secretariat which dealt in part with legal problems arising out of automatic data processing. One report contained a discussion of certain legal problems which arise in electronic funds transfers (A/CN.9/221).^b The second report contained a discussion of the work of other organizations in the field of transport documents, with a particular emphasis on the effect of the trade facilitation movement and of the use of automatic data processing in the preparation of these documents (A/CN.9/225).^c

2. In respect of electronic funds transfers

"The Commission decided that the secretariat should begin the preparation of a legal guide on electronic funds transfers, in co-operation with the UNCITRAL Study Group on International Payments.... The secretariat was also requested to submit to some future session of the Commission a report on the legal value of computer records in general."¹

3. In respect of transport documents, "The suggestion contained in the report that the secretariat would continue to monitor developments in this field was welcomed and the secretariat was requested to keep the Commission informed of any action which it might take."²

4. Subsequent to the fifteenth session of the Commission, the Secretary of the Commission received a letter from the Executive Secretary of the Economic

Commission for Europe dated 23 November 1982, which was sent at the request of the Working Party on Facilitation of International Trade Procedures, a body jointly sponsored by ECE and UNCTAD. The letter, which is reproduced in annex I, describes the activities of the Working Party in respect of the teletransmission of trade data. The letter also enclosed document TRADE/WP.4/R.185/Rev.1 which was submitted to the sixteenth session of the Working Party in September 1982. This document, which is reproduced in annex II, describes problems of a legal character encountered by the Working Party in these activities and puts forward suggestions for action in the competent international fora.

5. The conclusion reached in the document, and supported by the Working Party was

"that there is an urgent need for international action to establish rules regarding legal acceptance of trade data transmitted by telecommunications. Since this is essentially a problem of international trade law, the United Nations Commission on International Trade Law (UNCITRAL) would appear to be the central forum." (TRADE/WP.4/R.185/Rev.1, para. 4)

6. At its sixteenth session the Working Party requested the ECE secretariat to transmit the document to the Commission and to other international organizations with competence over specific aspects of the legal problems identified. The report of the session also indicates that it

"was agreed that the importance for world trade of finding solutions of relevance for all legal systems without undue delay should be mentioned when the ECE secretariat transmitted the study to the secretariats of UNCITRAL and of other international organizations involved". (TRADE/WP.4/141, para. 15)

^a18 March 1983. Referred to in Report, para. 117 (part one, A).

^bYearbook ... 1982, part two, II, C.

^cYearbook ... 1982, part two, VI, B.

¹Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17(A/37/17)*, para. 73.

²*Ibid.*, para. 104.

7. The reply by the Commission's secretariat to the letter from the Executive Secretary of ECE described the actions already taken by the Commission relevant to legal issues arising in automatic data processing. Furthermore, in order to ascertain the extent of co-ordination which might be possible for the Commission to undertake in this regard as the core legal body in the field of international trade law, a copy of the reply with a request for information on any of their relevant activities was sent to the international organizations to which the ECE letter had been sent. The replies received by the secretariat indicate a wide-spread interest in various aspects of these problems.

CONCLUSION

8. The Commission had already decided to undertake certain actions relevant to the concerns expressed by the Working Party when it agreed to prepare a legal guide on electronic funds transfers and when it requested the secretariat to submit to some future session of the Commission a report on the legal value of computer records in general. Moreover, it has expressed its interest in the effect of the teletransmission of trade data on the preparation of transport documents. Similarly, other international organizations have undertaken activities in sectors in which they are particularly competent. However without adequate co-ordination of these activities, inconsistent results may be adopted and important problems may be overlooked.

9. The Commission may wish to agree with the Working Party on Facilitation of International Trade Procedures that the legal problems identified in document TRADE/WP.4/R.185/Rev.1 are important to international trade and that solutions of relevance for all legal systems should be found without undue delay. The Commission may also wish to agree with the Working Party that, since this is essentially a problem of international trade law, the Commission would appear to be the central forum to undertake and co-ordinate the necessary action.

10. The secretariat intends to submit to the seventeenth session a report on the actions which the Commission might take to co-ordinate activities in this field, keeping in mind the areas of competence of the various international organizations concerned.

ANNEX I

Letter dated 23 November 1982 from the Executive Secretary, Economic Commission for Europe, to the Secretary, United Nations Commission on International Trade Law

Documentary requirements laid down in regulations and practices established for international trade result in high costs for the business community and the authorities concerned. An average figure of ten per cent of the value of the goods is often mentioned as the cost of completion of the large number of forms—to establish approximately one hundred

different documents—in which information is presented for selling, forwarding, transporting, insuring, and paying for goods and for fulfilling export/import requirements.

In an attempt to limit these high costs, the Committee on the Development of Trade, a Principal Subsidiary Body of the Economic Commission for Europe, set up a Working Party in 1963 for the facilitation of international trade procedures. The Working Party developed an ECE recommended-standard, now accepted on a world-wide basis, for the layout of trade documents which has resulted in very considerable cost reductions for enterprises using trade documents aligned to this standard.

Following subsequent technical developments, the Working Party's attention over the past five years has moved from standardization of documents and is not directed towards the standardization of data elements used for international trade transactions and the automatic interchange of such data elements.

Many different kinds of data are now transmitted automatically using intelligent terminals, and the economic gains resulting from the rapid error-free exchange of information for decision-making and further automatic processing have been fully realized; considerable national and international efforts are currently being made to take advantage of the increase in productivity that would result from the linking of computers and other office machines through different telecommunication techniques.

In its work on standardized trade data elements and harmonized rules for their interchange, the Working Party on Facilitation of International Trade Procedures has identified some problems of a legal character that it is unwilling to pursue since it is necessary to solve them in a wider context than that of trade facilitation. Amongst questions linked to these problems are the following:

- can teletransmitted data be admitted as evidence in Court? and
- can teletransmitted data be accepted for Customs clearance?

At its sixteenth session in September 1982, the Working Party noted document TRADE/WP.4/R.185/Rev.1^d—transmitted by the delegations of Denmark, Finland, Norway and Sweden—in which the main problems of a legal character encountered in its work were identified and suggestions put forward for action in the competent international fora.

The Working Party requested the ECE secretariat to transmit the document to the international bodies mentioned in the study and to other relevant international organizations:

“in order that their respective secretariats bring forward the problems raised in the paper to their competent bodies for possible agreement on international work aimed at harmonized rules concerning these matters”.

(TRADE/WP.4/R.185/Rev.1, para. 5)

In this context, the Working Party requested the secretariat to mention in the communication transmitting document TRADE/WP.4/R.185/Rev.1 that

“... there was urgency in giving legal security to business partners undertaking obligations or acquiring rights through means other than traditional paper documents”.

and to stress

“... the importance for world trade to find solutions of relevance for all legal systems without undue delay...”.

(TRADE/WP.4/141, para. 15)

I am sending to you under separate cover copies of “Legal Aspects of Automatic Trade Data Interchange”

^dReproduced below, annex II.

(TRADE/WP.4/R.185/Rev.1) issued in October 1982; further copies may be obtained on request.

This letter is being sent to the secretariats of the organizations indicated in the study, i.e. UNCITRAL, OECD, CCC and ICC, for possible action. A copy of the letter and its enclosure is being sent for information to the following organizations: The United Nations Centre on Transnational Corporations, UPU, ITU, ICAO, IMO, CEMT, Council of Europe, IBI, UNIDROIT and IATA.

(signed) Janez Stanovnik
Executive Secretary
Economic Commission for Europe

ANNEX II

Legal aspects of automatic trade data interchange

Transmitted by the delegations of Denmark, Finland, Norway and Sweden

(TRADE/WP.4/R.185/Rev.1)^e

FOREWORD

1. An important legal aspect of work on facilitation of international trade procedures is the acceptability of automatic data transmission to replace the movement of data by traditional paper documents and the resolution of legal insecurity that may arise through utilization of new techniques. The use of modern transmission methods in international trade, transport and payments depends on the legal force given to the information thus transmitted. The problem is more extensive than that of agreement between trading partners alone, since the principle of contractual freedom is limited by specific legal requirements of national or international law.

2. Amongst important questions asked are the following:

(a) Can teletransmitted data be accepted for customs clearance and other purposes such as the procedure for effecting international payments?

(b) Are teletransmitted data admissible as evidence in court?

(c) Does such evidence rank in the same way as a traditional document?

(d) Does authentication by electronic means equate with a traditional signature?

3. The purpose of this document is to outline what needs to be done—and why—and to suggest, even though to a limited extent, how and where action might be taken. The paper has been prepared on the initiative of the Nordic Legal Committee, with the aid of funds from the Nordic Council of Ministers. It is presented jointly by Denmark, Finland, Norway and Sweden.

4. The document concludes that there is an urgent need for international action to establish rules regarding legal acceptance of trade data transmitted by telecommunications. Since this is essentially a problem of international trade law, the United Nations Commission for International Trade Law (UNCITRAL) would appear to be the central forum. The work could be undertaken in co-operation with the Customs Co-operation Council (CCC), which is actively engaged in

establishing rules concerning important aspects of administrative law; with the Organisation for Economic Co-operation and Development (OECD) for aspects related to transborder data flows; and with other international organizations, such as the International Chamber of Commerce (ICC), in the commercial field, to ensure compatibility.

5. The UN/ECE Working Party on Facilitation of International Trade Procedures is invited to take note of the paper and to request the ECE secretariat to transmit copies to the above-mentioned and other relevant international organizations, in order that their respective secretariats may bring forward the problems raised in the paper to their competent bodies for possible agreement on international work aimed at harmonized rules concerning these matters.

Note: In this revised version minor changes have been introduced in paragraphs 11, 44, 72, 101, 105, 120, 126, 137, 138 and 145; a few editorial amendments have also been made.

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1. Introduction

1. International trade generates a large number of different procedures—a subject that was addressed by the Nordic Legal Committee some time ago (Cf. NORDIPRO special paper No. 1 "The export contract as a management tool", Oslo, March 1978). Traditionally, the information (data) required for these procedures has been transmitted through paper documents. The more obvious handicaps of this traditional method—which has been estimated to represent a cost of 7-10 per cent of the value of the goods traded—can be summarized as follows:

- (a) Too many documents are used or required;
- (b) Documents are too complicated and often contain both too many and unnecessary data;
- (c) The same data are repeated in many documents;
- (d) The movement of essential documents takes too long, and frequently leads to severe delays in securing release of goods at destination.

2. During the last decade there have been major developments both in automatic data processing (ADP) and in telecommunications, and further developments are expected. The cost of the necessary equipment is steadily decreasing; the use of ADP is spreading to all areas of society. Naturally, those involved in international trade wish to utilize modern technology to achieve less costly and more effective handling of trade data.

3. All this has led to the creation and growing use of standard trade data elements and their coded representation, as well as standards for interchange protocols and communication systems. It is increasingly apparent, however, that lack of agreed legal solutions, i.e. legal standards—as distinct from purely technical standards—may become a major obstacle in this field of ADP development.

4. Major economic gains would result from a change-over to "non-paper documentation", since many of the difficulties connected with present-day trade and transport procedures could be eliminated. The effects of new methods would extend to other areas also, with secondary savings and other positive results. "Non-paper" data handling would mean:

- (a) Fewer errors, since data would be transmitted and controlled by machines, thus eliminating errors which often occur through manual transmission of information;
- (b) Better cash flow management, with consequential financial savings;

(c) Availability of data for direct use in traders' own ADP systems, e.g. accounting, stock and production management, and a wide range of in-house statistics;

(d) Higher quality of national and international trade and transport statistics, since these would be based on standardized data governed by exact harmonized definitions;

(e) Fewer misunderstandings (through inaccurate translation) owing to use of international standard data elements and codes;

(f) Swifter turn-around of ships in port, since the necessary data would be available before the arrival of the goods.

5. Developing countries, in particular, would benefit from speedier clearance of ships and of goods, and from simplified procedures and the opportunity for more efficient decision-making offered by the use of standardized data. The argument, sometimes put forward, that developing countries see a disadvantage in computers replacing people is not supported in practice for the following reasons. First, it would not directly affect a great number of people; in fact, ADP would more especially concern qualified civil servants—who are in great demand in these countries. Further, the introduction of ADP would be gradual. The importance of automated procedures has already been accepted in many developing countries—and introduced in some of them—particularly in connection with main export items.

6. It must be stressed that traditional documents would not be completely abolished. They would remain a fact of life in trade with certain countries, or for certain types of transactions. There is nothing dramatic about the introduction of "paperless" procedures in international trade: it can be expected to take place, step by step, when the parties concerned feel assured that it would be to their mutual advantage and would not affect their individual proper interests. In any case, data processed and transmitted automatically may still be made visible on paper (e.g. by print-out). The paper document will thus continue to play its role in international trade procedures at the same time as modern and more efficient methods for production and transmission of data are introduced.

7. The use of ADP in industry and trade is already widespread. Enterprises have developed in-house systems and have secured special permission for acceptance and clearance of data transmitted to certain authorities by automatic means. Certain commercial banks have established the Society for Worldwide Interbank Financial Telecommunication (SWIFT), thereby introducing a message-switching system which could be used as a base on which to build a full electronic funds transfer system. Carriers and forwarders are working to develop automated systems for their own purposes, and in many countries trials are being conducted by groups of firms representing different trade interests to test the possibility of a matching full trade data interchange system.

8. The efforts of government officials and national trade facilitation experts within the many international organizations working with the UN/ECE trade facilitation bodies and UNCTAD/FALPRO have also done much to make it possible to replace paper documents by teletransmitted messages.

9. A major step forward was taken in 1972 when the UN/ECE re-organized its Working Party on Simplification and Standardization of External Trade Documents (which had been in existence since 1960) and established the Working Party on Facilitation of International Trade Procedures. In

1975, this Working Party set up several informal task teams to undertake special and urgent tasks. One of the teams was requested to study the legal problems of the use of automatic data processing and transmission of data in international trade. Its main conclusions and recommendations are recorded in the documents listed below:

Introductory paper (TRADE/WP.4/GE.2/R.79);

Overview of legal problems of trade facilitation (TRADE/WP.4/GE.2/R.102);

UN/ECE/FAL recommendation No. 12—Measures to facilitate maritime transport document procedures (TRADE/WP.4/INF.61:TD/B/FAL/INF.61);

UN/ECE/FAL recommendation No. 13—Facilitation of identified legal problems in import clearance procedures (TRADE/WP.4/INF.62:TD/B/FAL/INF.62); and

UN/ECE/FAL recommendation No. 14—Authentication of trade documents by means other than signature (TRADE/WP.4/INF.63:TD/B/FAL/INF.63).

10. It should be noted that the Customs Co-operation Council (CCC) has been actively involved in this UN/ECE work; it has established its own special Party on Customs Applications of Computers which is already carrying out important work in connection with "paperless" procedures in the customs field.

11. Other international organizations are also active. Especially interesting, in this connection, are two UNCITRAL studies concerning electronic funds transfers (A/CN.9/149/Add.3⁷ and A/CN.9/221⁸). This work is important both because interface between the transfer of trade data and finance data is essential and because UNCITRAL, as established by United Nations General Assembly resolutions, is the co-ordinating body of the United Nations organizations in the field of international trade law.

12. It would therefore appear both appropriate and desirable that UNCITRAL should initiate—or, preferably, undertake and co-ordinate—further international action required to resolve the legal problems of automatic trade data interchange.

13. The aim of the present paper is to outline what needs to be done—and why.

2. The background

14. World trade is the sum total of a multitude of different transactions—the swift supply of spare parts, the steady delivery of basic commodities, the accomplishment of long-term, complex construction projects—to mention only a few examples. From the legal point of view, all transactions are based on an international contract of sale: the seller in one country undertakes to supply a defined object to a buyer in another country against payment.

15. Since there is a basic common interest in the successful performance of sales contracts, there is a strong need for security. The buyer wishes to have assurance before payment is made that he will receive the goods or service which he has ordered. The seller wishes to have assurance that payment will be forthcoming before parting with the goods or performing the service. Agreed terms for delivery and payment therefore play an essential role in trade transactions.

16. Since goods have to be moved over long distances, specific provisions for transport and insurance have to be made. Further, since the goods may cross the frontiers of several countries, requirements for customs clearance (outwards, inwards and possibly transit) have to be observed, as well as regulations governing the transfer of payments.

17. A simple model of a trade transaction would therefore reflect not only the international trade contract but also independent and ancillary agreements of a contractual nature with banks and insurance companies—possibly also with freight forwarders and carriers. It would indicate the flow of goods and payments and also the movement of documents; this in turn would emphasize that international trade gives rise to two interlinked and opposite movements, i.e. that the purchase by a buyer in one country from a seller in another country involves the movement of goods in one direction and the movement of money in the opposite direction. These movements are initiated and controlled by a parallel flow of information, usually contained in documents.

18. From this very simplified description it may be appreciated that the several commercial parties involved in a trade transaction have different interests that must be safeguarded. Thus,

(a) The seller wishes to be certain of receiving payment;

(b) The buyer wishes to be certain of receiving the goods;

(c) The various intermediaries (forwarders, carriers, insurers and bankers) need to be certain that they can perform their services efficiently and to be assured of remuneration.

2.1 Administrative background

19. There is, however, another aspect of trade transactions which must be taken into account. The flows of information, the goods and the payments pass from one country to another. Therefore, the national authorities concerned have to exercise the necessary border controls. This is done on the basis of information which provides the acceptable evidence required to clear the goods and to monitor or control payment. The civil servants involved need to be formally satisfied of the legal acceptability of the information for each relevant step in the transaction; and they have to ascertain that the goods have been correctly defined and valued for duties and taxes, that one party has accepted formal responsibility in case of future discovery of errors or fraud, and that satisfactory evidence has been kept for later verification.

20. These considerations are of a nature different from commercial ones, and they are usually defined in formal enactments or, more often, in regulations issued by virtue of national laws. Whereas commercial parties are free to accept agreed standards or procedures, official control procedures can only be changed by law. However, a certain flexibility often exists by way of interpretation, or by amending regulations issued according to law. On the other hand, whereas private parties may agree on security levels that are acceptable in terms of cost, official requirements are of a more formal nature and the rules issued to implement them are often drafted taking into account other (and more abstract) considerations.

2.2 Technical background

2.2.1 Data communication

21. For the purpose of this paper, "data communication" is understood to mean the automatic transmission of messages by electronic or other means in such a manner that the possibility of automatic editing or processing of the text exists, or can be made available, if required.

22. Data communication may take place as direct transmission

between two or more computers;
from a computer to a terminal or to a printer or *vice versa*;
between terminals.

23. As the data processing of telex messages is possible at both transmitting and receiving ends, data communication is here deemed to include telex communication.

24. Data communication can also take place by sending the physical data carrier on which information is temporarily or permanently stored, e.g. a magnetic tape, a cassette, or a disk (or the somewhat out-dated punched card or punched tape).

25. Except when sending a data carrier, some form of electronic (or optical) communication network is needed to transmit data between hardware units.

26. In all cases, it is necessary to have a pre-determined method of communication providing the machines with the technical possibilities to process the data intelligently.

2.2.2 Different technical solutions

2.2.2.1 Public services

27. Telex has been available as a public data communications service for a long time. Various versions of data-processed telex messages exist. Some computer manufacturers offer direct access to the telex network.

28. Teletex involves using a miniprocessor with primary storage, various types of secondary storage, and printers. Although the main purpose of the teletex is to transmit and store messages, it can be used for other purposes, such as text processing. The teletex machine can be linked to other intelligent devices and can therefore be used as a communication unit in internal data systems.

29. Videotex (also known by other names) is another form of public data communication service that uses normal television sets as receiving terminals.

30. In some countries a public service for transmitting trade data does exist (in Canada, for example) or is being developed (in France). However, at present these are solely national systems.

31. One characteristic of public data communication systems is that a service is available to anyone who is prepared to accept the conditions of the system. Matters relating to liability are often regulated by means of statutes, statutory instruments and/or international conventions. The system is standardized and has an international range. A directory listing subscribers to the system exists and, in principle, each subscriber can reach any other subscriber at any time. The technical quality of the system is guaranteed within certain limits and there are possibilities of implementing certain technical and logical security features. Therefore, it may be possible to lay down certain legal rules as to responsibility of use and misuse.

2.2.2.2 Private data communication

32. Practically all modern computers afford possibilities for data communication, either under their own conditions or under general standardized conditions. Countless data communication systems between parties of various types are thus in operation. The technical quality of these data systems depends on agreements concluded between the parties concerned. As previously mentioned, internal computers can be used in conjunction with public data transmission services.

33. Data communication by sending physical data carriers has also been included under this heading. The exchange of magnetic tapes, for example, can be an economical form of data communication, particularly for mass data communication. With such means of data communication the parties often forgo the time gain that results from direct transmission. On the other hand, the information is usable as it is for further computer processing.

2.2.3 Transmission methods

34. Data can be transmitted by cable, electro-magnetically or optically, or by carrier. The user is uninterested in the medium or media used provided that the system satisfies his requirements regarding cost, efficiency and technical reliability.

2.2.3.1 Public data transmission networks

35. The most commonly-used public data transmission network is the telephone network, which has the advantages of being widespread and of high technical quality (although there are exceptions). Telephone networks use either dial lines or fixed lines; they do not offer data transmission services in the modern sense.

36. The telex network can also be used for data transmission in addition to telex messages. This network often has the same physical properties as the telephone network. Use of the telephone network is often more economic than use of the telex network.

37. In contrast to telephone networks, public data networks offer different forms of data services. However, in many cases not all possibilities are utilized, for cost reasons.

38. Examples of services that can be offered via public data networks are automatic dating, temporary storage, distribution to more than one record, automatic identification of parties and transforming transmission speeds, etc. Interface between different user equipment is handled by the network. The user does not know how his message is transmitted—transmission may take place via satellite, telephone, telex or other media, depending on the traffic volume. Line protocol within the network is standardized.

2.2.3.2 Open commercial networks

39. Where PTT administrations have a communications monopoly, open commercial networks usually offer data processing in one form or another, which makes them more service-oriented than public networks. Commercial networks often use parts of the public networks for data transmission. A number of commercial networks use information satellites as communication links. Identification in the form of code words is always required before contact is established between users of commercial networks.

2.2.3.3 Closed commercial networks

40. A characteristic of these networks is that only subscribers are permitted to use them. The subscribers may represent a particular branch of industry or a local region or any other group of common interest. As participation is

strictly on network conditions, the hardware can also be specified. This type of network often uses special data transmission computers with large temporary storage capacities and facilities for packing the data, with the result that extremely high transmission speeds can be attained within the network.

2.2.4 Transmission techniques

41. Apart from the data transmission hardware and the networks, both technical and logical rules are needed for data transmission. The most frequently occurring technical problems are the use of language or code and the type and speed of transmission. At the logical level, agreement must be reached on how transmission should be commenced and terminated, which control character should be used and, above all, how the information should be identified (if it is not printed out).

2.2.4.1 Closed systems (bilateral/multilateral agreements)

42. In a closed transmission system, the parties can of course make any agreement which they choose. Closed data communication systems between two, or only a few, parties are often efficient because the system can be designed to satisfy the needs of the parties and adapted to the hardware at their disposal. Problems may arise when it becomes necessary to link another party to the system when one or more of the participants wishes to contact an outside party or another closed system. However, in the short term, closed systems for a special purpose are often both efficient and economical. Security presents few problems, since the parties agree on a level that they consider to be both satisfactory and economic.

2.2.4.2 Open communication systems

43. Telex and teletex are typical examples of open communication systems, whereby, in principle, any subscriber is able to contact any other subscriber within the system. Open communication systems require strict technical standards and flexible data structures. If the information in an open system is to be machine-readable, a compromise between flexibility and standardization is necessary. To avoid the problems that arise in respect of technical compatibility, data transmission can—in theory at least—take place via exchanges whose principal purpose is to convert the message into a technical form suitable for the addressee's hardware. A serviceable model for this is the teletex. The data network also has possibilities, at least to a certain extent, for interfacing between hardware with different technical facilities.

44. Open data communication systems pose a security problem that must be solved before data communication can become operational on a large scale. Such security methods—of a legal or technical nature—are described below in sections 3.1.3, 3.2.2 and 3.2.3, and form the basis of the theories of 3.3.3.

2.3 Legal background

2.3.1 Documentary functions

45. Traditionally a trade document consists of a piece of paper bearing data of various kinds. Because of its lasting physical existence the paper functions as a carrier of data (information); documents thus have an *informative function*.

46. A trade document can also constitute evidence (documentary evidence). The evidence is the paper *per se* and the evidential content is the data carried on the paper. Documents therefore also have an *evidential function*.

47. Furthermore, legal systems have given to certain documents the characteristic that the paper document itself and the rights represented through it are so closely linked that it is reasonable to assume that the paper symbolizes the right. The document then has a further, *symbolic function* which today is related to an original paper document. Bills of lading and bills of exchange are typical examples of documents with symbolic function.

48. The functions which are connected with documents used in international trade and transport can be fulfilled only through exchange of these documents. This exchange, usually across frontiers, is traditionally achieved by mail or by courier.

49. The informative function, the evidential function and the symbolic function of paper documents are a consequence of the physical properties of the paper, of the exchange of documents and of the rules of the legal system concerning documents and their exchange. These rules are, to large extent, based on the physical properties of paper documents.

2.3.2 Factors of insecurity

50. Automatic data processing and data transmission are used as a means to dispense with the paper itself, but not its functions. Yet, although the elimination of paper and the use of other methods for the transmission of data can overcome many of the problems which are connected with paper documents, these other methods, in their turn, present certain aspects of insecurity.

51. These factors (or aspects) of insecurity—which are interlinked—arise mainly for the following reasons:

- (a) The physical characteristics of the paper document are absent;
- (b) Existing law is associated, to a large extent, with paper documents and their use;
- (c) Legal regulation of the field of ADP and data communication for trade is virtually non-existent;
- (d) The parties involved often lack the necessary technical and legal expertise to make use of the opportunities which are available and to interpret the consequences which arise from the utilization of new communication methods.

52. It may be said that the feeling of insecurity is mainly due to the fact that automated methods are new. Paper documents are well known and the degree of insecurity that they incorporate is generally accepted. Transfer of information by other means is new, and the security of such methods has yet to be proved. It is, therefore, necessary to look into the elements of insecurity in some detail.

53. The paper, and the written characters committed to it, are of a lasting nature. Once committed to paper a text is not easily removed, altered or added to without the paper showing some apparent signs thereof. The paper and its data content still retain their properties when the document has been transferred from one person to another. The holder knows what he has received, and can control its "safe custody".

54. The application of automatic transmission of data does not offer the same sense of security. Entering data from a document into a computer and sending the data content via teletransmission links to the recipient's computer does not enable the recipient to ascertain, from his visual display unit or from any print-out produced, whether any alterations have been made to the input data content. Moreover, the sender of

the data can transmit identical data to a third party. The element of control of "safe custody" is lost.

55. The technical elements of insecurity may be overcome by technical means (cf. sections 3.2.2 and 3.3.3.2). Another, and possibly more important, factor of insecurity is caused by the absence of legal rules corresponding to those governing the traditional trade documents and the rights and obligations vested in them.

56. Laws, conventions and usages of international trade are often applicable, in many cases compulsorily, to the traditional documents and their use. Procedural and criminal law often contains detailed provisions applicable to documents.

57. These rules cover the nature of the document, the concept of an "original", its format and detailed contents, and the application and legal implications. Up to the present time, these rules have been established on the basis of traditional paper procedures.

58. Further areas of insecurity may also be identified. For example, traditional communication services such as mail, telephone, telegraph and telex are, to a great extent, regulated nationally as well as internationally. For the new services which are being developed and which will eliminate the traditional paper document, regulation is apparently non-existent.

59. In most countries telephone, telegraph, telex and mail are State monopolies in one form or another. It is currently being studied to what extent the new data communication services will be regulated. If these State monopolies provide the new data transmission facilities, it is important that no new barriers be created. Any uncertainty with regard to private admission to the services and the operation of the necessary ADP and data communication equipment would create insecurity.

60. In certain countries concern over the protection of personal data has placed restrictions on the free flow of computerized data across frontiers. If such restrictions were extended unduly they might interfere with the free flow of data essential for an international trade transaction.

61. Many other factors that create insecurity are linked with current commercial and administrative practice.

62. It would seem necessary to provide an assurance to all the parties concerned, whether commercial parties, public authorities or Courts of law, that documentary functions can be retained in a paper-less system. This assurance must be provided by eliminating the insecurity factors.

3. Legal analysis

63. In this section particular emphasis is laid upon identifying those areas and problems where international efforts would be required.

3.1. Informative functions

3.1.1 The problem

64. How far is it possible to retain the informative function of paper documents in an ADP-based system in a manner that satisfies the need of the parties to achieve the same technical and legal standards as before?

3.1.2 Form and content

65. In principle, it is possible to print out data on paper in whatever format or design may be desired. The information presented on a document can be shown on a screen with approximately the same appearance. From the technical point of view, the A4 format often used for paper documents presents no difficulties in ADP systems.

66. It has been mentioned above that certain legislative texts may be seen to require the use of paper documents. However, most of these texts were issued before paperless trade and transport procedures became practicable. It would seem appropriate to adopt the attitude that ADP is acceptable as long as the functions of the traditional documents are retained.

67. In Scandinavia it may be assumed that the courts would accept these new procedures provided the documentary functions are retained. However, court decisions might be different in other parts of the world with different legal systems and traditions.

68. When an appendix to a legal text defines precisely how a document should be presented in order to be valid, courts consider this to be binding. It is therefore essential that those responsible for the drafting of relevant regulations become aware of the need to leave room for alternative information transmission methods.

69. When utilizing ADP and data communication it is important to avoid the long texts which are characteristic of standard contracts used in international trade and transport. One method is to refer to such texts by an "incorporation clause" in the form of code words—for example, "carrier's conditions" or "ICC rules". The validity of such "incorporation clauses" is being discussed in many fora and is accepted in most instances. (See Kurt Grönfors, *Cargo Key Receipt and Transport Document Replacement*, Gothenburg 1979, pp. 18-19; and E. du Pontavice: "Legal restraints on trade data interchange", ECE document TRADE/WP.4/R.116, para. 7 *et seq.*)

70. Although some persons consider that the use of ADP and data communication may cause problems with regard to laws concerning prescription, it would seem that in practice there is no difficulty in filing "print-outs" in the same way as paper documents are filed in present-day systems.

71. Many present-day concepts and notions will need to be revised as a result of the establishment of paperless procedures. Further questions will be asked. What is meant by a signature? Must it be a hand-written symbol, or can it be defined as the result of authentication by the use of mechanical or electronic means as provided in the Hamburg Rules? To eliminate possible problems in this context, it will be necessary to inform those involved and to train them. In some instances, information and education may not be sufficient. A solution must then be found by means of legal regulations, possibly based on some form of international instrument. As mentioned above, UNCITRAL would appear to be the appropriate body for this latter task.

72. Present administrative law or practice may also be a hindrance to the establishment of paperless procedures (cf. NORDIPRO special paper No.2 "Legal questions of trade facilitation", Oslo, June 1980). The CCC has a central position in this area and, as mentioned earlier, has already done important work to establish international legal standards for automated customs procedures. It would seem important that co-operation between UNCITRAL and the CCC should continue and be extended in the future.

73. As is implicit in paragraph 20 above, in many countries there exists a kind of legal pyramid. Although there are considerable variations, there is usually a solid core of primary law embodied in formal enactments of a constitutional body. On this base, there is built up a wider body of administrative regulations. These, in turn, delegate powers for a specific authority to lay down more detailed instructions. In this area of fast-moving technical developments it may be advisable to explore the possibility of limiting the primary law to essential matters of principle, since secondary law may usually be more easily amended.

3.1.3 Security methods: risk and responsibility

74. In an ADP system, data can either be in a process of input, storage, transmission or output. During processing data can be the subject of intentional or unintentional "attack". An intentional attack often takes the form of data misuse, i.e. data stored or under transmission are used in a way which is not permitted, or false data are fed in. These "attacks" of error and of fraud duplicate what can, and does, occur with regard to paper documentation.

75. Data misuse—fraudulent or otherwise—can occur in all phases of the data-handling process. The methods to prevent or restrict attacks on the content or use of data are, to a great extent, dependent on whether the attack is intentional or unintentional. Security methods depend on the stage in the data process where the attack occurs.

76. The following text makes a distinction between technical and legal security methods. These two methods should, however, be seen in the same context.

3.1.3.1 Technical security

77. Technical security methods can be classified (with regard to their structure and functions) as:

- physical security
- organizational security
- operational security
- system oriented security.

78. These security measures are not discussed in this paper. However, there is little doubt that a high level of security can be achieved—at a corresponding level of cost—thus protecting the data in the ADP system from intentional or unintentional attacks. Recent frauds involving ADP indicate that absolute security cannot be achieved although it can be asserted that it is perfectly feasible to establish a level of security equal to that in a paper-based system.

79. However, even in systems where costly technical measures have been taken against attack or malfunction, the possibility must be taken into account that breakdowns or accidents with grave economic consequences for the parties involved may occur. Security through legislation may therefore have to be considered.

3.1.3.2 Legal security

80. Methods of security based on administrative instruments and practices or Court procedures have the following purposes: first, they enable the parties to assess in advance, to a greater or lesser extent, the judicial and economic consequences of the use of automatic data transmission procedures and, second, they establish the way in which, and the extent to which, economic losses, which might occur as a result of the use of ADP, should be shared among the parties involved. It should be recalled that the applicability of such rules has an insurance aspect also.

3.1.3.3 Risk and liability

81. International trade procedures involve the exchange between the parties concerned of a great many messages of various kinds—e.g. messages concerning negotiation of contracts, messages constituting parts of contracts (e.g. offers and acceptances), messages containing information necessary for the performance of various parties under contracts, notices under a contract, objections against another party's performance, and declarations addressed to public authorities such as Customs.

82. Errors may occur in the exchange of these messages—e.g. a message may be delayed, or may fail to arrive or may arrive at the wrong place, or its contents may be altered in transmission. These occurrences are well known, and most legal systems have developed rules for dealing with these situations.

83. Obviously, some or most of these rules apply even if new processing and transmission methods are used. However, more detailed study should be made of how such problems may occur and should be dealt with when automatic methods replace manual systems.

84. An important question is to what extent the maker of a statement (e.g. an offer or an acceptance) should be legally bound by it even though the statement has been unintentionally altered in transmission or in the pre-transmission process.

85. A second question is how the risks involved should be apportioned between the parties involved.

86. A third question is whether, and to what extent, a party should be liable *vis-à-vis* the other parties for losses due to such errors.

87. Detailed evaluation of these and other questions of risk and liability is required based upon an analysis of various national solutions. There may not be a great difference between the rules already applicable for telex messages, telegrams, or leased public lines. However, where private rather than public networks are used for carrying trade data, new aspects of risk and liability may arise and need further study.

88. Another important question is that of liability of the intermediary who provides the transmission service. A contract for trade data transmission may contain clauses limiting the liability of the intermediary. These are, in general, binding upon the parties. If the contract is, on the other hand, rudimentary, liability is implicitly regulated by the rules of the legal system governing the contract. It is, however, not at all certain what these rules are. As regards public networks, the authorities do not usually accept responsibility—often not even in the case of negligence.

89. In respect of goods, the trend is towards imposing mandatory responsibility on the professional producer and trader for damage due to defects. The arguments may be equally strong for similar rules in respect of transmission services.

90. It should therefore be discussed whether such rules should be mandatory or only declaratory, whether the liability should be strict or based upon negligence and, in such cases, who should carry the burden of proof. Another problem is establishment of rules for assessing the damage.

91. A convincing argument is made in UNCITRAL document A/CN.9/149/Add.3, page 7, for a comprehensive

international legal framework for international electronic funds transfer, not least with regard to regulation of liability conditions. It should be stressed that the same conditions would apply to the transfer of other trade data/documents. It would seem reasonable to co-ordinate international efforts in this field also—amongst other reasons—because the problems are probably of the same legal character.

92. Another reason is that harmonization with existing rules is required. Usually accepted arguments would seem relevant, such as which party is the nearest to carry the risk; or who can best counteract an accident or minimize its effect. Not least important is the question of who can most easily insure against a possible loss, or equalize it.

3.1.4 Free flow of information

3.1.4.1 The problem

93. Paper documents can be freely transmitted across frontiers. A condition for retaining this informative function, as well as the evidential and symbolic functions—when data are processed and transmitted by automatic means in international trade—is that such data may be transmitted with equal freedom.

3.1.4.2 Personal data

94. In recent years, many countries have adopted data legislation, in some cases including provisions governing the right to transmit data across frontiers, *data export*. (Cf. *A Business Guide to Privacy and Data Protection Legislation*, ICC publication 384, Paris 1981.) Due to modern ADP and data transmission technology it has become possible to collect, store, process and transmit data efficiently, rapidly and at reasonable cost. It has become possible to monitor very large volumes of data covering a number of individual persons with a large amount of information on each person. ADP technology has made it possible to centralize the registration of such personal information, and to compare, sort and select information and process data from different information systems. It is obvious that this situation can involve a risk to the individual citizen's personal privacy. This is reflected in data legislation now being enacted in many countries, the principal aim of which is to strengthen an individual's control over the use of information pertaining to himself (information which may be classified as "private" or "sensitive").

95. Not all countries have adopted data legislation, however, and among those which have the protection of the citizen's personal privacy varies. This may make it tempting to export data files and personal data to countries having no—or less strict—legislation in this field. This explains why certain restrictions have been placed on the export of data files and personal data to foreign countries.

96. Among those whose work involves the transfer of international trade data by modern techniques there is some apprehension that—for a variety of reasons—legislation introduced to safeguard personal data may be extended to cover data concerning legal entities in such a manner that new barriers to trade will be erected.

97. ECE document TRADE/WP.4/R.99 analyses Nordic data legislation regarding the export of "personal data" across frontiers. However, this analysis focusses only on "goods"-related information. It is concluded that:

"...serious problems are unlikely to arise in connection with the Nordic data legislation when paper-less practices are pursued in international trade".

98. As to electronic funds transfer and the information transmitted across frontiers in systems created for such transfers, it is possible that national data legislation may create certain problems. This especially concerns transmission of credit information between countries. There is a need for further analysis of this problem.

3.1.4.3 Non-personal data

99. The protection of the individual citizen's personal privacy, however, is not the only consideration that could be taken into account when introducing restrictions in the free exchange of information across frontiers. Authorities have recently become aware of the fact that data transmission (for data processing) may lead to problems related to national security, economic independence, cultural independence and the safeguard of national employment.

100. This is described in more detail in a document issued by the ICC (document 191/124, Paris, 1979, p. 8 *et seq.*) where, amongst other things, it is stated that:

"...the ICC recognizes the legitimate aspiration of Governments to protect the economic and cultural well being of their citizens and their overriding responsibility to ensure the safety and security of their countries. The Chamber is concerned with ensuring that, in the course of such consideration, national Governments do not lose sight of the benefits which float to their citizens from a liberal international economic system and increasing inter-dependence through international trade. The ICC urges the business community to engage in the debate to ensure a proper balance in the interests of the individual citizen throughout the world."

101. A recently published report by the Organisation for Economic Co-operation and Development (OECD document DSTI/ICCD/81.9) contains suggestions for the development of guidelines for the free flow of information and is relevant for study of present problems. Several other international organizations study different aspects of transborder data flows; a survey is contained in documents TRADE/WP.4/R.200 and Add.1.

3.1.5 State monopoly in the field of telecommunications

102. A pre-condition for replacement of paper documents by automatic data transmission techniques is that the parties involved be given the possibility of obtaining, and using, the necessary technical equipment, at prices which are commercially attractive. It has already been mentioned that in most countries telephone, telegraph, telex and mail services are State monopolies, and in this connection the question arises as to the extent to which data communications would be regulated by State monopoly. Transmission equipment and the quality of the services made available from official sources might not always be sufficiently user-oriented. These problems have been analysed by the ICC Commission on Computing, Telecommunications and Information Policies in "The liberalization of telecommunication services—needs and limits" (ICC document 373-21/1 Rev, Paris, 1982). There may be a need for further studies in this area.

103. It should be realized that, also in the field of transborder data flows, extended international legal co-operation may be required, since measures intended to safeguard national positions may not be in the best interests of world trade.

3.2 Evidential functions

3.2.1 The problem

104. The essential feature of evidence is the need to verify at a later stage whether a certain event has happened or whether a certain fact is correct. Even so, there may be further questions of procedural law as to whether such verification is admissible and has legal force.

105. A paper document, signed in the traditional manner, can be said to constitute *prima facie* evidence. When ADP methods are used, instead of manual paper-related procedures, the problem concerning the evidential function is both technical and legal. It should thus be studied whether it is possible to provide technical solutions which result in data processed by automatic techniques retaining the same evidential weight as a traditional document signed in the usual way. Related legal questions are whether the law is a barrier to future developments and whether the parties involved can, and will, accept and use these solutions.

3.2.2 Technical solutions

106. Different technical solutions have been put forward, for example:

- logging
- print-outs
- passwords
- protocols
- confirmation and cryptography.

3.2.2.1 Logging

107. Logging is a method for internal control within a system through the recording of all or certain parts of incoming and/or outgoing messages. A complete log, which is often kept in a secondary memory of the computer, contains information on sender, receiver, type and content of message, and possibly some checking total ("hash total")—e.g. the total of the numerical values in the message. Logging of certain parts only of a message can be regarded as a register or diary. It is possible to protect the logged data so that they can only be changed by fraudulent means. Practically all medium sized to large sized computers have some form of automatic log built into the operative system, but they may be changed without the change being apparent. If the logging is done by a neutral third party, e.g. through the transmission system itself, the value as evidence is considerably enhanced. Complete logging at both ends of a transmission improves the situation, especially since messages normally carry a time indication down to seconds.

3.2.2.2 Print-out

108. A print-out on paper—produced continuously, if the transmission speed allows, or as soon as possible—is a way of providing a record which can have considerable evidential value; this value is increased if the print-out is combined with logging, and even more so if the functions of print-out and logging are separated and filing takes place in an appropriate and suitable manner. A record can also be preserved through transferring the information to an electronic data carrier, e.g. magnetic tape or disk. However, whereas an ordinary print-out has the advantages of a paper document, electronic data carriers can be the object of erasure or change without showing any signs of the operation.

3.2.2.3 Passwords

109. Protection against unauthorized use of the computer can be ensured by giving the sender of the message a code

word, password, without which he will be unable to establish contact with the computer of the receiver. The password is an identification of the sender and may contain codes that indicate the type of message that the sender could transmit. This type of control is customary in present data communications systems; and it gives a certain assurance concerning the identity of the sender. Password procedures may be established in different ways. One type of procedure presupposes only a contact impulse from the sender, upon which the receiver cuts the contact and re-contacts the sender as indicated, before the message can be transferred. Another type of procedure requires mutual logging; at the end of a message the receiver acknowledges by giving his diary log data whereupon he receives the sender's diary log data. Only then is the message valid. The second, more complicated, procedure offers higher value as evidence but is subject to the risk that logging procedures may be tampered with at a later stage without leaving any trace. This, however, calls for technical knowledge and, in certain cases, is the result of collusion between individuals.

3.2.2.4 Protocols

110. A protocol is a rule stating how to act in a given circumstance (cf. protocol for a royal reception, acting according to protocol, protocols to conventions). In data processing and trade data interchange the term protocol is used to describe agreed rules, e.g. how to represent the data in a commercial invoice (or any other message), how to establish a connection in a given communication network, etc. Protocols of primary importance for partners in trade relate to the structuring of messages (syntax), the representation of data (data elements) and the alphabetic and numerical characters required (capital and small, latin, greek, cyrillic, arabic, etc.). Processing and transmission protocols are handled by equipment manufacturers and transport service providers (PTTs), respectively. An example of a special protocol is the call-back procedure, through which the authenticity of a calling party is ascertained by the party called. Having been informed of the apparent identification of the caller, the party called terminates the call, identifies the first party in a directory prepared by a third party, and uses that information to call back to the first party.

111. The evidential value of a protocol would seem to be in the fact that it is used routinely for the interchange of messages and establishes an orderly procedure agreed between interchange partners. If errors occur, the message is rejected and an error correction procedure has to be used. Messages conforming to the protocol are more likely to be authentic than those which do not; deviation from the protocol could be an indication that the message has been tampered with.

3.2.2.5 Confirmation

112. Confirmation is a security feature which can be requested by the calling party to ascertain that the called party has received the message. The confirmatory answer may be a simple acknowledgement but in many cases some important data elements are included (repeated); the called party may, to protect himself, send a separate, confirmation message. (The call-back protocol referred to in paragraph 110 may be seen as one type of confirmation.) To ensure optimal security, the protocol should state that the party receiving a confirmation is obliged to check that it conforms to his earlier message and, if not, immediately to advise the other party.

3.2.2.6 Cryptography

113. Cryptography protects data against unauthorized access by making it unintelligible before transmission or storage and by reversing the process upon receipt or retrieval of the

data. These processes are called encryption and decryption, respectively, and generally consist of an algorithm that functions with a special key. In modern cryptography, two main categories of encryption methods can be distinguished, based upon key usage. They are:

(a) *Conventional crypto systems.* In these systems the same (secret) key used for encryption must be used for decryption.

(b) *Public key crypto systems.* In these systems a public encryption key is used, which is complementary to the secret decryption key, but in such a way that the decryption key cannot be derived from knowledge about the encryption key. (See, *inter alia*, Martin E. Hellman "The mathematics of public key cryptography", *Scientific American*, August 1979, pp. 130-139.)

114. The incorporation of a public key crypto system means that, from a technical point of view, it should be possible to "sign" information in a way which satisfies the parties' interest to the same degree as a traditional signature on a paper document. A data print-out which is produced on the basis of such electronically-"signed" data should normally be given the same—or greater—evidential weight and value as a paper document signed in the traditional way. Utilization of public key crypto systems would mean that information could be kept safe from bugging or tapping. The system can be used with any type of transmission network where data are processed in a data processor. It may also be used by successive transmissions, even if further data are to be added. (See also document TRADE/WP.4/R.98.)

115. With paper-borne data, a number of documents of varying content may be called for in order to supply the information needed for official purposes. Frequently, these documents have to be provided not only with an exporter's signature but also with certifications or endorsements by various official or semi-official authorities. This problem—the problem of dual signature/authentication—can be solved by incorporation in public key crypto systems.

116. Until now, however, the public key concept has not been implemented in practice and there have been no trials to determine the applicability of the public key crypto system in the area of trade and transport. It is therefore possible that in practice the system may not prove to be satisfactory. Moreover, the public key concept is not yet under consideration and in view of the rapidity of technical developments, other technical solutions may be produced in the interim.

117. Systematic use of technical security measures would seem to ensure a high degree of security—certainly higher than with traditional paper documentation. Further study and testing of such devices should therefore be given high priority and their validity when used for providing legal evidence should be explored. The need for procedural rules or guidelines facilitating questions of evidence should be looked into.

3.2.3 The legal problems

118. It is stated in UN/ECE document TRADE/WP.4/R.99 that Nordic Law would probably not pose any problems regarding the admissibility in evidence of records kept in computer systems. Such records could, for example, be submitted in the form of a computer print-out.

119. This would also seem to be the general tendency in other countries having civil-law-based legal systems. The legal situation is somewhat similar in certain countries having

common law of common law derived legal systems—except, perhaps, in respect of procedural rules for the acceptance of such "evidence". Nevertheless, these differences regarding the acceptability of computer-held information as documentary evidence do create problems. In UNCITRAL document A/CN.9/149/Add.3, page 5 (referred to in paragraphs 11 and 91 above), it is pointed out, among other things, that:

"Although some attempt has been made in a number of common law jurisdictions to resolve these problems either by statute or by pragmatic judicial interpretation of the rules of evidence, it is doubtful whether the underlying problem can be resolved short of some form of international agreement".

120. The Council of Europe Committee of Ministers, on 11 December 1981, adopted recommendation No. R(81)20 to member States on the harmonization of laws relating to the requirement of written proof and to the admissibility of reproduction of documents and recording on computers. This recommendation is a step in the right direction. Also of interest in this context are documents on "The use as evidence in arbitration matters of documents prepared by computers" (TRADE/WP.4/R.126) and on "Conferring legal force on documents recorded on magnetic tape or presented as computer print-outs" (TRADE/WP.4/R.178), both transmitted by the Government of the Union of Soviet Socialist Republics. Comments from the Federal Republic of Germany are contained in document TRADE/WP.4/R.201. It should also be mentioned that the Legal Committee of SIMPROFRANCE has transmitted two extremely valuable documents in this field, namely:

(a) TRADE/WP.4/GE.2/R.123: "Legal problems and ADP systems in international trade"; and

(b) TRADE/WP.4/R.116: "Legal restraints on trade data interchange" reproducing an article by Professor du Pontavice entitled "Automatic data processing and foreign trade documents".

In TRADE/WP.4/R.199 the Legal Committee of SIMPROFRANCE commented on the study referred to in paragraph 135 below.

121. When computer-held information is introduced, difficulties would arise if authentication had to be evidenced by the traditional signature method, where the signature is physically connected with the actual paper. When ADP methods are introduced for transmitting data the signed document itself is not sent, only the data contained in the document.

122. Legal requirements often exist regarding the use of a signature on documents used in international trade, although it is not always stated in what form the signature should be present. Many countries require that the signature appear in the form of a handwritten signature. In others, a less formal "signature" is permissible provided it is physically connected with the actual document.

123. It must be taken into account that an "electronic signature", although possibly an even better authentication of the source of the data message than the traditional signature, may not in itself be capable of overcoming the problem of "signature".

124. UN/ECE/FAL recommendation No. 14, represents a useful initial step towards resolving the problem. It reads as follows:

"...recommends to Governments and international organizations responsible for relevant intergovern-

mental agreements to study national and international texts which embody requirements for signature on documents needed in international trade and to give consideration to amending such provisions, where necessary, so that the information which the documents contain may be prepared and transmitted by electronic or other automatic means of data transfer, and the requirement of a signature may be met by authentication guaranteed by the means used in the transmission; and recommends to all organizations concerned with the facilitation of international trade procedures to examine current commercial documents, to identify those where signature could safely be eliminated and to mount an extensive programme of education and training in order to introduce the necessary changes in commercial practice".

125. In June 1981, the CCC adopted a recommendation concerning the transmission and authentication of goods declarations processed by computer, making it possible for declarants, under certain conditions, to transmit these declarations by electronic or other automatic means.

126. Certain recent international conventions have introduced rules which open up possibilities for electronic "signatures", as, for example, the Hamburg Rules or the United Nations Convention on Multimodal Transport. Such Conventions may, however, be of limited value as they often contain a reservation that the electronic signature cannot be used if it conflicts with the law of the issuing country.

127. There is therefore need to develop an international instrument concerning the requirements that would give an electronic "signature" or authentication of computer-transmitted information the same legal effects as a traditional signature.

3.3 Symbolic functions ("negotiability")

3.3.1 The problem

128. The symbolic function of a document can be defined as the legal effect attached to the possession and transfer of the original document. Certain physical characteristics of paper make it possible to establish an "original document". These physical characteristics are lost when data are processed and transmitted by automatic means, thus creating a problem that must be solved in order to retain the symbolic function.

129. The problem clearly exists in connection with the bill of lading. This document has an important symbolic function, and the study of solutions is therefore high on the priority list of those concerned. However, identified problems are regarded as difficult to solve and, in the context of trade facilitation, the advice is often given to avoid, as far as possible, the use of negotiable bills of lading. Research has shown that this type of transport document is issued far more often than is strictly necessary. UN/ECE/FAL recommendation No. 12, "Measures to facilitate maritime transport document procedures", deals with this matter and recommends, inter alia, that negotiable transport documents be used only when required, and encourages the use of the non-negotiable sea waybill or other alternative transport documents which do not have to be surrendered at destination to obtain delivery of the goods. Unfortunately, certain Governments insist on the continued use of negotiable bills of lading for import/export or exchange control purposes, and refuse to approve the use of a non-negotiable transport document.

3.3.2 The approach

130. The problem of retaining a document's symbolic function in ADP and data transmission-based systems can theoretically be solved by using two different methods of approach.

131. One possibility would be to refrain from using possession and surrender as legal points of fact in relation to the symbolic function. This would mean abandoning an established legal technique, whilst exploring the possibility of replacing this technique with another having the same legal effect. This approach is judicially complicated but technically relatively simple. It might therefore be called the legal approach.

132. Another possibility would be to use the existing judicial technique with possession and surrender as central features and to explore the possibility of recreating the rights and obligations of the paper document. This approach can be characterized as judicially relatively simple but technically complicated. It might therefore be called the technical approach.

133. Section 3.3.3 describes two theoretical studies which represent the legal and technical approaches. Section 3.3.4 outlines a major research project intended for practical application: the Cargo Key Receipt system. Finally, in section 3.3.5 a suggestion made by INTERTANKO's Documentary Committee is mentioned.

134. The mere fact that the above four projects have been developed over the last few years underlines the great importance attached to problems linked to the symbolic function. Ways are suggested in which to secure harmonized solutions, and the importance of international work in this area is emphasized. It would seem that sufficient material is now available for UNCITRAL and ICC to carry out a joint study on the subject.

3.3.3 Two theoretical studies

3.3.3.1 The legal approach

135. A study by Knut Helge Reinskou, "Bills of lading and ADP: description of a computerized system for carriage of goods by sea" (*Journal of Media Law and Practice*, volume 2, number 2, September 1981), develops the concept of a document-free system for the transport of goods by sea. Documents to be replaced are bills of lading, waybills and other documents which are used in documentary credits and other forms of payment settlement. (See also document TRADE/WP.4/R.159.)

136. The fundamental concept is that of a notification/confirmation system. Whenever a right in the goods is created or transferred, the creator or transferer notifies the carrier of the transaction. The carrier registers the change and sends the beneficiary or the transferee a confirmation of his acquired rights.

137. The transport agreement and the confirmation by the carrier contain special clauses which seek to establish the same legal relations as those which characterize the concept of negotiability. A "registering and clause" system is proposed. Under the draft system, a number of messages are exchanged between the participating parties' computers. The study emphasizes that such exchanges demand security and that the necessary level can be achieved by using a public key crypto system.

3.3.3.2 The technical approach

138. In a study by Roger Henriksen: "The legal aspects of paper-less international trade and transport" (Copenhagen, 1982), which presents a theory based on the application of a public key crypto system and describes special technical features, it is suggested that the present-day documents be replaced by a concept of "original data content", i.e. something tangible. Possession and surrender of the original data content, such as that of a bill of lading, shall in all respects be given the same legal effects as the possession and surrender of an original paper document. (See also document TRADE/WP.4/R.98.)

139. Under the present system, it is the wording on the paper (the data content) that determines the type of document that it constitutes, and this should not change when a new technical process is used. The desired legal relationships can be established through the data content.

140. If this is accepted, the symbolic function of a document will be linked with the possession of a text containing the necessary (original) data content and not with the possession of an original paper document as is present practice.

3.3.4 Cargo Key Receipt system

141. The aim of this project is to develop an operative system whereby the banker's need for security in connection with payment through documentary credit procedures can be safeguarded without the surrender of a traditional bill of lading or an international waybill. The aim is limited to this: where there is a need to sell a consignment in transit, use of the traditional negotiable bill of lading is still recommended.

142. The legal solution in this system is based on the international waybill, in many ways a "simpler" document than the bill of lading, and much easier to imitate in an ADP system.

143. The Cargo Key Receipt system operates as follows:

(a) The goods are sold ex works, FCD (free carrier named point of departure) or under any similar term of delivery which confers title of ownership to the buyer at the latest when a bank in the seller's country pays him. The sales contract thus stipulates that property to the goods sold shall pass at the moment when a bank at the place of departure pays the seller against his Cargo Key Receipt, in conformity with the instructions of the buyer—he has either arranged for the issue of a documentary credit or has ordered "cash on delivery" with instructions to pay against the Cargo Key Receipt. The buyer, by agreement with his bank, pledges the goods in transit as security and collateral for what he has instructed his bank to pay on his behalf;

(b) When the sender has delivered the goods to the carrier or his agent at the place of departure, he receives his Cargo Key Receipt, as the first print-out following input of all necessary particulars into the carrier's computer. This contains, *inter alia*, the following data elements:

- (i) The buyer's bank (financing the sales transaction), named as consignee;
- (ii) The consignor's "NODISP" statement, meaning that the seller in his capacity as party to the contract of carriage has irrevocably abrogated from his right of disposal to the goods during the transit;
- (iii) The carrier's "CLEAN" statement, meaning that the carrier, after the customary inspection of the goods taken in charge, has made no remarks

regarding their condition (such as "2 cases broken", "steel sheets rust marked");

- (iv) The carrier's "SECURITY" declaration, meaning that he holds the consignment specified on the receipt on behalf of and as collateral for the bank named as consignee;

(d) All particulars stored in the computer are forwarded from the place of departure to the place of destination by means of telecommunication;

(e) The authorized bank in the seller's country pays the seller against the Cargo Key Receipt and advises the buyer's bank by means of telecommunication;

(f) Shortly before the goods arrive at the place of final destination, the carrier sends an arrival notice to the buyer's bank, in its capacity as consignee, with a copy to the buyer, in his capacity as "notify address" only. The buyer then pays his bank against endorsement of the original notice of arrival to him and requests the carrier, by virtue of the endorsed notice, to deliver the goods to him instead of to the named consignee, the bank.

144. Only a modest percentage of all goods carried is sold while in transit from the port of loading to the port of destination. In liner trade, the percentage is even lower. It would therefore be possible to introduce ADP-based systems designed on the basis of the Cargo Key Receipt system; efforts to develop this system are being followed with great interest by those concerned.

3.3.5 The INTERTANKO project—sale of cargo through a clearing house

145. This system is being developed for bulk cargoes, especially for the tanker trade. It is suggested that the "key to the goods" function may be served by a register, based on agreement that all transactions regarding a shipment shall be handled through a central clearing house. Initially agreed between shipper and carrier, all subsequent buyers (assignees) have also to adhere to the system. It is part of the agreement that no bill of lading will be demanded, and that all transfers of rights to the goods will be effected by telex notification to the central register. All important telexes should be authenticated by cross-checking over the telephone and in writing.

146. This system could function in two ways: either as a central register (or registers) in some principal oil port (ports) or trade centres, or else simply as a private arrangement involving those who will take part in the transaction. In the latter case the register should be kept by a bank, and all payments should be made through that bank. In the case of the central register it needs be considered whether payments shall be made through the register or otherwise.

147. For a fuller description, reference is made to "Delivery of cargo without presentation of bills of lading", report dated 16 November 1980 from the Chairman of the Documentary Committee of INTERTANKO.

4. Conclusions

148. Automatic data transmission is gradually being introduced for documentation requirements in international trade. These methods comprise important advantages for all parties concerned and the technical, commercial and organizational conditions have already been established. However, the problem of legal acceptability remains, and the lack of legal rules both nationally and internationally leads to a feeling of insecurity which may hinder further developments (see paragraphs 1-7).

149. The problems involved have a bearing on different legal disciplines although it would appear that international trade law is most directly concerned. The co-ordinating body within the United Nations on questions of international trade law—UNCITRAL— which has already initiated studies on the related topic of electronic funds transfer should take this matter up for further action, in co-operation with other organizations, such as:

(a) The Customs Co-operation Council, on matters of administrative law and questions of transborder data flow (see paragraphs 19-20 and 72);

(b) The Organisation for Economic Co-operation and Development, on the need for international rules to safeguard the free flow of data for international trade transactions (see paragraphs 99-103);

(c) The International Chamber of Commerce, on the need for rules on negotiability (see paragraph 134).

150. Attention is also drawn to the more specific conclusions regarding the need to establish certain rules of material law. This is especially important with regard to questions of risk and liability where it would seem vital to take into account

existing international instruments and the legal doctrines on which they are based (paragraphs 87-92). Other conclusions that merit attention are those related to the need to avoid too rigorous drafting techniques (paragraphs 68-73), and the need for rules of evidence (paragraph 119) and on authentication (paragraphs 115 and 127).

151. Cryptography and the use of the public key crypto systems might well play an important role in solving some of the main technical/legal problems encountered in this field. It is recommended that the ECE Working Party on Facilitation of International Trade Procedures should study this matter with a view to ascertaining its usefulness for practical application.

152. Although the strong trend towards paperless procedures can be expected to continue and prevail, traditional paper procedures will still be used in many instances and new rules should be compatible with current practices and traditions. The rules should be international and, on the whole, mandatory and should embrace trade, transport and payments as well as administrative law.

VI. STATUS OF CONVENTIONS^a

Note by the Secretary-General: status of conventions (A/CN.9/241)^b

1. At its thirteenth session the Commission decided that it would consider, at each of its sessions, the status of conventions that were the outcome of work carried out by it.^c

^aFor consideration by the Commission see Report, chapter VII (part one, A).

^b31 March 1983. Referred to in Report, para. 119 (part one, A).

^cReport of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 163 (Yearbook ... 1980, part one, II, A).

2. The present note is submitted pursuant to that decision. The annex hereto sets forth the state of signatures, ratifications and accessions as of 25 March 1983 to the following conventions: Convention on the Limitation Period in the International Sale of Goods (New York, 1974); Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980); United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg); and United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980).

ANNEX

1. *Convention on the Limitation Period in the International Sale of Goods (New York, 1974)*^d

State	Signature	Ratification	Accession
Argentina			9 October 1981
Brazil	14 June 1974		
Bulgaria	24 February 1975		
Byelorussian SSR	14 June 1974		
Costa Rica	30 August 1974		
Czechoslovakia	29 August 1975	26 May 1977	
Dominican Republic			23 December 1977
Egypt			6 December 1982 ^e
German Democratic Republic	14 June 1974		
Ghana	5 December 1974	7 October 1975	
Hungary	14 June 1974		
Mongolia	14 June 1974		
Nicaragua	13 May 1975		
Norway	11 December 1975	20 March 1980	
Poland	14 June 1974		
Ukrainian SSR	14 June 1974		
USSR	14 June 1974		
Yugoslavia			27 November 1978

Signatures only: 11; ratifications and accessions: 7

Declarations and reservations

Upon signature Norway declared that in accordance with article 34 the Convention would not govern contracts of sale where the seller and the buyer both had their relevant places of business within the territories of the Nordic States (i.e. Denmark, Finland, Iceland, Norway and Sweden).

^dYearbook ... 1974, part three, I, B (A/CONF.63/15).

^eBy virtue of accession to Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980) (art. VIII(2) of the Protocol).

2. *Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980)*^f

<i>State</i>	<i>Accession</i>
Egypt	6 December 1982

3. *United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg)*^g

<i>State</i>	<i>Signature</i>	<i>Ratification</i>	<i>Accession</i>
Austria	30 April 1979		
Barbados			2 February 1981
Brazil	31 March 1978		
Chile	31 March 1978	9 July 1982	
Czechoslovakia	6 March 1979		
Denmark	18 April 1979		
Ecuador	31 March 1978		
Egypt	31 March 1978	23 April 1979	
Finland	18 April 1979		
France	18 April 1979		
Germany, Federal Republic of	31 March 1978		
Ghana	31 March 1978		
Holy See	31 March 1978		
Hungary	23 April 1979		
Madagascar	31 March 1978		
Mexico	31 March 1978		
Morocco			12 June 1981
Norway	18 April 1979		
Pakistan	8 March 1979		
Panama	31 March 1978		
Philippines	14 June 1978		
Portugal	31 March 1978		
Romania			7 January 1982
Senegal	31 March 1978		
Sierra Leone	15 August 1978		
Singapore	31 March 1978		
Sweden	18 April 1979		
Tunisia			15 September 1980
Uganda			6 July 1979
United Republic of Tanzania			24 July 1979
United States of America	30 April 1979		
Venezuela	31 March 1978		
Zaire	19 April 1979		

Signatures only: 25; ratifications and accessions: 8

Declarations and reservations

Upon signing the Convention the Czechoslovak Socialist Republic declared in accordance with article 26 a formula for converting the amount of liability referred to in paragraph 2 of that article into the Czechoslovak currency and the amount of the limits of liability to be applied in the territory of the Czechoslovak Socialist Republic as expressed in the Czechoslovak currency.

^fYearbook ... 1980, part three, I, C (A/CONF.97/18, annex II).

^gYearbook ... 1978, part three, I, B (A/CONF.89/13, annex I).

4. *United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980)*^h

<i>State</i>	<i>Signature</i>	<i>Ratification</i>	<i>Accession</i>
Austria	11 April 1980		
Chile	11 April 1980		
China	30 September 1981		
Czechoslovakia	1 September 1981		
Denmark	26 May 1981		
Egypt			6 December 1982
Finland	26 May 1981		
France	27 August 1981	6 August 1982	
German Democratic Republic	13 August 1981		
Germany, Federal Republic of	26 May 1981		
Ghana	11 April 1980		
Hungary	11 April 1980		
Italy	30 September 1981		
Lesotho	18 June 1981	18 June 1981	
Netherlands	29 May 1981		
Norway	26 May 1981		
Poland	28 September 1981		
Singapore	11 April 1980		
Sweden	26 May 1981		
Syrian Arab Republic			19 October 1982
United States of America	31 August 1981		
Venezuela	28 September 1981		
Yugoslavia	11 April 1980		

Signatures only: 19; ratifications and accessions: 4

Declarations and reservations

Upon signing the Convention the Governments of Denmark, Finland, Norway and Sweden declared in accordance with article 92(1) that they would not be bound by part II of the Convention (Formation of the contract).

^hYearbook ... 1980, part three, I, B (A/CONF.97/18, annex I).

VII. TRAINING AND ASSISTANCE IN THE FIELD OF INTERNATIONAL TRADE LAW^a

Report of the Secretary-General: training and assistance (A/CN.9/240)^b

1. The Commission, at its fourteenth session,¹ agreed that it should continue to sponsor symposia and seminars on international trade law. It was considered desirable for these seminars to be organized on a regional basis. In this way, it was felt, a larger number of participants from a region could attend and the seminars would themselves help to promote the adoption of the texts emanating from the work of the Commission. The Commission welcomed the possibility that regional seminars might be sponsored jointly with regional organizations. The secretariat was requested to make such arrangements as it found desirable in this regard. At its fifteenth session,² the Commission considered the progress made by the secretariat in organizing such symposia and seminars, and agreed that the secretariat should continue to explore various possibilities of collaborating with other organizations and institutions in the organization of such symposia and seminars.

2. By its resolution 37/106 of 16 December 1982, the General Assembly reaffirmed the importance, in particular for the developing countries, of the work of the Commission concerned with training and assistance in the field of international trade law, and welcomed the initiatives being undertaken to sponsor regional symposia and seminars. The General Assembly also expressed its appreciation to those States that had made financial contributions to be used towards the financing of symposia and seminars and of other aspects of the training and assistance programme of the Commission, and to those Governments and institutions that were arranging symposia or seminars in the field of international trade law. Furthermore, the General Assembly invited Governments, relevant United Nations organs, institutions and individuals to assist the secretariat in financing and organizing symposia and seminars.

3. The secretariat co-operated with the Organization of American States (OAS) in the annual international law seminar held at Rio de Janeiro in August 1982,

organized by the Inter-American Juridical Committee of the OAS. The seminar considered, *inter alia*, the activities of the Commission, and in particular the United Nations Convention on Contracts for the International Sale of Goods, Vienna, 1980 (hereinafter referred to as the Vienna Sales Convention).^c

4. In response to a suggestion made by the UNCITRAL secretariat to the secretariat of the Council for Mutual Economic Assistance (CMEA), the first CMEA regional seminar on UNCITRAL was organized by the CMEA (Moscow, 14-15 April 1983). The Convention on the Limitation Period in the International Sale of Goods, New York, 1974,^d and the Vienna Sales Convention were chosen as the subjects of the seminar because of the increasing interest in these Conventions throughout the world, and because their entry into force is foreseeable in the near future. The seminar was very well attended, and included as participants the heads of the legal departments of the Ministries of Foreign Trade of the countries belonging to the CMEA. The general conclusion at the seminar was strongly in favour of the two Conventions as an acceptable and workable compromise between the different approaches of national law in the areas covered by the Conventions.

5. The secretariat collaborated in a symposium (Baden bei Wien, 18-19 April 1983) organized jointly by the Economic University of Vienna, the Austrian Federal Ministry of Justice and the Oesterreichische Kontrollbank A.G. The symposium considered the Vienna Sales Convention, and its relationship to some civil law systems. The symposium included participants from Austria, Federal Republic of Germany, Hungary and Switzerland.

6. At its annual conference for 1983, the International Law Section of the American Bar Association will hold a symposium (Atlanta, 1 August 1983) on the Vienna Sales Convention. The Secretary of the Commission has been invited to participate in that symposium.

7. The secretariat co-operated with the Regional Centre for Arbitration, Kuala Lumpur (established under the auspices of the Asian-African Legal Consultative Committee), in a seminar organized by the Centre (Kuala Lumpur, 2-3 November 1982). Among the

^aFor consideration by the Commission see Report, chapter VIII (part one, A).

^b27 April 1983. Referred to in Report, para. 127 (part one, A).

¹Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 109 (Yearbook ... 1981, part one, A).

²Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17* (A/37/17), para. 132 (Yearbook ... 1982, part one, A).

^cYearbook ... 1980, part three, I, B (A/CONF.97/18, annex I).

^dYearbook ... 1974, part three, I, B (A/CONF.63/15).

subjects considered at this seminar were the conduct of institutional arbitrations under the rules of the Regional Centre (which rules are based on the UNCITRAL Arbitration Rules),^e *ad hoc* arbitration under the UNCITRAL Arbitration Rules, and the enforcement of arbitral awards under the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, New York, 1958.^f

8. The secretariat participated in the VIIth International Arbitration Congress (Hamburg, 7-11 June 1982). The subjects discussed at that Congress included the activities of UNCITRAL in the field of arbitration, and in particular the UNCITRAL Conciliation Rules^g and the UNCITRAL project on a model arbitration law.^h

9. The Ibero-American Seminar on International Commercial Arbitration (Madrid, 13-15 December 1982) was organized by the Superior Council of the Chambers of Commerce, Industry and Navigation of Spain and the Inter-American Development Bank. It considered, *inter alia*, the UNCITRAL project on a model arbitration law.

10. The VIIIth Inter-American Conference on Commercial Arbitration (Santiago de Chile, 6-9 April 1983) was organized in co-operation with the UNCITRAL secretariat. The Conference discussed extensively some of the activities of the Commission, such as the recommendations to assist arbitral institutions and other interested bodies with regard to arbitrations under the UNCITRAL Arbitration Rules and the UNCITRAL project on a model arbitration law.

11. A seminar will be organized for West Africa towards the end of 1983 at Abidjan by the Ivory Coast Chamber of Industry and the Institute of International Business Law and Practice of the International Chamber of Commerce, on the techniques of international commerce. This seminar will have the support of the UNCITRAL secretariat and the Economic Community of West Africa. It will consider, *inter alia*, the role of

uniform law in promoting international trade, and issues relating to international commercial arbitration.³

12. In addition to those seminars or symposia mentioned in the preceding paragraphs, there have been several occasions during the preceding year when the secretariat was invited to make the work of UNCITRAL known. The secretariat has been in contact with several organizations and some Governments with a view to exploring further possibilities of jointly organizing symposia or seminars. Organizations contacted include the Asian-African Legal Consultative Committee, the Centre de Droit des Obligations, Louvain, Belgium, the Commonwealth Secretariat, the International Law Institute, Georgetown University Law Center, and the International Trade Centre (UNCTAD/GATT). While the principal limitation on the organization of symposia and seminars is that not enough funds are available for this purpose, the secretariat will continue its efforts to explore all suitable opportunities for training and assistance and to make the work of UNCITRAL known.⁴

13. During the past year, three interns received training at the UNCITRAL secretariat, and were associated with the work connected with on-going projects of the Commission.

³The Institute of International Business Law and Practice of the International Chamber of Commerce holds regular symposia and seminars on international trade law and practice, and it is the intention of the Secretariat to collaborate with the Institute, whenever it is considered advisable, when the symposia or seminars will be held in developing countries.

⁴With regard to the Hamburg Rules (Yearbook ... 1978, part three, I, B), the report of the Secretary-General entitled "Co-ordination of work: in general" (A/CN.9/239) (reproduced in this volume, part two, V, A) notes that the Third Inter-American Specialized Conference on Private International Law (CIDIP-III) is likely to have an agenda item on international maritime transportation, which will focus on the Hamburg Rules. Furthermore, the secretariat of UNCTAD is collaborating with the UNCITRAL secretariat in the promotion of the Hamburg Rules, in particular because the entry into force of the United Nations Convention on International Multimodal Transport of Goods, Geneva, 1980, (which is based on preparatory work done by the UNCTAD secretariat) is linked to the entry into force of the Hamburg Rules. Furthermore, the finalization of the UNIDROIT project for a draft Convention on the Liability of International Terminal Operators, intended to fill a gap in the uniformity of legal rules in the chain of events which takes place in the transport of goods from the shipper to the ultimate consignee, will enhance the attention paid to the Hamburg Rules.

^eYearbook ... 1976, part one, II, A (General Assembly resolution 31/98 of 15 December 1976).

^fUnited Nations, Treaty Series, vol. 330, No. 4739 (1959), p. 38.

^gYearbook ... 1980, part one, II, A (General Assembly resolution 35/52 of 4 December 1980).

^hYearbook ... 1982, part two, III, B (A/CN.9/WG.II/WP.35).

I. SUMMARY RECORDS OF THE UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW FOR SESSIONS DEVOTED TO THE PREPARATION OF DRAFT CONVENTIONS AND OTHER LEGAL INSTRUMENTS

A. Universal Unit of Account

Summary records of the 254th to 256th meetings, fifteenth session (New York, 26 July-6 August 1982) (A/CN.9/SR.254-256)^a

254th meeting

Tuesday, 27 July 1982, at 10 a.m.
Chairman: Mr. EYZAGUIRRE (Chile)

[A/CN.9/SR.254]

The discussion covered in the summary record began at 10.35 a.m.

INTERNATIONAL PAYMENTS

(b) Universal unit of account

1. Mr. BERGSTEN (secretariat) said that at its eleventh session, the Commission had decided to study ways and means of establishing a system for determining a universal unit of account of constant value which would serve as a point of reference in international conventions for expressing amounts in monetary terms. At its fourteenth session^b the Commission had considered a report of the Secretary-General which had suggested that the most desirable approach would be to combine the use of the Special Drawing Right (SDR) with a movable index which would preserve over time the purchasing power of the monetary values set forth in specific international conventions. At the end of its discussion, the Commission had referred the matter to the Working Group on International Negotiable Instruments and asked it to prepare a text on the subject. At its twelfth session in Vienna, the Working Group had adopted two texts as alternative ways of preserving the purchasing power of monetary values. One of those, contained in paragraph 53 of document A/CN.9/215,^c was based on an indexing approach. The other, contained in paragraph 90 of the report, was an expedited revision procedure to be carried out by a committee composed of

representatives of the Contracting States. The Working Group had recommended to the Commission that it might adopt the two texts as alternatives and recommend them to various diplomatic conferences which in future would be adopting new conventions with limited liability provisions or which might be revising such conventions.

2. Subsequent to the meeting of the Working Group, the secretariat had submitted both texts to the Treaty Section of the Office of Legal Affairs which functioned as depositary within the United Nations for conventions and which had the expertise within the secretariat on certain depositary matters. That Section had, in document A/CN.9/220,^d recommended several modifications of the text. The Working Group had also made a third recommendation. During discussions in January 1982, the delegation of the Union of Soviet Socialist Republics had made a statement (annexed to the report of the Working Group) to the effect that, although the Union of Soviet Socialist Republics was not a member of the International Monetary Fund (IMF) and although the SDR could not be used as a means of payment under Soviet law, it was nevertheless willing to observe the use of the SDR as a unit of account in conventions of the type in question. As a result, the Working Group had recommended to the Commission the adoption of a text which would be based upon the SDR alone. Accordingly, the Commission had before it two texts adopted by the Working Group as alternative means of reflecting the changes in purchasing power of monetary values and a recommendation of the Working Group that the Commission might adopt a new text for the unit of account based substantially upon paragraph 1 of article 26 of the Hamburg Rules.^e

3. Mr. BYERS (Australia) suggested that the recommendations of the Working Group in paragraph 97 should be accepted. As his delegation understood it, the proposal in paragraph 53 was for the insertion in the text of an automatic corrector for inflation. That was perhaps the ideal method.

^aYearbook ... 1982, part two, II, B, 3.

^eYearbook ... 1978, part three, I, B (A/CONF.89/13, annex I).

^bThe summary records contained in this volume include the corrections to the provisional summary records that were requested by the delegations and such editorial changes as were considered necessary.

^cReport of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), para. 25 (Yearbook ... 1981, part one, A).

^dYearbook ... 1982, part two, II, B, 1.

4. The other recommendation related in the main to provisions concerning transport conventions and his delegation supported the view that the recommendations of the Working Group calling for a revision of limitations of liability based upon a simple majority should be accepted. His delegation also supported the view that the provisions which accommodated the measures of liability determined in the cases to which paragraphs 97 and 90, 93, 95, 94 and 96 referred should be included in future conventions. The most desirable approach would be to have a provision in a convention which automatically produced the result of killing the effect of inflation on the agreed measure of liability. Should other factors beyond inflation be present, some other method would obviously be desirable. That method would take into account not only the effect of inflation but also the effect of cheaper and improved technology. His delegation therefore supported the recommendation of the Working Group contained in paragraph 97 of the report (A/CN.9/215).

5. Mr. SEVON (Finland) said that one need not go further than the Hamburg Rules to appreciate the seriousness of the problem before the Commission. In some countries, concern was growing that, if the Hamburg Rules did not enter into force within a limited period of time, the amounts might prove too low to have any influence on inflation. Such an event would make it impossible to promote uniformity in liability conventions and transport conventions. His delegation therefore agreed with the Working Group's recommendations referred to by the delegate of Australia. He also felt that the Commission should make no choice between the various alternatives or express any preference for one over another but merely provide future diplomatic conferences with a variety of means to deal with the issues. His delegation felt that the Working Group's proposals fulfilled that task very well and should be adopted.

6. Mr. LARSEN (United States of America) said he agreed with the Working Group's view that a remedy was needed for the erosion of liability limits by inflation. The issue, however, was one of uniformity of law. The destruction of such uniformity was illustrated by the Warsaw Convention, whose liability limits had been unconscionably eroded by inflation, with the result that several diplomatic conferences had had to be convened to take account of the situation and to raise those limits. If the Montreal Protocols to the Warsaw Convention were adopted by States, a balance would be re-established but there would always be the inconvenience of having to maintain such a balance. Since uniformity was most important in that type of Convention, a solution to inflation erosion should be found which would be acceptable to all States.

7. Adoption of the indexation approach would not, in his delegation's view, establish the required uniformity of law. Several countries, including the United States, had been opposed to the indexation of liability limits in transportation conventions because indexation contributed to inflation and distorted commodity factor prices. His delegation had also pointed out the administrative difficulties of defining and maintaining separate price indexes for each of the liability conventions geared to the subject matter of each convention. His delegation therefore favoured the amendment procedure for adjusting liability limits. The method of adjustment by a review committee seemed to be acceptable to all States, even those which favoured indexation. That system was what the Working Group had adopted in the sample procedure for adjusting liability limits. The use of that system would result in the necessary uniformity of law in the setting of liability limits which was the main objective of private international law conventions.

8. Mr. SCHMID (Federal Republic of Germany) said he fully agreed with the representative of the United States that the indexation approach was not the best solution to the problem at hand. As his delegation had pointed out in Vienna, an indexation approach would contribute to inflation. His objection was based on the direct link between the increase in inflation that had already occurred in certain areas and the consequent increase in cost that he felt would occur in other areas as a result of the use of indexation. It was also very difficult to find an appropriate index to use for a specific convention; hence his delegation's proposal in the Working Group to solve the problem of adjusting the amounts of liability in international conventions by periodic revision of the amounts in question. For that purpose, the Working Group had elaborated a sample clause for an expedited revision process for the limited purpose of rewriting the limit of liability in a specific convention. His delegation supported the second alternative of the Working Group as set forth in paragraph 90 of document A/CN.9/215.

9. Mr. HARTKAMP (Observer for the Netherlands) said that his delegation found the Working Group's offer of alternatives very wise and that both should be recommended to future diplomatic conferences. Contracting States might, as suggested by the Working Group, either accept amendments or denounce the particular convention.

10. Mr. DUCHEK (Austria) said that his delegation also felt it wise that no preference should be expressed for either alternative. It would be up to conferences and international organizations to choose which approach they wanted to adopt. His delegation was also in favour of the clause on automatic adjustment by indexation. The question as to whether indexation rather than another form of adjustment should be applied, the composition of the basket on the basis of which the index was to be calculated and the body to be entrusted with preparing the index could all be decided at future conferences.

11. Mr. SEVON (Finland) said that there did exist currently, and would exist in future, conventions or bilateral agreements containing liability provisions to which the opponents of the inclusion of an indexation clause would not and could not be parties. In a spirit of co-operation, he would request those delegations not to prevent the recommendation of an indexation clause even if they would object to such a clause in the convention to which they became party. The idea was to provide the international community with different devices any of which might be used as deemed appropriate. It would be regrettable if the indexation clause were excluded from the Commission's recommendation.

12. Mr. MAGNUSSON (Observer for Sweden) said that both alternatives submitted by the Working Group could be useful. In most cases, perhaps, the specific amendment procedure would be the best course of action, but the option of adopting an indexation provision should also be left open. His delegation therefore supported the conclusions reached by the Working Group.

13. Mr. ROEHRICH (France) said that it was desirable that both alternatives should be available for consideration at future diplomatic conferences and that at such conferences the attention of States should be drawn to the possibility of adopting the automatic indexation alternative. That alternative might be useful in the future, particularly if the economic situation changed.

14. He supported the view expressed by the observer for the Netherlands with regard to the importance of paragraph 5 of the sample amendment procedure for limit of liability

recommended by the Working Group in paragraph 90 of its report.

15. Mr. FERRARI BRAVO (Italy) said that the results produced by the Working Group were entirely acceptable. Both alternatives put forward by the Working Group should be recommended for consideration at future diplomatic conferences. Although it was likely that the price index provision recommended by the Working Group would be used only rarely, it could nonetheless be useful.

16. Mrs. DAYER (United Kingdom) said that her Government had considerable reservations with regard to the inclusion of an automatic indexation provision in an international convention, both owing to the fact that it might increase inflation and because there were factors other than inflation that might call for the amendment of limits of liability. Her country would have to consider any convention containing such a provision with great care. However, consideration should be given in the case of each individual convention to what was most appropriate. Her delegation therefore supported the proposal that the Commission should put forward alternative procedures for use in international conventions.

17. Mr. SAWADA (Japan) said that his delegation shared the views expressed by the representatives of the Federal Republic of Germany and the United States. It also supported the view expressed by the representative of Finland with regard to the provision of alternatives. It considered the current wording of paragraph 5 of the sample amendment procedure for limit of liability put forward by the Working Group acceptable. It also felt that States should exercise extreme care in adopting any index.

18. Mr. CHAFIK (Egypt) said that his delegation believed that periodic revision of limit of liability provisions in conventions was a more practical procedure than indexation, although it did not object to indexation. It had no objection to the two alternatives in question being recommended to diplomatic conferences, since they could both be useful.

19. Mr. RAO (India) said that his delegation would support any consensus proposal with regard to the choice of a price index.

20. Mr. OLIVENCIA (Spain) said that the Commission should retain the Working Group's approach, which was based on the principle of providing two alternatives. It would be for future diplomatic conferences to choose one of those two alternatives.

21. Mr. BERGSTEN (secretariat), replying to the question as to how the Commission's views would be presented, said that, once the Commission had adopted the two texts before it, they would be included in its report for submission to the General Assembly. They would be drafted specifically as texts for use at future diplomatic conferences. In its report, the Commission would recommend that one of the two texts should be used at such future conferences. The General Assembly would therefore not need to adopt those texts. However, in its resolution on the Commission's report, it would undoubtedly make a recommendation itself that one of the two texts should be used at future diplomatic conferences.

22. Mr. LARSEN (United States of America) said that the Commission was primarily concerned with conventions that were already in effect and were also already widely accepted. Such conventions called for constant adjustment. It was important to draw attention to the fact that there was a consensus that that problem needed to be solved. He wished

to know whether the Commission could go further than making recommendations, not only in respect of future conventions, but also in respect of existing conventions.

23. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics), referring to the statements made in the Commission with regard to his country's agreement to the use of SDRs as units of account, said that use of such rights as units of account should not be regarded as the only possible solution that could be recommended.

24. The wording of the two alternatives set forth in paragraphs 53 and 90 of the report of the Working Group gave rise to certain questions. In paragraph 53 it was not clear who would adjust the amounts in question. Paragraph 3 of the sample price index provision put forward in paragraph 53 appeared to indicate that such adjustments were to be made by the depositary. He wondered whether that was what the drafters of that text had had in mind. Moreover, paragraph 5 of the sample amendment procedure for limit of liability put forward in paragraph 90 of the report might not be acceptable to sovereign States. His delegation therefore believed that that matter required further study.

25. Mr. WAGNER (German Democratic Republic) said that the competent authorities of his country were currently considering whether it would be possible for the German Democratic Republic to rely on the SDR as a unit of account in provisions relating to limit of liability in international conventions. His delegation was therefore not yet in a position to express a final view on that question. The method to be chosen for adopting limits of liability in transport conventions was of fundamental importance. His delegation was in favour of a system of automatic revision with intervals that were not too short.

26. With regard to recommendations to diplomatic conferences, his delegation supported the suggestion put forward by the Working Group that a choice between alternative methods should be offered.

27. The CHAIRMAN observed that there seemed to be a consensus on the need to find a solution to the problems caused by the effects of inflation and currency fluctuations on limits of liability in international conventions. A substantial majority of members of the Commission appeared to agree to the adoption of an automatic index provision, although the delegations of the Federal Republic of Germany, Japan and the United States, among others, were opposed to such a provision. If the Commission adopted the proposals contained in the Working Group's report, that would offer future diplomatic conferences the option of adopting an index provision or providing for the regular revision of limit of liability provisions. States participating in such diplomatic conferences would of course be entirely free to decide whether or not to avail themselves of either option.

28. Mr. LARSEN (United States of America) asked whether that meant that there was also general agreement on the recommendation to use SDRs as a universal unit of account.

29. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics) observed that the Commission was still at the stage of a general discussion of the Working Group's report and had yet to arrive at a specific formulation for the various proposals contained therein. In particular, a decision had yet to be taken on paragraphs 95 and 96 of the report.

30. Mr. SONO (Secretary of the Commission) said that it was his understanding that the Commission had considered the two alternative approaches proposed by the Working

Group but had not embarked on consideration of the question of establishing a universal unit of account for international conventions. Thus, the consensus that had emerged referred only to the two alternative approaches, and the matter of a universal unit of account would have to be considered subsequently.

31. Mr. SEVON (Finland) endorsed the Secretary's interpretation that the question of a unit of account had yet to be considered in depth. When the Commission came to deal with that particular point it might also consider the point raised by the United States, namely the action to be taken with regard to existing conventions. There was indeed general agreement on the two alternative approaches proposed by the Working Group, but a decision must also be taken as to whom to contact in the event of a decision to apply either approach.

32. Mr. SAWADA (Japan) said that, while his delegation believed that indexation would be very difficult to implement, it had not actually opposed the formulation of the two alternative approaches.

33. The CHAIRMAN said that, if he heard no objections, he would take it that the Committee approved the first part of the Working Group's report and decided to leave pending its consideration of the question of a universal unit of account and the procedure to be followed with regard to existing conventions.

34. *It was so decided.*

The meeting was suspended at 11.55 a.m. and resumed at 12.30 p.m.

35. The CHAIRMAN invited the Committee to take a decision on the text of the sample price index provision contained in paragraph 53 of document A/CN.9/215 and the amendment thereto proposed in paragraph 4 of document A/CN.9/220.

36. Mr. SEVON (Finland) observed that, when the sample price index provision came to be included in a future convention, the corresponding conference of plenipotentiaries would have to be told that it must consider not only the question of what index to use but also who should provide such an index and how, and how to notify States of any changes. A note suggesting the step which any future conference should take in that regard might be attached to the text of the provision, as a recommendation to those who were considering the adoption of such a provision.

37. Mrs. DAYER (United Kingdom) proposed that paragraph 2 of the text of the sample provision contained in paragraph 53 should be amended to make it easier to understand. The words "ratio of" in the second line should be deleted and the word "ratio" in the fourth line should be amended to read "change".

38. *It was so decided.*

39. The CHAIRMAN said that, if he heard no objections, he would take it that the Commission approved the remainder of the text of the sample price index provision as contained in paragraph 53, as amended by paragraph 4 of document A/CN.9/220, without prejudice to any later decision to attach thereto recommendations based on the proposals made by the representative of Finland.

40. *It was so decided.*

41. The CHAIRMAN said that, if he heard no objections, he would take it that the Commission decided to adopt the

text of the sample amendment procedure for limit of liability contained in paragraph 90 of document A/CN.9/215, as amended by paragraph 6 of document A/CN.9/220.

42. *It was so decided.*

43. The CHAIRMAN invited the Commission to consider the suggestions made by the Working Group in paragraphs 91-97 of document A/CN.9/215 with regard to the question of a universal unit of account for liability conventions and, in particular, the amendments proposed to paragraphs 95-97.

44. Mr. SONO (Secretary of the Commission) said that, in the light of the statements made at that meeting by the representatives of the German Democratic Republic and the Union of Soviet Socialist Republics and since many other States not members of IMF were considering their position on the matter, he felt that it would be too ambitious for the Commission to concentrate on the SDR as the sole unit of account. He therefore felt that the Commission might wish to consider the SDR as a preferred unit of account for international conventions of universal impact. If that was acceptable, the Commission could consider the approaches contained in paragraphs 95 and 96 of the report of the Working Group and, if one of them was acceptable, paragraph 4 of the Hamburg Rules could be drafted. He stressed, however, that the preparation of a formula based on the Hamburg Rules would be carried out on the understanding that the Commission was not preparing the text as the sole solution.

45. Mr. SEVON (Finland) suggested that the Commission should take account of all three possibilities by recommending a formula to be used if a conference of plenipotentiaries wished to use the SDR as the unit of account, by stating that, if a conference wished to use the SDR together with a monetary unit, it could use the existing formula in the Hamburg Rules, and, finally, by drawing attention to the issues to be considered if a diplomatic conference wished to use some other unit of account. There was no need to express any preference since that was a matter to be decided by the diplomatic conference itself.

46. Mr. LARSEN (United States of America) reiterated his delegation's support for a single system of calculating liability limits. He supported an approach along the lines of that suggested by the Soviet Union in the Working Group and felt that it should state the national currencies in the same real values as expressed in the SDRs in the conventions, and that States should communicate to the depositary the manner of calculation at the time of signature and whenever there was a change in their method of calculation. His delegation could accept any language changes required to reflect more accurately how IMF calculated the SDR and supported the suggestions made by the observer for IMF in the Working Group.

47. Mr. SCHMID (Federal Republic of Germany) supported the representative of the United States. He was gratified that the Union of Soviet Socialist Republics was prepared to accept the SDR as the sole unit of account, but realized that it was not in a position to speak for other countries not members of IMF. The Commission should therefore consider two formulas, the first for cases where the SDR was to be used as the sole unit of account and the second for cases where another unit of account was to be used, when article 26 of the Hamburg Rules as it stood should apply. There was no need to cater for a third alternative, as suggested by the representative of Finland.

The meeting rose at 1 p.m.

255th meeting

Tuesday, 27 July 1982, at 3 p.m.
Chairman: Mr. EYZAGUIRRE (Chile)

[A/CN.9/SR.255]

The discussion covered in the summary record began at 3.15 p.m.

INTERNATIONAL PAYMENTS (continued)

(b) Universal unit of account (continued) (A/CN.9/215, A/CN.9/220)

1. The CHAIRMAN said that the Commission had to choose one of the formulations proposed in document A/CN.9/215, paragraph 95 and 96, concerning the value of the SDR.

2. Mr. SCHMID (Federal Republic of Germany) said that his delegation would prefer the SDR to be the only unit of account to be used in future conventions. He did not believe that there was any substantial difference between the formulations proposed in paragraphs 95 and 96, but he would appreciate an explanation from the representative of the IMF as to why paragraph 96 had been worded as it had.

3. Mr. LAVINA (Philippines) said he agreed with the representative of the Federal Republic of Germany that the SDR should be the preferred unit of account. His delegation favoured the formulation contained in paragraph 95, which was simpler while adequately expressing the ideas set out in paragraph 96.

4. Mr. LARSEN (United States of America) said that his delegation could accept the phrasing proposed by the IMF in paragraph 96. It would, however, prefer "equivalence" to be used instead of "relationship", and would like to retain the essence of article 26, paragraph 4, of the Hamburg Rules, as was suggested in paragraph 97.

5. Mr. EFFROS (Observer for the International Monetary Fund) said that certain questions had been raised at the meeting of the Working Group concerning the formulation contained in paragraph 95. The second sentence of that formulation referred to the value of the SDR in terms of the national currency. The Hamburg Rules, however, referred to the value of a national currency in terms of the SDR. Paragraph 96, which referred to an equivalence or relationship between the national currency and the SDR, had been proposed in order to eliminate that contradiction and to avoid the controversy which certain provisions of the original formulation had apparently caused in respect of the domestic legislation of some countries.

6. Mr. HARTKAMP (Observer for the Netherlands) said that his delegation favoured the language contained in paragraph 96 and had no strong preference with regard to "relationship" or "equivalence", although it slightly preferred the latter.

7. Mr. MAGNUSSON (Observer for Sweden) said that his delegation endorsed the views expressed by the observer for the Netherlands.

8. Mr. DUCHEK (Austria) said that his delegation preferred the formulation contained in paragraph 96 because it corresponded to the situation of the IMF and brought out the relationship between the SDR and national currency

better than did paragraph 95. Moreover, paragraph 95 drew an illogical distinction between calculations in respect of States which were members of the IMF and calculations in respect of States which were not, whereas paragraph 96 met the requirements of both members and non-members of that Fund. His delegation preferred "equivalence" to "relationship".

9. Mr. VOLLZEN (Observer for Switzerland) said that his delegation preferred the formulation contained in paragraph 96. With regard to the choice between "equivalence" or "relationship", "equivalence" should be used throughout, except in the final sentence, where "relationship" should be retained to express the distinction between the SDR and the national currency of a country which was not already a member of the IMF.

10. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics) said that his delegation preferred paragraph 96 and thought that "equivalence" should be used throughout the text, including the last sentence.

11. Mr. BYERS (Australia) said that "equivalence" should be retained throughout the text. If in the last sentence a distinction was drawn by using "relationship" instead of "equivalence", it could give rise both to confusion and to difficulties of construction.

12. The CHAIRMAN said that, if he heard no objection, he would take it that the Commission wished to adopt the formulation contained in paragraph 96, using "equivalence" throughout.

13. *It was so decided.*

14. Mr. BERGSTEN (secretariat) said that since the formulation contained in paragraph 96 had been adopted, it would be necessary to prepare a paragraph to follow it. The Commission could entrust the secretariat with the preparation of a draft and could discuss and adopt the draft later in the session. As to the way in which the Commission should adopt such texts, he referred delegations to document A/CN.9/220, paragraph 11.

15. Mr. LARSEN (United States of America) said that the principle set forth in document A/CN.9/215, paragraph 97, and repeated in document A/CN.9/220, paragraph 10, was important and must be retained in the new formulation. The secretariat's draft must also include elements of article 26, paragraph 4, of the Hamburg Rules.

16. Mr. BYERS (Australia) said that his delegation endorsed the recommendations contained in document A/CN.9/220, paragraph 11.

17. Mr. SCHMID (Federal Republic of Germany) said that his delegation agreed with the representative of the United States that it was important to include a paragraph similar to article 26, paragraph 4, of the Hamburg Rules and that the secretariat should prepare a draft of such a paragraph.

18. Mr. RAO (India) observed that document A/CN.9/220, paragraph 11, referred to one of the two alternative provisions for adjusting the limit of liability; that should be taken into consideration.

19. The CHAIRMAN said that if he heard no objection, he would take it that the Commission wished to request the secretariat to draft a paragraph similar to article 26, paragraph 4, of the Hamburg Rules for the Commission's consideration and that it wished to make a recommendation to the General Assembly along the lines set out in document A/CN.9/220, paragraph 11.

20. *It was so decided.*

21. Mr. BERGSTEN (secretariat), replying to a question from Mr. LARSEN (United States) said that the Commission had decided to recommend two approaches—sample price indexing and a revision conference—for use in international conventions in the future. With certain modifications, texts on those subjects had already been adopted.

22. With regard to the establishment of a universal unit of account, the Commission had agreed to recommend the SDR as the preferred unit of account and had just adopted a formulation for use in international conventions in which the SDR was the preferred unit of account.

23. Mr. LARSEN (United States of America) recalled that at the preceding meeting the representative of Finland had raised the issue of how best to proceed with a recommendation on inflation erosion of the universal unit of account. Since that was an important issue, he hoped that the Commission would return to it; his delegation might have some suggestions to make in that regard.

24. Mr. SEVON (Finland), replying to a question from the CHAIRMAN, said that his delegation's statement had concerned the means of communicating the recommendation and had not been a proposal. He therefore suggested that the Commission should revert to that question when a text was available for discussion.

25. The discussion of agenda item 5 (b) ended at 3.55 p.m.

26. The CHAIRMAN invited the Commission to discuss agenda item 5 (c), which would not be covered in the summary record.

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256th meeting

Wednesday, 28 July 1982, at 10 a.m.
Chairman: Mr. EYZAGUIRRE (Chile)

[A/CN.9/SR.256]

The meeting was called to order at 10.10 a.m.

INTERNATIONAL PAYMENTS (continued)

(b) Universal unit of account (continued) (A/CN.9/XV/CRP.2)

1. The CHAIRMAN drew attention to document A/CN.9/XV/CRP.2 containing the draft provision on a universal unit of

account. It consisted of two paragraphs, the first of which had been approved by the Commission at its 255th meeting and the second of which had been drafted by the secretariat, following a request made by the Commission at the same meeting. If he heard no objection, he would take it that the Commission wished to approve that second paragraph.

2. *It was so decided.*

...

B. Draft Uniform Rules on Liquidated Damages and Penalty Clauses

1. Summary records of the 255th to 261st meetings, fifteenth session (New York, 26 July-6 August 1982) (A/CN.9/SR.255-261)

255th meeting

Tuesday, 27 July 1982, at 3 p.m.
Chairman: Mr. EYZAGUIRRE (Chile)

[A/CN.9/SR.255]

...

27. *The discussion covered in the summary record resumed at 5.55 p.m.*

¹The summary records contained in this volume include the corrections to the provisional summary records that were requested by the delegations and such editorial changes as were considered necessary.

INTERNATIONAL CONTRACT PRACTICES: DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES AND PENALTY CLAUSES (A/CN.9/218,² A/CN.9/219 and Add.1³)

28. Mr. BASNAYAKE (secretariat), introducing the item, recalled that the question had been taken up by the

²Yearbook ... 1982, part two, I, A.

³Yearbook ... 1982, part two, I, B.

Commission at its twelfth session.¹ The Commission had decided that work should be undertaken with a view to the formulation of uniform rules on damages and penalties applying to contracts and had entrusted that task to the Working Group on International Contract Practices. The Working Group had held two sessions of one week each, the first in 1979 and the second in 1981. At its second session, the Working Group had finalized the text of the rules currently before the Commission. The Working Group had formulated articles D, E, F and G in documents A/CN.9/218 and part of article A.

29. At its fourteenth session,² the Commission had considered the report of the Working Group and had asked the secretariat to complete the text of the rules with such provisions as might be required if the rules were to take the form of a convention or a model law. It had sent a questionnaire to States and international organizations eliciting their views and suggestions and had asked States to submit comments on the rules.

30. All that had been done, and the results were contained in document A/CN.9/218. The questionnaire contained summaries of the arguments for and against the possible forms which the rules might take and an analysis of the responses of Governments was contained in documents A/CN.9/219 and Add.1.

31. The questions of form and substance were interconnected. The secretariat felt that the best course would be to consider the form first, because it had a significant bearing on how the substance of the article should be considered. For example, if it was decided that there should be no convention, the relevant drafts need not be considered.

32. The Commission currently had before it all the necessary material for a decision on the form which the rules should take.

The meeting rose at 6 p.m.

256th meeting

Wednesday, July 1982, at 10 a.m.

Chairman: Mr. EYZAGUIRRE (Chile)

[A/CN.9/SR.256]

INTERNATIONAL CONTRACT PRACTICES: DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES AND PENALTY CLAUSES (*continued*) (A/CN.9/218, A/CN.9/219 and Add.1)

3. The CHAIRMAN invited members of the Commission to express their views on the form which the draft uniform rules on liquidated damages and penalty clauses should take.

4. Mr. BASNAYAKE (secretariat) said that a questionnaire on the subject had been addressed to Governments and international organizations requesting their views on the draft rules and on the most appropriate form they should take. An analysis of the responses received was contained in documents A/CN.9/219 and A/CN.9/219/Add.1. Of the 18 replies, 7 favoured the form of a convention, 5 supported a model law, and 6 had expressed a preference for general conditions.

5. Mr. ROEHRICH (France) said that his Government favoured a convention but would accept general conditions if the majority preferred such a form. It felt that a model law would not be effective.

6. Ms. VILUS (Yugoslavia) said that her delegation favoured a model law. If the majority preferred a convention, it should be adopted by the General Assembly on the recommendation of the Sixth Committee. As the subject

formed part of a larger area, a model law would be the ideal way of promoting unification.

7. Mr. SEVON (Finland) supported the comments made by the representative of Yugoslavia. A model law would enable Governments to adapt the rules to their national legislation. For example, his delegation had difficulties with article G as it currently stood. His delegation had strong reservations concerning general conditions and also felt that the prospects of concluding a convention in such a limited area were not very good. It would be unfortunate if UNCITRAL was to submit a draft convention which then did not enter into force.

8. Mr. PHAI CHENG (Singapore) said that his delegation preferred the form of a model law. A convention would cover only a limited subject and, in many countries, liquidated damages were applicable to a wide range of activities. It might not be possible for Governments to sign such a convention. Furthermore, the cost of concluding a convention was high.

9. Mr. SZASZ (Hungary) said that his delegation favoured a model law. The subject formed part of a broader area and it would be difficult to conclude a convention on it. In his opinion, such a convention would not be ratified by a sufficient number of States. He pointed to three reasons why the form of general conditions was impractical: first, it could conflict with the mandatory provisions of national legislation; secondly, he doubted whether the parties would be prepared to formulate general conditions on the basis of several documents; and, thirdly, the whole structure of the draft rules was inappropriate for the form of general conditions.

10. Mr. WAGNER (German Democratic Republic) felt that the form of a convention was the most appropriate one, being the most effective way of unifying law on the subject. It would provide an element of certainty in the unification of the legal provisions of various countries. Drawing attention to draft article C, he said that it would not conflict with national legislation governing consumer protection since it would affect only international contracts. He did, however, agree that there might be problems in convening a diplomatic

¹Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), paras. 32-40 (Yearbook ... 1979, part one, II, A).

²Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17* (A/36/17), paras. 23-32 (Yearbook ... 1981, part one, A).

conference on the subject. However, it would be possible to agree on a draft and request the General Assembly, through the Sixth Committee, to open a convention for signature. It might also be possible to seek one or a number of other issues and convene a diplomatic conference for the conclusion of several conventions.

11. If there was no majority in favour of a convention, his delegation could accept the form of a model law since that would have a certain unifying effect and would enable countries to incorporate the rules into their national legislations in accordance with normal legislative practice.

12. Mr. SAWADA (Japan) drew attention to the views of his Government as expressed in document A/CN.9/219. His delegation could not accept the form of general conditions since it would conflict with the mandatory provisions of national law. A convention could help to unify principles of common and civil law but it would be an expensive procedure—he had been informed that the cost would be around \$1 million—and it was not desirable to conclude a convention on a matter of such limited scope.

13. Mr. SONO (Secretary of the Commission) pointed out that the figure of \$1 million quoted by the representative of Japan was approximate and unofficial. The secretariat had not yet submitted any firm figure, since no decision had been taken on the matter. In any event, it was quite possible that most of the cost of a conference could be absorbed within available resources, depending on where and when the conference was held and how long it lasted.

14. Mr. CHAFIK (Egypt) said that his delegation favoured the form of a model law, which would be a useful one for developing countries. Given that conventions on a number of important matters had not yet been ratified, he felt that a convention on the subject before the Commission would have great difficulty in entering into force.

15. Mr. GUEST (United Kingdom) said that inquiries made in commercial circles in his country had revealed very little interest in the subject as far as the unification and harmonization of principles were concerned. Most of the comments that had been made were unfavourable. A convention was unlikely to attract sufficient support for it to enter into force. The subject matter was limited and the cost would be disproportionate to its value. Nor did he favour the adoption of a convention by the General Assembly on the recommendation of the Sixth Committee. Endorsing the objections to general conditions set forth by the representative of Hungary, he said that his delegation supported the form of a model law.

16. Mr. MAGNUSSON (Observer for Sweden) said that his delegation could not support the adoption of the rules in the form of an international convention, since it felt that the need for such a convention was limited, doubted whether it would attract wide support and was concerned about the cost and the length of the procedure involved. In its reply to the questionnaire, his Government had expressed its preference for the form of general conditions, which could be of value to parties drawing up contracts. Of course, there was some doubt as to the importance which would be attached to such general conditions and, in that respect, he agreed with the remarks made by, amongst others, the representative of Hungary. He emphasized that, if the form of general conditions was adopted, it would be necessary to omit or change certain articles. His delegation could also accept the idea of a model law but, in that case too, it would be

necessary to change some articles, especially articles F and G, amendments to which had been submitted by his Government in its reply to the questionnaire.

17. Mr. DUCHEK (Austria) said that his delegation would have liked to support the idea of the convention since it felt it would be the most effective form for unification. It did, however, realize that that idea lacked support and, therefore, favoured instead the form of a model law. He supported the arguments advanced against the idea of general conditions. It was unrealistic to assume that parties to a contract would be aware of such conditions and, even if they were, they would embody them in the contract.

18. Mr. AKINLEYE (Nigeria) supported the form of a model law. Many conventions did not attract sufficient support and, apart from the expense involved, there could be a conflict between the convention and domestic law. The form of a model law would give States sufficient leeway to make amendments appropriate to local conditions.

19. Mr. LAVINA (Philippines) supported the idea of an international convention since that would be binding and would be the surest way of promoting uniformity. A model law could not solve the problem of harmonizing different national rules. The same doubts about and arguments against concluding a convention had been put forward with respect to the United Nations Convention on the Carriage of Goods by Sea.^k However, expense was inevitable in the work of UNCITRAL and the limited scope of a convention on the subject was not a significant factor in view of its over-all importance.

20. Mr. LARSEN (United States of America) said that his delegation favoured the form of a model law.

21. Mr. AKDAG (Observer for Turkey) said that his delegation favoured the form of general conditions for reasons contained in document A/CN.9/219.

22. Mr. FERRARI-BRAVO (Italy) said that in general he shared the doubts expressed by the representative of Hungary and the practical arguments of the representative of Austria against the form of general conditions. There was a real danger that, if that form was adopted, the rules would be generally forgotten or ignored. A convention would certainly help the unification of law. However, apart from the financial implications, which, in his view, were not significant, he was concerned about the lack of support which such a convention might attract. Furthermore, it might establish a rigid system which would have an adverse effect on the future work of the Commission in the field of contractual liability, if, for example, it wished, at a later date, to conclude a more wide-ranging convention in the same area. Therefore, in spite of certain reservations, his delegation favoured the form of a model law as a first step towards the further development in the field. After a few years, the Commission might make inquiries to discover how many States had in fact incorporated the model law into their national legislation.

23. If the Commission chose to recommend adoption of a model law, it would also be necessary to recommend that States should not depart too far from the UNCITRAL text. That concern applied in particular to article A of the draft uniform rules with regard to problems arising from conflicts of law and when the rules of private international law led to the application of the law of the State adopting the model law (A/CN.9/218, p. 5, para. (1) (b)).

^kYearbook ... 1978, part three, I, B (A/CONF.89/13, annex I).

24. Mr. SCHMID (Federal Republic of Germany) said that his delegation might reconsider its position in favour of general conditions. It had been opposed to a convention because, in their current form, the draft UNCITRAL rules were in conflict with his country's mandatory rules protecting weaker parties to special contracts. His delegation had particular reservations with regard to article G and article A, paragraph 3, of the draft UNCITRAL rules and also with regard to article C of those rules, which did not go far enough. The model law solution would give rise to similar difficulties.

25. With regard to the option of recommending general conditions, a number of the draft UNCITRAL rules were superfluous in their current form, particularly those in conflict with mandatory national provisions, as in the case of article G.

26. If the draft UNCITRAL rules were amended substantially, his delegation might be in a position to accept them as a model law. It would be best if the rules only applied to international commercial contracts, even though it was difficult to define what a commercial contract was.

27. Mr. OLIVENCIA (Spain) said that his Government was in favour of the model law option, which appeared to be gaining the most support in the Commission.

28. It would not be wise to opt for a convention, since there was no longer wide acceptance of conventions. Moreover, the question of liquidated damages and penalty clauses was a topic that had only a limited scope and was of a somewhat accessory nature. Although the model law also had a limited scope, it could gain wider acceptance in practice.

29. His delegation supported the objections expressed in the Commission with regard to general conditions, particularly by the representative of Hungary. Although no possible solution should be excluded from the outset, the model law option must undoubtedly be regarded as being incompatible with the convention option, whereas it did not appear to be incompatible with general conditions, which could be regarded as being complementary to it. The Commission could therefore draft both a model law and general conditions. It could adopt a dual approach and make recommendations to legislators, on the one hand, and to individuals who were parties to international transactions, on the other hand.

30. Mr. PARK (Observer for the Republic of Korea) said that his delegation was in favour of adopting a model law approach for the reasons stated by the representative of Japan and other speakers.

31. Mr. YEPEZ (Observer for Venezuela) said that his delegation was in favour of drafting general conditions. A convention would not be appropriate, since the topic in question had a limited scope and was of a subsidiary nature, and a model law would represent no more than a recommendation to States. The drafting of general conditions would be advantageous because it would be possible to amend the conditions at a later stage. The suggestion put forward by the representative of Spain that it might be possible to recommend both a model law and general conditions might be an alternative that the Commission could consider.

32. Mr. VOLLZEN (Observer for Switzerland) said that his delegation was in favour of a model law and supported the objections raised by the representative of Hungary with regard to general conditions. A convention would present difficulties of a practical nature, particularly since there might

be too many conventions in the field in question. States wishing to revise their domestic legislation, or draft domestic legislation, could take the UNCITRAL model law as a basis.

The meeting was suspended at 11.25 a.m. and resumed at 12.05 p.m.

33. Mr. JEWETT (Canada) said that Canada, like the Federal Republic of Germany, had indicated a preference for the alternative of general conditions. Among the reasons which had drawn Canada to that alternative were a desire to preserve the principle of freedom of contract and a wish to avoid a solution the implementation of which would be likely to require significant changes in the national legislation of States. However, Canada was by no means unalterably opposed to a model law; indeed in that regard, his delegation simply wished to associate itself with the cogent remarks of the representative of Italy. Finally, Canada did not for the time being favour a convention and concurred with the views expressed in that regard by the representative of Venezuela. However, should a convention be the ultimate wish of the Commission, he would only say that, for many of the reasons which had led Canada to state a preference for general conditions, his delegation would prefer the inclusion of a rule requiring specific invocation by contracting parties.

34. Mr. MING-CHENG (China) said that, by working out the draft text on uniform rules on liquidated damages and penalty clauses,¹ the Commission would help ensure the fulfilment of contract, safeguard the legitimate rights of contracting parties and thereby facilitate the development of international trade. As to the form of the uniform rules, China was not in favour of a convention. The adoption, signing and entry into force of a convention would require an inordinately long period of time, as had been borne out by the Commission's experience. The text of the draft rules contained few clauses and was thereby ill-suited to the format of a convention. The adoption of a model law (with the consequent changes it would require to bring national legislation in line with it) would provoke conflict among different legal systems. On the other hand, the model rules or clauses in the set of general conditions ultimately adopted by the Commission could be directly recommended to contracting parties and could then serve as a basis for drafting contracts. Such model rules or clauses in a set of general conditions would lend themselves more readily to recognition by various national legislatures. Of the three alternatives, his delegation was in favour of the model rules or model clauses. However, should the majority of delegations prefer the model law approach, China was ready to go along.

35. Mr. MATHANJUKI (Kenya) said that his delegation was worried at the turn the discussion was taking. The Commission's work on liquidated damages and penalty clauses had all been aimed at unifying existing provisions contained in the laws of different countries. The question was therefore how the Commission could effectively harmonize such laws. Three ways had been suggested. One of them, a set of general conditions, would be forgotten as soon as the conditions were formulated. Another way, that of drafting a model law, would leave countries free to align their laws with the model or parts thereof. They could even choose to ignore the model law altogether. The third alternative, the convention, became the obvious choice because it would be binding on States and compel them to bring their legislation into line with it. His delegation was not unmindful of the fact that a convention must necessarily be rigid and supersede State laws, thereby infringing the principle of freedom of contract.

¹Reproduced in this volume, part three, II, A.

However, the whole purpose of the Commission's exercise was for States to bring their laws into line with the convention and thereby achieve the unification desired. Therefore, the argument that a convention would force States to conform against their will did not hold water. Obviously, States could continue the practice of not acceding to conventions to which they objected. Intractable as that problem might be, it should not prevent the Commission from thinking out effective ways of persuading States to accept such a convention. He found the opponents of the convention approach somewhat defeatist in their attitude. While Kenya would very much prefer to see a convention elaborated, it would not stand in the way should the preponderance of opinion in support of a model law prevail. Acceptance of such a consensus would, however, be subject to the reservations his delegation had expressed.

36. Mr. HARTKAMP (Observer for the Netherlands) favoured a convention as being most likely to help unify private law. He remained unconvinced by the practical argument put forward against the convention approach and shared the view of the representative of Kenya. It had been argued that a convention would not work. By the same token, he failed to see why a model law should. If a State, on account of variance with its national law, balked at adopting a convention, it would be even more unwilling to adopt a model law. His delegation therefore stuck to its original preference and favoured the idea of a convention.

37. Mr. JOKO-SMART (Sierra Leone) endorsed the views expressed by the representative of Kenya. Despite the shortcomings of conventions, they remained the best means of achieving uniformity and universal application. The model law approach would not have that universal character and only a handful of nations with vested interest would adopt them and incorporate them into their legal systems.

38. Mr. ROEHRICH (France) said that the proponents of a model law seemed to be in the majority. However, some of them had admitted that they were not fully enthusiastic about their position. As the representative of Kenya had stated, the difficulties arising from the adoption of a convention would be multiplied in the event of the adoption of a model law. Since the model law would not be binding, no country would have any obligation to comply with any provision to which it objected. The model law would have no unifying value. The arguments put forward in favour of and against a convention had no more scope than those put forward in favour of and against a model law. The most serious argument had been that advanced against general conditions, which his delegation had initially supported because they had the advantage of not directly committing States. They also recommended themselves to the users in international trade in that they were immediately applicable considering the universal character of UNCITRAL and its arbitration rules.¹⁷ The only snag he foresaw was the possibility of conflict with State policy. He felt the need for a list of all national provisions that might clash with the draft rules on general conditions. The most serious problem was in article G relating to the competence of the arbitration tribunal to rule on matters of damages or incomplete performance. That aspect would need further study. The Commission should make the effort to see if a convention were feasible, since it was the only way to achieve uniformity in law. A model law would contribute in no way to that end. There was no arbitration legislation in international trade and States were only beginning to realize the need for such legislation. The situation presented a perfect opportunity for model law because the penalty clauses of major legal systems were at variance and the Commission

might be tempted to draft a model law as an easy way out. Such a move would be futile. While it might absolve the Commission's conscience, it would also undermine the Commission's prestige.

39. Mr. GABAY (Observer for Israel) said that he sympathized with the position of the representative of Kenya that an international convention would be a most effective means of resolving the problem of uniform rules on liquidated damages and penalty clauses. As long as there were numerous international trade conventions to which only a few States had adhered, however, the Commission should not embark on the drafting of a new convention but should instead consider other possibilities. His delegation favoured the idea of drafting a model law but believed that that need not preclude the possibility of also drafting general conditions. All delegations were aware that a model law would be addressed to States and that it might be years before the law's provisions were incorporated into States' national legislation, while general conditions would be of immediate assistance to the parties to international contracts. The Commission should therefore work on both a model law and general conditions.

40. Mr. LEBEDEV (Union of Soviet Socialist Republics) observed that the Commission was discussing the question of uniform rules in detail for the first time. That morning's debate had shown the importance of the question and, from the views expressed, it was clear that the Commission must not take a hasty decision based purely on the number of delegations in favour of or opposed to a given approach. The ultimate effectiveness of the Commission's work would depend on which approach it adopted.

41. The Soviet position on the question of uniform rules was to be found in document A/CN.9/219. His delegation was in favour of a convention which could be adopted through the procedures of the Sixth Committee as other international conventions had been in the past. Clearly, account must be taken of the views of all those delegations who advocated such other solutions as the drafting of a model law or general conditions. If those other solutions were to be considered, however, the Commission must be fully aware that it would achieve very little if it opted for them.

42. A model law had very little chance of success, for experience had shown that model laws generally remained a dead letter. Many delegations shared the view of the Netherlands delegation that a convention, once drafted, would not be adopted, but that would also be true for a model law.

43. The fact that the Commission had yet to consider the substance of the draft uniform rules might explain the divergence of views among its members. His delegation could not accept as valid the argument that a convention would require changes in domestic legislation. It was precisely because different countries' domestic legislation contained different provisions on liquidated damages and penalty clauses that such legislation must be unified. When that matter had been raised during the drafting of the 1980 Convention,¹⁸ it had been clear to everyone that any international treaty on sales and purchases would include provisions on liquidated damages and penalty clauses. The Convention itself, however, did not address such practical issues. When the Convention had finally been adopted, there had been universal agreement that while the question of liquidated damages and penalty clauses was extremely important, it was

¹⁷Yearbook ... 1976, part one, II, A (General Assembly resolution 31/98 of 15 December 1976).

¹⁸United Nations Convention on Contracts for the International Sale of Goods, Vienna (1980), Yearbook ... 1980, part three, I, B (A/CONF.97/18, annex 1).

relevant not only to contracts of sale and purchase but also to many other aspects of international trade. It was for that reason that a decision had been taken to draw up clauses which had a broader application. Accordingly, in view of the importance attached to the question, his delegation believed that the best method of unifying the relevant national legislation was to adopt a convention.

44. The representative of Canada had pointed out that many countries' laws contained provisions on liquidated damages and penalty clauses and that a convention would require that such provisions be altered. The provisions of such a convention would refer only to international trade, however, and would not call for changes in domestic trade legislation in general.

45. Mr. BARRERA-GRAF (Observer for Mexico) said that, although his delegation believed that the ideal solution would be to draft a convention, it was clear from the difficulties raised by some delegations that the most realistic solution would be a model law. He agreed with the Observer of Switzerland that a proliferation of international conventions must be avoided not only because it would make the Commission's task more difficult but also because it would create difficulties for some countries' domestic legislation, Mexico among them. A convention would also take considerable time to draft and would face problems of adoption and ratification which countries such as his own would find difficult to overcome. The drafting of such a convention raised not only major legal issues but also political ones.

46. His delegation was therefore prepared to support the compromise solution of drafting a model law, not only in the present situation but also as a future UNCITRAL alternative to the drafting of conventions. The Commission had never recommended a model law and yet a proliferation of

conventions on subjects of minor importance should be avoided at all costs.

47. If the Commission opted for the idea of a model law, Italy had made a valid suggestion that a United Nations recommendation should be attached to or included in the law to the effect that no major changes should be made in the law when countries adhered to it and applied it internally.

48. The drafting of general conditions would, in his view, make the task of unification more difficult and must be discarded not only on those grounds but also for the reasons put forward by the representative of Hungary.

49. The representative of Spain had suggested that a model law and general conditions need not be incompatible. He agreed that a model law could in fact be supplemented subsequently by general conditions adopted by an international or regional organization.

50. Mr. CUKER (Czechoslovakia) observed that the chances of adoption of a convention or a model law were virtually the same. Whether or not either solution was adopted depended on whether or not individual States were willing to participate in the unification of international law. If they were, either a convention or a model law could be adopted. If they were not, then neither alternative would be feasible.

51. The present situation was different from that which had characterized the drafting of earlier conventions. Previous conventions had dealt with specific issues while the Commission was now seeking to draft rules which were applicable to a broad range of international contracts. The best way to draft such rules would therefore be in the form of a model law.

The meeting rose at 12.55 p.m.

257th meeting

Wednesday, 28 July 1982, at 3 p.m.
Chairman: Mr. EYZAGUIRRE (Chile)

[A/CN.9/SR.257]

The discussion covered in the summary record began at 3.25 p.m.

INTERNATIONAL CONTRACT PRACTICES: DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES AND PENALTY CLAUSES (*continued*) (A/CN.9/218, A/CN.9/219 and Add. 1)

1. Mr. MADDEN (Observer for Jamaica) said that his Government was still studying the draft uniform rules on liquidated damages and penalty clauses (A/CN.9/218) and considering their possible implementation in Jamaica. Pending further examination, it was inclined to the view that the rules should take the form of a model law. Uniform rules in the form of general conditions would not be the best solution as far as Jamaica was concerned.

2. Mr. SAMI (Iraq) said that he was not convinced by the arguments against the adoption of the uniform rules in the form of a convention. If the Commission decided to convene

a conference to adopt such a convention, that would not be the first time that it had used such an approach. A convention would facilitate the unification of international trade law. Although the process of adopting an international convention embodying the uniform rules could take time, such a convention would have great impact and would offer a set of equitable provisions governing liquidated damages and penalty clauses. Under the Convention, States parties would be obligated to bring their legislation into line with its provisions. It would constitute an internationally accepted legal instrument to which parties could have recourse with the assurance that their rights were guaranteed.

3. Mr. SCHMID (Federal Republic of Germany) said he agreed that a convention embodying the uniform rules would be a good way to harmonize provisions governing liquidated damages and penalty clauses. At the same time, he understood why some States were opposed to the form of a convention and why others would be reluctant to incorporate a model law in their respective legal systems. It was not that they were unwilling to impair the freedom of contract; rather it was because of their unwillingness to change legislative provisions that afforded protection to the weaker party to a contract. The uniform rules failed to offer such protection.

4. One solution would be to recommend the use of the uniform rules in the form of general conditions. The alternative was to make significant changes in the rules. He was open to suggestions concerning such changes.

5. Mr. BYERS (Australia) said that his delegation would like the uniform rules to be embodied in a convention. If no consensus to that effect could be achieved, it would not object to the form of a model law. The uniform rules should not, however, take the form of general conditions.

6. As far as the common-law countries were concerned, the uniform rules would necessitate changes in internal legislation as it applied to international contracts. For that reason, a convention seemed to be the best solution, though the situation with regard to the civil-law countries might well be different. A convention embodying the uniform rules would itself be an indication that certain domestic legislative reforms were imperative. A model law would lack that peremptory force.

7. The uniform rules in the form of general conditions would be of little value to the common-law countries. He still failed to see how, in that form, they would benefit the civil-law countries.

8. Mr. DUCHEK (Austria), referring to what the representative of the Federal Republic of Germany had stated about the reasons why some States were opposed to the form of a convention, said that one way of accommodating the concerns of those States would be to ensure that the uniform rules did not affect the application of provisions intended to protect consumers.

9. While there appeared to be a strong preference for the form of a model law, a number of States favoured the form of a convention. Other States had so far expressed strong support only for the form of general conditions. It was essential for the Commission to consider ways of improving the prospects for consensus. It was possible to accommodate the views of all the parties concerned. A convention embodying the uniform rules either in the main body of the text or in an annex could be drawn up. Such a convention could be submitted to the General Assembly, rather than to an international conference, for adoption. The Assembly could recommend that States not prepared to sign and ratify the convention should at least consider incorporating the uniform rules in the form of a model law in their national legislation. States which still strongly favoured the form of general conditions would be free to act accordingly.

10. Mr. PALAZZO (Observer for Brazil) said that his Government considered the adoption of the uniform rules to be an appropriate way of dealing with the subject, since the rules would afford protection to the contracting parties from imbalances which would certainly arise if the more powerful economic parties to a contract predominated. His Government understood that one of the major obstacles to general agreement in the formulation of uniform rules to regulate various aspects of compensation and default had to do with circumstances in which contractual clauses could be declared void because of differences in conflicting legal systems.

11. The uniform rules proposed by the Commission were not totally unlike some of the legal principles embodied in Brazilian trade legislation, which provided that contracts were valid by mutual agreement between the parties, regardless of any special procedure, unless the law so required. In the case of the uniform rules, agreement would be in writing, a formality which would ensure the legality required for

international trade transactions. The compensation and penalty clauses did not seem to conflict with the corresponding article of the Brazilian Civil Code, which was also intended to strengthen the force of the primary obligation and to protect the parties by making provision for compensation.

12. His Government believed that the Commission should recommend the adoption of uniform rules or general conditions which parties could incorporate in a contract.

13. Mr. SEVON (Finland) said that while all States appreciated the need for uniformity among the rules governing liquidated damages and penalty clauses, not all believed that the uniform rules should be embodied in a convention. The fact that his delegation would prefer the form of a model law did not mean that it was opposed to the concept of uniformity. For Finland and other States which did not want a convention embodying the uniform rules, it was not solely a question of consumer protection; there was also a broader problem relating to contracts in general. Finland had some difficulty with article F, for example.

14. The course of action suggested by the representative of Austria was worth considering. It would certainly help to accommodate the views of most delegations. The uniform rules could well follow the approach used in the Uniform Law on the International Sale of Goods;⁹ the text could stipulate that States parties agreed to incorporate in their legislation the provisions annexed to the text.

15. The elaboration of the uniform rules in the form of a model law would not rule out the possibility of embodying the rules in a convention. The inclusion in the text of a reservation clause could also serve to meet some of the concerns expressed.

16. Mr. RAO (India) said that the adoption of a convention would seem to be the approach best suited to promoting the cause of the unification and harmonization of international trade law. Model clauses would not result in unification, as they could be modified by different national laws of a mandatory character; nor would they override conflicting national laws. His delegation would go along with the majority view on the subject but thought that the convention approach was best. If it was felt that a plenipotentiary conference could not be scheduled immediately for the purpose of concluding a convention, his delegation had no objection to the convening of a conference at an appropriate time.

17. Mr. SONO (Secretary of the Commission) said that the representative of Finland had referred to the Uniform Law on the International Sale of Goods, but the Benelux Convention had a similar structure. That Convention contained articles which were to be found in the final clauses of the UNCITRAL draft Convention. Under article 1 of that Convention, the Contracting States agreed to bring their national legislation on penalty clauses into conformity with certain common provisions set forth in an annex to the Convention, at the latest by the date of entry into force of the Convention.

18. The CHAIRMAN said that the majority seemed to be in favour of embodying the uniform rules in a model law, but that many countries would prefer the adoption of a mandatory convention. Some intermediate positions had also been expressed and could bring together the desiderata expressed by the representatives of Austria, Finland and the Federal Republic of Germany. He wondered whether the possibility of combining a uniform law with a clause which could, at a

⁹United Nations, *Treaty Series*, vol. 834, No. 11929, p. 107.

given time, transform that law into a convention was acceptable to most delegations.

19. Mr. CHAFIK (Egypt) said that although his delegation would prefer a model law, it agreed with the delegations of Austria, Finland and the Federal Republic of Germany that the Commission should begin working on a model law and decide later if a convention should be concluded on the subject.

20. Mr. SCHMID (Federal Republic of Germany) said that the Commission seemed to agree that it would first discuss the provisions in the draft rules which were of a substantive nature—those contained in articles D, E and F—and, if agreement was reached on them, discuss at a later stage whether those articles should be adopted as a convention, model law or general conditions. The discussion of article G could perhaps be deferred for the moment, since that article seemed somewhat problematic. Articles D, E and F posed no problems for his delegation, as they were in complete conformity with his country's domestic legislation.

21. Mr. BYERS (Australia) said that his delegation did not agree that discussion of article G should be deferred, because it was essential to an understanding of articles D, E and F.

22. Mr. CHAFIK (Egypt) said that his delegation believed the articles should be taken up in the sequence in which they appeared; that would obviate the need for a decision on the order in which they should be considered.

23. Mr. SZASZ (Hungary) said that in the unification of laws, it was most important to be prepared to ask States to make certain amendments in their legislation. No solutions would be found without such an approach.

24. His delegation supported the proposal that a combined approach be adopted. It might be possible within the Commission itself to see how many States would prefer to adopt the rules as a model law and how many would prefer them to be incorporated in a convention. A problem still arose, however, because irrespective of whether the model law or convention approach was used, it had to be decided whether a State would have to incorporate the rules verbatim in its legislation, or whether the legislation had simply to reflect the rules. His delegation preferred the model law approach because it would be difficult to ask Governments to incorporate the rules verbatim in their national legislation.

25. Mr. SEVON (Finland) said that his proposal was more procedural than substantive. Before substantive work could be done, the Commission must know what form the final product would take. The possibility that a convention would be formulated should be left open, because some countries might feel more obliged to comply with a convention than with a model law. The idea behind his proposal had been to solve the problem of form at the outset, so that the Commission could then have a serious discussion of all the provisions, including those dealing with the scope of application and those contained in article D.

26. Mr. GABAY (Observer for Israel) said that his delegation supported the proposal made by the representative of Finland. With regard to the Uniform Law on the International Sale of Goods, however, he wished to recall that Israel had been one of the first to adhere to it and to introduce it into its national legislation, but had been disappointed to see that few countries had followed suit. That example illustrated the difficulties of incorporating a model law verbatim in national legislation.

27. Mr. SONO (Secretary of the Commission) said it was his understanding that there was a consensus that the Commission would first discuss the substantive provisions of the draft rules, especially articles D and G, and then, in the light of that discussion, take up the question of the final form of the rules.

28. The CHAIRMAN said that, if he heard no objection, he would take it that the Commission wished to begin its consideration of articles D through G.

29. *It was so decided.*

30. Mr. BASNAYAKE (secretariat) said that the main idea behind article D was that since liquidated damages or penalties were payable when there was a failure of performance, if the obligor was not liable for that failure—for example, if he had a defence such as *force majeure*—then he should not be held liable to pay or forfeit the penalty. That was a principle which was generally accepted in most legal systems.

31. Mr. HARTKAMP (Observer for the Netherlands) said that his delegation supported the contents of article D. Its wording was similar to articles E and F in that it was intended to be non-mandatory law, although that idea was expressed differently in the various articles. In articles D and F, the formulation was “unless the parties have agreed otherwise”. In article E, however, paragraph (3) stated “the rules set forth above shall not prejudice any contrary agreement made by the parties”. Article G contained no wording of that nature whatsoever, but the commentary on it indicated that it was meant to be mandatory law. He therefore suggested the deletion of the phrases he had just read out from articles D, E and F and the addition of a new article stating which articles were mandatory and which were non-mandatory law.

32. Mr. GUEST (United Kingdom) said that his delegation felt that the Commission should first discuss article A which contained the definition of liquidated damages and penalty clauses. Such an approach would facilitate the consideration of articles D through G.

33. Mr. ROEHRICH (France) said that his delegation supported the proposal made by the representative of the United Kingdom. Article A was important not only for the definition of liquidated damages and penalty clauses, but also for the scope of application of the uniform rules.

34. Mr. SMART (Sierra Leone) said that his delegation endorsed the views of the representative of the United Kingdom. It was important to start with definitions before going into the substance of articles D through G. He, himself, for example, was at a loss to distinguish between liquidated damages and penalty clauses and thought that that question should be cleared up first.

35. Mr. MAGNUSSON (Observer for Sweden) said that his delegation supported the proposal of the United Kingdom. Article A was of special interest to his delegation, because a problem arose as to how article D affected first demand bank guarantees. If article A was understood in a certain way, it would set those guarantees outside the scope of the rules.

36. Mr. YEPEZ (Observer for Venezuela) said that discussion of articles D through G was the only sensible way to begin.

37. Mr. CHAFIK (Egypt) requested clarification from the representative of the United Kingdom as to whether he had

proposed the discussion of article A as a whole or only of article A, paragraph (1).

38. Mr. GUEST (United Kingdom) said that he had wished to concentrate on the definition in article A, paragraph (1), of liquidated damages and penalty clauses, and specifically, on the explanation in that article that there was an agreement that, upon a total or partial failure of performance by a party (the obligor), another party (the obligee) was entitled to recover, or to forfeit an agreed sum of money.

39. Mr. FERRARI-BRAVO (Italy) said that the scope of the rules was defined not only in article A, paragraph (1), but also in article C, wherein some contracts were excluded from the scope of application of the rules. He suggested that the Commission should take a decision on the proposal made by the representative of the United Kingdom.

40. Mr. GUEST (United Kingdom) said that the scope of his proposal had been to concentrate on the definition in article A, paragraph (1) of liquidated damages or penalty clauses. At a later stage, the Commission should not overlook article C or the question of the scope of application of the text. It could return to those questions after it had dealt with the main substantive provisions.

41. Mr. SCHMID (Federal Republic of Germany) said he agreed with the United Kingdom representative. The Commission should first discuss the question of definitions. His delegation had no difficulty with the present definition; liquidated damages and penalty clauses were allowed under the law of his country. He questioned whether penalty clauses as such were allowed in common-law systems.

42. Mr. LARSEN (United States of America) agreed that, as the representative of the United Kingdom had said, the Commission should start at the beginning, with the definition, and then proceed to the scope of the application of the text, considering article A and then article C.

43. Mr. ROEHRICH (France) said that he endorsed the United Kingdom position. He had misgivings, however, about proceeding to discuss article D *et seq.* The Commission must know what it was talking about. There were different options before it. If it reached agreement on the question of geographical scope and the material field of application under article C, it would find it easier to consider the substantive articles. The Commission could deal with article A and the definition at the current stage.

44. The CHAIRMAN noted that the majority of delegations seemed to feel that the Commission should consider article A, paragraph (1), first. It could then, as the secretariat had recommended, proceed to consider articles D to G. If he heard no objection, he would take it that the Commission agreed to that course.

45. *It was so decided.*

46. Mr. BASNAYAKE (secretariat) said that the issue raised by article A was the nature of the clause which the Commission was trying to formulate. Article A, paragraph (1) of the draft Convention and article A, paragraph (1), of the draft Model Law were the same. The text of the draft Convention was given for convenience. Up to the reference to footnote 13, it represented the text adopted by the Working Group, and that part dealt with the issue under consideration. The clause in question was contained in a contract and dealt with the case of failure of performance by the obligor, the condition on which money was recovered or forfeited. Such failure was defined in the widest possible terms, i.e., "total or

partial". If failure occurred, the obligee had the right to recover or forfeit the agreed sum of money. It had been the understanding of the Working Group that the expression "agreed sum" did not necessarily mean an identified amount. There might be agreement about the method of arriving at the sum, e.g., \$ 100 per week of delay.

47. With regard to the comment of the representative of Sierra Leone, there had been no intention to distinguish between liquidated damages and penalty clauses under common law or to specify the function which the agreed sum might serve. It might serve to penalize non-performance or to induce performance. It had been felt that, because the purpose of the uniform rules was to unify the common law and the civil law systems, the clause might serve both purposes.

48. Mr. YEPEZ (Observer for Venezuela) said that, in principle, his delegation agreed with the drafting of article A, paragraph (1). He felt that the expression "total or partial" was superfluous, but if other delegations felt that it should be retained, he would not press the point.

49. He had doubts concerning the term "*confiscar*" in the Spanish text. In Venezuela, that term was used in administrative law in connection with the State's right to seize property if it was being used contrary to public order. He suggested that the word *embargo* might be used in the Spanish text and requested clarification on the point.

50. The word "agreed" before the word "sum" seemed unnecessary, because the agreement was obvious. However, he would not object to its retention.

51. Mr. BASNAYAKE (secretariat) said that, in its written comments, the Spanish delegation had made the same point regarding the Spanish translation of the word "forfeit". If the word "forfeit" was accepted in the English text, perhaps a change could be made in the Spanish text.

52. The CHAIRMAN said that the Venezuelan suggestion might be followed with regard to the translation of the word "forfeit" in the Spanish text, if there was no objection to the retention of that term in the English text.

53. Mr. SMART (Sierra Leone) thanked the secretariat for its explanation of the lack of definition of "liquidated damages" and "penalty clauses". The secretariat had now defined liquidated damages and penalty clauses by saying that there was no difference between them. However, for a person trained in the common-law system, there was a great difference. It should be stated that for the purposes of the Convention or the Model Law the two were the same.

54. Mr. ROEHRICH (France) said that he had a drafting comment to make along the lines of that made by the representative of Venezuela and that contained in Spain's written comments. The word "*abandon*" in French had no particular legal sense. He would like to find a simpler, more general translation for "forfeit". The expression "*prétendre au versement ou à l'abandon d'une somme convenue*" might be replaced by the expression "*se voir attribuer une somme convenue*". The word "*prétendre*" meant to claim. His delegation could accept the definition as a whole. He felt that the idea of an agreed sum should be retained.

55. The CHAIRMAN asked all the Spanish-speaking representatives to agree on a term to translate the English word "forfeit" and to submit their proposal to the secretariat. The French-speaking delegations could do the same for their language.

56. Mr. BASNAYAKE (secretariat) drew the attention of the Spanish-speaking and French-speaking delegations to paragraph 20 of document A/CN.9/218, which defined the concept of "forfeiture" as used in article A, paragraph (1), and pointed out that the term used in all languages must cover the two situations described in that paragraph.

57. Mr. MING-CHENG (Observer for China) said that the terms "liquidated damages" and "penalties" were not mentioned explicitly in the text of article A. For the sake of clarity, he proposed that the words "as liquidated damages or penalty" should be added at the end of article A, paragraph (1), of the draft model law.

58. With regard to the word "forfeit", he felt that some more appropriate word should be used. He pointed out that, under Chinese law, a decision on forfeiture could be taken only by the Government or the court. He noted that, in paragraph 20 of document A/CN.9/218, the words "retained" and "withheld" were mentioned but, as he understood it, the words "retain", "withheld" and "forfeit" were different in meaning. Where an agreed sum was to be paid, it should be made clear that it must be based on a written agreement between the parties.

59. Mr. HARTKAMP (Observer for the Netherlands) said that he shared the doubts expressed concerning the word "forfeit" but not the concept involved. The term was difficult to translate and recurred in almost every article. He suggested the addition of an explanatory phrase.

60. He would also like the word "agreed" to be deleted, because that was too narrow a concept. The parties might agree on a standard, index or currency, as the basis on which the sum was to be calculated.

61. He would like to see the scope of application extended to performances other than payment of a sum of money, such as goods to be handed over or an act to be performed if the main obligation was not performed.

62. With regard to the words "in writing", the issue involved was extremely delicate. In the case of the Vienna Convention on Contracts for the International Sale of Goods, the whole question of validity had been left out of the body of the Convention. It would be wise to adopt a similar approach in the current instance, even if that necessitated reservations, as in the case of the Vienna Convention.

63. Mr. LARSEN (United States of America) said, with regard to the question raised by the representatives of the Federal Republic of Germany and Sierra Leone, that one basic difficulty was that, in common-law countries, penalty clauses were not permitted but liquidated damages were. The Working Group had sought a compromise and had therefore avoided the use of those terms in the definition article.

64. The Government of Sweden had pointed out in its written comments that, read literally, the draft Convention or draft Model Law would apply to a bank guarantee. In the meetings of the Working Group which he had attended, there had been no idea of having the instruments apply to such banking instruments. It would therefore be advisable to state in article C that bank guarantees were excluded from the scope of the instruments.

65. Mr. GUEST (United Kingdom) said that he had some difficulty with the definition. He would cite certain factual situations.

66. If in the case of an ordinary contract for the sale of goods with the price payable upon delivery of those goods in conformity with the contract, those goods were not delivered on time or in conformity with the contract, would that fall within the definition?

67. Did the case of a contract for the supply and installation of machinery, where it was agreed that the purchaser was to pay to the seller an advance sum, to be repaid if the work was not done by a certain date, come within the scope of the definition?

68. If an employee hired on an international basis had a contract which stipulated that, if the employee was dismissed for cause, he would forfeit his pension rights, did that fall within the scope of the definition?

69. The same question arose with regard to the case of bank guarantees, already referred to by the Government of Sweden.

70. Where one party was allowed to withdraw from a contract upon payment of a sum of money, the draft instrument would not apply, because there had been no failure of performance. But the matter would not be clear to the person reading the draft for the first time. He wondered whether the situations he had enumerated did not fall within the definition contained in article A.

71. Mr. MAGNUSSON (Observer for Sweden) said that, in Sweden, there was some concern that bank guarantees and first demand guarantees should be left outside the scope of the uniform rules. Such exclusion would follow from the way in which article A was formulated, but he wished confirmation of the exclusion. He noted that Norway, too, had requested clarification on that point. He did not propose any change to the text. It would be sufficient if the exclusion was mentioned in the commentary.

The meeting was suspended at 5.20 p.m. and resumed at 5.45 p.m.

72. Mr. CUKER (Czechoslovakia) said that liquidated damages clauses should ensure the execution and performance of the contract. Payments should be recoverable in the case of non-performance even where there were no damages. It was clear from the comments made by other delegations on article A that under some legal systems penalty clauses could only be incorporated in the terms of a contract only if the parties concerned were agreeable. Finally, the words "in writing" should be kept in article A, paragraph (1).

73. Mr. SAMI (Iraq) said that the first part of article A had been drafted well, but that the expression "to forfeit" had a specific legal meaning in Arabic which rendered it inappropriate in that article. Once agreement had been reached on the essence of the matter, a more appropriate formulation in Arabic could be devised.

74. His delegation agreed with that of China regarding the need to define liquidated damages and penalty clauses. The proposals relating to recovery of advance payments should be clarified.

75. Mr. OLIVENCIA (Spain) said that the comment that writing appeared to be required by Spain's commercial code for the validity of international trade contracts, contained in

paragraph 18 of document A/CN.9/219, required clarification, since it did not reflect the essence of his Government's reply.

76. Under Spanish law the individual was free to bind himself contractually as he chose. Exceptions were made, however, in certain circumstances under private international law if the instrument governing the contract required a written form of contract to be employed. Thus, Spain's commercial code required a written contract in certain cases only.

77. The Commission was considering an article which would apply to a broad range of contracts, but which related to formal situations, in view of which his Government preferred to see a requirement that contracts be in writing.

78. The word "*confiscar*" in the Spanish text of article A was not appropriate, since it implied an act of authority. It could perhaps be replaced by the expression "*retener y hacer suya*", or "*retener y atribuirse*". That notwithstanding, the problem of terminology was less important than that of agreeing on the exact meaning of liquidated damages and penalty clause. Appropriate terminology could be devised once agreement had been reached on the definitions.

79. Spain agreed that bank guarantees should be excluded from the scope of the article. Finally, his delegation had no objection to the wording "agreed sum of money", although it could be replaced if other delegations wished.

The meeting rose at 6.05 p.m.

258th meeting

Thursday, 29 July 1982, at 10 a.m.
Chairman: Mr. EYZAGUIRRE (Chile)

[A/CN.9/SR.258]

The meeting was called to order at 10.10 a.m.

INTERNATIONAL CONTRACT PRACTICES: DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES AND PENALTY CLAUSES (*continued*) (A/CN.9/218, A/CN.9/219 and Add.1)

1. Mr. PARK (Observer for the Republic of Korea) expressed the hope that, on the basis of the discussion that had taken place at the previous meeting on article A, paragraph 1, of the draft uniform rules on liquidated damages and penalty clauses (A/CN.9/218), it would be possible to improve the wording of paragraph 1 in order to accommodate different countries' concerns. His delegation's views on that paragraph could be found in document A/CN.9/219 and included the view that the words "in writing" should be retained for the sake of clarity and in order to prevent possible disputes arising from the interpretation of unwritten agreements. Such an approach would also be in keeping with current practice in international trade contracts and with the relevant UNCITRAL Arbitration Rules. The actual term "in writing" should be interpreted more broadly to cover such possibilities as a clause in the contract itself, a separate agreement signed by the parties or an exchange of letters or telegrams as provided for in the Hamburg Rules.

2. With regard to paragraph 22 of the commentary on article A, paragraph 1, his delegation agreed that an acceleration clause providing for immediate payment of all outstanding instalments in the event of a single default would not normally come within the scope of article A.

3. Mr. SEVON (Finland) recalled that, at the previous meeting, the representative of the United Kingdom had cited a number of examples of situations relating to payment of the price for goods or services forming the subject of a contract. It was his delegation's understanding, however, that the draft rules dealt only with amounts agreed upon to secure performance of a contract. Article A, paragraph 1, should make that quite clear.

4. The representative of Sweden had mentioned the problem of performance guarantees entered into by a third

party. The draft rules dealt only with contracts under which one or other party agreed to pay or lose a certain sum of money if it failed to perform that contract, however, and did not cover situations in which a third party might agree to pay that sum if one of the two parties defaulted. That limitation could be made quite clear by amending the word "another" in the third line to read "the other", although such an amendment might create problems if there were several parties to the contract.

5. Many delegations had expressed a preference for retaining the words "in writing". To do so, however, presupposed that a separate contract on liquidated damages was intended. A separate contract was not normal practice: liquidated damage clauses were always included in the overall contract. Provision should not be made for the liquidated damages clause to take a different form from usual. If a contract was entered into orally, parties could refer to general conditions including liquidated damages clauses. Moreover, a contract in writing might not always fulfil all the requirements of form.

6. With regard to the expression "agreed sum", the representative of the United Kingdom had argued that article A was already extremely broad and to make it even broader would increase the risk of misinterpretation. Deletion of the expression would, however, create even more confusion and it would be preferable to clarify what was meant by it, for instance by using an alternative expression such as "determined" or "determinable" sum.

7. Mr. PERILLO (United States of America) suggested that, in order to avoid further repetition of the views and arguments put forward at the previous meeting, the secretariat should redraft article A, paragraph 1, to take account of the views expressed so far.

8. Mr. GUEST (United Kingdom) recalled that, at the previous meeting, he had cited a number of examples which came within the scope of article A, paragraph 1. He wished to reiterate one such example, namely situations in which a contract provided for advance payment of all or part of the price agreed to in the contract and a clause in the contract required that the price be recoverable if goods were not delivered by the due date. Such situations clearly came within the scope of paragraph 1 for they involved partial failure by

the seller and therefore entitled the buyer to recover the agreed sum.

9. The observer for the Republic of Korea had been of the view that accelerated clauses in situations where there was provision for payment by instalments did not come within the scope of paragraph 1. It was clear from the wording of that paragraph, however, that such a situation was covered for it involved partial performance of a contract by the debtor. Cases where default interest was payable when instalments were not paid on time would also come within the scope of that paragraph.

10. In his view, the Working Group had not identified adequately some additional characteristics of penalty clauses. For instance, an agreed sum represented the liquidation of damages or compensation payable on breach of contract in lieu of a secondary obligation to pay such damages or compensation. The representative of Finland had indicated that an agreed sum could be the sum obtained or retained as security for the performance of a contract. Neither of those concepts was mentioned in the draft rules and, before the present broad formulation of article A, paragraph 1, could be accepted it must be confined within limits appropriate to the subject matter in hand.

11. Mr. SZASZ (Hungary) observed that the concept of an "agreed sum" could refer to a situation in which the obligor's failure to perform the contract entitled the obligee to a reduction in the price of the goods or services provided for in that contract. The examples cited by the representative of the United Kingdom showed that there was a need to specify that the term "agreed sum" meant a sum other than that involved in the fulfilment of the obligation of the obligee. Such a clarification would obviate the need to cite examples.

12. The decision whether or not to retain the expression "in writing" would depend on whether a convention or a model law was to be adopted. There would be no need for the expression in a model law since the applicable national law would make it clear whether a contract must be in writing or not and to include such a requirement in the draft rules would only create problems. If, on the other hand, a convention was to be adopted, a solution similar to that adopted for the 1980 Vienna Convention would be in order.

13. Mr. AKINLEYE (Nigeria) observed that the United Kingdom delegation had cited interpretative examples of the expression "agreed sum" which would not normally be covered by article A, paragraph 1. With the paragraph as currently worded, however, that was not the case. The article must therefore be redrafted to show that the "agreed sum" was a sum to be paid in the event of failure to perform the contract.

14. His delegation questioned the need for a provision on liquidated damages. A standard formula could not be adopted for dealing with cases of breach of contract. Similarly, most countries whose legal system was based on common law were not in favour of penalty clauses and their courts rarely enforced such clauses since they gave a double advantage to the obligee: a remedy and a penalty for non-performance. The Working Group should completely redraft article A, paragraph 1, to resolve such problems.

15. Mr. DUCHEK (Austria), referring to the use of the expression "in writing", agreed with the representative of Finland that article A, paragraph 1, should not deal with the question of the form of a contract. He also agreed with the representative of Hungary that the expression would not be

needed were a model law to be adopted. In fact, it would not be needed even in a convention, since the uniform rules would refer only to liquidated damages and not to the law of contracts in general and the question of validity of contracts. General rules on the form and validity of contracts would have to be applied over and above the uniform rules, a fact that might usefully be mentioned in the uniform rules. The validity of a contract could be determined only by reference to the provisions of that particular contract. The expression "in writing" should therefore be deleted.

16. With regard to the question of definition raised by the representative of the United Kingdom, it was clear that any number of examples could be cited for a provision if the latter was taken literally. Some of the examples cited by the United Kingdom were valid, for instance those referring to quantified damages and security against performance. Again, the representative of Finland had interpreted the expression "agreed sum" to mean a sum intended to secure performance, while the representative of Hungary had suggested that it meant any sum other than the sum to which the obligee was bound by contract. He personally preferred the United Kingdom interpretation but wondered whether the definition meant that the two different cases cited would have different consequences which would have to be defined in subsequent articles.

17. Mr. BYERS (Australia) agreed that it would be wise to insert a provision which made it clear that the agreed sum was only the sum paid to secure performance of a contract or one or more of its provisions. Again, it was up to the parties to a given contract to decide on the form that that contract should take since the same result was sought whatever the form.

18. With regard to the use of the expression "in writing", if a convention omitted such an expression, its provisions would apply to contracts in writing and contracts not in writing alike and it would be the rules of the country applying the convention that would determine whether contracts must or must not be in writing. There was no need to follow the precedent of the 1980 Vienna Convention: it would be easier simply to omit the expression.

19. The expression "agreed sum", on the other hand, must be retained. Regardless of whether the sum was "determined" or "determinable", it must be "agreed". Contracts must stipulate a specific amount and the agreed sum would cover such amounts.

20. With regard to the suggestion made by the representative of Sierra Leone, he did not think it advisable to encumber article A, paragraph 1, with concepts of common law regarding the distinction between liquidated damages and penalty clauses when the paragraph was to be applicable to both common-law and civilian-law systems.

21. Ms. VILUS (Yugoslavia) observed that liquidated damages and penalty clauses should form an integral part of the over-all contract. If a model law was adopted, parties should be advised to put such clauses in writing since that would offer them greater security.

22. Mr. GUEST (United Kingdom), responding to the representative of Austria, observed that a single regime could be applied to both quantified damages and security. The provisions of article G could be applied in the first instance to determine whether the quantified sum was excessive and, in the second instance, to determine whether the security was excessive. He had not sought to make a distinction between the two cases but rather to highlight what they had in common.

23. Mr. SCHMID (Federal Republic of Germany) supported the view expressed by the representative of Austria that article A should not make any reference to the form of clauses. Therefore, the phrase "in writing" should be deleted. The question whether such clauses were valid should be left to national law and that should be stated quite clearly in the rules. Therefore, article G should state that national courts could decide whether liquidated damages clauses were valid, either in full or in part.

24. Mr. SAMI (Iraq) felt that the words "in writing" should be retained. In view of the importance of such contracts, it was imperative that the liquidated damages and penalty clauses should be in writing in order to prove the existence of such provisions in a clear manner and to show that a definitive sum had been agreed by the parties. The decision on the sum of damages to be awarded should be left to a court, which could judge whether the sum mentioned was in keeping with the actual damages arising as a result of partial or total failure to perform.

25. Mr. ROEHRICH (France) stressed that, for a number of delegations, the retention of the phrase "in writing" represented an important guarantee for the parties to a contract. He expressed concern at the remarks made by the representative of the Federal Republic of Germany, who felt that the courts should be given power in all cases to decide whether liquidated damages and penalty clauses were valid. To give national courts such power seemed to defeat the object of unification. With regard to the agreed sum of money, he had no objection to clarifying the idea, but felt that care would be necessary in drafting in order to find a formula that would not exclude too many things.

26. Mr. SONO (Secretary of the Commission) said that he had some suggestions to make regarding five important points which had emerged in the discussion on article A, paragraph 1.

27. Since the Working Group had not intended the draft rules to cover a third party guarantee, the Commission might be able to agree to change the word "another" to "the other", as proposed by the representative of Finland, if it felt that the latter could thus be clarified. A statement to the same effect could also be included in the commentary, as suggested by the representative of the Netherlands.

28. The Commission might also tentatively agree to delete the words "in writing". Such a deletion would make no difference if the rules were adopted as a model law, while, if the form of a convention was agreed, the Vienna Sales Convention formula could be used.

29. Since many delegations wished to confine the law to liquidated damages and penalty clauses, he felt that the phrase "an agreed sum" should be retained, although it might need some modifications, as suggested by the representative of the United Kingdom.

30. Since the whole point of the uniform rules was to avoid conflict between legal systems, he suggested that a specific mention of liquidated damages and penalty clauses might be unfortunate. An appropriate modification of the phrase "agreed sum" might ensure that the scope of the rules would be suitably narrow.

31. He had noted the concern expressed over the use of the word "forfeit" and the examples put forward by the representative of the United Kingdom, which could create a problem regarding the scope of the rules. It was clear that most

delegations wished to confine the application of the rules to liquidated damages and penalty clauses or similar situations. Adding the words "similar obligations" after the phrase "agreed sum of money" might create difficulties with respect to other articles, for example, article D. Therefore, he suggested that the Commission might wish to delete the words "recover, or to forfeit" for the time being, until agreement had been reached on other matters, including the changes to be made to the phrase "an agreed sum of money".

32. Mr. HARTKAMP (Observer for the Netherlands) agreed with the suggestions made by the Secretary of the Commission and drew attention to the proposal made by his delegation to extend the scope of the rules to cover matters other than money.

33. Mr. SONO (Secretary of the Commission) said that the Working Group had considered the proposal put forward by the representative of the Netherlands. However, research carried out by the secretariat had revealed that there were not many cases where performances other than monetary ones were requested. Since acceptance of the Netherlands proposal would entail additional work—article D, for example, related purely to money—he had ignored that possibility in the suggestions he had made.

34. Mr. PERILLO (United States of America) said that he agreed with the first four suggestions made by the Secretary. On the fifth point, however, he realized that the representatives of the non-English speaking countries were all unhappy with the word "forfeit", which was a concept in common law, but felt that the problem should be solved by using different language, since to remove the notion of forfeit would be to change the nature of the rules.

35. Mr. SONO (Secretary of the Commission), replying to the representative of the United States, said that the solution might be dependent on the phrase to be added after the words "an additional sum of money". He had suggested that the words "recover, or to forfeit" might be tentatively deleted until that phrase had been agreed. If the additional phrase did not cover the notion referred to by the representative of the United States, the Commission would have to consider the matter further. That was why he had suggested that discussion on the matter should be avoided until the additional phrase had been approved.

36. Mr. CHENG (Singapore) suggested that the concept of forfeit could be retained by using either the phrase "is entitled to an agreed sum of money for the failure to perform" or the phrase "is entitled to the retention or payment of an agreed sum of money for the failure to perform".

37. Mr. SEVON (Finland) agreed that the proposal made by the representative of the Netherlands should not be taken up. An amendment along the lines proposed would be easy in article A but would create difficulties elsewhere in the draft.

38. Mr. LAVINA (Philippines) expressed concern that an obligor might escape his obligation through a bank guarantee.

39. Mr. BYERS (Australia) said that he was satisfied with the suggestions made by the Secretary, which, in his opinion, could lead to a consensus.

40. Mr. SZASZ (Hungary) expressed general satisfaction with the suggestions made by the Secretary. A similar group had met during the drafting of the Vienna Sales Convention, and its work had greatly facilitated agreement on the wording of the article concerned.

41. Mr. SAWADA (Japan) supported the suggestions made by the Secretary. He agreed with the representative of Hungary that the Commission should conclude its discussion on article A, paragraph 1 before moving on to other matters. While not objecting to the proposal to modify the phrase "agreed sum", he felt that that phrase was probably sufficient and that it might be difficult to find a suitable addition. The proposal made by the representative of Iraq was a good one and the secretariat might collect specific proposals from delegations for modifying the phrase "agreed sum".

42. Mr. JOKO-SMART (Sierra Leone) said that his delegation accepted the clarification that no reference would be made to liquidated damages or penalties, but that a modification clause would be attached to the words "agreed sum of money".

43. However, he was puzzled at the indication made by the representative of the Federal Republic of Germany that the court of the country concerned should decide whether or not a particular clause referred to liquidated damages or penalties. It was not clear what system of law was going to govern the convention or model law.

44. Mr. SONO (Secretary of the Commission) agreed that there were considerable conflicts between common law and civil law. Although article G, paragraph 2, referred to the penalty clause, the uniform law would have no value at all if national law also came into play in that connection. He was sure that, having heard the statement made by the representative of Sierra Leone and the earlier statement made by the representative of France, the representative of the Federal Republic of Germany was aware of the difficulties involved.

45. Mr. HARTKAMP (Observer for the Netherlands) said that his country's new civil code covered types of penalty clauses relating to payment by a debtor other than in a monetary form. It had not proved necessary to amend other articles relating to penalty clauses. However, he acknowledged that it seemed that in international trade penalty clauses requiring payment in other than a monetary form did not occur frequently. He therefore wished to withdraw the proposal he had put forward.

The meeting was suspended at 11.55 a.m. and resumed at 12.30 p.m.

46. Mr. MUCHUI (Kenya), referring to the problem raised by the representative of Sierra Leone, of how to distinguish between liquidated damages and penalty clauses, said that it

was important to establish whether the Commission was envisaging a situation where penalties would be accepted. It was not clear whether article A, paragraph (1), covered liquidated damages alone, penalties alone, or liquidated damages and penalties. It appeared to envisage liquidated damages and penalties. The representative of the Federal Republic of Germany had pinpointed the problem.

47. Mr. OKWONGA (Uganda) said that his delegation supported the statement made by the representative of Kenya. Perhaps the Commission could deal with the problem by introducing a suitable reservation clause.

48. Mr. GUEST (United Kingdom) noted that, in the case of the civil law system, certain degrees of control were exercised over clauses in contracts providing for compensation or payment. The only question was really the degree of control and the method of approach of the two legal systems, which was a matter that should be considered under article G.

49. Mr. BYERS (Australia) said that his delegation entirely agreed with the statement made by the representative of the United Kingdom. Article G would apply both to liquidated damages and to penalties.

50. Mr. JOKO-SMART (Sierra Leone) said that article D introduced the concept of penalties. Articles D and G did not appear to be compatible.

51. Mr. MUCHUI (Kenya) said that the wording of article G appeared strange to those delegations that had reservations with regard to penalties. His delegation could accept article A as it was currently drafted, provided that thorough consideration was given to the wording of article G.

52. Mr. CHAFIK (Egypt) noted that reduction of penalties was possible under the civil law system, and he therefore did not believe that there was any fundamental difference between the two systems in that connection.

53. Mr. SONO (Secretary of the Commission), referring to the statements made by the representatives of Kenya and Uganda, said that article G represented a compromise between common law and civil law. If the approach incorporated in the draft text before the Commission was adopted, a number of common-law countries might have to modify their position, but the civil-law approaches would also have to be modified.

The meeting rose at 12.55 p.m.

259th meeting

Thursday, 29 July 1982, at 3 p.m.
Chairman: Mr. EYZAGUIRRE (Chile)

[A/CN.9/SR.259]

The meeting was called to order at 3.20 p.m.

INTERNATIONAL CONTRACT PRACTICES: DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES AND PENALTY CLAUSES (*continued*) (A/CN.9/218, A/CN.9/219 and Add.1)

1. Mr. BASNAYAKE (secretariat) said that article D provided for a situation in which a party had not fulfilled its obligations, but had a valid defence. In general, in such

circumstances there was no liability for damages, but article D would allow the parties to agree otherwise. The amount involved need not be a penalty: the parties could, for example, estimate the amount of any loss to determine an appropriate figure for compensation.

2. Mr. GUEST (United Kingdom) asked whether, where the parties had made such an agreement in accordance with article D, the sum in question would be subject to article G.

3. Mr. BASNAYAKE (secretariat) said he thought that that would be the case, although it was not entirely clear.

4. Mr. CHAFIK (Egypt) said that he also thought that article G would apply in such cases.

5. Mr. PERILLO (United States of America) agreed that any such agreement would be subject to articles F and G. It might be appropriate to state that explicitly in article D.

6. Mr. LAVINA (Philippines) said that his delegation had no difficulties with article D as currently worded. The United States proposal would make the relationship between articles D and G more explicit, but it should be understood that the articles were to be read as a whole.

7. Mr. BYERS (Australia) said that it would be sufficient to say that article D was subject to article G, since the latter was the overriding provision and it was not possible to contract out of it.

8. Mr. AKINLEYE (Nigeria) said that since, in keeping with the interpretation offered by the secretariat, any amount recovered would be compensation rather than a penalty, it would be appropriate to replace the concept of forfeit with that of compensation in article D.

9. Mr. SONO (Secretary of the Commission) said that the point raised by the representative of Nigeria was interesting, although it should be recalled that the wording should be consistent throughout the draft rules. Article D would be qualified by articles F and G. Article D also had another function, relating to the burden of proof: it was often difficult to establish loss or negligence or the extent of liability. If the parties applied the waiver available under article D, the question of determining responsibility would not arise, thus expediting matters. The United States proposal might be superfluous, since the main aim of the article related to the burden of proof.

10. Mr. SEVON (Finland) said that the proposal to include a separate provision stating which articles were mandatory would make it easier to draft articles D, E and F, which were not mandatory.

11. Mr. GUEST (United Kingdom) said that article D covered two types of situation, which might be dealt with separately. Firstly, an agreed sum could not be recovered or forfeited if there was a defence to the allegation of a failure of performance. Secondly, there were situations in which certain events led to a failure of performance, although there was no breach, for example, *force majeure*. In that case the sum which had been agreed upon by the parties was subject to article G. However, the brevity of article D made it difficult to see whether that was actually its aim.

12. Mr. BASNAYAKE (secretariat) said that that was indeed the intent.

13. Mr. SAMI (Iraq) said that article D meant that the question of compensation did not arise if a party was not responsible for the failure of performance. Where a party was responsible, article G applied. Where there was non-performance and the contract provided for a specific sum to be paid, but no loss or damage had been incurred, a court might reduce the sum agreed upon.

14. The CHAIRMAN said that article D established the principle that the obligee was not entitled to compensation if there was no responsibility for the failure of performance. However, unless the parties had agreed otherwise, there was a relationship between the introductory wording of article D and article G.

15. Mr. DUCHEK (Austria) said that he wished to support the proposal made earlier by the Netherlands to include a separate provision stating that article G was mandatory and that the other articles were not.

16. Mr. JOKO-SMART (Sierra Leone) said that the words "Unless the parties have agreed otherwise" should be deleted from article D. If that wording were left, it would be possible for parties to opt out of all the defences available to the obligee, a state of affairs which no legal system could permit.

17. Mr. SONO (Secretary of the Commission) said that unless the parties agreed otherwise, liquidated damages and penalty clauses applied only where one party was at fault. Under article D, the parties could agree that the question of negligence would not be raised and agreement could be reached without any attempt to determine where the fault lay. That was the object of the first part of the article.

18. Mr. CHAFIK (Egypt) said it was clear that, if there was no liability for the failure of performance, there could be no damages. The aim of the text was to establish that, if the parties so chose, there could be an agreed compensatory sum.

19. Mr. SEVON (Finland) said that a number of problems which had no intrinsic connection with each other were being discussed at the same time. He supported the statement made by the representative of Sierra Leone; no legal system could tolerate a situation in which one party could opt out of all sanctions.

20. Yet the rules did not deal with that problem, they merely dealt with the question of whether the parties could agree that an amount was to be payable even if it was not established that there had been a failure of performance. If the introductory wording of article D merely meant that, to the extent that the parties could exercise freedom in their contractual relationship, the matter could be resolved in various ways, for example, as proposed by the representative of the Netherlands; the question was really one of drafting. In that connection, it would be interesting to know what plans the secretariat had for making drafting changes on the basis of proposals made by the members of the Commission.

21. Mr. LAVINA (Philippines) said that the opening clause of article D should be placed elsewhere in the Rules. Under most legal systems, if there was no fault, there was no liability. The Commission might wish to rewrite article D. In general, freedom of contract existed only where there was no violation of the law or of public policy. Under article D it might be possible to obtain compensation even if the law had been violated.

22. Mr. ROEHRICH (France) said that his delegation was concerned by statements that if there was no liability there was no need to pay any sum. There was also the problem of the burden of proof. Article D made it possible to derogate from the rule, but placed an obligation on the obligor, if he did not wish to pay the agreed sum, to prove that he had not committed the failure of performance. That did not, however, mean that the obligee was required to prove that the obligor had failed to perform.

23. In principle, the article meant that there was *a priori* recognition of validity of a clause in a valid contract, and that the agreed sum had to be paid once the necessary conditions had arisen. If the obligor did not wish to pay he would have to prove that he was not liable for the failure of performance.

24. Mr. GUEST (United Kingdom) said that the rule might be embodied in article D without the qualification contained

in the opening clause, but instead with the addition of a second clause stating that the parties could agree on a sum to be forfeited or recovered even if the obligor was not liable, but that the amount would be subject to article G.

25. An example would be that of a situation in which one party was free to withdraw from a contract on payment of a certain sum. There was no question of liability in such a case, which was separate from other events which could also trigger the liability to make a payment where there was no breach. It would be better if those concepts could be dealt with separately.

26. Mr. HARTKAMP (Observer for the Netherlands) said that, to some extent, he shared the concern expressed by the representative of Sierra Leone. If the agreed sum was to be payable even though the obligor was not liable for the failure of performance, the rules should allow the parties to include a provision to that effect. That could have the added advantage of preventing litigation. It was also important for the rules to forestall a possible injustice: the obligor could be required to pay a penalty in cases where there were damages for which he was not liable.

27. Article G should provide for a reduction in the agreed sum where it was manifestly excessive. The article should be redrafted to ensure that, in addition to the relationship between the loss suffered and the penalty, the reasons for the failure of performance would be taken into account by a court or arbitral tribunal. It would be unfair to require payment of the entire sum when the loss resulted from *force majeure*. Such a redrafting might go some way towards accommodating the concerns of the representative of Sierra Leone.

28. Mr. YEPEZ (Observer for Venezuela) said that the introductory words of article D should be deleted.

29. Mr. SZASZ (Hungary) said that article D clearly expressed the three ideas it was intended to express: the obligor had to pay only if he was liable for the failure of performance; there existed a burden of proof; the parties could agree otherwise. However, having heard the statements by other representatives, he could understand why the article gave rise to diverse interpretations. Although it was acceptable to his delegation as it stood, it was perhaps worded in too concise a manner. The three ideas to which he had referred might therefore be formulated in three separate sentences, instead of being compressed into one complex sentence.

30. The provisions of article G were applicable to articles D, E and F, as far as the agreed sum was concerned.

31. Mr. OLIVENCIA (Spain) said that he agreed in principle with the wording of article D. It was clear that the obligee was entitled to recover the agreed sum, except when the obligor was not liable. The article, like the uniform rules as a whole, related to general principles. While it could not cover every possible aspect of the question, it managed, in a very concise formulation, to take account of various legal systems. Article D embodied the basic principle that, within the framework of the concept of liability in relation to contracts, the parties were free to proceed on the basis of agreement.

32. Mr. ROEHRICH (France) said he had some difficulty with the statement that one of the three ideas expressed in article D was that the obligor had to pay only if he was liable for the failure of performance. It was no accident that the article had a negative formulation. The purpose of the provision was not to establish a comprehensive code on

liability, but to lay down certain principles on the validity of rules governing liquidated damages and penalty clauses. The affirmative formulation suggested by the representative of Hungary, to the effect that the agreed sum would be payable only if the obligor was liable, would not be satisfactory to his delegation.

33. However, he emphasized that, in his view, the parties were entitled to agree on another arrangement.

34. Mr. MUCHUI (Kenya) said that article D was quite straightforward. It underscored the principle of freedom of contract, the freedom of the parties to agree that compensation should be paid even when the obligor was not liable. The crucial question was whether delegations wanted that principle to be embodied in the article. Neither the deletion of the introductory words nor the inclusion of a new sentence stating which articles were mandatory would answer that basic question.

35. With regard to article G, the question was whether a court or arbitral tribunal would have the power to decide on the equitableness of compensation.

36. Mr. SAWADA (Japan) said that article D should make it clear that the burden of proof rested with the obligor.

37. Mr. MAGNUSSON (Observer for Sweden) said that he was sympathetic to the proposal to deal with the question of a contrary agreement between the parties in a separate sentence. However, article D as it stood, read in conjunction with article G, left no doubt that the agreed sum could be reduced in certain circumstances. It might be desirable, though, to redraft article G along the lines suggested by the representative of the Netherlands.

The meeting was suspended at 4.25 p.m. and resumed at 5 p.m.

38. Mr. PARK (Observer for the Republic of Korea) said that his delegation supported article D as it stood. It expressed a legal principle, often referred to as *faute commune*, that where the obligor was not guilty he should not be held responsible for failure of performance. In accordance with freedom of contract, the parties should be left free to include anything they wished in a contract, unless it conflicted with mandatory laws. Article D was still, however, subject to article G in respect of the intervention of the court on behalf of the weaker party. His delegation was prepared to go along with the United Kingdom proposal for a separate sentence, as long as the basic idea behind the article was retained.

39. He requested clarification as to whether the words "if the obligor is not liable for the failure of performance" should be understood as meaning partial as well as total liability. Throughout the draft, those two concepts were linked, but article D was silent on that subject. The scope of the article was therefore not clear, and in order to make it consistent with other articles and to specify that the obligee was not entitled to recover or to forfeit the agreed sum where the obligor was not liable for the failure of performance, some adjustment should be made to the draft. Furthermore, as the representative of Japan had pointed out, article D did not settle the question of the burden of proof. Although article F covered that subject adequately, he thought that some element of the subject should be reflected in article D.

40. Mr. BASNAYAKE (secretariat), replying to the question raised by the Observer for the Republic of Korea, said that the agreed sum would be stipulated for a particular failure of

performance, and if the obligor was not liable for that particular failure, the obligee would not be entitled to recover the sum.

41. Mr. SAMI (Iraq) said he agreed that the freedom of the parties should be respected in the implementation of a contract, but felt that the Commission should not go beyond that. It should not accept any condition, even if the condition were demanded by one of the parties. It was not logical or reasonable for a party to be expected to pay for damages when he was not liable for those damages. If the text was left as it was, it could open the door to further disputes and could create problems for both parties. In developing countries, when a contract was entered into with a company, the contract often stipulated that, in the case of non-execution by one of the parties, that party would have to pay a given sum to the party which had sustained damages. His delegation therefore supported the proposal made by the representative of Sierra Leone to delete the introductory words of article D.

42. With regard to the burden of proof, he said that that was something the Commission should allow to be determined by the legal system which was applicable in the case or, as the representative of France had proposed, that subject could be dealt with in an additional paragraph.

43. The CHAIRMAN said that the following aspects of article D had been touched on in the debate. The article provided that the obligor must pay an agreed sum in the case of failure of performance, but it also established the fundamental legal principle that the obligor could be excused from his obligation to pay if he was not liable for the failure of performance. One problem which it did not entirely clear up was that of the burden of proof, which could fall upon either party.

44. As the representative of the United Kingdom had pointed out, an agreement could be made between the parties which might furnish a different solution in the case of a failure of performance or for other reasons, and in such cases the article permitted the parties not to comply with the legal system set up in the Rules.

45. It appeared that the basic question before the Commission was whether the article should be left as it was or, as proposed by the representative of the United Kingdom, whether reference should be made to the general principle of freedom of contract in a separate article or even within the article itself. It was also necessary to include a provision to prevent the abuse of the rights of the weaker party. For that purpose, the Working Group and the secretariat had found an adequate solution in article G, the drafting of which could be adjusted in accordance with what was decided on article D.

46. He believed that there was general agreement on the basic principles expressed in the article but that the drafting led to conflicting interpretations. If the principles could be summed up in a more appropriate way, it might be possible to adopt the article.

47. Mr. SONO (Secretary of the Commission) said he understood that the Commission had tentatively agreed to retain article D as it was, but that in order to accommodate the wishes of some delegations which had expressed concern regarding a situation in which the obligor might have to pay compensation even if he were not at fault, consideration of that aspect would be taken up in connection with article G, paragraph (2), as suggested by the representative of the Netherlands. It appeared that the proposal to delete the words "unless the parties have agreed otherwise" was not generally

acceptable. There was a possibility that, as the representative of the Netherlands had suggested, the words "manifestly unfair" might be included at a later stage. With regard to whether or not the freedom of the parties to agree otherwise should be consolidated in the article, that problem had not been resolved but it could be dealt with later, when the Commission finalized the text.

48. Mr. LAVINA (Philippines) noted that several delegations had expressed reservations on the text of article D as it stood, and especially on its opening clause. It had been argued that that clause was illogical, since the law exempted the obligor from his obligations by reason of force majeure, and the parties could therefore not stipulate that the obligor must pay. His delegation had difficulty agreeing to the proposal to retain the article as it was and to make the necessary changes in article G.

49. Mr. SAWADA (Japan) said that the Chairman, the Observer for the Republic of Korea and his own delegation had touched on the question of burden of proof. Ideally, that issue should still be left to national law, without any addition to article D.

50. The CHAIRMAN said that article D did not distinguish the cases where liability or guilt occurred. The question of the burden of proof was not covered in article D and would thus fall within the purview of the applicable law.

51. Mr. CHAFIK (Egypt) said that he fully agreed with the Chairman. There was no question of proof. Article D was based on the assumption that the question of liability was resolved.

52. Mr. SONO (Secretary of the Commission) noted that the representative of the Philippines had entered a reservation about the emerging consensus. He drew the Commission's attention to the fact that, in the case of failure to perform, regardless of who was liable, one party must bear the risk. It was a question of allocation of risk. Traditionally, in most legal systems, in a case of *force majeure*, one party had to suffer. Which party depended on the situation.

53. If the Netherlands proposal for an addition to article G, paragraph (2), was adopted, unfair situations would be covered in that article.

54. It seemed reasonable to leave the question of the burden of proof to the applicable law. If the applicable law did not provide a rule, then the text of the Rules might prevail, and article D gave clear guidance in that regard. The obligor must prove that he was not liable for the failure of performance.

55. The CHAIRMAN said that the secretariat had incorporated that idea in the commentary. It would not be inconsistent to rely on the applicable law and to find a solution in the uniform law in cases where the applicable law did not provide an answer.

56. Mr. SAMI (Iraq) said that, unfortunately, the proposed addition did not give good guarantees, because the principle would remain untouched. His delegation, therefore, maintained its reservations. In the case of non-performance or delayed performance, one party suffered damage and not the other. That did not mean that the other party was not obliged to pay compensation, even if he was not at fault.

57. The CHAIRMAN said that, if there was agreement, the secretariat could record the Iraqi representative's observations and reservations.

58. Mr. SONO (Secretary of the Commission) explained the secretariat's envisaged course of action for finalization of the draft articles. All decisions tentatively agreed upon regarding the text would be reflected in the draft report of the Commission, and the revised text would be incorporated in the draft report. It would be unfortunate to leave the question without finalizing certain texts. It would expedite the matter if there was at least a tentative text.

59. While the secretariat could not foresee that all texts would be finalized at the current session, it hoped that articles D to G might be finalized, at least tentatively. In that case, it would be better to leave the question of scope for discussion at the next session, where the Commission would be able to agree on adopted texts in the form of a model law or convention. He noted that the last phrase of article A, paragraph (1), or the question of a need for a last phrase was still left open. The secretariat was willing to prepare texts if the basic discussion could take place at the current session. Otherwise, it would incorporate article A, paragraph (1), as revised, in the report, with the rest of the text undecided.

60. Mr. GUEST (United Kingdom) said that it was not clear whether the Commission would be asked, when considering its draft report, to approve the secretariat text as final or whether it would be made clear that the text would be regarded as tentative for subsequent approval. He hoped that the latter was the case.

61. Mr. SONO (Secretary of the Commission) said that it would be difficult for the Commission, when considering its report, to reopen the debate on the substance. Accordingly, the second course outlined by the United Kingdom representative would be followed.

62. He stressed, however, that the secretariat would not incorporate in the draft report any change that had not been agreed upon. For example, the text of article A, paragraph (1), would read: "This Convention applies to contracts in which the parties have agreed that, upon a total or partial failure by a party (the obligor), the other party (the obligee), is entitled to [recover, or to forfeit] an agreed sum of money and [...]". The report would indicate that the retention of the words "recover, or to forfeit" would be subject to the decision on the last, bracketed portion, as had been agreed.

63. The report would show the text tentatively agreed upon and show how it would look if drafted in a legal form.

64. Mr. CHAFIK (Egypt) asked what was the position of the Working Group which had prepared the text contained in document A/CN.9/218. If it was still in existence, it would be best to send the revised text back to it, with all the Commission's comments.

65. Mr. SONO (Secretary of the Commission) said that such a course would create technical difficulties, because the Working Group was currently preparing a model arbitration law. It would be difficult for the Commission to get authorization to establish another working group. He felt that

the Commission must now proceed to finalize the text. The substantive discussion had taken place in the Working Group. Moreover, consideration of the text by a working group consisting of only 15 States would not expedite its finalization.

66. Mr. DUCHEK (Austria) said that he supported the idea of incorporating the results of the Commission's discussion in the report, and the Commission would have no commitment with regard to what was described in the report as undecided.

67. He questioned the idea of placing a blank in square brackets in article A, because if no further work was done on the blank portion until the next session of the Commission, there was a risk that there might not be enough time for finalization. There had been some consensus on the wording of article A. The secretariat should not hasten to prepare a text. He proposed that the discussion should be continued, in the hope that a consensus might emerge, and that the secretariat should present, for the next session, a new draft on the basis of the discussion. At its next session, the Commission could then concentrate on the text and approve it.

68. Mr. SZASZ (Hungary) said that he could go along with any procedure suggested. It was natural that there should be differences of approach. It was the Commission's tradition, after hearing statements, to prepare a draft immediately, with the involvement of the different groups. That committed the groups to some extent, and then an effort was made to gain the approval of other delegations. It was impossible ever to win 100-per-cent support. He feared to go along with the procedure of resuming consideration of the question the following year, because the same situation would arise. The issue should not be left in the air and the burden left to the secretariat. It was essential to have a text which was backed by an important number of delegations. However, he did not insist on his point.

69. Mr. SEVON (Finland) said that, in one and a half days, the Commission had discussed one article, the easiest one, and part of a second. He did not feel that it would get through the draft articles. If it deferred consideration until the following year, there would be a change in membership and the Commission would have to start from scratch. He therefore supported the suggestion of the representative of Hungary that a small drafting group should be established and should submit texts to the Commission.

70. Mr. HARTKAMP (Netherlands) and Mr. ROEHRICH (France) supported the proposal made by the representatives of Finland and Hungary.

71. Mr. SEVON (Finland) proposed that the secretariat should make suggestions, at the opening of the next meeting, for the composition of the drafting group.

72. *It was so decided.*

The meeting rose at 6 p.m.

260th meeting

Friday, 30 July 1982, at 10 a.m.

Chairman: Mr. EYZAGUIRRE (Chile)

[A/CN.9/SR.260]

The meeting was called to order at 10.15 a.m.

**INTERNATIONAL CONTRACT PRACTICES:
DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES
AND PENALTY CLAUSES (continued)
(A/CN.9/218, A/CN.9/219 and Add.1)**

1. The CHAIRMAN recalled that, at the previous meeting, it had been proposed that an informal drafting group be set up to consider all the views put forward on the draft uniform rules at the current session. If he heard no objections, he would take it that the Commission agreed to set up such a drafting group composed of the representatives of Egypt, Finland, Hungary, Sierra Leone, Spain and the United States and open to any other representative who wished to participate.

2. *It was so decided.*

Article E

3. Mr. BASNAYAKE (secretariat), introducing article E of the draft uniform rules, explained that the article dealt with the question of how to regulate the relationship between the remedy of recovering the agreed sum and the remedy of enforcing performance of the obligation. In formulating that article, the Working Group had taken into account two principles: what was the normal intention of the parties in formulating the rules and what would be the fair result to be achieved in deciding on a possible combination of remedies.

4. Thus, paragraph (1) was designed to ensure that performance, although delayed, did take place at some point in time. The obligee might suffer loss as a result of such delay and the agreed sum would compensate him for it; provision for payment of such a sum would also encourage the obligor to perform on time. It was therefore reasonable for the obligee to be able to secure both performance and agreed compensation for the loss arising from any delay.

5. The key to paragraph (2) was the proviso "unless the agreed sum cannot reasonably be regarded as a substitute for performance". The agreed sum could reasonably be regarded as a substitute for performance when it was equivalent to performance and compensated for all losses arising from non-performance. In such cases the obligee had the option of recovering the entire sum, as a substitute for performance, or requiring performance, but was not entitled to both remedies. On the other hand, if the proviso was applicable and thus the agreed sum could not reasonably be regarded as a substitute for performance, the rationale for offering the obligee one or other option disappeared and both remedies became available to him. Some States had commented in documents A/CN.9/219 and Add. 1 that the paragraph as currently drafted might not lend itself to such an interpretation, but it was his firm understanding that that interpretation had been what the Working Group intended.

6. Paragraph (3) simply allowed parties to vary the rules set forth in paragraphs (1) and (2).

7. It was also his understanding that, when paragraphs (1) and (2) stated that the obligee was entitled to performance, that did not mean that, in countries whose legal system did not normally enforce performance, the obligee would be entitled to demand it. The entitlement to performance would not be available to the obligee in such cases and instead what was probably envisaged was the solution in article 28 of the Sales Convention.

8. Mr. CUKER (Czechoslovakia) said that his delegation had certain doubts concerning article E. So far, the Commission's work had been based on the principle that the rules governing the nature of guarantees must be combined with those governing compensation for damages. Paragraph (2), however, provided no compensation for damages or loss suffered as a result of non-performance or defective performance. Since, in practice, non-performance always began with a delay in performance as envisaged in paragraph (1), the combination of the two paragraphs was confusing and could create doubts as to how obligations arose at the beginning of a case of non-performance. It might be necessary for the parties to a contract, at the time of concluding that contract, to agree clearly on the intention of the compensation and penalties provided for therein.

9. The objectives of paragraph (2) could be achieved by means of a broadly formulated paragraph (1), combined with articles F and G. Paragraph (2) should therefore be deleted and paragraph (1) redrafted in broader terms to cover all cases of non-performance to which the agreed sum applied under the terms of that paragraph.

10. Mr. SAWADA (Japan) said that, while he appreciated the intention of paragraph (2), he had problems with its drafting. The paragraph should simply state when the obligee was entitled to recover or forfeit a given sum and when he was not. The formulation proposed by Norway in paragraph 7 of document A/CN.9/219/Add.1 was therefore more appropriate. Japan had suggested an alternative wording for that article which would also affect articles F and G, and he would like to submit that alternative in writing to the drafting group just established.

11. Mr. BASNAYAKE (secretariat) explained that the Working Group had held in-depth discussions and negotiations on article E. One of the main difficulties with that article lay in the fact that some countries' legal systems always conferred the right to performance, and their delegations therefore had wanted that right to be the *prima facie* right in article E. Other delegations had held quite the opposite view and the Working Group had had to strike a balance between the two positions.

12. Mr. GUEST (United Kingdom) said that he doubted whether the content of article E was a question on which unification was either necessary or desirable. The issues raised by paragraphs (1) and (2) would generally depend on the construction of the relevant clause in individual contracts. His delegation, like that of Czechoslovakia, had had doubts about the need to lay down specific rules, especially after hearing Mr. Basnayake's introduction to article E.

13. In view of Mr. Basnayake's latest comment, however, and of the diversity of legal approaches that existed, he now believed that some sort of régime was needed to bridge the

gap between those different approaches. That gap was very wide, however, and could have repercussions on aspects of law and questions of attitude in different legal systems. The compromise offered by the present draft was not totally satisfactory, as could be seen from the comments made in paragraphs 26 to 30 of document A/CN.9/219, in particular those made by Spain. As currently drafted, article E was too rigid; it should take account of the relevant clause in each individual contract and the way in which a national court would approach the question of the relationship between performance and the agreed sum.

14. Mr. VOLLZEN (Observer for Switzerland) said that, if a rule was to be drafted on the subject, it should be better structured. Article E was designed to govern the relationship between performance and the agreed sum. Now, as currently drafted, paragraph (1) made such a relationship cumulative while paragraph (2) made it alternative in most cases but cumulative in some. Article F also made the relationship alternative, but cumulative in some cases. Article E would gain considerably in clarity, if it was limited to the relationship between the main obligation and the agreed sum and stated clearly whether, in general, that relationship was to be alternative or cumulative. If, as a general rule, it was to be alternative, a list of exceptional cases in which it would be cumulative could be added.

15. Finally, paragraph (1) provided for entitlement to both performance and the agreed sum in cases of delay in performance. There might, however, also be situations where the obligee suffered a loss not from delay but from performance of the obligation in a place other than that stipulated in the contract. In such cases, too, the obligor should be liable to pay compensation for the loss incurred, in addition to being required to perform.

16. Mr. JOKO-SMART (Sierra Leone) observed that article E envisaged three different forms of breach of contract: delay, non-performance and defective performance. The legal consequences of delay, as set forth in paragraph (1), were perfectly clear. Paragraph (2), on the other hand, was not very clear as to the consequences of non-performance and defective performance and seemed to provide for the same remedies in each case. Such a formula did not seem fair. The remedy for non-performance should be either performance or recovery or forfeiture of the agreed sum. In the case of defective performance, however, it would be asking too much of the obligor to require performance when he had already proved unable to perform. In such a case, it would be better to provide only for recovery or forfeiture of the agreed sum.

17. Mr. BYERS (Australia) asked whether it had been the Working Group's understanding that paragraph (2) should not create a mandatory rule entitling the obligee to performance in countries whose legal system did not provide for such entitlement.

18. Mr. Basnayake (secretariat) explained that the Working Group had not actually discussed that point but that it had been understood that, where a country's legal system did not permit the remedy of demanding performance, that remedy would not be available.

19. Mr. SEVON (Finland) said that he was curious to know whether the secretariat had found any clause in current contract practice in which the questions raised in article E were left unresolved. Clearly a model law must address itself to those questions.

20. Moreover, since he felt that paragraph (2) should not deal with the right of the obligee to demand performance, he

preferred the formulation proposed by Norway in paragraph 7 of document A/CN.9/219/Add.1. There was also merit in the Soviet proposal in paragraph 28 of document A/CN.9/219, for there might often be situations which did not involve a clear-cut case of applying one remedy over another. If the Commission pursued the course suggested by the Soviet Union, it might also be able to deal with the problem raised by Sweden, namely that it was not always easy to determine whether a case involved delay or rather defective performance; in the latter case, the obligee might reasonably be entitled to part of the agreed sum in addition to performance.

21. Mr. PERILLO (United States of America) sought clarification as to whether the phrase "entitled to performance" meant that a court could order performance. His understanding of the Working Group's intention was that, if performance was not forthcoming, one was entitled to some sort of remedy, which might be that of damages. Consequently, the Soviet Union's request for clarification on that requirement of performance might have been because it did not have the same understanding of the Working Group's intention.

22. The extreme difficulty of finding a satisfactory wording to meet the concerns addressed in the article arose from the fact that some legal systems relied on penalties as an inducement to performance. In addition to the penalty, the performance had to be rendered. Other legal systems, like that of the United States, held that a breach of contract should not be penalized. While article E was not totally satisfactory, it would be hard to produce a text that would satisfy all the diverse legal systems represented in the Commission.

23. Mr. HARTKAMP (Netherlands) said that he had no problems with the substance of the article. His delegation's views submitted in writing had been merely of a drafting nature but had not been correctly reflected in the secretariat's analysis. Paragraph (2) of article E provided no solution to a case in which the proviso applied. It merely stated that the obligee was entitled to performance or to recovery of the agreed sum; it did not state what should happen if the proviso applied. That event raised two possibilities: either the obligee was entitled to both performance and the agreed sum or was entitled neither to performance nor the agreed sum. Obviously, the intention was that the obligee should be entitled to both. A slight drafting change could be made to rectify the anomaly by adding to the text the phrase "in the latter case"—i.e., where the proviso applied—"he is entitled to both performance of the obligation and the agreed sum".

24. The wording proposed by Norway (A/CN.9/219/Add.1, para. 7) implied a substantive change which his delegation could not accept. By stating that the obligee was entitled to the agreed sum but was not so entitled if performance had been effected, the Norwegian proposal left open the case where once the agreed sum had been paid the obligee was no longer entitled to performance.

25. While his delegation accepted the substance of article E, it found nowhere in the article the stipulation that, if the proviso applied, the obligee was entitled to both performance and the agreed sum.

26. Mr. LAVINA (Philippines) agreed with the approach taken to the problem by the representative of Sierra Leone. The main point of article E was that the obligee should be compensated for delay, defective performance or non-performance. In the case of defective performance, the obligor should be obliged to perform and also to pay the agreed sum to compensate for the defective performance. In the case of non-performance, the obvious recourse was recovery or forfeiture of the agreed sum.

27. He agreed with the comments made by the representative of the Netherlands regarding the Norwegian proposal. The second sentence of that proposal did not cover defective performance, which should likewise be compensated.

28. Mr. WAGNER (German Democratic Republic) said that his delegation would like to formulate paragraph (2) in a positive manner and replace the proviso "unless the agreed sum cannot reasonably be regarded as a substitute for performance," by "if the agreed sum can reasonably be regarded as a substitute for performance". Furthermore, regarding the obligee's choice between performance and recovery of the agreed sum, his delegation supported the Soviet suggestion that, whenever the obligee requested performance, he nevertheless retained the right of compensation for losses suffered.

29. Mr. ROEHRICH (France) said that on the whole, his delegation found the wording of article E fairly well balanced between the various legal systems. He agreed with the representative of the United States that it was the most business-like way of reconciling the various approaches. He endorsed the view expressed by the representative of the Netherlands that the Norwegian proposal concerning paragraph (2) involved substantive rather than drafting changes. The obligee should have the choice of either performance or recovery of the agreed sum. As regarded performance, the representatives of the United Kingdom and the Union of Soviet Socialist Republics had expressed concern that performance might be ordered by the court. It was better not to discuss means of securing performance. In France, if the obligation to perform could not be discharged then damages had to be paid to the obligee. Had the text reflected that notion, his delegation could have endorsed it.

30. Mr. BASNAYAKE (secretariat), referring to the drafting proposal made by the representative of the German Democratic Republic, noted that the obligee's choice would depend on the satisfaction of the condition that the agreed sum could reasonably be regarded as a substitute for performance; however, if the sum could not reasonably be so regarded, both remedies should be available. Words to that effect should be incorporated in the proposal if it were adopted.

31. Mr. BYERS (Australia) said that, under a common-law system, the obligee would normally be entitled to an order for the agreed sum and not to an order for performance. Under a civil-law system, he would be entitled either to performance or the agreed sum but not to both. When the proviso operated in a common-law system, one could not have both an order for performance and the agreed sum. Each system had radically different remedies and results. It would be worth stating clearly the consequences in cases where the proviso applied, as well as in cases where the application of article G reduced the amount of the agreed sum.

32. Mr. OLIVENCIA (Spain) said that failure to perform an obligation could be divided into a number of categories ranging from complete non-performance through defective and partial non-performance to irregular non-performance. His Government's response in document A/CN.9/219, paragraphs 29 and 30, combined the expectations of the parties when drafting the contract with cases of non-performance.

33. In the case where the parties had provided for non-performance but partial or irregular non-performance occurred, the obligee would have a right either to demand performance of the rest of the obligation or to avail himself of the indemnity or penalty clause. If the first option were available under the applicable legal system, there would be no problem.

If the obligee had recourse to the penalty clause, he would be demanding the part of the performance carried out and in addition the sum agreed by the parties should non-performance occur. His Government had suggested that article G should be regarded as a moderating clause since it would be unfair for the obligee to keep, in such a case, the part of the performance received and to demand *in toto* the implementation of the penalty clause. His delegation agreed with the penalty clause, but the penalty could not be claimed or demanded simultaneously or cumulatively with completion of the performance unless otherwise agreed.

34. Mr. BASNAYAKE (secretariat) said that, where a penalty was fixed for complete non-performance and defective non-performance occurred, or it was fixed for defective non-performance and complete non-performance occurred, since the breach envisaged had not occurred, the penalty question did not arise: a penalty was payable only on breach of a specifically defined obligation. If that particular breach of obligation had not occurred, the matter was open to general damages or other forms of remedy.

35. Mr. AKINLEYE (Nigeria) said that his delegation agreed with the representative of the United States that, even though the wording of subparagraph 2 of the article as it stood was not ideal, it would be hard to reformulate it in such a way as to cover all the legal systems involved. He suggested, however, that paragraph (2) might be divided into two parts, one part could state that, where the proviso applied, the obligee would be entitled to performance or recovery of the agreed sum; the other part could state that, where the agreed sum could not be regarded as a substitute for performance, the obligee would be entitled to both. That would make the intention behind the proviso clear and he strongly recommended such a change to the drafting group.

36. Mr. SCHMID (Federal Republic of Germany) said that his delegation had no serious difficulties with the substance of article E. While it could be improved by the drafting changes proposed by the delegation of the Netherlands, his own delegation could accept the article as it stood.

37. Mr. GUEST (United Kingdom) said he wondered how paragraph (2) would operate in a common-law system. If the object of the first part of the paragraph was that the agreed sum was to be an alternative to performance, then the proviso, which made the agreed sum and the performance cumulative, could not apply.

38. The representative of the secretariat had stated that the word "entitled" was not intended in a common-law system to mean that the court would be bound to award specific performance. The inference was that in a common-law system where specific performance would not be granted, the words "entitled to performance" would mean "entitled to damages for non-performance" or "entitled to damages for defective performance". The obligee would therefore be entitled to choose either damages for non-performance or defective performance, or to choose the agreed sum. In the situation where the agreed sum had been fixed as liquidated damages, the result would be that the obligee could opt either for damages or the agreed sum, whichever was the larger. The damages would obviously be subject to article F, which established a somewhat different régime. He sought clarification from the secretariat as to whether his reasoning so far had been correct.

39. Mr. BASNAYAKE (secretariat) said that in the situation where the proviso did not apply, the obligee would be entitled to the agreed sum or to performance. In a legal system in

which the court did not order performance, there would be only the entitlement to claim the agreed sum. Where accumulation was possible, the position would be that, as stated by the delegation of Australia, the obligee would still be restricted to the agreed sum. It could well be that the obligee had been unwise enough to fix a very low sum and that that sum did not provide adequate compensation, but the intention was to restrict him to the agreed sum.

40. Mr. GUEST (United Kingdom) said that he was not so much concerned with the question of accumulation as with the two alternative remedies which appeared to be open to an obligee. The interpretation given was that entitlement to performance existed only if performance could be decreed by the legal system in a particular country, something that the draft did not make clear.

41. Mr. YEPEZ (Observer for Venezuela) said that his delegation had certain problems with the article as it was currently drafted and also felt that it might be difficult to combine the various ideas which had emerged during the discussion. The article could, of course, be drafted in very broad terms, but that would not give a sufficiently precise text. An effort had to be made to clarify the positions so that each of the three possible cases—failure to perform, delay in performance and defective performance—had its own solution. In particular, paragraph (2) of the article had to be clarified and the interpretation, application and consequences of the final proviso had to be amplified. His delegation was also unhappy with the use of the word “obligee” in article E and elsewhere in the text. In any contract, each party undertook obligations toward the other and was thus both an obligor and obligee. It would therefore be preferable to state that, if one party did not fulfil his obligations, the other party had certain rights and remedies available to him.

42. Mr. SZASZ (Hungary) said that his delegation could accept the over-all régime provided for in article E. As far as the application of that régime was concerned, he said that it was important to make it clear in the commentary that the purpose of the article was simply to clarify the relation between performance and the agreed sum and not to deal with the question of damages. He agreed with those representing countries with a common-law system that paragraph (2) did not differentiate between systems under which it was possible to go to court for performance and those in which the court could only award damages. That should be clarified by means of an additional clause.

43. On a different note, he felt that it should be pointed out that article E did little to promote the unification of law, since the fate of parties to a contract would be different depending on the legal system prevailing in the countries concerned. Finally, he said that, in the interests of clarity, the final proviso of paragraph (2) should be drafted as a separate sentence.

The meeting was suspended at 11.50 a.m. and resumed at 12.20 p.m.

44. Mr. DUCHEK (Austria) said that the system provided for in article E was acceptable to his delegation. Paragraph (2), however, needed to be clarified and improved. In that connection, he agreed with the analysis made by the representative of the Netherlands and recommended that his formula should be considered. He did not feel that the proposal made by the representative of Norway met the point at issue. As the draft stood, two different interpretations were possible, and it was therefore essential that the Commission should make its intention clear.

45. Mr. OLIVENCIA (Spain) said that his delegation still had problems concerning cases which might arise under article E, paragraph (2). He was unhappy with the distinction made between non-performance and defective performance other than delay, since that could cause complications if, for example, a contract contained a clause referring to “any case of non-performance”, in which case non-performance could cover defective performance. Under various systems, a court could use its influence to moderate the implication of a clause covering both non-performance and defective performance other than delay where one party had only partly performed his obligation. Instead of having two distinct possibilities in paragraph (2), it might be better to refer to any failure to carry out a contract properly.

46. Mr. CHAFIK (Egypt) said that his delegation would have no problems with article E if certain drafting changes were made. He noted the distinction made between delay in performance and defective or non-performance. However, while special rules existed for delay in performance, there was no special régime covering defective performance. There was no point in mentioning defective performance if there were no special conditions governing it. He expressed concern at the implication of the final proviso contained in paragraph (2) that, in the event that the agreed sum could not reasonably be regarded as a substitute for performance, the obligee would be entitled to both the agreed sum and performance. He felt that that was excessive, since it meant that the obligee would obtain somewhat more than complete satisfaction. He could, however, agree to the proviso if suitable modifications were made. He would reserve his position on the matter until article G had been fully discussed and a final decision taken.

47. Mr. SAWADA (Japan) supported the proposal made by the representative of Norway, feeling that it was sufficient to state in paragraph (2) when entitlement to payment existed and when it did not. That proposal seemed to be a logical solution.

48. Mr. RAO (India) said that the provisions of article E were reasonable, and he did not wish to see any changes made to the draft. He noted the importance of paragraph (3), which gave parties to a contract the freedom to reach a different agreement, thus accommodating legal systems where performance could not be enforced.

49. Mr. BASNAYAKE (secretariat), replying to a matter raised by the representative of Czechoslovakia with regard to the word “non-performance” in article E, paragraph (2), said that, in situations where there was difficulty in ascertaining whether a case fell under paragraph (1) or (2) owing to uncertainty as to whether it was a question of non-performance or delay, the matter would have to be settled by the authority handling the dispute. The arbitrator or court might enter an order for performance, in which case it would be a question of delay, or, in cases where performance was no longer possible, the remedies for non-performance would come into play.

50. Mr. CUKER (Czechoslovakia) said it appeared to him that paragraph (2) envisaged cancellation of the contract owing to non-performance. He wondered what possibilities there were, following cancellation of the contract, with regard to actual performance or payment of a sum of money.

51. Mr. BASNAYAKE (secretariat) said that, in the case of non-performance or delay, it might not be possible to rely on any contractual remedy under the applicable law. However, it might be possible to rely on the penalty, despite cancellation or termination. He did not believe that the draft attempted to

determine what happened in the case of cancellation or termination.

52. Mr. GOH (Singapore) said that his delegation supported the views expressed by the representatives of countries with the common-law system and had particular difficulties with regard to paragraph (2). He suggested that a note should be inserted to clarify the meaning of the concept of entitlement to performance in that paragraph. It seemed that there was a basic contradiction in paragraph (2), since an obligee who was unable to perform could not be expected to perform. However, in view of the difficulties involved, his delegation was ready to support any suitable compromise.

53. His delegation did not agree with the view expressed by the representative of India that paragraph (3) was an escape clause for the parties to a contract. In most cases the parties would not make any contrary agreement, since they would assume that the law would regulate their transaction.

Article F

54. Mr. BASNAYAKE (secretariat), introducing article F of the draft uniform rules on liquidated damages and penalty clauses, explained that that article regulated the relationship between the right to obtain an agreed sum and the right to obtain damages for breach of contract. The obligee would be able to discharge his burden of proof in only a limited number of cases, and the agreed sum would therefore be maintained.

55. Mr. PERILLO (United States of America) said that the normal situation was reversed in article F since the normal rule was that, unless otherwise agreed, the amount of damages to be paid should not be increased; it was common practice to include penalty clauses in which liability was limited.

The meeting rose at 12.55 p.m.

261st meeting

Friday, 30 July 1982, 3.30 p.m.
Chairman: Mr. EYZAGUIRRE (Chile)

[A/CN.9/SR.261]

The meeting was called to order at 4 p.m.

INTERNATIONAL CONTRACT PRACTICES: DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES AND PENALTY CLAUSES (continued) (A/CN.9/218, A/CN.9/219 and Add.1)

1. Mr. GOH (Singapore) said that in his country's legal system it was a rule of law that, where a contract provided for liquidated damages payable upon failure of performance, the obligee was entitled to liquidated damages and no more. That was acceptable, because it was felt that the liquidated damages were a genuine pre-estimate of loss in the case of non-performance. His delegation felt that, if the Commission approved article F as it stood, that would open the door to claims for sums much greater than those originally agreed upon.

2. Mr. JOKO-SMART (Sierra Leone) said that his delegation found article F as acceptable as it stood. However, if the obligee was to be entitled not only to the agreed sum but to a further amount, it would be equitable to provide that, where the obligor was able to prove that less damage had been suffered, an amount less than the agreed sum should be paid.

3. Mr. PERILLO (United States of America) associated himself with the comments made by the representatives of Sierra Leone and Singapore. His delegation viewed the liquidated damages clause as serving a variety of purposes. One was certainty and simplicity and another the avoidance of litigation. However, if article F was to provide that excess damages might be paid, then the whole planning structure of the contract would be destroyed.

4. Article F as it stood made the opposite presumption to what was desirable. The general rule should be that the obligee was not entitled to damages in respect of the loss not

covered by the agreed sum. Article F, however, placed the accent on the recovery of additional damages. He would prefer the accent to be on the general rule.

5. Mr. BASNAYAKE (secretariat) said that that question had been discussed in the Working Group. It had been felt that the opening words of article F might take care of the point raised by the United States representative. To indicate that the liquidated damages constituted a ceiling would be sufficient to exclude excess damages.

6. Mr. MUCHUI (Kenya) associated himself with the comments made by the representatives of Singapore, Sierra Leone and the United States. Obviously, article F gave undue advantage to the obligee *vis-à-vis* the obligor.

7. Mr. DUCHEK (Austria) said that his delegation had no problem with the system as drafted. He understood that the United States representative felt that some compromise was needed concerning the subject-matter of article F, and that that concern could be met by changing the order in which the ideas were presented. His delegation in fact favoured the presentation suggested by the United States.

8. Mr. SEVON (Finland) drew attention to the comment by the Netherlands in paragraph 8 of document A/CN.9/219/Add.1, in which a drafting change to article F was proposed, namely, that the article should state only that, in the circumstances specified therein, the obligee was entitled to damages to the extent of the loss not covered by the agreed sum.

9. He had seen the draft text prepared by the Working Group, and there were a number of passages with which his delegation was not satisfied. In his opinion, the draft as a whole constituted a compromise; if it was altered to conform to the common-law systems at all points, it would no longer be a compromise.

10. Mr. GUEST (United Kingdom) said that the representative of Finland had given the Commission a salutary reminder that the purpose was to find a reasonable solution,

not necessarily one which was acceptable to one system or another. If the parties to a contract stipulated that, in the case of failure of performance, a certain sum was to be paid, the natural inference was that, if failure occurred and one party sustained loss, he was to recover the agreed sum, the agreed sum forming the upper limit of the liability of the other party.

11. As an earlier speaker had said, a contract was sometimes a method of forward planning. A contract might be concluded in order to regulate a relationship and plan for the contingency of a breach and exposure to liability. He preferred to have as a main rule a provision that, if failure occurred and was covered by liquidated damages, the parties should be presumed to agree that that sum only was recoverable. There might be a situation where that was not the intention of the parties, but such a situation would be reflected in the contract, and if the parties had so agreed, there was no reason why effect should not be given to their agreement.

12. Article F, on the contrary, established a rule allowing the agreed sum to be increased in special circumstances, unless the parties had agreed otherwise. He preferred a régime comprising two clauses. First, where the parties stipulated that the agreed sum might be recovered or forfeited for non-performance, that sum only was recoverable. Secondly, where it appeared from the contract that the parties did not intend that the agreed sum should form the upper limit but that the full loss should be recoverable, it should be open to the obligee to claim damages in excess of the agreed sum.

13. Mr. OLIVENCIA (Spain) said that his country followed the civil-law system of codified law. He did not understand, in those terms, the transaction covered in article F, because, under his country's legal system, the solution was the same as that proposed by the representative of the United States and others from common-law countries. In the civil-law countries, the clause which was used replaced entitlement to damages unless the parties to a contract agreed otherwise. That would be the exact reverse of article F as it stood. One solution advanced would accord with the Spanish civil-law system, i.e., unless the parties agreed otherwise, the liquidated damages clause would apply.

14. The system of the proposed convention or model law had to be viewed as a whole, and there was a need to consider articles F and G together. While article F empowered the obligee to recover the greatest possible damages when they grossly exceeded the agreed sum, article G established moderation. Any compromise solution should take into account the rules set forth in articles F and G. His delegation's position was the opposite of what was provided in article F as it stood. If the solution arrived at came too close to the common-law system, he did not feel that it would be a compromise solution. He would accept a compromise, but so far he had heard more critics than supporters of the régime provided for in article F.

15. Mr. BYERS (Australia) said that it would be unwise to stray too far from the language of the Working Group unless there were strong reasons for it. According to the text, the rule was that the agreed sum was the measure of reimbursement. In exceptional cases, a larger sum might be recovered if there was a gross disproportion between the loss suffered and the agreed reimbursement. That seemed reasonable to his delegation. It established a contractual situation in all cases except when a gross disproportion occurred. He supported the text of article F as it stood.

16. Mr. LAVINA (Philippines) said that delegations should set aside their national law systems for the moment and try to

harmonize legal rules on damages. In article F, the main idea was that, if the agreed sum was demonstrably less than the loss suffered, the obligee would be entitled to additional damages. That was a fair arrangement, and he agreed with the text submitted by the informal drafting group. He could agree with any proposals to improve it, such as the United Kingdom proposal or the Netherlands proposal contained in document A/CN.9/219/Add.1, and any new additions based on those proposals.

17. Mr. MAGNUSSON (Observer for Sweden) said that there might be different types of agreement, as pointed out by the United Kingdom representative. In some cases, the contract might need to be adapted in order to take account of circumstances; for example, not only might the loss exceed the agreed sum but gross negligence on the part of the obligor might have occurred.

18. Mr. ROEHRICH (France) said that the approach taken by the Working Group represented a satisfactory compromise between different systems. The main point of article F was to determine those cases in which the obligee could receive more than the amount agreed upon. The existing wording of the article should therefore be retained, although some drafting improvements were possible in the light of the observations made by members of the Commission. The words "Unless the parties have agreed otherwise," should be deleted, bearing in mind that the case provided for in the article should be one of those in which the parties agreed otherwise and that the article therefore dealt, in principle, only with those cases where the parties had not reached a specific agreement.

19. The obligee should be entitled to damages greater than the agreed sum only if he could prove a loss which greatly exceeded that sum. His delegation agreed with the views expressed by the representative of the Netherlands on what constituted the agreed sum. The Commission was merely trying to cover those cases where the obligee could recover more than that amount.

20. Mr. VOLLZEN (Observer for Switzerland) said that article F would enable the obligee to recover a sum in excess of the agreed sum only if he could prove that his loss had greatly exceeded that sum. Nevertheless, the article seemed to give no thought to the question of liability for failure of performance, and he asked whether that aspect had been deliberately omitted.

21. Mr. BASNAYAKE (secretariat) said that article F did, in fact, presuppose a failure of performance. The words "if a failure of performance in respect of which the parties have agreed that a sum of money is to be recoverable or forfeited occurs," qualified the right to recover the agreed sum and the right to recover damages in excess of that sum if the conditions for recovery were satisfied.

22. Mr. SZASZ (Hungary) said that the text of article F represented an acceptable compromise between those legal systems which approached the question from the point of view of the pre-estimation of damages and those which stressed the purpose of the sum as being to secure performance. From the latter point of view there was no need for the corollary that if the loss incurred was lower, there was no need to pay the agreed sum.

23. His delegation had agreed to accept a solution which was not contemplated in Hungary's own legal system and which was closer to those which stressed the liquidated damages element. What appeared logical in the context

depended largely on how the question of the agreed sum was approached. In the Working Group, the developing countries had argued in favour of a solution granting the right to request excess damages even if there was an agreed sum. His delegation agreed with those which had expressed a preference for omitting the opening words of the article.

24. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics) said that article F represented a compromise, reached after long debate. In the Soviet system it was always possible to claim damages when the loss incurred exceeded the agreed sum. Article F should be viewed in conjunction with article G, under which it was possible to reduce the agreed sum where it was disproportionate to the loss actually suffered. The two articles together represented a balanced approach, so that the Commission might well adopt a less exigent attitude towards article F.

25. Mr. CHAFIK (Egypt) said that the Working Group had attempted, in the text of article F, to strike a balance between the situation of an obligee who had suffered a loss far in excess of the agreed sum and that of an obligor who would have to pay a sum greatly exceeding the loss incurred by the obligee. Where there was a pre-estimate of damages, or an agreed sum in the case of damages, it amounted to a limitation of liability, and it was unlikely that any court would award a higher sum. The situation would be different if both parties had agreed that higher damages could be recovered.

26. Mr. SCHMID (Federal Republic of Germany) said that there were different ways of viewing the agreed sum. In his opinion, it was primarily a penalty. In the Federal Republic the aim of such penalty clauses was to ensure performance of the contract and not to provide a pre-estimate of damages, so that the law of the Federal Republic went somewhat beyond the provisions of article F. Nevertheless, the article was acceptable to his delegation.

27. Mr. GUEST (United Kingdom), referring to the question of whether the power to exceed the agreed sum applied only where there was liability for the failure of performance, said that in discussing article D the Commission had approved the principle that the agreed sum should not become payable if there was no liability, although the parties might agree otherwise. For example, in the case of *force majeure*, the parties could arrange in advance how any loss would be apportioned. In general, the Commission had supported the idea that the parties should be free to provide for payment in such a situation. It had also been established that article G would apply in such situations.

28. The question then arose, of whether article F applied to situations in which the parties had agreed that in the event of *force majeure* a certain sum should be payable by one party to the other, or that one party could buy itself out of the contract. That, in turn, raised the question of whether, if one party could show that his loss greatly exceeded the agreed sum, he could recover damages.

29. It seemed from the words "and is entitled to damages to the extent of the loss not covered by the agreed sum" that article F would not apply in such a case, although a considerable amount of deduction was needed to reach that conclusion. In any event, there should be no risk of the agreed sum being increased in the case of non-liability.

30. Mr. JOKO-SMART (Sierra Leone) said that the Commission appeared to have gone into a discussion of unjustified enrichment, which was not permissible under

many common-law systems. The argument for accepting article F as it stood was that the obligee should not be made to suffer any loss because of a breach by the obligor, so that he would receive full compensation for his loss. His delegation supported the argument that the obligee should be entitled only to reparation for the loss he had suffered. Yet an explanation was required of the view whereby if the loss exceeded the agreed sum a party could recover the full amount of the loss, but where the loss was less than the agreed sum the party should still receive the full amount of the agreed sum. No legal system could tolerate such an iniquitous situation.

31. Mr. SEVON (Finland) said that article F should not deal with the question of whether the obligee was entitled to the agreed sum or with that of the circumstances in which the obligee would be entitled to damages, when the issue of the relevant law would arise. The article merely stated that damages might be available in excess of the agreed sum in certain circumstances. If that view was correct, the article failed to deal with the question of whether the obligee was entitled to damages in excess of the agreed sum in cases where there was an intentional breach of contract or gross negligence.

32. It had been suggested that provision should be made for reducing the agreed sum where the loss incurred was smaller. In his view, the agreed sum should be an incentive for the debtor to perform, and in any event, article G was intended to deal with that very situation, so that the system as proposed would operate in a just way. It was quite acceptable to his delegation.

33. Mr. ROEHRICH (France) said that article F should focus not on the reasons why the agreed sum was due, but on what the obligee was entitled to. Article A stated the circumstances in which the parties were entitled to recover or to forfeit an agreed sum of money. Since article F was concerned with the entitlement to damages in excess of that sum, there was little need for it to refer to the concept of failure of performance, already dealt with in article A.

34. The representative of Finland had made very pertinent remarks concerning article F.

35. Mr. SAWADA (Japan) said that the spirit and substance of article F were acceptable to his delegation, which would suggest only a drafting change. The second half of the article should be amended to read: "...in respect of the failure, to recover or forfeit the sum, and is not entitled to damages to the extent of the loss not covered by the agreed sum, unless he can prove ...".

36. Mr. HU (Observer for China) said that since the agreed sum had to be estimated in advance, it could later prove to be inadequate. If the difference between the loss and the agreed sum was minor, the obligee should be entitled only to that sum. If, however, the loss grossly exceeded the agreed sum, the obligee should be entitled to an appropriate increase in the damages payable. That was the only fair and reasonable approach.

37. Mr. VOLIZEN (Observer for Switzerland) said that, according to article F, the obligee was entitled to damages to the extent of the loss not covered by the agreed sum, but only if he could prove that his loss grossly exceeded the agreed sum. That would be fair only in cases where it was the obligor's fault that the loss exceeded the agreed sum. In other cases, the provision could clearly work unfairly against the obligor.

38. The CHAIRMAN said that, if he heard no objections, he would take it that the Commission agreed to refer article F to the Drafting Group and to request it to take into account the views and suggestions of delegations.

39. *It was so decided.*

40. Mr. BASNAYAKE (secretariat) said that he understood that the Commission had reached the following consensus: it should be clarified that, under article F, the obligee would be entitled to damages in excess of the agreed sum, where there was an entitlement to an agreed sum under the applicable provisions and where the loss grossly exceeded that sum. He also understood it to be the Commission's consensus that redundant references to the conditions in which the agreed sum was payable should be deleted.

Article G

41. Mr. BASNAYAKE (secretariat) said that article G was intended to provide a controlling mechanism with respect to an agreed sum that was considered excessive. One of the main reasons for agreeing on a sum was to make the extent of liability clear. That principle was embodied in article G, paragraph (1).

42. Paragraph (2) stated the two conditions to be met before there could be exceptions to the rule laid down in paragraph (1). The second condition ("if the agreed sum cannot reasonably be regarded as a genuine pre-estimate") had been introduced primarily because of the situation in the common-law countries. In those countries, if the agreed sum was a genuine pre-estimate of the loss likely to be suffered, the sum was regarded as liquidated damages, remained valid and would not be reduced. Since both conditions had to be met, there would be very few cases in which the agreed sum could be reduced under article G.

43. Mr. SEVON (Finland) said that his delegation would have preferred the middle of paragraph (2) to read: "...suffered by the obligee, and/or if the agreed sum ...". Since the use of the word "and" did not appear to be an error, his delegation felt that the second condition should be deleted.

44. Mr. CHAFIK (Egypt) said that the balance between articles F and G was disrupted because the conditions in paragraph (2) would both be met only in a very few cases. He therefore agreed that the second condition should be deleted.

45. Mr. SWEENEY (United States of America) said that his delegation had a number of misgivings concerning paragraph (2). Its effect would be to leave it to the national court to decide whether or not to reduce the agreed sum when both conditions were fulfilled. The reduction would not be mandatory. Moreover, the paragraph failed to specify what the extent of the reduction should be, whether the agreed sum should be reduced to the actual amount of the loss or whether the aim should simply be to eliminate the grossly disproportionate element.

46. The court had the power merely to reduce the agreed sum. Under the common-law system, if the agreed sum was not a genuine estimate, it was invalid, and only damages for the loss actually suffered could be claimed. In certain circumstances, in countries which did not apply the common-law system, a court might invalidate *in toto* a clause providing for an agreed sum.

47. As the representative of the secretariat had stated, the agreed sum was likely to be reduced only in a very few cases.

In practice, the results would be similar to those obtained under the common-law system. There the obligor would normally dispute the agreed sum only if it was grossly disproportionate in relation to the loss. A reduction was difficult because the condition concerning a genuine pre-estimate also had to be met.

48. Although there was a note of criticism in his remarks, his delegation was not necessarily adopting a position with regard to article G.

49. Mr. LAVINA (Philippines) said that in the light of the explanations given by the representatives of Egypt and Finland, he could support the proposal to end article G, paragraph (2), after the first use of "obligee".

50. Mr. AKINLEYE (Nigeria) asked the secretariat to explain the rationale of article G, paragraph (1). It was formulated as a mandatory provision, and he wondered whether there was a precedent for that formulation.

51. Mr. BASNAYAKE (secretariat) said that there was no precedent for that formulation. The intention had been to emphasize that the agreed sum was to be maintained and not reduced. On the other hand, there were hardship cases in which the sum had to be reduced, and for that purpose article G, paragraph (2), had been added.

52. Mr. SCHMID (Federal Republic of Germany) said that the acceptability of the article depended on the scope of application of the Rules as a whole. His delegation could not accept a formulation of article G, paragraph (2), which required both conditions to be fulfilled before the sum could be reduced. He therefore proposed changing "and" to "or", or, as proposed by the representative of Finland, ending the paragraph after the first use of "obligee".

53. Mr. JOKO-SMART (Sierra Leone) said that his delegation was in partial agreement with the proposals made by the representatives of Egypt, Finland and the Philippines, but felt, that for the sake of completeness and clarity, "and the obligee shall be entitled to the actual loss suffered and no more" should be added after the first use of "obligee".

54. Mr. VOLLZEN (Observer for Switzerland) said that his delegation endorsed the proposal made by the representative of Finland.

55. Mr. ROEHRICH (France) said that his delegation agreed in general with the representatives of Finland, the Federal Republic of Germany and the Philippines. It might be possible to find a compromise by treating the two conditions as alternatives. Otherwise, he would support the proposals made in the Working Group, including the use of the words "manifestly unfair". With regard to the points made by the representative of the United Kingdom, he said that the Working Group had wished to assign the court or arbitral tribunal their proper role while allowing them the necessary flexibility. The reduction of the sum was a step that was open to the courts, but they were free to decide whether to take it or not. It might be useful to indicate in the draft rules that the reduction could be such as to diminish the sum to zero.

56. Mr. DUCHEK (Austria) said that he was not familiar with the second condition set out in article G, paragraph (2), as it was not used in his country's commercial legislation. He was afraid, however, that it might be difficult to apply in practice. If the conditions were to be cumulative, that would reduce the application of the Rules and only in a few cases would a real reduction be possible. He therefore believed that

only the first condition should be mentioned. That approach would, moreover, establish a balance with article F.

57. Mr. BYERS (Australia) said that in view of the positive rule set out in article G, paragraph (1), it might be wise to state explicitly in paragraph (2) that it was possible to set aside the contractual agreement. That flexibility was especially desirable for countries with common-law systems. The first condition set out in article G, paragraph (2), envisaged damages after they had been sustained and been shown to be grossly disproportionate. The second condition, however, went back to the time when the contract had been entered into. It reflected the common-law notion that if at the time of concluding the contract the agreed sum had been a genuine pre-estimate, that sum should not be changed, even though it might not be adequate compensation. His delegation did not oppose the proposal to end the paragraph after the first use of "obligee", provided the amount of the loss to be reimbursed was made clear somehow.

58. Mr. GUEST (United Kingdom) said that his delegation favoured the requirement of a genuine pre-estimate, but would go along with the Commission if it decided to delete it. With regard to the proposal made by the representative of Sierra Leone to add the words "and no more", he said he would prefer the words "and no less" to be added. The drafting group should consider whether the requirement of reduction should be stiffened, because it was possible that some courts could take a more obdurate attitude toward that requirement.

59. Mr. OLIVENCIA (Spain) said that his delegation had doubts about the amendments proposed to article G, paragraph (2). In his view, the paragraph would be incomplete if only one of the conditions was included. The first condition presupposed that the loss was less than the agreed sum, but that was only an economic consideration. If it went no further than that, the wishes of the parties would be left out. In article F, the possible intention of the parties to make a reasonable pre-estimate had been allowed for; article G should do the same. As an earlier speaker had said, the responsibility was negotiable and the parties could establish maximum or minimum limits of responsibility or a fixed sum, irrespective of the real amount of the loss that had been suffered. Unless the second condition was included, it would be difficult for the legislation of his country to be brought into line with the provisions of the article.

60. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics) said that the most important aspect of article G, paragraph (2), was the possibility of reducing the agreed sum if it was grossly disproportionate to the loss. His delegation would have no objection to the deletion of the second condition. If both conditions were left in, however, they

should be related alternatively and not cumulatively. The idea of drawing attention to cases where the sum was manifestly unfair was not acceptable to his delegation, because it introduced a subjective element. There was a logical contradiction between paragraph (1), which provided that the agreed sum could not be reduced, and the initial phrase of paragraph (2), which stated that it might be reduced. He suggested that "changed" should replace "reduced" in the first paragraph in order to avoid that logical contradiction. With regard to the question of the extent to which the sum could be reduced, he said that that should be up to the court or arbitral tribunal. Finally, he said that if it was generally agreed to retain paragraph (2) as it stood, his delegation would go along with that.

61. Mr. MUCHUI (Kenya) said that if the proposal made by the representative of Sierra Leone was accepted, the drafting group should look into the possibility of deleting "grossly". The effect of the provision would then be that, if it was shown that the agreed sum was grossly disproportionate to the loss, the payment should be reduced to the actual loss suffered; however, if the agreed sum was merely disproportionate but not grossly disproportionate, the court should not interfere.

62. Mr. PERILLO (United States of America) said that there was a policy problem connected with article G: it was an attempt to combine two conflicting systems. As the representative of the Soviet Union had pointed out, there was a logical contradiction between the first and second paragraphs. Paragraph (2) referred to reducing the agreed sum if it was shown to be grossly disproportionate to the loss, but that was the language of excess, which his delegation believed should be avoided. If a reduction was to be permitted, the courts must be given guidelines on how to implement it. His delegation had considerable difficulty with the pre-estimate condition in the second part of paragraph (2). The word "genuine" seemed to refer to the intent of the parties, not to the reasonableness of the forecast which they had made.

63. Mr. MADDEN (Observer for Jamaica) said that his delegation shared the concerns voiced by the representative of the United Kingdom and agreed with the proposals made by the representatives of Australia, Sierra Leone and the United Kingdom. Paragraph (1) was mandatory, while paragraph (2) was discretionary; it might be useful to include wording in paragraph (1) indicating that it was subject to paragraph (2).

64. The CHAIRMAN said that a drafting group would be formed to redraft the articles in the light of the discussion held in the Commission.

The meeting rose at 6.05 p.m.

2. Summary records of the 270th to 278th, 282nd and 283rd meetings, sixteenth session (Vienna, 24 May-2 June 1983) (A/CN.9/SR.270-278, 282 and 283⁹)

270th meeting

Tuesday, 24 May 1983, at 2 p.m.

Chairman: Mr. CHAFIK (Egypt)

[A/CN.9/SR.270]

The discussion covered in the summary record began at 2.40 p.m.

INTERNATIONAL CONTRACT PRACTICES: DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES AND PENALTY CLAUSES

(A/CN.9/218, A/CN.9/219 and Add.1⁹ and A/CN.9/235⁹)

1. The CHAIRMAN invited the Commission to consider first of all the form to be taken by the uniform rules—a convention, or a model law.

2. Mr. BASNAYAKE (secretariat) reminded the Commission that at its fourteenth⁹ session it had considered a set of draft uniform rules submitted to it by the Working Group on International Contract Practices and had decided to request the Secretary-General to draft such supplementary provisions as would make the text adaptable to the form either of a convention or of a model law. The Commission had also decided to ask the Secretary-General for a commentary to be prepared on the rules and for a questionnaire on the matter to be submitted to Governments and appropriate international bodies.

3. At its fifteenth session,¹⁰ the Commission had considered the draft uniform rules, the secretariat's commentary and an analysis of Governments' replies and comments concerning the questionnaire. It had considered the question of what form the rules should take and had also discussed the substance of some of the rules. Lack of time had precluded any final decision on either form or substance. The secretariat had been requested to submit a revised text of the draft uniform rules to the Commission at its sixteenth session,¹¹ taking into account the comments made at the fifteenth session. The revised text was contained in document A/CN.9/235. It incorporated all points on which there had been general agreement. It also reflected the various views expressed on other points; if any such views had been omitted, the matter could doubtless be rectified during the current discussion.

4. The debate at the Commission's fifteenth session had resulted in a fair majority in favour of a model law, substantial support also being shown for a convention and some support for general conditions. At the General Assembly's thirty-seventh session there had been a small majority in favour of a model law, considerable support also being shown for a convention.

⁹The summary records contained in this volume include the corrections to the provisional summary records that were requested by the delegations and such editorial changes as were considered necessary.

¹⁰Yearbook ... 1982, part two, I, A and B, respectively.

¹¹Reproduced in this volume, part two, I.

¹²Yearbook ... 1981, part one, A.

¹³Yearbook ... 1982, part one, A (A/CN.9/230).

¹⁴Reproduced in this volume, part three, II (A/CN.9/243).

5. He went on to recapitulate the explanatory notes which the secretariat had sent to Governments with the questionnaire, as follows.

6. A convention embodying the uniform rules could be adopted by a plenipotentiary conference or by the General Assembly on the recommendation of the Sixth Committee. Such a convention, having been negotiated among a large number of States, would be widely acceptable. The uniform rules it embodied might also serve as a model for national legislation. Once adopted in that form, the text could be altered only through a subsequent revision of the convention. A State acceding to a convention must apply the rules as long as it remained a party to it.

7. The adoption of a convention at a conference of plenipotentiaries entailed considerable expense for the United Nations unless a State acted as host to the conference at its own expense. Instruments previously drawn up by the Commission in the form of a convention had had a wider scope than the uniform rules under consideration. Furthermore, for some States the normal procedure to become a party to a convention was time-consuming.

8. A model law would be drafted by the Commission at a regular annual session, and the expense involved in adopting a convention at a conference of plenipotentiaries would be avoided. The difficulties which a State might face in incorporating the model law into its legal system would be the same as those involved in enacting any domestic legislation. Any modifications necessary to make the model law effective in a particular legal system could be introduced at the time of incorporation.

9. Some felt that a model law might not generate the same interest as a convention. Furthermore, legislatures could make substantial changes in the model law, either at the time of incorporation or subsequently, thereby reducing the desired uniformity.

10. The uniform rules, with certain modifications, might also take the form of general conditions which parties could incorporate into a contract. The Commission would then recommend the use of such general conditions. However, the conditions so incorporated would be invalid when they conflicted with mandatory provisions of the applicable law regulating a liquidated damages or penalty clause. The uniformity achieved by such incorporation might thus be limited.

11. Mr. YOUSSEFI (Egypt) said that his delegation would prefer a convention—a form which had proved its usefulness in the past. The arguments against a convention were unconvincing: experience did not suggest that a plenipotentiary conference would be unduly expensive; nor were there grounds for asserting that a convention would take more time to prepare than a model law—the reverse might well be the case. Moreover,

in the case of a model law there would be no established procedure for introducing it into national legislations; as a result, national legislatures might be tempted, when doing so, to insert amendments of their own.

12. Mr. OLIVENCIA RUIZ (Spain) noted that his country had already expressed its preference for a model law. Whilst that form might indeed have some disadvantages, they were outweighed by those of an international convention, such as the expense and the complexities that could arise from the application of a convention to rules governing liquidated damages and penalty clauses, precisely on account of the nature of liquidated damages—a point which his delegation had stressed at the Commission's previous session.

13. Mr. MAGNUSSON (Sweden) said that his country remained unconvinced that a set of uniform rules was necessary or feasible. It would hesitate to relinquish its own up-to-date rules for others which might not have the same flexibility.

14. The latest text was a great improvement on the one submitted to the Commission at its fifteenth session; but it was still unlikely to enable universally acceptable solutions to be reached.

15. Although a convention might, at first sight, appear to offer greater uniformity, it would probably not do so in practice because it would gain only limited acceptance. On grounds of practicality and flexibility, therefore, Sweden would prefer a model law, if a choice had to be made.

16. Mr. BARRERA-GRAF (Mexico) said that a convention or a model law would be preferable to general conditions.

17. A convention should not be appraised solely on financial and related grounds: it would above all lead to greater uniformity. However, the experience of that form in many international organizations had been discouraging, particularly because of the low level of ratification—which was not to say that means to ensure wider ratification should not be sought.

18. His delegation was in favour of a model law. That form did indeed have some disadvantages, particularly in regard to disparities which might appear during its introduction into national legislations. But it had a number of advantages, including its suitability for adoption by countries belonging to regional institutions such as CMEA and OAS. Experience showed that such instruments had been of assistance to countries with differing legal systems with a regional context.

19. Mr. GOH (Singapore) urged the Commission to take a decision as soon as possible so as to be able to complete its work on the model rules at the present session. On the question of form, a convention was not advisable in view of the disappointing experience with the earlier conventions which had emerged from the work of the Commission; ratifications had been very slow in coming. He therefore recommended that the draft model rules should be given the form of a model law.

20. MR. GUEST (United Kingdom) said that, of the three choices before the Commission, the idea of general conditions had to be ruled out, because it would give rise to the intractable problem of mandatory law. The choice therefore lay between a convention and a model law.

21. The subject matter of the model rules was much too narrow, and not of sufficient importance, to justify a

convention. In the commercial codes of most countries, the subject took up barely one or two articles of small scope. Clearly, the form of the convention should be reserved for more important matters.

22. Another reason for discarding the form of a convention was that it would not command support from States. Experience had shown how difficult it was for conventions of major importance to be accepted. The ratification of a convention meant bringing into play political processes and political will which would simply not be there for a convention embodying the model rules.

23. His delegation accordingly favoured the form of a model law, while at the same time remaining very sceptical as to whether any rules could be found which would reconcile the fundamental philosophical differences existing on the subject. Of course, if any such rules could be drafted, they could be appropriately embodied in a model law, to be used by those countries that found them acceptable.

24. Mr. SMART (Sierra Leone) said that from a theoretical point of view a convention was undoubtedly the best of the three suggested methods, but pragmatically the form of a model law was to be recommended.

25. If the form of a convention were to be adopted, there would be two possibilities. The first was that it might be adopted by a General Assembly resolution. Unfortunately, such a resolution would not be binding and would easily be ignored by States. Another possibility was to convene a diplomatic conference, but conventions adopted in that way took a long time to come into force. Bearing in mind also that the subject matter of the model rules was very narrow in scope, his delegation therefore favoured the form of a model law. He was not convinced by the argument that a model law would not attract interest; that argument would apply with even more force to a convention.

26. Mr. MUCHUI (Kenya) reminded the Commission that the question of the form its work would take had already been discussed at the previous session and that his own delegation had then stated its preference for a convention. The purpose of the draft was surely to codify and unify the law in the matter, and that could only be achieved by means of a convention which attracted general acceptance.

27. The majority of States now appeared to favour the form of a model law, and obviously those members of UNCITRAL which in the first instance had expressed their preference for a convention would not insist on their viewpoint. Clearly, if they were to press for a convention, the result would be an instrument that would simply join the others which had for many years been awaiting acceptance from a sufficient number of States to bring them into force.

The meeting was suspended at 3.35 p.m. and resumed at 3.55 p.m.

28. Mr. FRANCHINI-NETTO (Brazil) said the text of the model rules was still capable of improvement. He therefore considered it premature to decide at the present stage whether it should take the form of a convention or of a model law. His delegation preferred to await the results of studies under way in regional centres.

29. For the time being, he preferred the form of general conditions, which would be easier to incorporate into his country's existing law.

30. Mr. PFUND (United States of America) said that his delegation gave its preference to the form of a model law. At the same time, it shared the pessimism already expressed by the representatives of Sweden and the United Kingdom with regard to the real chances of success in the work on the model rules.

31. Mr. TARKO (Austria) said that his delegation had already expressed its preference for the form of a convention at the previous session. The purpose of the draft under discussion was to reconcile the common law and civil law systems in order to give the parties to a contract greater legal security. The need for some unified rules in the matter was apparent, and unification could only be obtained by means of a convention that was binding upon States. If, however, the majority of the members favoured the form of a model law, his delegation would accept that approach as the second best choice. A limited unification was better than no unification at all.

32. Mr. QIU (China) said that drafting of the uniform model rules was a commendable achievement on the part of the Commission but that his delegation felt a convention would not be the appropriate form for them. It would be difficult to convene a diplomatic conference to adopt such a text. The ratification process was invariably a slow one, and entry into force of such conventions was always uncertain. It should be borne in mind that if a convention remained for too long after its adoption awaiting the necessary number of ratifications, its status was undermined.

33. At the same time, his delegation did not find the form of a model law acceptable. In view of the considerable differences between existing legal systems, countries would experience great difficulty in adapting their national legislations to conform with the proposed model law.

34. That being so,¹ his delegation found the form of general conditions a more practicable one. In the first place, it would involve an easier procedure, consisting simply in the adoption of the model rules by UNCITRAL, which would recommend them to States. In that way, the draft would play its proper role at a much earlier date. It would thus be of greater help to the parties concluding a contract. Once the general conditions were widely applied, States would appreciate their advantages and the rules they embodied would find their way quite naturally into domestic legislation. Lastly, general conditions had the great advantage of flexibility, because they were not mandatory in character. They could always be supplemented or improved by States so as to bring the rules they contained more into conformity with the requirements of each particular country.

35. In conclusion, his delegation favoured the form of general conditions. If, however, the majority of the members did not favour that approach, his delegation would not oppose the form of a model law, in the interests of reaching an agreement.

36. Mr. SAMI (Iraq) drew attention to the disparity of legal systems, which fell broadly into two categories: common law systems and civil law systems; it would therefore not be at all easy to embody the model rules into a convention suitable for all the countries concerned. That was particularly true in view of the complexity of the subject matter. If a convention were to be adopted, it would be difficult for countries to ratify it. They would encounter serious problems in trying to adapt their own laws to conform with the model rules. Accordingly, his delegation had a strong preference for the form of the

model law, which afforded much greater flexibility for the adaptation of national legislations.

37. Mr. KOJEVNIKOV (Union of Soviet Socialist Republics) said that in the end the effectiveness of the draft uniform rules would depend largely on the form of instrument in which they were embodied. He wished, however, to stress an important aspect of the problem, namely, the significance of the draft rules themselves. They were few in number, but they were extremely important from the practical point of view. In international trade there was practically no contract of any kind—contract of sale or otherwise—which did not contain a provision on the subject of penalties. The experience of Union of Soviet Socialist Republics organizations in their relations with enterprises in other countries showed that clauses on the subject of penalties were included in all contracts. That being so, very real problems arose with regard to the legal systems governing those clauses. It was extremely important to solve those problems in a uniform manner. If identical procedures were applied in all countries, the result would be a very valuable contribution to smooth world trade.

38. It was of course true that the various rules contained in the draft were susceptible of improvement. That fact, however, did not alter the firm view of his delegation that the form of a convention was preferable to that of a model law. It should be remembered that UNCITRAL conventions (A/CN.9/241²) had in the past received considerable support. In a great many countries the ratification of those instruments was being actively discussed. Their adoption by a considerable number of countries could be reasonably expected within the near future. As for the form of a model law, on the other hand, it could be said to have achieved absolutely nothing in practice, with a few very minor exceptions. It was thus not likely to arouse enough interest in the present case.

39. At the previous session the secretariat had put forward a very constructive idea, which could help to bring together the different views. It was that the conventions should embody the substantive rules in the form of an annex, as had already been the case with a number of international instruments on uniform laws. In addition, the convention would specify the right of every State to make a declaration to the effect that the application of the model rules would be subject to agreement by the parties concerned in each particular contract. He drew attention in that connection to paragraph 17 of the report on the previous session (A/CN.9/230³). He was convinced that those ideas could provide a solution for the very important problem of the form which the draft under discussion would take.

40. Mr. SAWADA (Japan) said that, as at the fifteenth session, his delegation was once more in favour of a model law. Considerable interest had already been shown in the draft model law on international commercial arbitration. He agreed with the Union of Soviet Socialist Republics representative's emphasis on uniformity, but there was no guarantee that uniformity would be achieved by a convention. Moreover, conventions were not always ratified. The question of expense was a secondary one.

41. He would not, however, oppose a convention if the majority preferred it.

42. Mr. KIM (Observer for the Republic of Korea) also supported the form of a model law, as the most practicable method from the point of view of domestic legislation. It was

¹Reproduced in this volume, part two, VI.

²Yearbook ... 1982, part one, A.

important that the rules should be as widely applicable and as effective as possible.

43. Mr. EDWARDS (Australia) reaffirmed his country's consistent support for a model law. He was opposed to general conditions and to a convention for reasons which had been well summarized by the representatives of the United Kingdom and Japan.

44. Mr. HERBER (Federal Republic of Germany) said that his delegation's first choice would be general conditions. A number of delegations had referred to the lengthy ratification procedures for conventions; but the procedures would be even more prolonged in the case of a model law. General conditions offered the speediest and easiest method of introducing uniform rules in practice. Provided the commercial world applied the rules, it was probable that national legislators would adapt their laws accordingly.

45. He realized, however, that there was a risk in recommending rules which might conflict with mandatory national laws. If the majority were not in favour of general conditions, his second choice would be a model law.

46. Mr. ROEHRICH (France) reaffirmed his delegation's support for a convention. Those who had spoken in favour of a model law, both at the fifteenth and at the present session, had not fully considered its disadvantages. Its major advantage was undoubtedly its flexibility and its easy adaptation to national laws; but its adoption would still leave a gap in the process of unification, which was the Commission's main task. Particularly where penalties were concerned, the adoption of such a law would amount to an avoidance of reality, since when it came to modifying national laws, it would be hard to resist pressure from the international trade lobby.

47. There was a recognized difficulty in reconciling civil law and common law, and the answer seemed to be to create a third law—international trade law—provided it was acceptable to the international trade world. That could most effectively be done in the form of an international convention. Given goodwill and the readiness to make concessions the third method might be successful in achieving the desired unification.

48. While maintaining its preference for a convention, his delegation would nevertheless join in a consensus if the majority favoured a model law.

49. Mr. BONELL (Italy) said that his delegation favoured a convention, as the best means of achieving unification. However, it appreciated the difficulties of certain Governments and would reconsider its position if the Commission as a whole preferred a model law.

50. A model law should not be regarded merely as a simpler alternative to a convention. The Commission should endeavour to draft a genuine model law recommending model procedures. While appreciating the efforts made to produce the draft now before the Commission, he doubted whether it fulfilled that requirement.

51. Mr. RUZICKA (Czechoslovakia) said that his delegation was in favour of a model law.

52. Mr. SEVON (Observer for Finland) agreed with the view that if the aim was uniformity, a convention would

ideally be the proper form. He did not accept the arguments concerning the cost of a convention, the lack of ratification of previous conventions, or the limited scope of the subject matter. The real issue, however, was whether people believed in the exercise; if they did not, a convention would serve no purpose, and the Commission should have the courage to decide not to pursue the matter. He did not believe that the drafting of a model law would achieve much, either, and he would therefore be in favour of abandoning the project.

53. Mr. YOUSSEFI (Egypt) said that he doubted whether the adoption of a model law would result in uniformity, especially for the developing countries, where it would merely be pigeon-holed and forgotten. He would not, however, be in favour of abandoning the project. Efforts must be made to find a compromise, possibly on the lines suggested by the representative of the Union of Soviet Socialist Republics or in the form of a legal guide, rather than a model law, which Governments might be reluctant to introduce into their national law. Failing a convention, other possibilities must be sought.

54. The CHAIRMAN, summing up, said that there was a divergence of view in the Commission. Some members believed that unification could not be achieved, because it would mean combining two different systems; they thought that few States would ratify a convention and few would adopt a model law. Others considered that the question was very important for international trade and that efforts should be made to achieve unification. The matter was not one of choosing between two systems but of creating a third system through which unification of the relevant laws would be achieved.

55. He noted that three members were in favour of general conditions, five (if Finland was included) in favour of a convention and 13 in favour of a model law. The Commission therefore seemed to have decided in favour of a model law and of continuing to seek unification in that form.

56. He wondered whether the members who had indicated a model law as their second choice would now support it.

57. Mr. DIXIT (India) said that the number of ratifications of previous conventions was not relevant in the present case. Conventions that failed were not necessarily unsatisfactory ones: ratification was a continuous process; Governments wanted to know how many other countries had signed, or they wanted further assurance, or they sometimes changed their minds. He would have like the Commission to consider why it was impossible to have a convention on the present subject. One of the Commission's main objectives was to try to secure uniformity. While he would not oppose what had been agreed, he felt that the reasons why uniformity was no longer to be sought should be stated. The Commission could always adopt a draft convention and leave the question on the agenda of the General Assembly; or it could have further discussion on the question.

58. The CHAIRMAN suggested that the Commission should continue the discussion and endeavour to reach a decision on the basis of the Union of Soviet Socialist Republics representative's proposal, on the lines set forth in paragraph 17 of the report on the work of the fifteenth session (A/37/17).

271st meeting

Wednesday, 25 May 1983, at 9.30 a.m.

Chairman: Mr. CHAFIK (Egypt)

[A/CN.9/SR.271]

The meeting was called to order at 9.40 a.m.

**INTERNATIONAL CONTRACT PRACTICES:
DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES
AND PENALTY CLAUSES (continued)**

(A/CN.9/218, A/CN.9/219 and Add.1, and A/CN.9/235)

1. The CHAIRMAN, recalling the discussions at the previous meeting, said that a consensus did not yet appear to have emerged with regard to the appropriate form for the uniform rules. A suggestion had been made that the Commission revert to the compromise solution advanced at its fifteenth session, namely that the uniform rules could be cast in a form which might enable them to be used for several purposes.
2. Mr. BASNAYAKE (secretariat) read out paragraph 17 of the report of the Commission on the work of its fifteenth session (A/37/17) which summarized the substance of that compromise formula.
3. The CHAIRMAN said that the proposed solution, whereby there would be a convention with an attached annex containing the uniform rules, appeared to meet the concerns of all parties. The convention could moreover contain a reservation to the effect that the uniform rules would apply only when the parties to a contract had so agreed (as, for example, had been done in the 1964 Hague Convention^a).
4. Mr. WAGNER (German Democratic Republic) agreed that that approach, which was the same as the proposal made by the Union of Soviet Socialist Republics delegation at the previous meeting, was the most promising one. It had the additional virtue of leaving the door open for States which were at present in favour only of a model law to ratify the convention at a future date.
5. Mr. HERBER (Federal Republic of Germany) said that he also favoured the compromise formula outlined in paragraph 17 of the Commission's report.
6. The major problem was that in many countries existing mandatory legislation was not compatible with the recommended clauses. It would therefore be preferable to proceed in the first instance to the drafting of general provisions, as opposed to legal provisions, which would be suitable for immediate use by commerce. An umbrella convention could then be added at a later stage, obliging States which ratified it to apply the uniform rules, or at least recommending that they should do so, even when national mandatory law in force was not compatible therewith—the device used in the 1964 Hague Convention. It was also possible that commercial circles would exert pressure on Governments to ratify a convention at a later stage.
7. Furthermore, since mandatory law was usually designed to protect consumers, whereas the draft uniform rules were intended for commercial use, it would be appropriate to insert a clause in the rules exempting private parties.
8. So far as the costs involved in drafting a convention were concerned, he believed that matter could be discussed at a later stage, although such a relatively short instrument could presumably be drafted during the course of the work of the Sixth Committee.
9. Ms. VILUS (Yugoslavia) said that, although her delegation had formerly favoured the model law option, it had come to the conclusion, after extensive study, that such an approach was unlikely to promote the unification of international trade law. It was accordingly prepared to support the formula advanced in paragraph 17 of the Commission's report as the one most likely to bridge the gap between common-law and civil-law countries.
10. Mr. YOUSSEFI (Egypt) also supported the compromise proposal, insofar as the form, as opposed to the substance, of the draft uniform rules was concerned.
11. Mr. GUEST (United Kingdom) said his delegation did not believe that the subject of liquidated damages and penalty clauses was an appropriate topic for further consideration by UNCITRAL. First, there was a basic difference between the approach of common-law countries on the one hand and civil-law countries on the other. Secondly, the sphere of application of liquidated damages and penalty clauses was determined by national jurisprudence which varied considerably from country to country. Thirdly, drafting uniform rules on the subject was tantamount to isolating a limited aspect of general contract principles from the system of contracts and forming it into a régime on its own—an endeavour he considered unlikely to succeed.
12. If the Commission wished nonetheless to proceed, it should focus on drafting clauses that could eventually form part of a general contract code, based also on the work of the Commission in such areas as arbitration rules. If the compromise formula outlined in paragraph 17 of the fifteenth session report was the approach adopted, it was important to understand what was involved. It appeared from the proposal that the régime would apply only when parties had adopted it as part of their contract: his delegation was prepared to go along with the proposal only on that understanding, and provided that the principle of "contracting-in" was maintained inviolate. It would not be able to countenance attempts at a later stage to turn the convention into an instrument which would be applicable unless a State contracted out.
13. He believed that the substance of the draft rules should be taken up before the form of a possible convention was discussed.
14. Mr. FRANCHINI-NETTO (Brazil) said that his delegation was prepared to support the model law option if that was the majority view of the Commission, although all its legal implications would have to be carefully analysed. His delegation attached particular importance to the protection of the weaker party to a contract.
15. Mr. PENKOV (Observer for Bulgaria) said that the question of liquidated damages and penalty clauses was a fundamental one which arose in respect of every contract. Whether the Commission opted for a model law or a contract was an important decision which would have considerable impact on the uniform rules themselves.

^aUnited Nations, *Treaty Series*, vol. 834, No. 11929, p. 107.

16. The existence of various legal systems complicated the matter: his delegation believed that the only means of giving the uniform rules practical value was to opt for a convention. The problems of ratification which had been pointed out could be resolved in the course of time: they were not an argument against a convention as such.

17. If, however, the Commission as a whole did not favour the drafting of a convention, his delegation would be prepared to go along with the compromise formula.

18. Mr. FARNSWORTH (United States of America) said that the net result of adopting the compromise formula based on paragraph 17 of the Commission's report on its fifteenth session would be the same as opting for the model law approach, the only difference being that at some stage the Commission would have to prepare an umbrella convention. His delegation believed it would be appropriate to proceed forthwith with the drafting of a uniform or model law and to defer to a later stage a decision on the precise nature of a convention or perhaps even whether there should be one, given that some doubts had been expressed as to the Commission's ability to produce a successful instrument of that nature.

19. He did not, on the other hand, believe that the Commission should draft general conditions, and would welcome clarification in that respect of the interpretation given by the representative of the Federal Republic of Germany to paragraph 17 of the Commission's report.

20. Mr. MAGNUSSON (Sweden) said that, while his delegation was not an enthusiastic advocate of the unification of international law in respect of liquidated damages and penalty clauses, it believed that the valuable work already done by the Commission on the subject should be utilized. The text of the draft rules as they stood had certain merits, and could be improved upon.

21. The compromise formula proposed had the disadvantage of being complicated: it would involve the drafting of both a model law and a convention. His delegation would, on the other hand, be prepared to follow the approach suggested by the representatives of the United Kingdom and the United States.

22. Mr. BONELL (Italy) said that he had understood the suggestion made by the representative of the Union of Soviet Socialist Republics at the preceding meeting to have been that the Commission should adopt the solution set forth in paragraph 17 of its report on the work of its fifteenth session (A/37/17), namely that it should prepare a convention with annexed uniform rules, and with provision for a so-called "contracting-in" reservation. Some statements at the present meeting had made him wonder whether all delegations interpreted the proposal in the same way. For instance, the representative of the Federal Republic of Germany had suggested that the proposal might mean that, initially, the Commission might consider the drafting of general clauses for use in contracts. That suggestion had little to do with paragraph 17, apart from its penultimate sentence, which he found somewhat misleading; parties could always take contract clauses from any source they wished and it seemed superfluous to mention the fact unless only such an approach was envisaged from the beginning. That would cause his delegation great difficulties. A solution along the lines set forth in article G giving a court or arbitral tribunal the right to intervene in certain cases in order to reduce the amount due was a well-established principle, in the Italian system at least, applying also to contracts between two merchants, and

his delegation would be extremely reluctant to abandon such a principle.

23. Although the United Kingdom representative had also indicated readiness in principle to accept the "paragraph 17" formula, he seemed to see the whole exercise in terms of "contracting-in". That would be quite a different approach; paragraph 17 allowed for the possibility of a reservation, but that was not the same thing.

24. The representative of the United States also seemed to have an interpretation of the paragraph 17 solution which did not coincide with that of the Italian delegation, or, he thought, with that of the representatives of the Soviet Union and France; he seemed to consider a uniform law annexed to a convention more or less in the same terms as a model law. He thought there was general agreement on the difference between a uniform law and a model law. His delegation fully endorsed the approach suggested in the fourth sentence of paragraph 17, according to which "States might adhere to the convention, thereby obligating themselves to adopt the uniform rules". Such an obligation would not follow if the so-called uniform law was considered merely as a model law, States being free to adapt the rules when introducing the model law into their national legislation.

25. He would be grateful for further clarification of representatives' opinions on those points.

26. The CHAIRMAN observed that the States which could use the uniform rules as a model law were those which had not adhered to the convention, whereas the rules would be obligatory for States which had adhered to it, although the latter were entitled to make certain reservations.

27. Mr. ROEHRICH (France) said that the Chairman's statement had added to his conviction of the merits of paragraph 17. He shared the concern expressed by the representative of Italy at the statements made in particular by the representatives of the United Kingdom and the United States. The approach set forth in paragraph 17 allowed for various possibilities. States willing to adhere to the convention would adhere to it and consequently to the uniform rules, and States having a little difficulty in adhering could take advantage of the possibilities of a reservation such as that included in the 1964 Hague Convention. Finally, the uniform law could be made use of in other States which did not want to adhere to the convention for various reasons, by parties to international contracts. The approach therefore seemed capable of satisfying all the States participating in the session.

28. It was difficult to draft clauses without some idea of the final document to be produced. It was impossible to foresee the exact form of the document, but it should be possible to draft uniform rules with an outline in mind in such a way that States with difficulties concerning the fundamental legal approach of the present draft document should be able to co-operate fully, since they would know that if they encountered insurmountable obstacles to fundamental concepts concerning liquidated damages and penalty clauses they need not adhere to the convention or could adhere to it with the reservations permitted by the "contracting-in" clause.

29. The representative of Italy had referred to article G. It might be questioned whether such a provision was still justified when the field of application of the future instrument was restricted to international trade, which excluded contracts made by consumers. That type of problem should be studied in the light of other problems which arose during the drafting of the uniform rules.

30. Mr. BOGGIANO (Observer for Argentina) said that at the beginning of the session he had been inclined to favour the drafting of a convention. However, having listened to the various statements made by other representatives, he suggested that two possible approaches should be considered. The Commission should start by studying the draft uniform rules before it (A/CN.9/235) but should also admit the alternative possibility of a convention or model law, in both cases restricting the drafting to the elaboration of rules which might meet with a certain degree of agreement with a view to a future convention. With respect to both uniform rules and the convention, he suggested that in order to avoid conflicts between civil-law and common-law systems and with respect to the scope of application of the clauses, both texts should include a final clause providing that questions not covered by those rules remained subject to national law. Such flexibility would make it easier to draft a generally acceptable convention or model law.

31. Mr. VOLKEN (Observer for Switzerland) said it was true, as the Legal Counsel had pointed out in his statement at the opening of the session, that there were different legal harmonization techniques. However, the question to be considered was which subject was suited to which form of harmonization. To justify a convention, the subject must be important, there must already be a certain degree of harmony, a detailed study of comparative law must have produced specific results and there must be practical evidence of need. If those criteria were applied to the subject of liquidated damages and penalty clauses, it would be seen that the subject was of rather limited scope, despite its practical importance. If a convention was drafted on every subject of practical importance, there would be a proliferation of conventions on the subject of contracts alone.

32. It had been repeatedly stated that the problems of harmonization arose from the differences between the civil-law and common-law systems. It was doubtful whether those were the only difficulties, and many others would probably arise in the course of drafting. Moreover, even within the civil-law and common-law systems legislations were not identical.

33. All those points called for very detailed comparative study in order to find a common denominator between the civil-law and common-law systems and the various civil-law legislations. Such a study would make it possible to identify the crucial points and see whether solutions could be found. Until such a study was completed, he did not think that the subject was suited to the drafting of a convention.

34. Mr. SONO (Secretary of the Commission) noted that the Commission itself had been doing substantive work in the field for the past four years, taking into account work done by the Council of Europe and the studies made in Belgium by an international institute. Documents had also been prepared on the substantive side, analysing various approaches in different legal systems. All those documents were available to representatives.

35. Mr. EDWARDS (Australia) thought that some of the reservations expressed about the direction which the Commission's work should take reflected misgivings on the part of a number of delegations concerning the likely quality of the result of that work. Many delegations were not confident at the current stage that the work would be of sufficient quality to justify a convention. He therefore endorsed the United States representative's suggestion that the Commission should concentrate on drafting a useful and constructive set of rules. That might dissipate many of the reservations of its members as well as facilitate the eventual preparation of a convention.

36. Mr. TARKO (Austria) said that his delegation had always expressed preference for a convention or at least a model law. He fully endorsed what the representative of Italy had said concerning the proposal made by the Union of Soviet Socialist Republics at the previous meeting. He was also not very happy with a "contracting-in" clause, because States were always free either to accede to a convention or use the rules as a model law; he could, however, agree to the solution provided in paragraph 17 of the report on the Commission's last session (A/37/17) as a compromise. On the other hand, he would not be in favour of a compromise on the compromise.

The meeting was suspended at 11 a.m. and resumed at 11.30 a.m.

37. Mr. DIXIT (India) said that his delegation's overriding concern was that the Commission should fulfil the purpose for which it had been established, namely to bring uniformity into international trade law. It had taken up the subject under discussion because of the great differences between the laws of various countries. Uniformity was particularly important to the developing countries. However, he did not want to see a model law which would not be binding. Uniform rules must be drafted and could be adopted without the need for a plenipotentiary conference. Once such rules were adopted, countries could make reservations if they so desired, but it would be understood that they were reservations to an adopted set of rules.

38. Mr. SEVON (Observer for Finland) said that the pessimism of his statement at the preceding meeting had been due to concern that the Commission, which so far had produced results which had met with broad appreciation and had been found acceptable by States all over the world, might produce something which it did not even believe in itself.

39. Attention had been drawn to the problems posed by the mandatory law of different States. That could easily be overcome by drawing up a convention containing little more than a provision stating that, in international contracts, the parties would be at liberty to agree on such liquidated damages or penalty clauses as they might see fit. A State ratifying such a convention would have to provide in its internal legislation that clauses on liquidated damages and penalty in international contracts were not subject to the mandatory rules otherwise imposed. That would be a simple way of dealing with the main issue without trying to reach agreement on points where national laws were very divergent.

40. The Commission seemed to be discussing two different issues, namely how to proceed in its work over the next few days and what form that work should take. If it was agreed that what the Commission was trying to achieve was uniform rules that could, but might not, be attached to a convention, it would solve both problems.

41. The representative of Italy had made a distinction between a model law and a uniform law. If the proposed method of work were adopted, it would have to be accepted that a uniform law could also serve as a model law.

42. Having elaborated the provisions of a uniform law, the Commission could then consider whether or not it was appropriate to draw up a convention. If it had agreed on those provisions it would be a minor task to do so, whether or not a "contracting-in" provision was included. As some delegations had expressed hesitation about such a provision, the Commission should not strive for uniformity where that could not be achieved. If such a clause was necessary to make

the result acceptable to certain countries, it would be a small price to pay for uniform rules.

43. Mr. SAWADA (Japan) endorsed the preceding speaker's statement. At the previous meeting, his delegation had supported the drafting of a model law and had said it could also agree to a convention. The form of document to be drafted had been exhaustively discussed at previous sessions and he suggested that the Commission should start work on draft uniform rules, which could also become a model law, and then discuss whether or not to draft a convention and whether a "contracting-in" clause should be included.

44. Mr. GOH (Singapore) endorsed that proposal. The subject was a difficult one because of the vast differences between the civil-law and common-law systems. The uniform rules could perhaps include a provision that countries should allow parties to opt out of national legislation. However, his concern was that the Commission should start on its substantive work immediately. He therefore proposed that it should begin work on the uniform rules and see later whether a compromise could be achieved on the question of form.

45. Mr. SMART (Sierra Leone) said that the important thing was to adopt rules relating to liquidated damages and penalty clauses, and that the question of the form those rules might take was of lesser significance.

46. The CHAIRMAN said that, if he heard no objection, he would assume that the Commission wished to proceed to discuss the substance of the draft rules, deferring a decision on their ultimate form until they were finalized.

47. *It was so decided.*

48. Mr. BASNAYAKE (secretariat), introducing draft Article A, paragraph (1) (A/CN.9/235), said that general agreement had emerged from the discussions at the previous session that the rules would not apply where a penalty or liquidated damages were claimed under a bank guarantee, and wording had been added to ensure the exclusion of such cases from the rules. It had also been agreed that the rules should be strictly confined to agreed sums which were liquidated damages or penalties, since it had earlier been pointed out that, under the previous draft, certain other forms of contractual arrangement might also be covered by the rules. The revised text reflected that concern.

49. A further question raised was whether the phrase "in writing" should be added so as to restrict the application of the rules to contracts in writing. The prevailing view was that, if the rules were to be adopted in the form of a convention, a reservation on those lines could be incorporated, whereas in the case of a model law each State would determine the question for itself.

50. A paragraph (1 *bis*) had been added to eliminate any uncertainty as to the extent to which the rules were concerned with the validity of the contract. The wording chosen corresponded to that of the Convention on Contracts for the International Sale of Goods (Sales Convention²).

51. Paragraph (1) of draft article A defined the scope of the rules. In the previous versions of the paragraph the question of the function of the "agreed sum" was not clearly defined. For that reason, two alternative versions had been inserted in order to make it clear that the "agreed sum" must be intended as a pre-estimate of damages or as a penalty. The two versions expressed the same idea, and did not differ in

substance. The second alternative was a more expanded wording, and the Commission might wish to consider whether the shorter version might not be fully adequate.

52. In connection with bank guarantees, he said that the question had been taken care of by the provision in the revised draft that the obligee was entitled to an agreed sum of money from the obligor. The draft thus confined itself to a provision under which the obligee could recover money from the obligor. If there was a contractual arrangement in which the obligor could obtain that sum of money from a financial institution, such an arrangement would not fall within the scope of the rules.

53. In earlier versions of paragraph (1) the phrase "to recover, or to forfeit" had been used. While that wording gave rise to no problems in common-law systems, it had public law implications in some systems based on civil law, and was, moreover, difficult to translate into other languages. For that reason it had been suggested that either the words "to recover or to withhold" should be substituted, or that the text should simply read "is entitled to an agreed sum of money".

Draft article A, paragraph (1) (a) (A/CN.9/235)

54. Mr. SAWADA (Japan) thought that perhaps the words "recover or to withhold" were unnecessary and could be omitted. He also felt that the first of the bracketed alternative wordings of the last part of paragraph (1) (a) was the more satisfactory of the two.

55. Mr. EDWARDS (Australia) said that "to recover or to withhold" was an improvement on "to recover, or to forfeit". Of the bracketed alternative wordings for the end of the paragraph, his delegation favoured the second, which was less ambiguous.

56. He wondered whether there was a need to refer to "an agreed sum". Liquidated damages could sometimes be provided for otherwise than by an agreed sum, for example by an agreed formula, and the words "an agreed sum" might accordingly be omitted.

57. He also wondered whether the text should not include a reference to defective performance as well as to total or partial failure of performance. Such a reference would be consistent with other provisions in the draft rules.

58. Mr. ROEHRICH (France) thought that the best wording might be "is entitled to an agreed sum". The term "agreed sum" was fully adequate if the commentary were to make it clear that it meant any sum arrived at by calculation.

59. Of the bracketed alternative wordings for the end of subparagraph (a) his delegation preferred the first, since the idea of a penalty in the second was out of place in the context of the draft rules. However, the drafting group could consider whether it might not be possible to improve on the existing wording of the second alternative.

60. Mr. TARKO (Austria) said that he agreed with the representatives of France and Japan that the first of the two alternative wordings was preferable, particularly as the second implied that there had to be a loss suffered by the obligee, who would not otherwise be entitled to the agreed sum. That approach was not, in his view, consistent with the substantive provisions of the draft.

²Yearbook ... 1980, part three, I, B (A/CONF.97/18, annex I).

61. Mr. BARRERA-GRAF (Mexico) said that his delegation favoured the second of the two alternative wordings, which would be compatible with either a convention or a model law. The disadvantage of the first bracketed wording was the difficulty of defining "security for performance". The term "an agreed sum" should be retained, but he agreed with the representative of France that it would be helpful to explain it in the commentary.

62. Mr. FARNSWORTH (United States of America) said that his delegation would not object if "to recover or to withhold" was substituted for "to recover, or to forfeit". He did not share the Australian representative's reservations with regard to "an agreed sum" but felt that the drafting group could be asked to consider that question.

63. A more important issue was raised by the bracketed alternative wordings for the end of the subparagraph. He noted that those favouring the first alternative were all from civil-law countries. Its adoption would not in fact have much effect in common-law countries, where the overriding question would be whether the sum was a pre-estimate of damages or a penalty. If the rules applied only to pre-estimates of damages, a common-law judge would assume that penalty provisions

were not implied at all. It was therefore essential to include the concept of penalty in the paragraph. A drawback of both the suggested versions was the phrase "is intended", which would appear to invite speculation as to the state of mind of the parties. That was not, presumably, the intention of "is intended", but he felt that it might be better if the text were to read "an agreed sum of money from the obligor, as damages or as a penalty". It might also be possible to incorporate some reference to security or to loss suffered by the obligee.

64. Mr. MAGNUSSON (Sweden) said that his delegation had no strong feelings about the inclusion or omission of the words "recover or to withhold", and had no difficulties with the term "an agreed sum". He agreed with the view that the phrase "as a penalty for that failure" in the second bracketed wording proposed for the end of the subparagraph was not wholly satisfactory. On the other hand, the phrase "as security for performance" in the first of the alternative versions was not altogether acceptable either because of its ambiguity. The best solution might be to refer the second alternative wording to the drafting group for appropriate revision.

The meeting rose at 12.35 p.m.

272nd meeting

Wednesday, 25 May 1983, at 2 p.m.
Chairman: Mr. CHAFIK (Egypt)

[A/CN.9/SR.272]

The meeting was called to order at 2.10 p.m.

INTERNATIONAL CONTRACT PRACTICES: DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES AND PENALTY CLAUSES (continued) (A/CN.9/218, A/CN.9/219 and Add.1, and A/CN.9/235)

Composition of drafting group

1. The CHAIRMAN announced that the drafting group would be composed of the following countries: France, India, Sierra Leone, Spain, Union of Soviet Socialist Republics and United States.

Draft article A, paragraph (1) (a) (continued) (A/CN.9/235)

2. Mr. BONELL (Italy) said that he had no strong feelings regarding the words "recover or to withhold" in square brackets in the third line, or the reference to an agreed sum of money in the third and fourth lines.

3. With regard to the two alternative versions in square brackets of the last part of the paragraph, the questions raised by the supporters of both alternatives should be taken into account. He took the view that it would be more appropriate to refer to a "penalty" (second alternative) than to "security for performance" (first alternative); penalty clauses were mentioned in his country's civil code. He would also suggest that the last part of the paragraph should be composed of the first part of the first alternative, with the words "intended as" deleted, and the second part of the second alternative, with the word "as" deleted, so that the text would read: "where such sum is a pre-estimate ... or a penalty ...".

4. He had doubts about the words "total or partial failure of performance" in the first and second lines, which were inconsistent with the wording in paragraph 2 of article E, "non-performance, or defective performance". Perhaps the wording should be harmonized and brought into line with that of other instruments. He would prefer the use of verbs rather than nouns: for example, "failure to perform...", rather than "failure of performance".

5. Mr. GUEST (United Kingdom) said that he too had doubts as to whether the phrase "total or partial failure of performance" was apt to describe a number of separate situations, namely, non-performance in whole or in part, delayed performance and defective performance. There was also the question whether the draft as a whole was intended to operate only in the event of breach of contract by the obligor, or whether it was to be extended to such cases as payment of additional sums under a building contract, e.g. for bad weather or other conditions holding up performance, or other cases not involving a breach of contract.

6. With regard to the words "recover or to withhold" in the third line, if those words were omitted, a judge in the United Kingdom would construe the words "entitled to an agreed sum" as being confined to the recovery of an agreed sum from the other party. It was doubtful whether the word "withhold" was appropriate. Two separate situations seemed to be involved. First, retention of money already paid to the obligee by way of deposit (*arra* under Roman Law) for security of performance; the word "retain" would be apposite to that situation, where money had been paid by one party to another and it was agreed that if the other party broke the contract, it should be forfeited. Secondly, a situation where money had not been paid but was to become due; the word "withhold" would be appropriate there, one party having been given the option to withhold payment in the event of default by the other party. Whether that was intended to be

covered was a matter of speculation. If it was to be excluded, he would prefer the word "retain" rather than "withhold". Regarding the words "an agreed sum", referred to by the Australian representative, if members felt that the phrase should be more explicit, he would suggest the words "a fixed or determinable sum".

7. With regard to the two alternatives for the last part of the paragraph, three situations should be covered: where the sum was intended as a pre-estimate of damages; where the sum had been lodged as security for a performance (the *arra* concept); and where the parties stipulated for a penalty—an important matter for common-law systems. Those three ideas could be covered by amending the first alternative text.

8. Mr. HARTKAMP (Observer for the Netherlands) said that he shared the doubts of the representative of Italy concerning the words "total or partial failure of performance" and suggested that the words "total or partial" should be replaced by the word "any". That would conform with article D and would make it clear that cases not involving breach of contract were covered—as agreed by the Commission at its fifteenth session after considerable discussion.

9. With regard to the two alternative texts in square brackets, he agreed with the United States representative that it would be advisable to change the wording, for the reasons given, and also because a "sum" could not be described as a pre-estimate, but was the compensation itself. He recommended the wording used by the Council of Europe "by way of penalty or compensation".

10. Mr. HERBER (Federal Republic of Germany) supported the Netherlands representative's proposal to replace "total or partial" by "any".

11. The words "recover or to withhold" were not needed for the purposes of his country's law, but if other countries required them, he would support the United Kingdom proposal to replace "withhold" by "retain".

12. With regard to the last part of the paragraph, he supported the United States proposal for combining the two alternatives and agreed with the comments of the representative of Italy. In principle he would favour the first alternative, but the addition of a reference to "penalty" would be useful for both continental law and common law. It was important to exclude the words "loss suffered by the obligee" because the matter being dealt with was the sphere of application and the definition should therefore not be too narrow.

13. He supported the United Kingdom representative's suggestion to find a wording covering the three situations in question and proposed that it should be referred to the drafting group.

14. Mr. SAMI (Iraq) said that when a contract was being drafted, both parties could be required to deposit a sum which they would forfeit in the event of defective performance or complete non-performance. The idea of a deposit had been referred to at the previous session, but was not covered in the present text, which only provided for a penalty and an award for loss suffered. In his opinion, the article should be reformulated to cover all three possibilities. It should stipulate *expressis verbis* that both parties should state what the amount should be and whether it was an award for loss suffered, a penalty, or a deposit liable to be forfeited.

15. Mr. OLIVENCIA (Spain) said that the word "failure" (*incumplimiento*) as a legal concept was often questioned and

ought to be clarified. He would prefer the Spanish term "*falta de cumplimiento*", to cover a failure or non-performance whether attributable to the obligor or not.

16. Regarding the phrase "recover or to withhold", while he welcomed the deletion of the word "forfeit" used in the previous draft, he still had misgivings concerning the word "withhold" because it did not imply a penalty. He shared the doubts that had been expressed concerning the interpretation of the term *arra*.

17. With regard to the two alternatives in square brackets, he had the impression that the different language versions did not tally. In the Spanish version, the words "*se establezca*" ("is intended") would presuppose security for performance. He suggested that the texts should be harmonized and that the purpose of the sum in question should be clearly specified. He preferred the first alternative in square brackets but had reservations on the term "security for performance". It would be advisable to avoid terms which gave rise to problems of interpretation, and he would prefer to see the idea of "security" replaced by the idea of "penalty".

18. As a minor point, he suggested that in the second alternative in square brackets, damage as well as loss should be covered.

19. The CHAIRMAN, having ascertained that the last point applied only to the Spanish text, suggested that the representative of Spain should raise the matter in the drafting group.

20. Mr. MUCHUI (Kenya) said that he did not entirely share the United Kingdom representative's views concerning interpretation of the words "recover or to withhold" under common law. If the words referred solely to recovery and had nothing to do with withholding or retention of an earlier payment made as security for performance, he would have no serious problem with them. He would, however, prefer the shorter version, without those words.

21. With regard to the Australian representative's question concerning the term "agreed sum of money", he suggested that the issue was one of drafting rather than substance and that the drafting group might consider whether the term necessarily excluded a formula for establishing a sum of money.

22. He had some difficulty in deciding in favour of either of the two alternatives in square brackets and would like some clarification. As he understood it, the provision concerning security for performance in the first alternative was the equivalent to the provision for a penalty in the second alternative. If, however, the United Kingdom representative's proposal to add a reference to penalties in the first variant were adopted, it would seem to mean that the obligor might not only lose the sum intended as security for performance, but also be required to pay an additional penalty.

23. Mr. BASNAYAKE (secretariat) said that the only two ideas taken into account by the drafting group at the Commission's fifteenth session had been pre-estimate of damages, as liquidated damages, and security for performance, intended to cover the notion of penalty. It was important for the drafting group to know whether a further possibility was being envisaged.

24. Mr. GUEST (United Kingdom) said that there were four possibilities: the estimation of damages payable on breach of contract; the fixing of compensation payable in a

situation which might not be a breach of contract—for example, demurrage; the depositing of a sum as security for performance; and a penalty for improper performance. His delegation felt that, in keeping with the Commission's intentions, all such situations should be provided for.

25. Mr. DIXIT (India) agreed that those four possibilities should be covered. The paragraph in question must be comprehensive, since it defined the application of the entire rules. Perhaps, therefore, the Chairman could list, for the attention of the drafting group, the various omissions brought to light during the discussion.

26. The first of the two alternative final clauses seemed unsatisfactory. The fact that there was an obligation should be established, and the various aspects of incomplete performance should all be covered. And the term "a pre-estimate of" should be replaced by "predetermined".

27. Mr. DUCHEK (Austria) said that there were two points at issue: what kind of sum was involved—one to be put down in advance, or one that might have to be paid in the future; and what purpose it was to serve. On the first point, the Commission ought to clarify its intentions; in Austrian law, for example, penalty clauses related only to sums payable in the future. With regard to the purpose, the sum could represent a pre-estimate of damages, on the one hand, or a penalty or security, on the other. His delegation saw no real difference between "penalty" and "security"; it would prefer "penalty", but could accept "security" if, for example, the representatives of the English-speaking nations preferred it.

28. Mr. BASNAYAKE (secretariat), in response to an observation by the CHAIRMAN, said that the title of document A/CN.9/235 defined the scope of the rules. And indeed it had been felt, at the Commission's fifteenth session, that care should be taken to exclude any type of arrangement which could not properly be deemed liquidated damages or penalty clauses. He agreed with the representative of Austria that an agreed sum should be deemed either a pre-estimate of damages or a penalty. Agreed sums to be paid in events not constituting a failure of performance should be excluded from the scope of the rules. In his view, demurrage was such an event, since it involved the notion of delay, not of failure to perform.

29. One way to deal with the matter would be to use the term "breach of contract", thus clarifying that the sum in question was a pre-estimate of damages or a penalty. That term, it would be recalled, was used in the Vienna Convention on Contracts for the International Sale of Goods.

30. Mr. FARNSWORTH (United States of America) said that, if the scope of the rules was to be confined to breaches of contract, article D would have to be deleted.

31. Mr. HARTKAMP (Observer for the Netherlands) agreed that a distinction should be made regarding the nature of the sum to be paid, i.e. whether it was compensation or a penalty. But the text before the Commission already made that distinction and seemed to reflect what the Commission had agreed upon at its fifteenth session. The matter was surely one for the drafting group.

32. The CHAIRMAN said that, if that was so, the word "security" could not remain.

33. Mr. ROEHRICH (France) noted that the term "pre-estimate" had not appeared in the previous draft.

34. Attempts to specify intentions in too much detail would lead to difficulties; in his view, the adding of terms such as "pre-estimate" and "penalty" did not really affect the substance of the matter, which was failure to perform. Items other than those of substance could be left to the drafting group.

35. If it was agreed that the purpose was to cover as many different situations as possible, a suitable formula should be easy to find, making the purpose clear whilst not seeking to be exhaustive. But problems could arise if the notion of breach of contract was reintroduced, since the term created difficulties for civil-law countries.

36. On that basis, he agreed that the text should be referred to the drafting group.

37. Mr. SMART (Sierra Leone) agreed that all types of situations should be covered by the text and that four possibilities were involved, as stated by the United Kingdom representative. But difficulties could arise from the differences of approach between the civil-law and common-law systems. In the latter, for example, a distinction could be made between damage and loss. Perhaps it would assist the drafting group—of which he was a member—if the text was amended to read:

"(a) to contracts in which the parties have agreed that the obligee is entitled to an agreed sum of money from the obligor as damages or as a pre-estimate of damages or as a security for non-performance".

The meeting was suspended at 3.35 p.m. and resumed at 4 p.m.

38. The CHAIRMAN, summing up the discussion, said it seemed to be generally agreed that the various situations envisaged must all be covered by the text. Some doubts had been voiced in regard to expressions such as "total" or "partial failure of performance"; and a suggestion had been made that the term "retain" was better than the term "withhold". Likewise, the term, "agreed" was unsatisfactory to some speakers, and some felt that the word "intended" was subjective and should be eschewed. A few speakers had preferred the first of the two alternative final clauses, some preferring the term "penalty" to the term "security"; but the majority seemed to prefer the second alternative. Some speakers had felt that the notions of penalty, security and pre-estimate should all be covered in the text. The representative of Italy had proposed a combination of the first and second parts of the first and second alternative final clauses respectively.

39. On that understanding, and if there was no objection, he would refer the text of paragraph (1) (a) to the drafting group.

40. *It was so agreed.*

Draft article A, paragraph (1) (b)

41. Mr. BASNAYAKE (secretariat) drew attention to two points. Firstly, the uniform rules were intended to apply only to international contracts the parties to which had their places of business in different States. Secondly, the subparagraph dealt with the question of when the model law would apply; in other words, it was to deal with situations in which the model law had been adopted by the State whose law was applicable pursuant to private international law. The scope of application, therefore, was limited.

42. Mr. VOLKEN (Observer for Switzerland) felt that the text might be too restrictive and ought perhaps to be expanded so as to allow the application of the law of a third-party State in appropriate situations. Perhaps the drafting group could attend to that matter.

43. Mr. DUCHEK (Austria) agreed. The wording should reflect the same approach as the corresponding subparagraph in the text for a draft convention. His Government would in any case prefer the words "a State" instead of "the State" before the words "adopting the Model Law".

44. Mr. SEVON (Observer for Finland) said that it would be difficult to try to formulate a text so that it could serve either as a uniform law to be attached as an annex to a convention or as a draft model law. As to the particular point now under discussion, if it was desired to deal with it, that should be done in the convention itself, not in the annexed rules.

45. The solution suggested by the Austrian representative could lead to strange results. It should be borne in mind that a country would be free to adopt the model law and give it any form it desired. The forum State and the third State in question could well have both adopted the model law but introduced different changes for purposes of their internal law. Clearly, therefore, the problem could not be solved in the manner proposed by the Austrian delegation; it could only be solved by means of a provision in the convention itself.

46. Mr. HERBER (Federal Republic of Germany) said he fully agreed with the previous speaker. The difficult question of geographical scope could only be solved by means of a provision in the convention itself and not in the uniform law, because it constituted an element of the mandatory character of the rules in that law. It was therefore not a matter on which States could "opt in" at their discretion. It would be recalled that the point had led to considerable discussion at the United Nations Conference on Contracts for the International Sale of Goods held at Vienna in 1980.

47. As far as the text of paragraph (1) (b) was concerned, he suggested that the words "and the rules of private international law lead to the application of the law of a Contracting State" should be deleted. The reasons for adopting that course had been expounded at the 1980 Vienna Conference.

48. Mr. SAMI (Iraq) pointed out that the reference to the "places of business" of the parties would lead to great difficulties of interpretation in the frequent case where one or other of the parties had several places of business; in those cases, it was difficult to determine which one of those places had the closest relation with the execution of the contract. He accordingly proposed an amendment worded on the following lines: "If either party has more than one place of business, the term 'place of business' will be understood to mean the place where the contract will be actually carried out". His proposal was based on the logic that the place of execution of a contract was the most important one for both parties to the contract.

49. Mr. BONELL (Italy) said that he could not support the change proposed by the Austrian representative. He agreed with the criticisms put forward by the representative of Finland. It should be remembered that a State adopting the model law would not know which other States had also done so and, more important, to what extent the rules it contained had been adopted.

50. As he saw it, the proposed text of paragraph (1) (b) stated a self-evident rule, namely, that the model law must

have been accepted by a State and that the law of that State must be applicable to the contract.

51. That being said, he had a procedural proposal to make. At the previous meeting, the Commission had decided to leave aside the discussion on the form of the instrument and accordingly not to deal with the first few articles of the draft, dealing with the territorial application of the instrument. The present discussion had clearly shown that the provision in paragraph (1) (b) could not be discussed without deciding the form which the whole instrument would take. The only exception was the issue of the object of the convention in article A, a matter which had already been dealt with. He therefore proposed that the Commission should defer consideration of the remainder of article A, together with articles B and C, and proceed to discuss article D.

52. Mr. SONO (Secretary of the Commission) said that the approach suggested by the Italian representative conformed with what the Commission had done at its previous session. Perhaps the Commission could now proceed to deal with the substantive articles, beginning with article D, and leave until a later stage the questions that would form part of the "umbrella" or introductory portion of the convention.

53. Mr. ROEHRICH (France) said that paragraph (1) (a) dealt with the field of application of the rules, so that it had been useful to discuss it before dealing with the substantive rules. Paragraph (1) (b), however, dealt with the question of substance relating to the places of business of the parties to the contract, a matter which was connected with that of the scope of the model law. As for paragraphs (2) and (3) of article A, their contents served to explain the provision in paragraph (1) (b). Article B, for its part, set forth a consequence of the provision in paragraph (1) (b). Article C set forth certain cases of non-application of that provision. Their consideration could be postponed. Lastly, the new article X dealt with the question of agreement of the parties to derogate from articles D, E and F, and could be deferred until after those articles.

54. He shared the misgivings of the representative of Finland regarding the attempt to include in a draft intended for the unification of the law a rule of private international law, and more particularly one dealing with the problem of choice of law. Actually, the words "and the rules of private international law lead to the application of the law of a Contracting State" did not really express a rule of private international law; they simply recognized the operation of the rules of that law. His own proposal would be to drop from the draft rules any reference to questions of applicable law.

55. Mr. KOJEVNIKOV (Union of Soviet Socialist Republics) said that it would not be possible to solve the problem of paragraph (1) (b) of article A before taking a decision on the choice between the form of a convention and that of a model law. Since the Commission had agreed not to decide that issue for the time being, it would not be possible for it to deal with paragraph (1) (b) either. Accordingly, he supported the Italian proposal to defer consideration of the remainder of article A and of articles B and C.

56. Mr. FARNSWORTH (United States of America) said that he agreed with the remarks by the representative of Finland.

57. Mr. GUEST (United Kingdom) said that he also supported the Italian proposal for the same reasons as the representative of the Union of Soviet Socialist Republics.

58. Mr. DUCHEK (Austria) said he had no objection to the Italian procedural proposal but wished to clarify his earlier statement. Like the representative of Finland, he had no liking for the inclusion of any rule of conflict of laws in a uniform law. All he had said was that the concluding portion of the proposed text of paragraph (1)(b) constituted a conflict-of-law rule and he had accordingly suggested an improvement to its wording.

59. The CHAIRMAN said that, since there were no further comments on the Italian proposal, he would take it that the Commission agreed to defer consideration of the remainder of article A, and of articles B and C, together with article X, and to proceed to the discussion of article D.

60. *It was so agreed.*

Article D

61. Mr. BASNAYAKE (secretariat), introducing the revised draft of article D, said that it did not alter the substance of the previous text in any way. The opening words of the previous draft: "Unless the parties have agreed otherwise" had been deleted, as had also been done in articles E and F, because the substance of that proviso had now become the new article X reading: "The parties may by agreement only derogate from or vary the effect of articles D, E and F of this (Convention) (law)".

62. The rule in article D was one which existed in virtually all legal systems. A party which failed to perform its obligations where under a contract was not liable for damages—or for the agreed penalty—in cases where the obligor was not responsible for his failure to perform, e.g. *force majeure*.

63. At the previous session, there had been general agreement on the substance of the rule in article D. Only some drafting changes had been made, including the introduction of the words "proves that he", placed between square brackets, before the words "is not liable". The purpose of those words was to make it clear that the burden of proof was upon the obligor to show that he was not responsible for the failure of performance. It was only where such proof could be brought that the obligor was released from liability to pay.

64. Lastly, he pointed out that article D was one of the articles of the draft which the parties could modify if they so wished.

65. Mr. FARNSWORTH (United States of America) said that his delegation preferred the previous draft because of its economy of language. That earlier text was parallel in form to paragraph (1)(b) of article A, without the words in square brackets.

66. He suggested the deletion of the words "[proves that he]"; they dealt with a matter which was one for local law to decide. It was for that law to determine whether a person was excused from liability and, also, who was to bear the burden of proof.

67. Mr. HARTKAMP (Observer for the Netherlands) said that, like the previous speaker, he agreed with the substance of article D but preferred the previous drafting.

68. He also agreed that the words "[proves that he]" should be omitted as unnecessary. They embodied, moreover, a provision on the burden of proof which was legally incorrect. It was not true to say that the obligor had to prove that he was not liable. What he was called upon to do was to establish the facts on the basis of which the competent court (or arbitrator) would be able to say that there was no liability.

69. Lastly, he drew attention to the manner in which the United Nations Convention on Contracts for the International Sale of Goods signed at Vienna in 1980 had dealt with a similar problem. Article 79 of that Convention stated that the party in default had to prove that the failure of performance was "due to an impediment beyond his control". That article of the 1980 Convention thus stated the facts which the obligor was called upon to prove; it did not say that the obligor had to prove that he was not liable.

70. Mr. MUCHUI (Kenya) said that he would be prepared to accept the revised draft but supported the suggestion to delete the words "[proves that he]".

71. He agreed, moreover, with the United States representative that the language of the previous draft was more elegant. One reason for altering the drafting of the article at the previous session had been the difficulty created by the opening proviso "Unless the parties have agreed otherwise". Now that the opening proviso had been transferred elsewhere, there was no reason why the Commission should not revert to the previous draft.

72. Mr. SEVON (Observer for Finland) said that he also preferred the previous draft, on the understanding of course that the opening proviso "Unless the parties have agreed otherwise" would be dropped.

73. Lastly, he strongly urged the deletion of the words "[proves that he]", which implied a dangerous over-simplification. The inclusion of those words could well lead to a party having to pay damages simply because it experienced difficulties with regard to the burden of proof—a totally unacceptable situation.

The meeting rose at 5 p.m.

273rd meeting

Thursday, 26 May 1983, 9.30 a.m.

Chairman: Mr. CHAFIK (Egypt)

[A/CN.9/SR.273]

The meeting was called to order at 9.40 a.m.

**INTERNATIONAL CONTRACT PRACTICES:
DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES
AND PENALTY CLAUSES (continued)**
(A/CN.9/218, A/CN.9/219 and Add. 1, and A/CN.9/235)

Article D (continued)

1. The CHAIRMAN recalled that, at the previous meeting, four delegations (Finland, Kenya, Netherlands and the United States) had all expressed preference for the previous draft of article D.
2. Mr. ROEHRICH (France) said that his delegation wished to associate itself with the views expressed by the four delegations referred to.
3. Mr. BARRERA-GRAF (Mexico) said that his delegation also supported the previous draft of article D, but felt that the phrase "unless the parties have agreed otherwise" was redundant. That contingency was covered by article X, which, like the Sales Convention, provided that parties could derogate from or modify the substantive provisions of the convention or model law.
4. In the Spanish text the word "*confiscar*" should be replaced by "*retener*" in the interests of clarity.
5. He wondered whether the phrase "failure of performance" was adequate in the context of article D, and felt that the wording could usefully be supplemented by a reference to defective or delayed performance. The drafting group could be asked to supply appropriate wording.
6. Mr. CHO (Republic of Korea) said that after the previous session of the Commission his Government had held consultations in business, academic and governmental circles on the specific issue of burden of proof. The conclusion had emerged that the burden of proof did not reside with the obligor, and that the question was one to be resolved by the court or arbitrator.
7. The CHAIRMAN pointed out that the previous version of the draft article, for which there seemed to be a prevailing preference, made no reference to the burden of proof.
8. Mr. QIU (China) said that the question of burden of proof was important, and that the text should contain some reference to determination of proof before a court or an arbitral tribunal.
9. Mr. OLIVENCIA RUIZ (Spain) said that his delegation was in favour of the original draft of article D. However, it might be better to phrase the article in a positive way, i.e. to state that the obligor must pay the agreed sum if held liable for the failure of performance.
10. Mr. HERBER (Federal Republic of Germany) agreed that it might be better to formulate the article positively, since it would be strange to start a substantive provision with an exception.

11. The CHAIRMAN said that there seemed to be general acceptance of the previous version of article D. However, the suggestions that the phrase "unless the parties have agreed otherwise" should be deleted, that some reference should be made to delayed and defective performance, that the phrase "to recover or to forfeit" should be deleted and that the provision as a whole should be recast in a positive form would all be brought to the attention of the drafting group.

Article E

12. Mr. BASNAYAKE (secretariat) said that article E regulated the relationship between two potential rights of the obligee, namely the right to obtain performance and the right to obtain the agreed sum. Too great an advantage would be conferred on the obligee if the article were to provide that in all cases he could exercise both rights. On the other hand, to provide that he could only exercise one of those rights would be unfair in certain cases. The article therefore set out two rules, under the first of which the obligee was entitled both to the performance and to the agreed sum, while under the second he was entitled to opt for one or the other.
13. The reasoning behind paragraph (1) was that, where a contract so provided, the agreed sum would be quantified on the assumption that it was intended to compensate the obligee for loss suffered during the period of delay. The sum was not regarded as a substitute for performance, but rather as a compensation for the loss. In the discussions at the most recent session of the Commission there had been no serious objections to the substance of that rule.
14. Paragraph (2) provided for the case in which the agreed sum was determined as being payable in the case of non-performance of an obligation or defective performance other than delay. In that case the obligee had the option of obtaining either performance or compensation. The idea was that the agreed sum should be commensurate with the performance in monetary terms. In such a case it would be unfair if the obligee were to be entitled to both the performance and the agreed sum. However, paragraph (2) went on to say that, if the agreed sum could not reasonably be regarded as a substitute for performance, the obligee was entitled both to performance and the agreed sum.
15. It was to be noted that the rule was one to which article X applied, and which could thus be modified by consent of the parties.
16. Mr. MUCHUI (Kenya) said that his delegation preferred the earlier draft, which had the merit of brevity.
17. Mr. SEVON (Observer for Finland) said that it had been suggested in the context of article A, paragraph (1), that the circumstances of non-performance should be enumerated. The same question arose in connection with article E, and he wondered whether such a list should not be included in paragraph (1) of that article.
18. The CHAIRMAN said that, if article A was explicit as to the categories of non-performance, there was perhaps no need to reiterate those categories in article E. In any case, the wording of article E would be determined by that of article A.

19. Mr. SMART (Sierra Leone) said that, although neither draft indicated the reasoning behind article E, his delegation would prefer the earlier version. In either version, article E assumed that the obligee would be entitled to the agreed sum even if he had not suffered any loss whatsoever, provided there had been a delay. His delegation felt that something had to be added after "the agreed sum" to make it clear that the obligee would be entitled to that sum only if he had suffered actual loss during the period of delay.

20. Mr. FARNSWORTH (United States of America) said that he preferred the revised version of the article. It was true that the previous version was brief, but he would like to suggest a still more concise text, which would read: "Where the obligee is entitled to the agreed sum on delay in performance, he is entitled to both performance and the agreed sum." The fundamental question was the legal entitlement of the obligee, irrespective of whether the contract made a specific provision to that effect or not. The term "of an obligation" was deleted in his proposed version because it did not appear in article A, paragraph (1), and was redundant. The remaining alteration was more important for common-law countries, in that, while the Sales Convention had dealt with specific relief in sales contracts, and a compromise solution on that issue had been reached, the draft rules concerned liquidated damages and penalty clauses, and were not intended to impose a general requirement that specific relief should be accorded. Nonetheless, the language of the revised draft seemed to introduce that element by stating that the obligee was entitled to "require performance". He hoped that such an implication was unintended, and suggested that the words "require" should be deleted.

21. The representative of Finland had suggested that the various types of non-performance should be specified in the draft. In view of the drafting difficulties involved, the best solution might be to have a general formula for non-performance and then to be more specific in article E, paragraph (1), where it was important to identify delay as the type of non-performance concerned. Such an approach would preserve the clarity of the draft.

22. Mr. ROEHRICH (France) said that his delegation preferred the revised version of article E, paragraph (1). He did not, however, agree with the United States proposal to delete the words "the contract provides that": while there was no reference to the contract in the original draft, it seemed to his delegation that such a reference was fundamental to the text. The aim of the exercise was simply to ensure uniformity in provisions relating to contracts.

23. With respect to the discussion on the question of including a more detailed list of categories of non-performance, he fully agreed with the representative of the United States. Those categories should be enumerated in article A; paragraph (1) of article E, however, should refer to delay in performance.

24. Mr. BONELL (Italy) said he was pleased to note that other delegations shared his concern regarding the manner of definition of the various kinds of non-performance or defective performance. He agreed with the view that the best way of dealing with that problem would be through the inclusion of a general phrase in article A. Objective distinctions between the concepts, which were understood differently in the various legal systems, was well-nigh impossible; moreover, the current trend was away from attempts at such distinctions.

25. So far as the wording of article E, paragraph (1) was concerned, his delegation's preference was for the revised text,

with the oral amendments suggested by the United States representative, which improved the drafting. In his delegation's view, there were sound reasons for dealing with delay in a different manner from all other cases of non-performance, which were quite properly the subject of paragraph (2) of the article. He thus supported the existing division.

26. Mr. MAGNUSSON (Sweden) said that his delegation had no difficulty with the substance of article E, paragraph (1), and agreed that only cases of delay should be covered. It considered the revised draft an improvement over the previous draft. The amendments suggested by the United States representative would also be acceptable, although he would prefer the retention of the phrase "the contract provides that".

27. The clarity of article E, paragraph (1), might be improved by replacing the existing reference to required performance with wording to the effect that the obligee was entitled to the agreed sum even if he required and received performance. That alternative could perhaps be studied by the drafting group.

28. Mr. VOLKEN (Observer for Switzerland) said that delay in performance also involved non-observance of the place of performance; that element could be included in article E, paragraph (1).

29. Ms. OYEKUNLE (Nigeria) said her delegation preferred the revised text of article E, paragraph (1). The changes suggested by the United States representative had the merit of making the text more succinct, but care should be taken not to sacrifice precision to brevity. For example, the deletion of the phrase "the contract provides that" could lead to different interpretations under different legal systems, and place the obligee under an additional burden of proof.

30. She agreed that the paragraph should be restricted to delay in performance, and opposed the idea of listing the various kinds of non-performance, in view of the difficulty of drawing accurate distinctions between them.

31. Mr. BARRERA-GRAF (Mexico) said that his delegation preferred the revised draft of article E, paragraph (1), and was satisfied with both the wording and scope of the provision. He agreed that a general phrase should be included in article A to cover the various kinds of non-performance: specific kinds of non-performance should be dealt with only in exceptional cases.

32. Mr. DUCHEK (Austria) said that his delegation could accept the previous draft of article E, paragraph (1); alternatively, it could agree to the revised draft if some changes were made to the text. Thus, he did not consider the reference in that paragraph to the provisions of the contract to be necessary, since the uniform rules as a whole applied to contractual clauses; reference to the provisions of a contract would have to be made in all articles where an agreed sum was referred to, or not at all. He agreed that the reference to required performance was unnecessary and possibly misleading; he would therefore support the deletion of the word "require" in the third line of the paragraph.

33. His delegation fully supported the view that article E, paragraph (1), should apply only to cases of delayed performance; other cases of partial or defective performance could best be dealt with by means of a general provision in article A.

34. Mr. SMART (Sierra Leone) said that his delegation was now more than ever convinced that the revised draft of article

E, paragraph (1), should not be retained. With regard to the previous draft, he reiterated his concern that the wording did not clarify the intent of the provision as explained by the secretariat, namely that the obligee was entitled to the agreed sum only when he had suffered actual loss as a result of the delay. His delegation believed that the text should be amended to include that element.

35. Mr. SONO (Secretary of the Commission) said that the draft had been prepared on the assumption that, even if the obligor was not liable for failure of performance, he might still be held to be liable if agreement to that effect had been reached in accordance with article X. If, however, the agreed sum was shown to be grossly disproportionate in relation to the loss actually suffered by the obligee, that amount could be reduced in accordance with article G, paragraph 2. Efforts to link the amount of the sum paid to actual loss sustained would surely render meaningless the establishment of liquidated damages and penalty clauses.

36. The point raised by the representative of Sierre Leone could thus perhaps better be dealt with in the context of article G.

The meeting was suspended at 11 a.m. and resumed at 11.35 a.m.

37. Mr. SMART (Sierre Leone) said that following consultations with the secretariat he was prepared to have his proposal to amend article E, paragraph (1), discussed in the context of article G. While it was true that article G, paragraph (2), established a degree of equity in respect of the payment of the agreed sum, the burden of proof lay with the obligor, while his delegation would prefer it to remain with the obligee.

38. Mr. HERBER (Federal Republic of Germany) said that his delegation attached importance to the clarity of the uniform rules, which should contain as few elements subject to subsequent interpretation or ruling as possible.

39. His delegation was not convinced that the phrase "the contract provides that" was superfluous, since one of the conditions that would normally have to be met was to demonstrate that the contract made specific provision for the payment of a sum in the case of delay in performance.

40. His delegation would likewise prefer the retention of the word "require"; while it might admittedly be in contradiction with article Y, there was no reason why the substantive provisions should not specify exceptions to the general rules as laid down in the general provisions.

41. His delegation supported the substance of the revised draft as it stood, although it was open to drafting improvements.

42. Mr. FARNSWORTH (United States of America) said that, while his delegation did not at all support the idea of categorizing kinds of non-performance in article E, he considered it would be important for any delegation that did favour such an approach to submit a written proposal to that effect.

43. He wished also to suggest that the words "of the obligation" should be deleted from the third line of article E, paragraph (1).

44. Mr. HARTKAMP (Observer for the Netherlands) expressed support for the comments made in particular by the

representatives of France, Italy, and the United States. However, one point which was essentially of a drafting nature had not been mentioned. The paragraph stated that the obligee was entitled both to require performance and to the agreed sum. However, the right to require performance could be qualified in the contract. The article did not purport to deal with all cases, but it might be desirable to make the situation clear by inserting after the word "performance" (or the phrase "performance of the obligation") in the third line the words "as specified in the contract". That would leave the extent to which the obligee could require performance to be decided by agreement between the parties.

45. Mr. SZASZ (Hungary) said that he agreed with the ideas expressed in article E, paragraph (1), which were almost identical in the previous and the revised drafts. He did not attach great importance to the wording, provided that it expressed the idea clearly, because he presumed that, as the text would be used in the context of different civil laws, the actual wording would vary from country to country.

46. His delegation could accept the previous draft, the revised draft as it stood or the revised draft amended in the manner suggested by the representative of the United States. He had a preference for the last-mentioned solution because of its simplicity. Experience had shown that the longer and more specific a provision was, the more room there was for discussion.

47. Mr. SEKHON (India) said that he had been concerned that the article might lead to unjust enrichment of the obligee, but had been reassured by the Secretary's explanations. If, however, discussion on article G showed that it should be amended, a corresponding amendment should be made to article E.

48. Mr. MUCHUI (Kenya) said that his understanding of paragraph (1) was that it laid down a clear principle of law, namely that in a contract where an agreed sum was recoverable on delay in performance, once the delay had occurred the obligee was entitled to the agreed sum whether or not he had suffered any loss. Payment of that sum had naturally nothing to do with other remedies concerning performance, damages for delay, etc. In some cases, that provision might be very hard on the obligor, because the loss suffered by the obligee might be non-existent or insignificant. However, he understood that article G was intended to soften the harshness of the provision.

49. Mr. SAMI (Iraq) agreed with the view that the articles should contain general formulae and not enter into detail, as that was often a source of error and might lead to different interpretations.

50. Article E, paragraph (1), seemed to give rise to some misunderstanding. His delegation considered it to be subject to the general rule set forth in article D that the obligee was not entitled to the agreed sum if the obligor was not liable for the failure of performance. However, it had been suggested that the paragraph constituted an exception to the general rule set out in article D, taking into account the right of the parties under article X to derogate from or vary the effect of article D. He felt that the misunderstanding was caused by the phrase "the contract provides that". If the phrase was deleted, it would be clear that the principle set forth in article D was applicable to article E, paragraph (1). His delegation supported that interpretation; the Commission's task was to draft general rules, leaving exceptional cases to the contracting parties.

51. With regard to the suggestion of the representative of Finland concerning mention of different types of non-performance, he thought that a formula to cover the various cases might be included in paragraph (2) of article E.

52. The CHAIRMAN said it appeared that the reason why the representative of Iraq favoured the deletion of the words "the contract provides that" was that if those words were maintained the provision could be seen as an exception to article D. The point was one of substance rather than of drafting.

53. Mr. BOGGIANO (Observer for Argentina) expressed support for the revised text. The question of whether or not an obligee was entitled to the agreed sum even when the delay had not caused loss was of decisive importance. There was an assumption that where there was delay there was also loss. However, account should also be taken of the rules in article G; paragraph (1) of article E should be brought in line with article G in order to give equitable treatment to both parties.

54. With regard to drafting, in view of the points raised by the representatives of France, the Federal Republic of Germany, the Netherlands and the United States, it might be preferable to delete the phrase "the contract provides that" at the beginning of the paragraph and replace the words "an obligation" in the second line by the words "a contractual obligation".

55. Ms. OYEKUNLE (Nigeria) wondered whether, if the words "as specified in the contract" were added in the third line, as suggested by the representative of the Netherlands, the words "the contract provides that" in the first line should be deleted.

56. Mr. HARTKAMP (Observer for the Netherlands) said that he would like both phrases to be retained because it was important to make clear the exact rights of the obligee in cases of delay or non-performance.

57. Mr. TOLENTINO (Philippines) expressed his delegation's agreement with the substance of article E, paragraph (1). When the contract provided that the obligee was entitled in case of delay to an agreed sum, that amount had been agreed upon by the parties to cover damages for delay. The paragraph should not, however, be considered in isolation but read in conjunction with other provisions such as those in articles D and G.

58. His delegation felt that the words "the contract provides that" were not essential but was willing for them to be maintained if the majority so desired. In the third line of the paragraph, the sentence would be editorially neater if the word "require" were deleted.

59. Mr. SONO (Secretary of the Commission) said that many representatives had proposed the deletion of the phrase

"the contract provides that". The representative of the Netherlands had suggested the insertion of the words "as specified in the contract" in the third line of the paragraph; if that suggestion was adopted, he did not think that the words "the contract provides that" in the first line would be necessary.

60. Some representatives had suggested the deletion of the word "require". If that word was deleted, the new article Y would, he thought, become superfluous.

61. The general understanding seemed to be that article E, paragraph (1), was not an exception to article D but supplementary to it. The drafting group would clarify all those points.

62. Mr. OLIVENCIA RUIZ (Spain) thought that the reference to the contract at the beginning of paragraph (1) should be maintained because the function of the agreed sum could be determined only with reference to the contract. However, the wording of the revised text was too specific and could be misinterpreted. He therefore suggested that the words "the contract provides that" should be replaced by the words "in conformity with the contract". His delegation was not in favour of the amendment suggested by the representative of Argentina because there might be obligations of other contractual origin.

63. With regard to the loss suffered by the obligee, it was difficult to discuss separately clauses which were part of a whole. The matter should be considered again when the Commission discussed article G. However, he wished to point out that, with respect to delay in performance, the agreed sum had the function of a penalty or sanction. Consequently, a direct link should not be established between the agreed sum and the loss sustained.

64. He was in favour of retaining the word "require" because any other wording would be too vague.

65. Mr. ROEHRICH (France) thought that, since it seemed agreed that article E, paragraph (1), was a special case of application of articles A and D, the reference to the contract was not after all necessary. The scope of the rules had been defined in article A as covering contracts and the application had been set forth in article D. The delay was a matter of fact and not a contractual provision. The drafting group should find a simpler wording along the lines suggested by the representative of the Netherlands.

66. The CHAIRMAN said that he hoped that any fears that article E, paragraph (1), was an exception to article D had been dispelled. It had been thought desirable to mention the special case of delay in performance, but it was understood that article D was still applicable.

The meeting rose at 12.40 p.m.

274th meeting

Thursday, 26 May 1983, at 2 p.m.²

Chairman: Mr. CHAFIK (Egypt)

[A/CN.9/SR.274]

INTERNATIONAL CONTRACT PRACTICES:
DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES
AND PENALTY CLAUSES (continued)
(A/CN.9/218, A/CN.9/219 and Add. 1, and A/CN.9/235)

Article E, paragraph (1)

1. The CHAIRMAN, summing up the discussion on paragraph (1), said that only two points of substance had been raised. The first was the observer for Switzerland's suggestion that the paragraph should cover, in addition to the question of late performance, that of defective performance, e.g. execution in a place other than that specified in the contract. Since none of the member delegations had endorsed that suggestion, it could be treated as rejected.

2. The second point of substance was the concern expressed by the representative of Iraq that the provision in paragraph (1) might be construed as an exception to article D. An assurance had been given that no such interpretation could be placed on that paragraph. The drafting group would of course bear that in mind when deciding on the text of paragraph (1).

3. With regard to the wording of paragraph (1), a number of drafting points had been raised by the United States representative, who had proposed the deletion of the opening words, "Where the contract provides that", and also of the words "of an obligation", which appeared in two places in paragraph (1). Those suggestions would be examined by the drafting group.

4. There had also been some criticism of the use of the verb "to require", and it would be for the drafting group to seek more appropriate language.

5. In conclusion, he noted that the majority of members favoured the revised draft of paragraph (1) and suggested that it should be referred to the drafting group.

6. *It was so decided.*

Article E, paragraph 2

7. Mr. BASNAYAKE (secretariat) explained that paragraph (2) covered both the case of non-performance and that of defective performance other than delay. If the contract specified that the obligee was entitled to the agreed sum on non-performance or defective performance other than delay, the obligee then had to choose between claiming performance or demanding the agreed sum; he could not have both.

8. The second sentence of paragraph (2) embodied a reservation; it specified that the obligee did not have to make such a choice where the agreed sum did not constitute a substitute for performance. The alternative provided for in the first sentence was based on the assumption that the agreed sum could be regarded as a substitute for performance; in that

case, it would be excessive to give the obligee both the agreed sum and the right to claim performance. In the situation envisaged in the second sentence, however, it was fair to give both.

9. Turning to the drafting changes introduced into the statement of that exception, he said that there had been a strong feeling that the circumstances for setting aside the rule now contained in the first sentence should be embodied in a separate sentence and not in a concluding proviso as in the previous draft. The appropriate changes had therefore been made in order to clarify the presentation.

10. Lastly, there had been a suggestion to include a reference to the issue of burden of proof; hence the introduction of the words "the obligee proves that", placed between square brackets.

11. Mr. BARRERA-GRAF (Mexico) suggested that, instead of mentioning different kinds of failure of performance, paragraph (2) should refer to "failure of performance" in general, which would cover non-performance due to delay, defective performance and other cases as well.

12. He urged that the words "the obligee proves that" should be dropped, as had been done in article D.

13. Turning to the substance of paragraph (2), he drew attention to footnote 24 (A/CN.9/235, page 12), and in particular to the concluding sentence, to the effect that the cumulation of remedies provided in the second sentence of paragraph 2 might in some circumstances unjustly enrich the obligee. He considered that the point should be left in abeyance until the Commission came to consider article G, in which paragraph (2)(a) dealt with the case where the agreed sum grossly exceeded the loss suffered by the obligee. Paragraph (2) of article E obviously had to be dealt with in conjunction with that provision.

14. In conclusion, he said he found paragraph (2) acceptable, provided that the words "the obligee proves that" were dropped.

15. Mr. BONELL (Italy) said that it would be the task of the drafting group to examine the text of paragraph (2) in the light of the amendment of paragraph (1) and to bring the two into harmony. That would dispose of such problems as the proposal to drop the opening five words, the suggestion to delete the words "is entitled to" and other similar points of drafting.

16. With regard to references to defective performance and to non-performance, he shared the misgivings of the representative of Iraq. Perhaps a formula similar to that used in article A might be appropriate. He would himself suggest a wording on the following lines: "On failure of performance other than delay ...", so as to avoid any specific reference to particular cases of non-performance and defective performance.

17. On the question of the words "the obligee proves that", he agreed with the Mexican representative but wished to point out that the question had already been decided with respect to article D. As he saw it, the decision then taken was applicable to article E as well.

²In the original Summary Record there is no note of the exact time the meeting was called to order.

18. Turning to the substance of the second sentence of paragraph (2), he stressed that he would have himself preferred to drop the sentence altogether. Nevertheless, he realized that it reflected a compromise achieved as the result of a lengthy debate and would not press his viewpoint.

19. The CHAIRMAN said that the question of the reference to burden of proof had indeed been decided in connection with article D in relation to the creditor. If the drafting group dropped the reference to burden of proof in article D, it would automatically have to do the same in article E, which concerned the debtor. The two points were obviously interconnected.

20. Mr. ROEHRICH (France) said that the Commission itself had taken a decision of substance in the matter; the question was not a point of drafting to be settled by the drafting group.

21. The CHAIRMAN concurred with the French representative's interpretation. The passages in square brackets dealing with burden of proof in both article D and article E had to be regarded as definitely deleted.

22. Mr. SAMI (Iraq) said that it would be for the drafting group to find a sentence which would adequately express the idea that the provisions of paragraph (2) were applicable in the other cases of non-performance.

23. With regard to burden of proof, he welcomed the decision to drop the words "the obligee proves that" in articles D and E. Questions of proof should be left to the local law. There was therefore no need to specify the person upon whom the burden of proof rested.

24. Turning to the substance, he strongly felt that a person demanding performance could not in the same breath ask for damages. The obligee had the right to demand fulfilment of the obligation or, alternatively, to claim damages for the losses incurred by him as a result of delay. There would be no justification for his retaining the agreed sum and still asking for performance.

25. Mr. ROEHRICH (France) said that he favoured the general philosophy and the underlying principle of paragraph (2). The rule on the choice between the agreed sum and performance was a crucial one for the whole draft.

26. With regard to the drafting, he agreed with the Italian representative on the need to bring the wording of paragraph (2) into line with that of paragraph (1). The problems dealt with in the two paragraphs were similar in character.

27. The text of paragraph (2) reflected a welcome compromise between opposing views. Its consideration should not be postponed pending the examination of article G, which was a separate provision dealing with a more general problem. Even if article G were to be kept in the draft, paragraph (2) of article E should still be retained.

28. Mr. TOLENTINO (Philippines) said that he accepted the principle embodied in the first sentence of paragraph (2) but agreed that its wording should be brought into line with that of paragraph (1). In particular, he favoured dropping the words "to require" before the word "performance". That deletion would not involve any change in meaning.

29. With regard to the operation of the provision in that first sentence, he had in mind a case which he felt should receive attention, namely, that of a defective performance

which nevertheless amounted to substantial, though not full, performance. In that situation, the obligee could retain the benefit of that substantial performance and then go on to claim the agreed sum from the obligor, and the two benefits together might well be excessive and amount to unjust enrichment. That being so, the provision in the first sentence of paragraph (2) should be correlated with the principle embodied in article G.

30. Another case which he had in mind was that of an irregular performance or defective performance which was not attributable to the negligence of the obligor but was due to circumstances beyond his control. There appeared to be no reason why the obligee should be entitled either to performance or to the agreed sum. That situation was governed by totally different principles of law.

31. With regard to the cumulative effect provided for in the second sentence of paragraph (2), the same problem arose. Performance and the agreed amount taken together might well be excessive, thereby resulting in an unjust enrichment of the obligee. Here again, it was necessary to correlate the provision with the provisions of article G.

32. Lastly, he wished to mention the problem of a case in which the obligor had not performed his obligation in time, so that there had been delay in performance, but before the obligee could take legal action with regard to that delay, there was a defective or irregular performance on the part of the obligor. That situation did not appear to be covered by either paragraph but if the provisions of paragraph (1) were to operate, a cumulative claim would arise. If, however, the situation was considered as falling under paragraph (2), the obligee would have the option of either claiming performance or demanding the agreed sum.

33. In that situation, another problem arose if the obligee accepted the defective performance, namely, the question whether such acceptance constituted a waiver of his right under delay.

34. Mr. OLIVENCIA RUIZ (Spain) also favoured for paragraph (2) a formulation similar to that of article A and urged the use of the comprehensive expression "failure of performance" (*falta de cumplimiento*) so as to cover with that one formula all cases of non-performance other than delay. Actually, those cases were many and varied—a fact which explained the doubts of the representative of the Philippines. The general formula which he favoured would cover such cases as partial performance and defective performance.

35. The application of the same rule to a number of very diverse cases could give rise to hardship in some situations, but the provisions of article G should serve to attenuate those results.

36. There was also the problem of a delay which did not prevent late performance. The solution depended on whether, in the particular case, the time-limit was an essential factor in the contract.

37. As to the concluding sentence of paragraph (2), his delegation had always favoured compromise solutions. It felt, however, that the language should be improved. The use of the expression "substitute for performance" gave rise to serious problems. It should be remembered that paragraph (1) of article A specified that the agreed sum could be intended either as "a pre-estimate of damages" or as "a penalty for failure" of performance. The expression "substitute for performance" had not been used before and should not now be introduced as an extraneous concept in article E.

38. The concept of "a substitute for performance" could suggest the interpretation that the obligor might himself have a choice in the matter and be able to offer the agreed sum in lieu of performance. Obviously, that could not be the case. He therefore urged that an effort should be made to find a better expression. He stressed that the point was one of substance, and not merely of drafting.

39. Mr. MUCHUI (Kenya) supported the suggestion that the terms "non-performance" and "defective performance" in the first sentence should be replaced by a general term such as "failure of performance other than delay".

40. Regarding the second sentence, he agreed with the representatives of Iraq, Philippines and, to some extent, Italy that it tilted the balance of the paragraph in favour of the obligee. His delegation could not envisage a situation in which an agreed sum would be paid for failure of performance other than delay and the obligee would also be entitled to require performance. It was essential to consider what precisely the agreed sum was intended to cover. The problem arising out of the second sentence of paragraph (2) might better be dealt with under article G.

41. The CHAIRMAN said that a serious question of substance had arisen concerning the second sentence of paragraph (2). The Commission would have to decide between three possibilities: to retain paragraph (2); to delete it; or to postpone the debate until it came to article G.

42. Mr. BONELL (Italy) while agreeing that the Commission was faced with an important issue on which a decision of principle was perhaps needed at the present time, said that he could not consider the idea of postponing a decision until article G was reached, since that would mean linking two entirely different questions. Some representatives argued that there was no difference between the situation under article G, where the agreed sum itself was excessive, and the situation under article E (2), where the agreed sum appeared excessive because it was added to performance, the obligee being entitled to require both performance and the agreed sum. However, the Commission was drafting different provisions and must keep them separate. Indeed, the question whether the agreed sum was excessive or not was totally irrelevant to the question that the Commission had to decide in the second sentence of article E (2), namely, whether in the particular circumstance envisaged the two remedies should be cumulative. He urged that the Commission should decide, if possible at the present time, whether or not to maintain the second sentence, but should in any case not postpone a decision until it reached article G.

43. The CHAIRMAN said that he had merely sought to summarize the discussion. Personally he agreed with the representative of Italy.

44. Mr. SONO (Secretary of the Commission) said that it would be unfortunate to link the present provision with article G, which was an umbrella provision to take care of all situations where the outcome was unfair. It would also be unfortunate to delete the second sentence of paragraph (2), since, while the wording "substitute for performance" might need clarifying in the drafting, situations did occur where a party was entitled to both the agreed sum and performance. He instanced the case of delivery of a machine 10 per cent below capacity, where the parties agreed on a sum to cover the defect and the buyer retained the machine and also obtained the agreed sum. Alternatively, a small sum might be agreed upon as compensation and if the defect was remedied within a certain period there would be the possibility of the

cumulative application of paragraphs (1) and (2). As long as there was a common understanding of what was intended, the wording could be clarified by the drafting group. It would, however, be unfortunate to delete the second sentence of paragraph (2) because there was a connection between it and paragraph (1), both being based on similar ideas. Confusion might have arisen from the phrase "as a substitute for performance", and if that could be clarified by the drafting group to establish a common understanding, he did not see much substantive difference of view among delegations.

45. Mr. MAGNUSSON (Sweden) endorsed what had been said by the representative of Italy and the Secretary. Articles E and G were both needed, and he would favour retaining both sentences in article E (2). He could accept that paragraph in substance, although it needed redrafting so as to be more consistent with paragraph (1). Indeed, there was no reason why the two paragraphs should not be combined—as the Secretary seemed to have hinted. He was in favour of the idea of rewording the first sentence of paragraph (2) on more general lines, because if the obligee was entitled to an agreed sum on delay, that sum could not reasonably be regarded as a substitute for performance.

46. Mr. ROBINSON (Observer for Jamaica) said that the answer to the question raised by the representative of the Philippines depended on whether the rules were meant to be exhaustive in respect of relations between the obligor and the obligee. In his opinion they were not and would not preclude application of domestic law where appropriate.

47. He was pleased to note that a distinction had at last been made between the situations covered by articles G and E respectively, because they were very different in substance. He agreed with the views of the representatives of India, Kenya and Sierra Leone but was not in favour of postponing the problem until article G was discussed.

48. Regarding the view that coupling performance of an obligation with the agreed sum might result in inequity—or unjust enrichment—it might be advisable to include a special provision identifying the situations in which performance of the obligation might equitably be required as distinct from the agreed sum.

49. Mr. TARKO (Austria) said that in a spirit of compromise, his delegation supported the revised draft of paragraph (2) as it stood, which did not differ in substance from the previous draft. It could, of course, be improved by the drafting group, e.g. by replacing "non-performance" and "defective performance" by "failure of performance".

50. He was opposed to linking articles E and G, because they dealt with opposing situations. He supported the views of the representative of Italy.

51. With regard to the question raised by the representative of the Philippines, the relationship between delay and effective performance depended on what the parties had stipulated. If the obligor was to pay a sum for delay, the obligee would be entitled to claim that sum in the event of delay. In the event of subsequent defective performance, if the parties had stipulated a penalty clause, the obligee would also be entitled to ask payment for effective performance.

52. Mr. GUEST (United Kingdom) said that despite the misgivings of certain delegations, there was nothing inherently wrong in giving one of the contracting parties the right to claim an agreed sum in addition to the right to performance of the contract. An example was the case of the purchaser of a

computer system with hardware and software, for use, say, by a travel agency, where the contract provided that in the event of down time on the computer due to mechanical defects in excess of 20 hours a month the seller should pay the buyer a fixed sum by way of liquidated damages for every hour in excess of the 20 hours down time, even though the buyer was still entitled to performance, namely, that the computer system should be made to operate for the purposes for which it was required. The difficulties in respect of paragraph (2) were, he felt, caused by the wording. For example, the phrase "substitute for performance" was not entirely satisfactory, for the reasons expressed by the representative of Spain; and he had doubts over the words "the agreed sum cannot reasonably be regarded as a substitute for performance", which seemed to indicate that there was some criterion of reasonableness, or reasonable regard, apart from the terms of the contract itself. He would prefer to see the idea more closely linked to the intentions of the parties as expressed in the contract. The drafting group might then consider providing a more general clause in paragraph (2) simply stating in principle that in cases other than those in paragraph (1) the question whether the obligee was entitled either to require performance or to the agreed sum, or to the agreed sum in addition to performance, was a matter to be determined by the terms of the agreement made between the parties. That would constitute approval of the principle of cumulation where cumulation had been provided for by the parties, leaving to a later stage—possibly under article G—the question of the control to be exercised against abuse of that type of situation.

53. Mr. HARTKAMP (Netherlands) supported the earlier statement by the representative of Italy on the first sentence of paragraph (2). Regarding the second sentence, in the light of the Secretary's explanation and the comments of the United Kingdom representative, he was not certain whether the problem was one of drafting or substance. The Secretary's example would not fall under the second sentence as it stood, because it involved defective performance and not performance—which he understood as perfect performance. There would be performance if the seller repaired the machine, and then it would be unfair to add the agreed sum. Perhaps the difficulty lay in the word "performance": he would find it odd for creditors to require both performance and the agreed sum. It would be better to leave the matter to the drafting group.

54. With regard to paragraph (2) as a whole, if his proposal at the previous meeting to insert the words "as specified in the contract" in paragraph (1) was adopted, a similar insertion should be made in the second paragraph, in both the first and second sentences if retained.

The meeting was suspended at 3.30 p.m. and the discussion covered in the summary record was resumed at 4.10 p.m.

55. Mr. SAWADA (Japan) said that the substance of article E (2) was different from that of article G and that he fully agreed with what the Italian representative had said. The reasons for retaining the second part of paragraph (2) had been fully explained by the Secretary of the Commission. His delegation was in favour of retaining paragraph (2), although some changes in the wording might be desirable.

56. Mr. FARNSWORTH (United States of America) said that article E was one of the provisions about which he felt uneasy. It was dangerous to write simple rules for complex situations. He agreed with the representative of Italy that the only question of concern was whether the agreed sum was cumulative or alternative. Paragraph (1) covered the only case

on which everyone was agreed, namely, delay, when it was cumulative. Paragraph (2) covered all other cases, when it was sometimes alternative, sometimes cumulative. In his opinion, both possibilities should be maintained. If, however, the second sentence were to be deleted, the first sentence should also be deleted. He also supported the United Kingdom representative's suggestion for making the matter dependent on interpretation of the contract.

57. In fact, however, little of value had been said: paragraph (1) dealt with a case so simple that there could scarcely be any disagreement; and paragraph (2) dealt with something which was already a matter of law.

58. However, considering the question raised by the representative of Switzerland in connection with paragraph (1), as to what would happen in the event of delivery to a different place, the answer lay not in paragraph (1), but in the second sentence of paragraph (2), which was therefore necessary. But how would paragraph (2) be applied where there was, say, a contract for the sale of goods for delivery in Zurich and provision for liquidated damages, or penalty, if delivery was made to Basel? There was clearly an entitlement to performance as well as the penalty, but it was impossible to tell from the draft how it was intended to be applied in practice. However the paragraph was drafted it would be at such a general level that it would not answer any useful questions. He therefore suggested that the Commission should consider the possibility of deleting the article, on the grounds that nothing useful could be put into paragraph (2) and nothing significant was contained in paragraph (1).

59. Mr. HERBER (Federal Republic of Germany) thought the drafting group could attend to the wording of the first sentence of paragraph (2), to take into account the observations made by previous speakers.

60. He shared the view that the second sentence was necessary, whilst agreeing that it should be amended so as to provide more objective criteria for deciding whether the agreed sum referred to could reasonably be deemed a substitute for performance—a matter of substance rather than of drafting.

61. In his view, the chief difficulty arose from the attempt to deal simultaneously with liquidated damages and penalty clauses, which had different purposes. The question was how to determine the purpose intended by the parties—such as compensation, security or penalty.

62. In substance, therefore, he agreed with the United Kingdom representative on the need for the second sentence to make it clear, without being too explicit, that the sole criterion was what the parties intended—an additional penalty or a pre-estimate of damages. He hoped that the drafting group could amend the text along those lines; it could perhaps add wording to the effect that the provision would apply also if the sum in question was too low to be reasonably regarded as damages. In view of the article's purpose, the Commission's main concern should be to achieve the utmost clarity.

63. Mr. ROEHRICH (France) said that any attempt to reflect the contracting parties' intentions would simply create problems and was unlikely to lead to the establishment of precise criteria. The criterion referred to by the United Kingdom representative was in any case subjective. National laws differed in the way they sought to establish intentions if those intentions were unclear; and if they were clear the matter fell within the scope of article X.

64. Perhaps, as the representative of the Federal Republic of Germany had suggested, a more specific approach could be made in the second sentence of paragraph (2), by means of wording such as "compensation for lack of performance"—a matter which the drafting group could be asked to consider; but it would be dangerous to attempt, under article E, to cover the question of the parties' intentions.

65. Mr. BOGGIANO (Observer for Argentina) referring to the second sentence of paragraph (2), said it was a question not of a sum being excessive, and thus related to article G, but rather of whether or not it was justified. It should be noted that the examples cited by previous speakers had all related to non-performance or imperfect performance. He agreed with the representative of Spain that the grounds for the agreed sum would have to be established; and if the possibility of complete performance plus an agreed sum was accepted, the expression "a substitute for performance" could not be used. Perhaps the sum could be deemed compensation; but that was a matter of substance, not of drafting.

66. If, as he understood it, the sentence was intended to be based on proper performance, the reason for providing an agreed sum in addition should be clarified. If clarification was not possible, the second sentence of paragraph (2) should be deleted.

67. Mr. KOJEVNIKOV (Union of Soviet Socialist Republics) considered that article E related to an important substantive rule on a matter which reflected some disparities among national legal systems: according to some, penalty and performance were cumulative; under others, they were alternatives.

68. Paragraph (2) of the revised draft was a reasonable compromise stemming from intensive deliberations in the Working Group and the Commission at the latter's fifteenth session; to unbalance that compromise by amending the paragraph's second sentence would be undesirable. He agreed with the representative of France about the United Kingdom representative's observations; textual amendments relating to interpretation of the contracting parties' intentions would in any case merely duplicate the provisions of article X. The second sentence of paragraph (2) was not perfect, and the desire expressed by some speakers for a better wording was understandable. The important point, however, was that the criteria expressed in that sentence should be as objective as possible, even though their application might be determined by the contracting parties' intentions. As it stood, the text had that objective element, and he therefore hoped that the Commission would approve paragraph (2). Perhaps the drafting group could try to improve the text, whilst respecting the compromise reached.

69. Mr. SAMI (Iraq) said that the text seemed to be raising unforeseen problems. To pursue the example cited by the secretariat, two points must be distinguished. Firstly, if defective performance was established before, say, the time for full commissioning of a plant had elapsed, the question then was whether the obligee could in fact require both performance of the obligation and the agreed sum, or simply completion of performance, since delay had not yet been incurred. In cases where delay had been incurred, the

provisions of paragraph (1) would apply. In his view, therefore, the second sentence of paragraph (2) served no purpose and should be deleted.

70. Mr. BONELL (Italy) said that the debate had heightened his original misgivings about the second sentence of paragraph (2). For one thing, the parties could derogate from its provisions under article X. Moreover, in all cases it would have to be determined whether the agreed sum could be regarded as a substitute for performance—which meant determining the parties' intentions. That implied either a reference to article X—and in that connection he could not agree with the representatives of France and the Union of Soviet Socialist Republics or, as mentioned by the United Kingdom representative and some other speakers, the addition to the second sentence of wording which, whilst not affecting the substance, would relate the matter to the parties' intentions. In his view, the question of interpretation must always arise.

71. It seemed to him that an obligor would surely object to providing performance of the obligation as well as an agreed sum; given the provisions of article X, therefore, the second sentence of paragraph (2) seemed of no effect.

72. The observations by the representative of the Federal Republic of Germany about differing purposes applied only to a certain extent, since the text of article A, which referred to a pre-estimate of damages, or penalty, or both, implicitly recognized that the parties' intentions could be a combination. Moreover, as the Netherlands and United Kingdom representatives had noted, it was possible to expand the number of specific situations which could be covered by the rules.

73. Since it was a question of interpreting the parties' intentions, and in view of the provisions of article X, the first sentence of paragraph (2) would suffice.

74. The CHAIRMAN said that a majority of speakers had been in favour of retaining paragraph (2). Opinions had differed with regard to the wording, but it seemed generally agreed that the text required improvement; whilst some speakers thought only minor amendments necessary, others had proposed more substantial changes, such as additional wording based on the need to interpret the contracting parties' intentions. It seemed generally agreed that the wording "not reasonably be regarded as a substitute for performance" should be amended. If there was no objection, therefore, he would ask the secretariat to consider the various points raised, with a view to submitting some compromise proposals for the Commission to consider at its next meeting.

75. *It was so agreed.*

76. Mr. SONO (Secretary of the Commission) said that the general feeling seemed to be in favour of retaining the second sentence of paragraph (2), although a literal interpretation of the text as it stood had created some difficulties. He would therefore seek consultations with the drafting group with a view to improving the text.

The meeting rose at 5.05 p.m.

275th meeting

Friday, 27 May 1983, at 9.30 a.m.
Chairman: Mr. CHAFIK (Egypt)

[A/CN.9/SR.275]

The meeting was called to order at 9.40 a.m.

**INTERNATIONAL CONTRACT PRACTICES:
DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES
AND PENALTY CLAUSES**

(continued)

(A/CN.9/218, A/CN.9/219 and Add.1, and A/CN.9/235)

Article Y

1. Mr. BASNAYAKE (secretariat) introducing article Y, said that it was designed to protect those jurisdictions, notably common-law jurisdictions, in which the grant of specific performance was an exceptional remedy. During the discussion on the United Nations Convention on Contracts for the International Sale of Goods, it had proved impossible to unify laws on enforced performance and article 28 had therefore been included, which was almost identical to article Y. At the previous session, representatives of the common-law systems had suggested that such an article should be included in the convention under discussion.
2. The basic idea behind article Y was to ensure that a court retained the right to apply rules that it would apply with respect to specific performance in the case of contracts not covered by the rules under discussion.
3. Mr. ROEHRICH (France) asked if the Commission had taken a decision on the word "require" in article E, paragraph (1), which was closely linked to article Y.
4. The CHAIRMAN replied that there had been a clear majority in favour of deleting the word and that it had been left to the drafting group to find the exact wording.
5. Mr. WAGNER (German Democratic Republic) said that his delegation was in favour of deleting article Y, because the uniform rules should deal with liquidated damages only and not with performance as such.
6. Mr. FARNSWORTH (United States of America) pointed out that the Convention on Contracts for the International Sale of Goods had dealt with buyers' and sellers' remedies in general and had given both buyer and seller the right to require performance. The Commission was not currently dealing with remedies in general and should not give a party a right to require performance, but should leave that to domestic law or to the earlier Convention if applicable. It should, however, deal with the effect of a right to an agreed sum in a case in which a party would under domestic law have the right to require performance. He did not think that article Y helped to achieve that aim. However, its deletion would require an addition to article E, along the lines that if the obligee would otherwise be entitled to require performance, then the fact that he was entitled to an agreed sum did not preclude him from doing so. Some such general statement would avoid the problem of saying in article E that the obligee had a right to require performance when that was not a function of the rules under discussion.
7. Another problem was related to articles E and X. Once the right to require performance was stated, the question arose as to whether the obligee was entitled to the agreed sum if he had succeeded in obtaining performance. He hoped the drafting group would deal with that problem on the basis of the discussion in the Commission. There should be an initial paragraph in article X saying what it was trying to express, namely, that if an obligee had the right to require performance, he was not precluded from doing so just because the parties had agreed on a specific sum.
8. Mr. MAGNUSSON (Sweden) fully endorsed the view that article Y should be deleted, and also that the rules should avoid referring to the right to require performance as far as possible. He therefore preferred that article E should be redrafted in such a way that article Y was no longer needed. At a previous meeting he had made some proposals concerning the redrafting of article E, paragraph (1), which might say that the obligee was entitled to the agreed sum even if he required and obtained performance.
9. Mr. EDWARDS (Australia) said that, for his delegation, a provision such as that in article Y was clearly necessary so long as article E carried with it a possible implication that it conferred the right to performance. Merely to delete the word "require" would not satisfy his delegation because the words "the obligee is entitled both to performance of the obligation and the agreed sum" would still remain and might be interpreted by a common-law court as conferring a right and not just as referring to a right which might already exist. Any decision with regard to article Y must therefore depend on satisfactory drafting of article E. What the Commission was concerned with was liquidated damages and penalty clauses; the entitlement to those remained, and performance was a secondary matter. It should be made clear in article E that the right to the agreed sum was independent of the conferment of a right to performance under the applicable national law. If that was done, his delegation would not oppose those who wished article Y deleted.
10. Mr. GUEST (United Kingdom) agreed with the previous speaker. He would welcome a reformulation of article E which rendered article Y unnecessary, but could not make any decision on the deletion of article Y until he had seen the wording produced for article E. Mere deletion of the word "require" would certainly not eliminate the need for article Y.
11. Mr. SMART (Sierra Leone) said that whatever wording was used in article E, the remedy of specific performance would remain, because the obligee was entitled both to performance and to the agreed sum in cases of delay. Under common law, the remedy of performance was not available as a matter of course. Article Y was trying to protect that remedy and should therefore be retained.
12. Mr. LEBEDEV (Union of Soviet Socialist Republics) suggested that when the drafting group was studying alternative wordings for article E it might consider the formulation which had already appeared in one draft and which stipulated that the right of the obligee to the agreed sum did not exonerate the obligor from his duty to perform the contract. Such a wording would deal with the question of specific performance and thus dispose of the problem in article Y.

13. The CHAIRMAN asked if the representative of the Union of Soviet Socialist Republics wished to postpone the discussion of article Y until article E had been redrafted.

14. Mr. LEBEDEV (Union of Soviet Socialist Republics) replied that since article Y had been drafted at the request of common-law countries, many of which apparently preferred to postpone a decision on its deletion pending the redrafting of article E, that seemed the best course to pursue.

15. Mr. SONO (Secretary of the Commission) asked whether the representative of Sierra Leone too would be willing to reconsider the matter if the redrafting of article E, paragraph (1), took care of the problems which concerned him.

16. Mr. SMART (Sierra Leone) said that as long as a remedy of performance was available to the obligee under article E, it was necessary to retain article Y, because under common law specific performance was not available to any litigant as a matter of course and the court had to consider the circumstances of each case.

17. Mr. MUCHUI (Kenya) pointed out that the performance referred to in article E was not specific performance as understood in common-law countries, but was really the other rights available to the obligee such as a claim for damages. If, therefore, article E was redrafted in such a way that that fact became perfectly clear and that the recovery of the agreed sum did not affect the obligations of the obligor with regard to performance as part of the contract, he could agree to the deletion of article Y.

18. Ms. OYEKUNLE (Nigeria) endorsed the statements made by the representatives of Australia and the United Kingdom. The idea introduced in article Y should appear somewhere in the uniform rules, but the present wording might cause difficulties for the courts. She supported the view that the idea should be included somewhere in article E.

19. Mr. BONELL (Italy) fully supported the statement by the representative of Kenya, who had brought out the essential point, which was that the reference to performance in article E had nothing to do with a judgment for specific performance. He would go even further and say that even a hint that the article was dealing with questions of remedy could be misleading. The underlying idea was that in addition to the sum fixed in advance, the obligor was still bound to perform. The redrafting of article E should take that into account. The idea suggested by the representative of the Union of Soviet Socialist Republics was a good one. Another possibility was to use a wording such as "is entitled to require from the obligor either". If that essential fact was taken into account, the discussion about article Y would be superfluous.

20. The CHAIRMAN said that the majority clearly wished to postpone consideration of article Y until the drafting group produced a revised text of article E.

21. *It was so agreed.*

Article F

22. Mr. BASNAYAKE (secretariat) explained that the article regulated the relationship between the right to receive the agreed sum and the right to receive damages for failure of performance. It embodied a compromise between the systems which said that when an agreed sum was stipulated, that sum and no more could be claimed, and those which permitted the recovery of damages if loss could be proved which was not covered by the agreed sum.

23. The reason for the alternatives between square brackets had arisen out of discussion at the previous session, when it had been asked on what basis the obligee could claim damages. It had been suggested that the basis was article F itself, but the prevailing view had been that the applicable law was the law of contract. It had been felt that substitution of the phrase "may not assert a claim for damages" would bring out the point that when the obligee was trying to obtain damages he was asserting a claim which related to the applicable law of contract.

24. Mr. HERBER (Federal Republic of Germany) pointed out that the last phrase of the article introduced an element of uncertainty. The need to decide what "grossly" exceeded the agreed sum might lead to controversial judgments in the courts. He would therefore prefer that phrase to be deleted.

25. Furthermore, article F should be read in conjunction with article E. Under the latter, it was assumed that the agreed sum was an advance estimate of possible damages. The first sentence of paragraph (2) of that article stated that on non-performance, the obligee was entitled either to require performance, or to the agreed sum. However, article F raised the possibility of a claim for damages if the loss grossly exceeded the agreed sum. If the obligee wished to invoke that clause, was he obliged to choose performance under article E or if he had chosen the agreed sum, did article F modify the rules concerning that sum?

26. Mr. BASNAYAKE (secretariat) said that article F was intended to apply to a case in which the agreed sum was claimed by an obligee but was much less than the loss he had suffered.

27. Mr. HERBER (Federal Republic of Germany) said that the import of the article could perhaps be made clearer.

28. Mr. OLIVENCIA RUIZ (Spain) said that under article A the sum could be agreed upon either as an indemnity or as a penalty for failure of performance. If the agreed sum was intended as an indemnity, the general rule should be that it was a substitute for liquidated damages. However, if article F was intended to provide a sanction for failure of performance, the request for liquidated damages should not be excluded. There remained the question of the amount involved, and he felt it was important to ensure that there was no disproportion between the agreed sum and the actual loss suffered.

29. Mr. MAGNUSSON (Sweden) said that the underlying meaning of the article had been made clearer in the revised draft, which was more closely based on the law of contract. His delegation did not find the word "grossly" in the second sentence altogether satisfactory, but could accept it as a compromise. Although the obligee should be entitled to claim extra damages in certain circumstances, it would be excessive to permit him to claim such damages if they were not clearly greater than the agreed sum.

30. Mr. FARNSWORTH (United States of America) said that he found the relationship between articles E and F somewhat confusing. The footnotes were helpful, but he understood that the text in its final form would not be accompanied by footnotes.

31. Article F in its revised form could lead to confusion in cases where the parties provided for a sum to be paid in the event of a specific kind of breach of contract. The meaning of the term "not covered by" in the second sentence was unclear in that context.

32. In common-law countries the general rule was that a liquidated damages clause determined the amount of compensation and that further claims were inadmissible. It was, however, sometimes possible in common-law countries to obtain further compensation by proving that the clause was unfair or fraudulent or had been included under duress; such a recourse was provided for under article A, paragraph (1 *bis*). It would thus be difficult to persuade businessmen in common-law countries that the provision formulated in article F was acceptable.

33. In general, he felt that there was an incompatibility between articles F and G. It might be better to adopt one or the other, but taken in combination the two articles could prove counter-productive.

34. Ms. VILUS (Yugoslavia) said that her delegation preferred the revised draft of article F in general, and the second bracketed alternative wording of the second sentence in particular. It would be happier, however, if a simpler and less negative wording could be found for the second sentence. One possible wording would be: "Nevertheless, the obligee is entitled to damages to the extent of the loss not covered by the agreed sum if he can prove that his loss greatly exceeds the agreed sum." An alternative formulation might read: "Nevertheless, if the damage greatly exceeds the agreed sum, the obligee is entitled to damages to the extent of the loss not covered by the agreed sum." Yet another possibility was simply to delete the second sentence.

35. Mr. GUEST (United Kingdom) said that, if the agreed sum was intended as a pre-estimate of damages, there were grounds for suggesting that an obligee should not be in a position to claim damages for a loss actually suffered which was in excess of the agreed sum. A fixed sum might also be regarded as security for performance, and in that case the intention of the parties might be that the damages should not be limited to that sum. Such a contingency could be considered as falling under article X, on the grounds that the parties had implicitly demonstrated an intention contrary to article F. A further problem was that in some cases the provision on the agreed sum might be intended as an exculpatory clause limiting the damages recoverable, for example, if the parties agreed that the recoverable damages would be the price of the goods. Many legislations had provision for exculpatory clauses, which could be overruled if they were unreasonable, unfair or otherwise unsatisfactory. The provision in article F established a régime for exculpatory clauses, but that régime might not be compatible with national legislation intended to protect weaker parties against stronger.

36. Mr. EDWARDS (Australia) said that, while the provision in article F would raise problems for businessmen in common-law countries, he was prepared to go along with it in a spirit of compromise. He felt, however, that the word "grossly" in the second sentence was too strong and that "manifestly", on the lines of the French text, might be more suitable.

37. Mr. SMART (Sierra Leone) agreed with the views expressed by the representative of the United Kingdom, but felt that the second sentence of the revised draft should be deleted. The deletion of that sentence, however, would require deletion of article G *in toto*, in order to ensure parity between the parties.

38. Mr. ROEHRICH (France) said that, unlike article G, article F related specifically to damages. He did not feel that it would be justifiable to delete the second sentence in article F, but agreed that the word "grossly" was undesirable, being

quantitative in its implications. Its elimination, however, might have consequences contrary to those intended. The French version of the text was easier to accept than the English. At the same time, logic demanded that, if the second sentence was to be deleted, the first would also have to be removed. The representative of the secretariat had already said that the wording of the second sentence, as enclosed in the second set of square brackets, was intended to indicate that any claim for damages was justified not by the rules under consideration but by the applicable law. That was not, unfortunately, the impression given by the text, which should therefore be improved. It was important not to make any quantitative prejudgment of any loss involved, but rather to establish a threshold above which a claim for damages might be entertained. The legitimacy of the claim would be determined by the competent judicial authorities.

The meeting was suspended at 11.15 a.m. and resumed at 11.45 a.m.

39. Mr. GOH (Singapore) expressed concern that, given the fundamental difference in approach between common-law and civil-law countries, the uniform rules might be reduced to a series of compromises which would be of little practical value or interest to businessmen operating under either legal system. The compromise solution offered in the revised text of article F illustrated that dilemma.

40. Mr. SAWADA (Japan) said that his delegation could accept the revised text of article F as it stood, although it believed that the concept of burden of proof should be eliminated from that article, as had been agreed in respect of other provisions.

41. Mr. BONELL (Italy) shared the view that the compromise formula contained in the revised draft of article F appeared to be the worst possible option: it would only create grounds for litigation, which was surely not the purpose of the rules. The Commission should adopt either the principle that any losses in excess of the damage sustained were recoverable, regardless of the extent of the disparity (by deleting the word "grossly"), or the principle that no such losses were recoverable (by deleting the second sentence of the article). His delegation's preference would be for the latter solution, bearing in mind the possibility afforded in exceptional cases by article X. If the existence of article X was not, however, considered a sufficient safeguard, an express reference could be made in article F to a contrary intention clearly indicated in the contract, in order to make it clear that the rule laid down in article F was of a non-mandatory nature.

42. Mr. TOLENTINO (Philippines) said that the considerable difficulties arising in connection with article F were due in large part to the fact that the revised draft failed to distinguish between two ideas: the agreed sum in the case of non-performance could either be a pre-estimate of damages (liquidated damages) or security for performance (penalty clause). In the former case, there could be no possibility of recovering an amount in excess of the agreed sum, since the will of the parties was that the amount fixed in advance represented the entirety of whatever damages might be suffered by the obligee in the case of failure of performance. In cases where the agreed sum was in the nature of security for performance, it might be justifiable to allow the obligee to recover damages in excess of the amount covered by the agreed sum. In that case, the word "grossly" would become redundant.

43. The revised draft did not make it clear in what sense it was referring to the agreed sum. The previous draft had made the distinction between the two ideas clearer, by using the

phrase "Unless the parties have agreed otherwise...". The Commission should make up its mind what position it wished to adopt on the matter.

44. Mr. BOGGIANO (Argentina) supported the view that the agreed sum should be understood as a substitute for damages paid. The logical consequence of that interpretation would be that losses in excess of the agreed sum were not recoverable and that the second sentence of article F should be deleted.

45. Nevertheless, taking that sentence in conjunction with article G and with the new text being drafted for article E, paragraph (2), he believed that a formulation similar to the existing one could in fact be adopted for application in genuinely exceptional cases. Cases where the agreed sum proved to be unreasonably high in relation to the damage suffered would result in a disruption of the basic equilibrium between the parties and would run counter to general principles of contractual law.

46. His delegation would thus be in favour of a formulation along the lines of the second sentence of the revised draft or the end of the previous draft, which would, under certain legal systems, permit the adjustment of the agreed sum in such cases. So far as the Spanish text was concerned, the word "*considerablemente*" should be replaced by "*manifiestamente*".

47. Mr. MUCHUI (Kenya) said that the solution to the problems presented by article F suggested by the representative of Sierra Leone was the only means of ensuring that equality between the two parties was maintained. If the future model law permitted the obligee to claim damages in excess of the agreed sum in cases where the loss suffered exceeded that sum, it should by the same token make provision for downward adjustment of the agreed sum where the actual loss suffered was less than that sum. Parity and equality were principles of particular importance to the developing countries.

48. Mr. HERBER (Federal Republic of Germany) said that a possible solution to the difficulties being created by the existing text of article F would be to adhere in principle to the so-called "common-law" solution, but to admit the possibility of claims in cases where the parties had clearly not intended the agreed sum to be the final estimate of damages awarded. That could be done by replacing the words "...he can prove that his loss grossly exceeds the agreed sum." by the wording used in the second sentence of article E, paragraph (2): "...the agreed sum cannot reasonably be regarded as a substitute for performance". That solution would admittedly not remove all ambiguity from the article, but it would have the virtue of bringing article F into line with article E as it now stood.

49. His delegation did not agree with the proposal that the problem should be solved in the context of article G, whose provisions should be invoked only in highly exceptional cases.

50. Mr. SZASZ (Hungary) agreed that the revised text of article F, which had been intended as a constructive compromise, would in fact introduce uncertainty and ambiguity into international transactions. The only genuine solution to the problem was to opt for either the penalty clause or the liquidated damages approach. The only problem was which of those approaches to select, given that both had their merits and were based on well-established practice. After weighing the pros and cons, his delegation had decided, for a variety of reasons, in favour of the solution of permitting claims for any damages over and above the agreed sum, which would entail the deletion of the word "grossly" in the penultimate line of the revised draft.

51. He did not believe that the problems raised by article F could be dealt with by means of article G, which was strictly for emergency use.

The meeting rose at 12.35 p.m.

276th meeting

Friday, 27 May 1983, at 2 p.m.
Chairman: Mr. CHAFIK (Egypt)

[A/CN.9/SR.276]

The meeting was called to order at 2.05 p.m.

INTERNATIONAL CONTRACT PRACTICES: DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES AND PENALTY CLAUSES (*continued*) (A/CN.9/218, A/CN.9/219 and Add. 1, and A/CN.9/235)

Article F (*continued*)

1. Mr. DUCHEK (Austria) said that both of the different systems reflected in the revised draft of article F (A/CN.9/235, p. 7) were to be found in Austrian law. Commercial contracts were covered by the system which allowed excess damages to be claimed in addition to an agreed sum; for other contracts, only the agreed sum could be claimed. Adoption of one of the two systems, rather than a compromise, would seem the best way to avoid difficulties in practice; of the two, his delegation would prefer the one under which additional damages could be claimed.

2. Since it seemed, however, that the Commission might have to be content with a compromise, the revised draft might not be so bad as some speakers had suggested, particularly if some acceptable solution could be reached concerning the word "grossly".

3. The law in many countries, including Austria, contained a provision similar to that of article G, under which an agreed sum could be reduced by the court at its discretion—an effective device. To broaden the rule in the other direction might lead to too many legal disputes.

4. The other compromise solution envisaged, which sought to distinguish between the purposes of agreed sums, would have disadvantages on account of the vagueness of the term "grossly"; and it might often be highly difficult to determine what the parties' intentions were. The solution presented by the text as it stood was at least based on objective criteria. Its drafting was indeed rather awkward, but only minor points were involved. The question was whether the members of the Commission felt that a compromise could be reached, or whether they felt bound to adhere strictly to their respective legal precepts—in which case the draft would have to be abandoned.

5. Mr. LEBEDEV (Union of Soviet Socialist Republics) said that his delegation did not share the misgivings of some other delegations regarding article F. In his view, the difficulties arose chiefly because the text was being appraised on the basis of national legal concepts—whereas the intention was to establish an independent set of uniform rules relating solely to international contracts and applicable, in any State, independently of domestic legislation and the country's legal philosophy. As he understood it, that concept had been acknowledged during discussion of article A.

6. He agreed that to opt for one of the two fixed systems—based either on an agreed sum alone or on entitlement to claim damages in excess of the agreed sum—would be the best solution. However, since the divergence of views remained as wide as ever, with no discernible majority in favour of either system, his delegation would be prepared to seek a compromise based on the revised draft. The word "grossly" would be better dropped.

7. It had been suggested that, if the second sentence of the draft were deleted, the matter could be dealt with by agreement between the contracting parties. However, he felt that some rule must be set forth in article F; otherwise matters would still have to be decided on the basis of applicable law, as they had always been.

8. Concern had been voiced about a possible misuse of agreed sums as a means to limit liability; but such instances related chiefly to questions of consumer protection, which, pursuant to article C, did not fall within the scope of the rules. Reference had also been made to cases where an agreed sum was intended as a genuine pre-estimate of damages; such cases would surely be covered by the provisions of article X. Problems might indeed arise in border-line cases, which could be left to the courts to rule upon; the uniform rules being drafted were intended for general application and could not cover every possible situation.

9. The substance of the revised text seemed the best possible compromise, but perhaps the drafting group could improve its wording.

10. Mr. BARRERA-GRAF (Mexico) said he thought an acceptable solution was possible; a suitable basis might be that suggested by the representative of Spain.

11. The first part of the revised draft could perhaps be retained, since it related to the preceding article. And if the second part could be clarified with regard to the penalty element a major obstacle to a compromise solution would have been overcome. Likewise, a decision on an appropriate word—"manifestly" for example—in relation to the excess loss would remove another problem.

12. Perhaps a formula on the lines suggested by the representative of the Federal Republic of Germany could be considered, involving the notion, reflected in article E, that the agreed sum could not reasonably be regarded as a substitute for performance; the drafting group could consider a text on those lines. There was also a relation with articles X and G.

13. Mr. GUEST (United Kingdom) said that the views expressed included two extreme positions: namely, that in no circumstances might an agreed sum be increased, and that an agreed sum could be increased in all cases where it had been manifestly exceeded by the loss incurred. There seemed no way of bridging the gap between the two; the compromise embodied in the last sentence of the revised draft would not work in practice.

14. Progress seemed possible only along the lines suggested by a number of delegations: the article would provide that a sum intended as a pre-estimate of damages could not be increased but, by means of some suitable provision, possibly aligned to the revised version of article E, an increased award would be allowed in appropriate circumstances. The solution was admittedly not ideal; but no perfect solution seemed possible.

15. The legal presumptions embodied in articles E and F posed no real problem for the United Kingdom, whose courts would concentrate on the parties' intentions. But his delegation could go along with the approach mentioned.

16. Mr. WAGNER (German Democratic Republic) said that his delegation preferred those provisions, in both the previous and revised drafts of article F, which would enable an excessive loss to be recovered. Under his country's law, virtually every contract contained provisions relating to liquidated damages and to entitlement to excess damages; in practice there was little litigation, because the contracts themselves and the parties' intentions made matters clear.

17. With regard to the second position, he had no strong feelings concerning the word "grossly"; it seemed to him that only if a loss were grossly excessive would an obligee trouble to take action in any case.

18. Mr. SEKHON (India) thought that the difficulties stemmed chiefly from divergences between the common-law and civil-law systems.

19. India's law of contract provided that, in a breach of contract, when a sum or other provision had been stipulated by way of penalty, a complainant was entitled, whether or not actual damage or loss was proved, to receive reasonable compensation not exceeding the amount or provision stipulated. The law thus steered clear of any distinction between pre-estimated damages and penalty. On that basis, his delegation would prefer deletion of the second sentence, which in any case did not seem linked with the first.

20. Bearing in mind the need for harmonization, he suggested that the two sentences of the revised draft could become two paragraphs, with minor drafting amendments in the first paragraph. The second sentence could stand as a second paragraph, its provisions being subject to article X; if thought desirable, a formula allowing derogation from the provisions could be included in article F.

21. However, if the second sentence was thus maintained, there was still the problem of the word "grossly". Of the alternatives mentioned, the word "manifestly" seemed to him inappropriate; "substantially" might be more suitable.

22. The CHAIRMAN said that the discussion had revealed four approaches. One was to approve the revised text, possibly with some minor amendments—for example, with regard to the word "grossly". A second view was that the text should be deleted altogether, thus leaving an obligee entitled to claim additional damages. A third approach was to entitle an obligee to claim damages without specifying the degree of loss in comparison to the agreed sum. The fourth view was that a distinction should be made between two types of agreed sum: a pre-estimate of damages, in which case no amount in excess of the agreed sum would be permitted; and a sum as a penalty or security, to which an increase could be awarded. Although the revised text seemed to represent a compromise solution, it had been argued that it was impracticable.

23. Perhaps the drafting group could prepare two alternative texts based on the two extreme positions that had been mentioned, in the hope that one or the other might attract a clear majority.

24. Mr. FARNSWORTH (United States of America) said that, apart from the four different approaches mentioned by the Chairman, there had been an oral proposal by the Federal Republic of Germany which his delegation, for one, was prepared to support.

25. Mr. ROEHRICH (France) said that an article which simply set out in precise terms the two different systems in existence and did not attempt any unification of the relevant rules would be of little use.

26. Mr. SAWADA (Japan) opposed the idea of entrusting the drafting group with the preparation of two alternative texts—a course which could only lead to a resumption of the whole discussion when the group reported back to the Commission. The task of the drafting group was to formulate the necessary wording, once the Commission had settled all points of substance. He therefore urged that a decision be taken on the various different proposals, possibly with the aid of informal consultations, after which the drafting group would be entrusted with the formulation of article F.

27. Mr. HERBER (Federal Republic of Germany) said he wished to make a formal proposal to replace in article F the concluding proviso “unless he can prove that his loss grossly exceeds the agreed sum” by the following words: “unless the agreed sum cannot reasonably be regarded as a substitute for performance”.

28. It would be noted that the language had been taken from the second sentence of paragraph (2) of article E. Since the drafting group had not yet settled the wording of article E, it should be understood that his proposal would be adjusted so as to be identical with whatever language the drafting group finally adopted for article E.

29. As to substance, his proposal was intended to leave the matter in principle with the common-law rule, which was contrary to the rule obtaining under other legal systems, including that of his own country.

30. Mr. FARNSWORTH (United States of America) and Mr. GUEST (United Kingdom) supported the proposal made by the representative of the Federal Republic of Germany.

31. Mr. OLIVENCIA RUIZ (Spain) said that he, too, supported that proposal but urged that the unsatisfactory expression “substitute for performance” should be replaced by the formula used in article A; the text would read “unless the agreed sum cannot reasonably be regarded as representing a pre-estimate of damages [or liquidated damages]”.

32. Mr. SAMI (Iraq) supported the proposal with the amendment suggested by the representative of Spain. However, the adverb “reasonably” was imprecise and he suggested that it should be dropped.

33. Mr. HERBER (Federal Republic of Germany) urged the Commission to take a decision on the principle of his proposal—on which most representatives appeared to be agreed—on the understanding that the wording would be adjusted by the drafting group so as to bring it into line with whatever language it adopted for the second sentence of paragraph (2) of article E.

34. Mr. ROEHRICH (France) said that the proposal by the representative of the Federal Republic of Germany was a novel formulation, unrelated to any of the existing systems. The Commission should take its decision thereon in full realization of that fact.

35. Ms. VILUS (Yugoslavia) said that she would find it difficult to accept the proposal of the Federal Republic of Germany. Her delegation felt strongly that the revised secretariat draft (A/CN.9/235, p.7) should constitute the basis for the Commission's work.

36. Mr. MUCHUI (Kenya) supported the proposal of the Federal Republic of Germany, without the change suggested by the Spanish representative.

37. Mr. MAGNUSSON (Sweden) urged the Commission to seek a compromise solution.

38. Mr. SAWADA (Japan) said that his delegation supported the secretariat's revised draft, subject to elimination of the unsatisfactory adverb “grossly” and its replacement by a more suitable one.

39. Mr. HARTKAMP (Observer for the Netherlands) said that he had difficulty in understanding the proposal of the Federal Republic of Germany. For one thing, the relationship between the concept of performance and that of loss was not clear. Compromises were always desirable, but it would be unwise to accept a compromise without understanding its meaning clearly.

40. Ms. OYEKUNLE (Nigeria) said that, at first glance, she found acceptable the proposal of the Federal Republic of Germany. She noted, however, that it placed the emphasis on performance, whereas the secretariat's revised draft placed the emphasis on loss; now the concept of loss covered much more ground than that of failure of performance and comprised other elements of damage.

41. Mr. SMART (Sierra Leone) said that he was prepared to support the proposal of the Federal Republic of Germany if its sponsor agreed with his interpretation of it, namely that the obligee was entitled to claim more than the agreed sum when the obligor was not able to perform the contract, provided the obligee had suffered a loss of more than the agreed sum as a result of the failure of the obligor to perform.

42. Mr. HERBER (Federal Republic of Germany) said that his reference to the concept of failure of performance in article E appeared to have been misunderstood. His intention was to make use of the definition contained in that article in order to distinguish between a clause which constituted a pre-estimate of damages, a clause providing for a security, and a penalty clause.

43. Under his proposal, where an obligee—in the circumstances set forth in paragraph (2) of article E—opted in favour of the agreed sum, he had to take that sum exclusively. He could not claim anything beyond the agreed sum unless he proved that the clause had not been meant to solve finally or exclusively the problem of pre-estimated damages, i.e. that the sum therein agreed was not meant as the “liquidated damages” of common law.

44. Mr. SMART (Sierra Leone) said that, following that explanation, he was prepared to support the proposal of the Federal Republic of Germany.

45. Mr. DUCHEK (Austria) said that the reference to performance, which was appropriate in article E, was altogether unsuitable in article F. The problem was one of damages, and the words "substitute for performance" were out of place.

46. He recalled that, at the previous session, it had been agreed to eliminate the concept of pre-estimate of loss. The result had been a very weak formula for article F, which made for uncertainty in its legal effects.

47. When the suggestion had first been made to state that the uniform rules served a threefold purpose (liquidated damages, penalty clauses and security), his delegation had asked whether the intention had been to create two different systems. The answer at the time had been a firm negative. The position, however, appeared to have changed with the proposal now under discussion.

48. He suggested that a better compromise formula would be to take the proposal of the Federal Republic of Germany as a basis but to amend it by incorporating the concept of pre-estimated damages.

49. Mr. FARNSWORTH (United States of America) proposed, as a matter of procedure, that the Commission should not take a decision on the proposal of the Federal Republic of Germany until its exact formulation had been settled, i.e. when the text of article E emerged from the drafting group.

50. Mr. GUEST (United Kingdom) proposed the following paragraph for consideration by the representative of the Federal Republic of Germany and by the drafting group after it had considered article E, since it contained a point not covered by that article at present:

"Where the agreed sum is intended as a pre-estimate of damages, the obligee may not assert a claim for damages in excess of the agreed sum. However, in other cases the obligee may assert a claim for damages to the extent of the loss not covered by the agreed sum if the agreed sum cannot reasonably be regarded as compensation for that loss."

The meeting was suspended at 3.50 p.m. and resumed at 4.30 p.m.

51. Mr. EDWARDS (Australia) said that the most recent proposals and discussions had not yet pointed the way to a compromise. When the drafting group ultimately produced a text the Commission might still find itself in the same position. His delegation believed that past achievements should be respected: it doubted whether a new compromise would be an improvement on the previous one, which had been the result of intensive effort.

52. If the Commission agreed to work on a model law, in accordance with its earlier majority view, accepting the previous compromise and the fact that there was no possibility of bettering it, that would not be an unsatisfactory result. True, States would have to face up to the difficulties presented by the compromise if and when they gave effect to the model law, but at least something would have been achieved. It might be argued that there was no point in a model law when the compromise was a fragile one, but the Commission should not be too ambitious. It would be taking a first and important step towards some sort of unification of ideas and law in a most difficult area. It should remember that the present task was part of an evolutionary process.

53. Ms. OYEKUNLE (Nigeria) urged that the Commission should consider the United Kingdom proposal and see whether it met the different points of view that had been expressed. It covered her own point of view in emphasizing loss rather than performance.

54. Mr. HERBER (Federal Republic of Germany) said that he could support the United Kingdom draft but would prefer the words at the end, "if the agreed sum cannot reasonably be regarded as compensation for that loss", to be deleted.

55. He could not support the idea that if the aim was a model law there was no need to reach agreement. Although a model law would not be binding, the Commission should not recommend something on which it could not agree.

56. There seemed to be a majority in favour of seeking a compromise rather than adopting one of the two extreme positions referred to earlier. If, after reflection, the members of the Commission were ready for a compromise on the lines of the United Kingdom representative's proposal, he would withdraw his own.

57. Mr. ROEHRICH (France) said that he would regret the withdrawal of the proposal of the Federal Republic of Germany since, while he was not enthusiastic about it, it did at least offer some hope of a compromise.

58. The United Kingdom proposal was not a compromise and was in fact equivalent to one of the two extreme positions.

59. Mr. HERBER (Federal Republic of Germany) suggested that an indicative vote should be taken on the various compromises before the Commission.

60. Mr. FARNSWORTH (United States of America) said that it would be difficult to decide between the proposals of the Federal Republic of Germany and the United Kingdom.

61. Mr. LEBEDEV (Union of Soviet Socialist Republics) said that there was a precedent for an indicative vote, although voting was contrary to the principle of consensus. However, the Commission was still seeking a compromise and the Australian suggestion offered a possibility.

62. Mr. TANG (China), supported by Mr. ROEHRICH (France), said that his delegation thought it better to avoid any vote. There was still a chance of reaching a compromise.

63. Mr. HARTKAMP (Observer for the Netherlands) said he also felt that there was no need for an indicative vote at the present stage as there was still room for compromise. He suggested that a small drafting group should be appointed to work on a compromise during the week-end.

64. Mr. EDWARDS (Australia) said that if there had to be an indicative vote it would be better to leave it until the next meeting. He asked whether the secretariat could prepare a short paper setting out the options before the Commission.

65. Mr. SONO (Secretary of the Commission) said that he would prepare such a paper for the next meeting, though it might not be possible for it to be produced in all the working languages.

The meeting rose at 5.10 p.m.

277th meeting

Monday, 30 May 1983, at 9.30 a.m.

Chairman: Mr. CHAFIK (Egypt)

[A/CN.9/SR.277]

The meeting was called to order at 9.40 a.m.

**INTERNATIONAL CONTRACT PRACTICES:
DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES
AND PENALTY CLAUSES (continued)**
(A/CN.9/218, A/CN.9/219 and Add.1, and A/CN.9/235)

1. The CHAIRMAN said that the lengthy discussions on article F had finally crystallized into certain well-defined proposals, which had been reproduced in writing in document A/CN.9/XVI/CRP.2. In order to save time, the Commission should proceed to an informal indicative vote on each of the five alternative proposals contained in that document, on the understanding that the preferred alternative would then be referred to the drafting group.
2. Mr. BASNAYAKE (secretariat) said that alternative 1 in the document afforded the greatest latitude for the assertion of a claim for damages: although the obligee could not assert a claim for damages to the extent of the loss covered by the agreed sum, he could make a claim for the balance if he could prove that the loss sustained was not covered by the agreed sum. In practice, such claims would be infrequent, because the obligee would have the burden of proving loss and would be unlikely to go to litigation unless his loss greatly exceeded the agreed sum.
3. Alternative 2 placed the greatest emphasis on the effect of the agreed sum: once the parties had agreed on a sum, no claim could be made, even if the loss exceeded the agreed sum.
4. Alternative 3, which was based on the proposal of the United Kingdom representative, drew a distinction between two different circumstances, depending on the nature of the agreed sum: if that sum was intended as a pre-estimate of damages, the obligee could not assert a claim for damages in excess of it; in other cases, however—usually where the agreed sum was introduced as a penalty clause—the obligee could assert a claim for damages to the extent of the loss not covered by that sum, if his loss could not reasonably be regarded as being compensated for by the agreed sum.
5. Alternative 4 was based on the proposal advanced by the representative of the Federal Republic of Germany: it began with a reiteration of the broadly accepted rule that the obligee was not entitled to loss covered by the agreed sum; in this case, however, his entitlement to claim depended on whether the agreed sum could reasonably be regarded as a substitute for performance; the alternative wording in the second set of brackets had been proposed by the representative of Spain.
6. Alternative 5 was basically the revised draft of article F appearing in document A/CN.9/235, with some drafting changes, in particular some suggested alternatives to the word "grossly" which had given rise to some dissatisfaction in the Commission.
7. Mr. SONO (Secretary of the Commission) explained that informal indicative voting was not an official vote under the rules of procedure, but rather a search for a basis on which consensus could be achieved. He suggested that all participants, including observers and organizations participating in an observer capacity, should be able to vote on all the proposals contained in document A/CN.9/XVI/CRP.2. The one which received the highest majority would be regarded as having the Commission's preference.
8. The CHAIRMAN said that if there were no objections, he would take it that the procedure outlined by the Secretary was acceptable to the Commission. He invited the Commission to proceed to an informal indicative vote on the five alternative proposals on article F contained in document A/CN.9/XVI/CRP.2.
9. *The results of the informal indicative vote on the alternative proposals on article F were: Alternative 1, 11 votes in favour and 22 against; Alternative 2, 9 votes in favour and 20 against; Alternative 3, 18 votes in favour and 13 against; Alternative 4, 13 votes in favour and 17 against; Alternative 5, 21 votes in favour and 11 against.*
10. The CHAIRMAN noted that alternative 5 commanded the greatest support in the Commission. That version was thus adopted and referred to the drafting group.

Article X

11. Mr. BASNAYAKE (secretariat) reminded the Commission that in the previous draft, the power of the parties to modify the rules contained in articles D, E and F had been stated in each of those articles. It had been generally agreed that the parties should not have the power to modify the rules contained in articles A and B, since those provisions defined the scope of application of the uniform rules. Article G should also not be subject to modification, since it contained the procedure for controlling the effect of articles D, E and F. As to the drafting, it had been felt that the power of modification should be set forth in a separate article. Article X had accordingly been added to the rules.
12. Mr. BONELL (Italy) said that his delegation was in agreement with the substance of the proposed text, but felt that for the sake of consistency and in order to avoid possible difficulties of interpretation, the wording of article X should be brought into line with that of article 6 of the United Nations Convention on Contracts for the International Sale of Goods.
13. Mr. HERBER (Federal Republic of Germany) also had no basic problems with the substance of the proposed article, but felt that it would be clearer if it were recast to state that the parties could derogate from the rules with the exception of article G. He wondered in that connection whether the exclusion of articles A, B and C from the scope of derogation might not cause problems inasmuch as the parties might agree to a different scope of application in respect of their particular contract.
14. The CHAIRMAN said that those proposals would be referred to the drafting group.
15. Mr. EDWARDS (Australia) said that his delegation believed that the reference to article D should be deleted from

article X. In the first place, it was unlikely that parties to a contract which were in equal bargaining positions would ever agree that in the event of a breach of contract, one party would be obliged to make payment under a liquidated penalty clause irrespective of the fact that he was not personally liable for the breach. Secondly, parties to a contract should not have the right to override applicable national legislation governing liability for breach of contract.

16. Mr. SONO (Secretary of the Commission) said that in discussing article D, the Commission had already decided that the sense of the phrase "Unless the parties have agreed otherwise ...", would be covered by article X. While the Commission could reopen the discussion on that issue, the point raised by the representative of Australia could be dealt with in the context of article G, leaving article D subject to contrary agreement by the parties.

17. Mr. EDWARDS (Australia) said that he was prepared to agree to that course of action.

18. Mr. MUCHUI (Kenya) said that his delegation shared the concern expressed by the representative of Australia. At the previous session, it had voiced strong objections to the phrase "Unless the parties have agreed otherwise ..." in article D; that phrase had now been deleted, but the same effect was now included in article X. While prepared to defer to the Secretary's proposal, he did not see how the matter could be dealt with in the context of article G.

19. Mr. MAGNUSSON (Sweden) said that his delegation agreed with the substance of the proposed article X. So far as the drafting was concerned, he supported the proposal made by the representative of the Federal Republic of Germany.

20. Mr. GUEST (United Kingdom) said that the discussions so far had demonstrated the importance of article X. While he could agree to the substance of the proposed text, he believed that article X should be drafted along more explicit lines; perhaps the secretariat could study similar provisions in other instruments with a view to submitting appropriate proposals to the drafting group.

21. The CHAIRMAN said he would take it that article X was adopted and referred to the drafting group, on the understanding that the points raised by the representatives of Australia and Kenya would be taken up under article G.

22. *It was so decided.*

Article G

23. Mr. BASNAYAKE (secretariat), introducing article G, said that it could not be varied by the parties. The first sentence had been placed in a separate paragraph to emphasize the fact that the Working Group believed that a reduction of the agreed sum should be permitted only in very exceptional cases. That statement was, however, qualified in paragraph (2). There were two sets of square brackets in the introduction to that paragraph. The word "shall" had been introduced because the word "may" in the previous draft had implied that even if the conditions necessary for the reduction specified later in the paragraph were satisfied, the court or tribunal had discretionary powers whether or not to reduce the agreed sum. The view expressed at the Commission's last session had been that if those conditions were satisfied, the court should always reduce the agreed sum. The words in

square brackets at the end of that phrase had been introduced to cover the extent to which the agreed sum should be reduced.

24. The idea expressed in subparagraph (a) had been included in paragraph (2) of the previous draft, the second part of that paragraph having been deleted at the last session because it had been considered unnecessary. The two alternatives in square brackets were merely a drafting matter: it might be considered preferable to use the words "grossly exceed", which were those used in article F to justify damages in addition to the agreed sum.

25. Subparagraph (b) had a relationship to article D. There had been considerable opposition at the previous session to the possibility of the parties being allowed to alter the rule set forth in article D, and a compromise had been reached that they might be permitted to do so provided that some provision was introduced in article G to the effect that when the rule had been altered, there was a special case for reducing the sum. Sub-subparagraph (i) envisaged the case in which the parties had exercised the freedom given by article X to alter the rule in article D. The phrase "manifestly unfair" in sub-subparagraph (iii) had emerged from discussions at the previous session.

26. The CHAIRMAN requested members to refer only to the substance of the article in the initial discussion.

27. Mr. SAMI (Iraq) said that the present wording of the article might lead to complications and misinterpretations. The Commission's aim must be fairness combined with clarity. It had been agreed in previous articles that the agreed sum might be raised in certain circumstances. Under article G the court or tribunal was being given the right to reduce the sum in other circumstances. The revised draft, however, was unnecessarily complicated. His delegation would prefer a text consisting of a single paragraph and wished to propose the following wording: "The court or arbitral tribunal may reduce the agreed sum unless the agreed sum can be regarded as a pre-estimate of the loss." There was no need to go into further details, which were superfluous in a legal instrument and should be left to the competence of the court in interpreting the contract under the applicable law. The principle was that the court or tribunal should be given the right of assessment and that the parties' attitude to the agreed sum as a pre-estimate of possible losses or damage should be respected. He believed that the text he had proposed could reconcile the two schools of legal thought.

28. Mr. SEKHON (India) said that failure to perform was the very foundation of a claim for breach of contract. The inclusion of subparagraphs (b) (i) and (ii) ran counter to the basic principles of the law of contract, notwithstanding the principle of autonomy. They should therefore be deleted.

29. Mr. OLIVENCIA RUIZ (Spain) considered that the court or arbitral tribunal should have the power to reduce the agreed sum. Under article F, the obligee was entitled to damages in excess of the agreed sum under certain circumstances, and it should also be possible to reduce the sum if it grossly exceeded the actual loss or damage. Consequently, article G should correspond in form to article F, since they were complementary in substance.

30. Despite the simplicity and clarity of the text proposed by the representative of Iraq, which was very similar to his own proposal with respect to article F, he was afraid that the wording was too different from that finally adopted for article F.

31. His delegation was ready to accept subparagraph (a) but had serious reservations on subparagraph (b). The wording and substance of sub-subparagraph (iii), in particular, were unfortunate. An entitlement could not be "unfair", although it could be abusive. Either the principle that a person who was not liable for failure could be obliged to pay an agreed sum must be accepted without qualification or the whole idea must be abandoned. He was therefore in favour of deleting subparagraph (b).

32. Another aspect to be considered was the power of the court or arbitral tribunal to reduce the agreed sum in cases of partial or defective performance, where the obligee should not necessarily have the right to the whole of the agreed sum.

33. Mr. SZASZ (Hungary) said that, as he understood it, the aim of article G together with article F was that the obligor should not have to run an unreasonably high risk; he should only be obliged to pay damages if they were actually suffered. The agreed sum was to be regarded as a pre-estimate of damages; it could be reduced under article G or raised under article F, both in certain circumstances.

34. However, if it was proposed that the agreed sum should be regarded as more than a pre-estimate of damages, that is, as a means of putting pressure on the obligor to perform, he was afraid that articles F and G would not achieve that aim. The effect would simply be to reverse the burden of proof, because the obligor would have to pay the actual damages whether or not there was an agreed sum. That might create problems in certain legal systems.

35. He therefore considered article G too comprehensive. He could accept the idea set forth in paragraph (2) (a), even though it was much broader than the previous draft, which had been a compromise and maintained a balance with article F. But he endorsed the reservations expressed concerning paragraph (2) (b) and supported its deletion.

The meeting was suspended at 11.05 a.m. and resumed at 11.30 a.m.

36. Mr. SMART (Sierra Leone) pointed out that by adopting article F the Commission had accepted the principle that if the obligee had suffered a loss greater than the agreed sum he could claim the excess. That led to the point which he had raised at an earlier meeting concerning the effect of article E, which it had been decided to postpone until the Commission discussed article G. If the obligee could get more than the agreed sum when he had suffered greater loss, then an adjustment should also be made when he had suffered no loss at all. However, subparagraph (b) (ii) seemed to allow the obligee to claim the agreed sum even if he had suffered no loss at all. His delegation therefore felt that the only way to achieve fairness and balance in the rules was to delete the whole of paragraph (2) (b). It would, however, prefer the simple wording proposed by the representative of Iraq.

37. The CHAIRMAN, noting that most members seemed to be in favour of deleting paragraph (2) (b), asked if anyone wished to maintain it.

38. Mr. MAGNUSSON (Sweden) thought there was a need for an escape clause which gave courts the right to adjust the agreed sum, but would like the rule to be as simple and flexible as possible. He would prefer a rule which said only that the agreed sum could be reduced if it was seen to be unfair when all the circumstances were taken into account. The most important of those circumstances could be included in the commentary. The courts should study the contract and

the circumstances of its conclusion as well as the balance between the parties.

39. However, if other delegations wanted more specific rules, he could accept the substance of the revised draft, since it was wider in scope than the previous draft and had been improved in other ways. He would prefer to retain subparagraph (b) with drafting amendments.

40. Mr. MUCHUI (Kenya) said that when the Australian representative had raised the problem posed by article X in relation to article D, the Secretary had suggested that the problem might be dealt with in connection with article G. Presumably he had been referring to paragraph (2) (b). If that provision was now to be deleted, the problem of whether or not article X should apply to article D would still remain.

41. Under article G, where the parties had provided that the obligor must pay the agreed sum even if he was not liable for the failure of performance, the court was given authority to reduce that sum. Could it also decide that no sum should be payable at all?

42. His delegation was not opposed to the deletion of paragraph (2) (b), which confused the issue, but if it was to be deleted the simplest solution would be to exclude article D from article X.

43. Mr. SONO (Secretary of the Commission) said that he understood that delegations which had suggested the deletion of subparagraph (b) were doing so for the sake of simplicity, on the understanding that the underlying ideas could be expressed somewhere else in the article. In fact, paragraph (2) of the previous draft had expressed the idea contained in subparagraph (a).

44. Mr. EDWARDS (Australia) confirmed that he had proposed that the reference to article D should be deleted from article X. Consequently, if subparagraph (b) was to be deleted, he maintained his proposal with regard to article X. He had no objection to including a provision in paragraph (2) of article G to cover the circumstances which had just been discussed, but considered that the language of articles F and G should be symmetrical.

45. Ms. VILUS (Yugoslavia) said that she too was in favour of a simple formula and preferred the wording of paragraph (2) of the previous draft, provided that the last two lines were deleted and that it was slightly reworded.

46. Mr. SONO (Secretary of the Commission) reminded the Commission that the last two lines of paragraph (2) of the previous draft had been deleted at the previous session.

47. Mr. WAGNER (German Democratic Republic) said that his delegation favoured the substance of the previous draft and accordingly could only support paragraph (2) (a) of the revised version. However, the Iraqi proposal was acceptable in principle, being concise and to the point.

48. Mr. TOLENTINO (Philippines) said that article X allowed the parties to derogate from or vary the effect of, *inter alia*, article D. Paragraph (2) (b) of article G seemed to be at variance with that principle, however. If the will of the parties was that the obligor should be liable, even if the failure of performance was not his fault, then, in effect, the parties were making the obligor a kind of insurer. The intention behind paragraph (2) (b) was to make the obligor liable only for a smaller amount if it appeared from the circumstances that the obligee's recovery of the agreed sum

would be manifestly unfair. In his delegation's view, if it was the will of the parties that the obligor should be liable whatever the circumstances, their will should prevail. The effect of paragraph (2) (b) would be to contradict that principle. It might, on the other hand, be possible as a compromise to state that, if the parties had agreed that under any circumstances the obligor would be liable, there should be no reduction in the agreed sum. Failing that, he would favour deletion of the subparagraph.

49. Mr. GUEST (United Kingdom) said that in considering paragraph (2) (b) it was necessary to envisage a situation, such as *force majeure*, in which there was no responsibility for failure of performance, but in which the parties had provided that an agreed sum should be paid. In such a case it was likely that loss would be suffered by one or other party, or possibly both, and it was entirely reasonable for the parties to make arrangements for payment of compensation if they wished. They should thus be allowed to derogate from or vary the provisions of article D. Ideally, it would be desirable to establish some kind of control over their decision, but in practice it was perhaps best left to the parties to determine, in most cases, the compensation to be paid in *force majeure* situations.

50. It might have been preferable to have a provision incorporating wording from paragraph (2) of the previous draft of article G. That, however, had been deleted.

51. A further aspect of the problem was whether it was mandatory or optional for the court to reduce the sum. His delegation inclined to the former.

52. Still more important was the question of the guidelines to be given to the court in respect of the amount by which the agreed sum should be reduced. Article G, paragraph (2), provided no guidelines at all beyond establishing a maximum reduction. In his view, the best way to ensure uniformity of interpretation was to require the court to reduce the sum to the actual loss suffered by the obligee, thus mirroring article F as adopted, under which the obligee could recover his loss if he could prove that it grossly exceeded the agreed sum.

53. Mr. HARTKAMP (Netherlands) said that paragraph (2) (b) of article G represented a satisfactory compromise and should be retained in substance. A similar compromise had been discussed at the previous session solely in connection with article D, but the same problem could arise in respect of derogations from articles E and F as well. If the parties had derogated from or varied articles D, E or F, and if as a result of those derogations the agreed sum was manifestly unfair, a court should be empowered to reduce the agreed sum. It was to be noted that paragraph (2) (a) of article G did not cover a case in which both the agreed sum and the loss could be recovered from the obligor.

54. Mr. KIM (Republic of Korea) said that his delegation would prefer to delete paragraph (2) (b) in the interests of preserving the balance between articles F and G.

55. Mr. BONELL (Italy) said that, in the light of the comments made by the representatives of the Netherlands and the United Kingdom, his delegation no longer felt that it would have been better to preserve the original draft of article G, or to substitute a single sentence on the lines suggested by the Iraqi delegation.

56. The absence of any indication of the criteria to be followed by a court or arbitral tribunal could lead, at the international level, to a large measure of uncertainty. The provision might therefore be redrafted to state that the agreed

sum could be reduced if its amount was proved to be excessive, taking into account the other remedies available and the circumstances of the case. Such a formulation would, he thought, be sufficiently broad.

57. Mr. HERBER (Federal Republic of Germany) said that the discussion seemed to indicate that article G should be simplified. In the first place, paragraph (2) (b) should be deleted, since it added nothing and was liable to create uncertainty. Noting that paragraph (2) (a) referred to the idea of gross disproportion, whereas paragraph (2) (b) used the term "manifestly unfair", he said that the latter wording was the narrower in its implications and should be preserved in any future revision of the text. It was not so important to state whether the court "may" or "shall" reduce the sum, since if a court determined that the sum was manifestly unfair it would be bound to reduce it. The court should be authorized to reduce the amount to the maximum that could be considered fair, but the amount should in no case be lower than the actual loss suffered.

58. In conclusion, he did not think it useful to distinguish in paragraph (2) between the circumstances of subparagraph (a) and those of subparagraph (b). The provision would best be formulated in a single sentence, as in the previous version of the draft, but should incorporate the criterion of manifest unfairness.

59. Mr. LEBEDEV (Union of Soviet Socialist Republics) said that article D should not be mandatory, which would exclude the possibility that parties might extend the rules to cover cases such as those involving *force majeure*. Under the Vienna Sales Convention the provisions on liability were facultative, and the Convention in no way made it impossible to determine liability, even in cases of *force majeure*. He saw no need to depart from that approach in article G.

60. Paragraph (2) (b) added nothing useful to the article from a practical standpoint and would introduce confusion. There was no great difference between saying that the court "may" and that it "shall" reduce the agreed sum, but the latter expression, in certain countries at least, might give rise to difficulties. The mandatory form was used to state the fundamental principle in paragraph (1). From a technical point of view it would therefore be more logical to state in paragraph (2) that a court "may" reduce the agreed sum.

61. Turning to the extent to which the agreed sum might be reduced, he said that in the course of the discussion it had been maintained that a reduction of that sum to the level of the actual loss incurred would be in accordance with article F. However, articles F and G covered completely different situations, so there was no need for total correspondence between them. In his delegation's view, it would be most satisfactory and practical if the reduction of the agreed amount were to be a discretionary right, and not an obligation, of the court, and if the rules were to determine only the lower limit of the amount. As had been pointed out, the circumstances of each case could be very different, and the court in some cases might determine a slightly higher level than that of the actual loss incurred.

62. His delegation also thought that the phrase "though not below the extent of the loss suffered by the obligee" in paragraph (2) should be included in a separate paragraph at the end of the article. In its existing context it could encourage an assumption contrary to the intention of the article by implying that the obligee would have to prove his actual losses.

278th meeting

Monday, 30 May 1983, at 2 p.m.

Chairman: Mr. CHAFIK (Egypt)

[A/CN.9/SR.278]

The meeting was called to order at 2.15 p.m.

**INTERNATIONAL CONTRACT PRACTICES:
DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES
AND PENALTY CLAUSES (continued)**
(A/CN.9/218, A/CN.9/219 and Add.1, and A/CN.9/235;
A/CN.9/XVI/CRP.3 and 4)

Article G (continued)

1. The CHAIRMAN said that, since the previous meeting, a number of proposals had been given to the Secretary, from which the following three main points emerged. First, there was a predominant opinion in favour of deleting subparagraph (b) of paragraph (2) in the revised draft (A/CN.9/235, p.8). Secondly, the question was raised whether, if the conditions for reducing the agreed sum were satisfied, the reduction should be mandatory or should be left to the discretion of the court ("shall" or "may"). Thirdly, should a criterion or guideline be provided for determining the amount of the reduction, or would it be better to leave the matter to the discretion of the court?

2. He suggested that the text of article G should be sent to the drafting group for redrafting, taking into account the three points he had outlined.

3. Mr. BARRERA-GRAF (Mexico) said that he agreed with the Chairman's suggestion, but considered that the drafting group should be given guidance on certain aspects, in particular the question whether a reduction of the agreed sum should be mandatory or discretionary.

4. Subject to those comments, his delegation agreed with paragraphs (1) and (2) of the revised draft, on the understanding that the introductory part of paragraph (2) would make the reduction discretionary. With regard to the criteria for the court to follow in deciding on the reduction, a maximum reduction was proposed in the revised draft of the second set of square brackets in paragraph (2); the minimum reduction should, he felt, be based on what the court considered reasonable in the light of the circumstances of the case. However, in his opinion paragraph (2) should contain a specific reference to the principle of autonomy of will, so that the parties could establish in their agreement the possibility of a reduction and of a minimum and maximum.

5. Mr. MAGNUSSON (Sweden) said that he would have no strong objection to the whole of article G being sent to the drafting group, provided directives were given regarding paragraph (2) (b). Many representatives felt that the sense of the subparagraph should be preserved. It was important, especially for international trade, to respect the will of the parties, but it must also be borne in mind that all parties were not equal; it would be desirable to have a provision allowing the parties' agreement, on occasion, to be set aside by the court. A decision must be taken on those questions before the article was sent to the drafting group.

6. On the other two points: he had no strong views on the use of the word "may" or "shall"; "may" was perhaps more

customary, and he would prefer the court to be left as much freedom as possible. The drafting group could decide. Regarding the possibility of setting limits to the court's powers to adjust a contract to reduce the agreed sum, he would prefer not to set a limit and to rely on the common sense of the court, but he had an open mind.

7. Mr. DUCHEK (Austria) said that his delegation would not oppose deleting subparagraph (b) or paragraph (2) if that was the majority wish. In many cases the result of a lawsuit would probably be the same whether the subparagraph had been deleted or not. Other laws were applicable, such as those concerning contracts, and there might well be cases where a judge would decide to reduce a sum which he considered unfair, not because of the rules now being discussed by the Commission, but because of the rules of the applicable law. The reasons why a sum was manifestly unfair might have existed at the time the contract was concluded: an error might have occurred, or there might be inequality of negotiating power, as referred to by the representative of Sweden. All laws must allow for the possibility of eliminating imbalance in respect of contractual obligations. Circumstances which made the agreed sum manifestly unfair could arise after conclusion of the contract; changed circumstances might cause an imbalance. That situation was covered in many legal systems and in many cases a manifestly unfair sum would be reduced regardless of the existence of rules such as those under consideration. The only disadvantage of deleting paragraph (2) (b) would be that interpretations would perhaps vary in different courts. It might be better to retain the sense of the provision as suggested by the representative of Sweden.

8. Mr. SAWADA (Japan) said that he would support the Swedish representative's suggestion regarding paragraph (2) (b) if a satisfactory standard or guideline were provided, but the standard of manifest unfairness was not very clear or helpful. He would be in favour of deleting paragraph (2) (b).

9. Regarding the other two points: he was in favour of the word "may", which would give the court more discretion; and since it was hard to find a clear standard regarding the extent to which the agreed sum might be reduced, or to improve the existing text, it would be better to leave the revised draft as it stood apart from the deletion of paragraph (2) (b).

10. Mr. VOLKEN (Observer for Switzerland) said that the second and third points mentioned by the Chairman were to some extent linked. The second point involved the question whether, if the conditions were satisfied, the reduction was mandatory or whether a judge would have discretion. In his opinion, the judge would necessarily have discretion, because it would not be possible to give him precise criteria; if, in addition, the word "may" was used, the judge would have two opportunities for discretion, and in his opinion one would be enough.

11. Mr. EDWARDS (Australia) said that his delegation favoured discretion for the court and therefore preferred the word "may". He had no objection to the deletion of the words "though not below the extent of the loss suffered by the obligee", and would prefer to rely on the court's discretion.

12. Mr. ROEHRICH (France) said he largely agreed with what had been said by the representative of Austria on the

deletion of subparagraph (b) of paragraph (2) (b). He saw no problem in deleting the subparagraph.

13. Regarding the Chairman's second point, paragraph (1) of article G was the basic rule and in his opinion paragraph (2) should be merely an exception. The judge should have a measure of discretion in examining all the circumstances of the question and the contractual relations between the parties. He was strongly in favour of retaining some form of wording which would specify that discretion and provide guidance. As far as limits were concerned, a minimum should be set, and objective criteria were needed to define the limit. The notion of "the loss that has been suffered by the obligee" seemed satisfactory. With regard to the criterion to be used in paragraph (2) (a), he would not favour the introduction of the subjective notion of "unfairness". He appreciated that the judge was to be allowed some flexibility, but the notion of unfairness would allow too much freedom. He would prefer the expression "grossly exceed", which was quantitative in character; the drafting could perhaps be improved.

14. Mr. FARNSWORTH (United States of America) said that in his delegation's view the convention should have a more modest role than many delegations would give it. The main problem regarding liquidated damages and penalties was that common-law countries—and some others—had special rules concerning penalties which were not applied to other contract clauses, and that special treatment caused difficulties, especially in countries which did not distinguish between penalty or liquidated damage clauses on the one hand and other kinds of clause on the other hand. He assumed that all systems had rules concerning unfairness, so that if a clause in a contract was unfair or coerced or the result of misapprehension or mistake, or was extremely burdensome to one party, there were rules to take care of the matter. It would be unwise to endeavour to make a law on unfairness in the short time remaining to the Commission.

15. Article G, paragraph (1), met the main purpose of the article and he would regret it if another special rule for liquidated damages and penalties were created in paragraph (2) simply to replace the special rules in common law that some people found troublesome. He would like to see the shortest possible provision, and favoured deleting the cumbersome provision in paragraph (2) (b). He agreed with the representative of the Union of Soviet Socialist Republics that a choice between "may" and "shall" was unimportant, but if a choice had to be made he would prefer "may". It would be better not to refer to unfairness.

16. Mr. BOGGIANO (Observer for Argentina) said that, with regard to the Chairman's first point, the judge's powers of discretion to reduce the agreed sum should be optional but genuine, and should be exercised in the light of the circumstances of the case. Regarding the second point, the principles concerning limits on the reduction of the agreed sum should be flexible and should allow for a fair reduction, taking into account the degree of loss, the reasonable expectations of the parties concerned and the law applicable to the contract. As for the deletion or otherwise of paragraph (2) (b), either way the result would probably be the same, in view of the application of existing legislation. On the whole, he would be in favour of deletion.

17. Mr. MUCHUI (Kenya) said that despite the comments of the United States representative he preferred the word "shall" in paragraph (2). If the obligor could show that the agreed sum was grossly or manifestly disproportionate to the loss suffered, it should not be left to the court's discretion to decide whether it should be reduced or not, since that would

leave the obligor in a state of uncertainty. He did not understand why the problem was being raised, in view of the provisions of article F as adopted at the previous meeting. With regard to the level of the reduction, it would be very difficult to set a guideline or criterion without applying the same sort of criterion as had been applied in respect of article F. Perhaps the only way to give a guideline which would leave no doubt in the mind of the court would be to relate the reduction to the actual loss suffered. He was aware that that would not be a popular solution, but he could see no other which would not give rise to problems of interpretation in different legal systems.

18. With regard to paragraph (2) (b), which was intended to take care of the problem raised by articles D and X, he wondered whether if it were deleted the general rule in article G would still be applicable. He assumed that the provision in subparagraph (b) (iii) referred not to reduction but to the entitlement to the agreed sum as a whole. Paragraph (2) (b) did perhaps serve some useful purpose. Where there was agreement between the parties that even where liability for failure of performance did not lie with the obligor he still had to pay the agreed sum, he felt that even without paragraph (2) (b) the right to reduction in the event of manifest unfairness would still remain in law. He felt, however, that it would be useful to state that particular provision specifically in the uniform rules. In that connection the point raised by the representative of Sweden concerning inequality of parties was very important.

19. Mr. MAGNUSSON (Sweden) said there seemed to be a majority view that, if article D was to be retained, there should be provision to allow derogation from it. If the parties' agreement was to be subject to the court's discretion to some extent, the court's power should not be limited to reducing an agreed sum only to the extent of the loss suffered; and if it was felt that there should be some control on the parties' power to derogate from article D, the courts should have the power to reduce an agreed sum to zero.

20. In the case of force majeure, the obligor would not be liable for failure to perform. And even if the parties had intended an agreed sum to be payable in any circumstances, the courts should have power to set that aside and even rule no payment at all. The question of damages would be decided according to general principles, including the principle that there was no right to damages in cases of *force majeure*.

21. Mr. BONELL (Italy) said that there were various aspects which could not necessarily be covered within one framework. It was quite possible, for example, that a liquidated damages clause could have been stipulated, but not in a valid form—which meant that a ruling must then be made pursuant to applicable law. As for inequality of the parties, the question was simply one of whether or not the clause concerned was valid; he understood article G to refer exclusively to clauses deemed valid by the courts. It seemed to him that an entirely new aspect was now being raised; in particular, he was surprised at the suggestion of the representative of Sweden that a court could reduce an agreed sum to zero.

22. Article G should be redrafted in a shorter form, as a single paragraph, omitting paragraph (2) (b), which had no place in that article.

23. The CHAIRMAN said that a majority seemed in favour of deleting paragraph (2) (b) of the revised draft and merging paragraphs (1) and (2) if possible. With regard to whether the word "shall" should be replaced by "may" in

paragraph (1), some delegations thought that a reduction should be mandatory, but a majority seemed to think that the courts should be allowed wider discretion. Some delegations thought that the courts should not be empowered to reduce a sum beyond the loss suffered; others thought the matter should be left to the courts' discretion, subject to the parties' intentions, the applicable law and the circumstances of the case.

24. On that basis, and if there was no objection, he would submit the revised draft of article G, together with the relevant proposals submitted, to the drafting group.

25. *It was so agreed.*

Note by the secretariat (A/CN.9/XVI/CRP.3)

26. Mr. SONO (Secretary of the Commission) summarized the contents of document A/CN.9/XVI/CRP.3, which the secretariat had prepared in order to give the Commission an idea of the stage reached in the drafting of various articles.

27. The text of article A was, of course, still before the drafting group. With regard to article A *bis*, the formula used in the Vienna Sales Convention could not be used with regard to paragraph (a), since it was tentatively being assumed that the rules were to take the form of an annex to a convention. With regard to paragraphs (b) and (c), however, the formulation followed the lines of the Sales Convention, and was as shown in document A/CN.9/235—as were articles B and C.

28. With regard to the scope of the rules of private international law in relation to the scope of the application of the rules, the Vienna Sales Convention approach might be used; but the matter need not be settled at the Commission's current session. Paragraph (a) of article A *bis* concerned the definition of internationality; if the form of a convention was opted for, a formula similar to that of article I of the Vienna Sales Convention might perhaps be adopted.

29. Mr. HERBER (Federal Republic of Germany) said that, in principle, the rules embodied in prescriptive and sales conventions applied to private individuals also. Article C sought to exclude contracts relating to personal, family or household purposes; but he wondered whether the text of that article was broad enough. The Commission should perhaps seek wording which would clearly restrict the scope to commercial contracts. That would mean amending paragraph (c) of article A *bis* and deleting article C.

30. Mr. BONELL (Italy) said he agreed in principle with the representative of the Federal Republic of Germany but felt that to define a commercial contract was virtually impossible; different legal systems embodied different notions of such contracts.

31. In any case, the provisions of article C and of paragraph (c) of article A *bis* left little room for confusion. The up-to-date approach was surely not to seek to distinguish between civil and commercial contracts but to regard as commercial all those not of a clearly consumer nature.

32. Mr. GUEST (United Kingdom) thought that the matter posed no serious problem if the question were one of a model law; and if the rules were to be in the form of a convention the difficulty could perhaps be overcome by providing the possibility of reservation.

33. Mr. HERBER (Federal Republic of Germany) withdrew his suggestion.

34. Mr. SEKHON (India) said that national laws—for example, the provisions enacted in the United Kingdom in 1977—drew a clear distinction between contracts for personal services and other contracts. On that basis, there was an essential difference between article C and paragraph (c) of article A *bis*.

35. Mr. SAWADA (Japan) suggested that article C should be so worded as to exclude contracts for the lending and borrowing of money.

36. Mr. ROEHRICH (France) asked whether loans to commercial undertakings would be excluded.

37. Mr. SAWADA (Japan) agreed that there could be a distinction between loans contracted for personal use and those for commercial purposes. In his view, the whole matter warranted discussion by the Commission.

38. Mr. GUEST (United Kingdom) said that the text as it stood did imply that questions of default in repayment, including default in purchase-price payment, should fall within the scope of the article. The representative of Japan had raised a cogent point which the Commission should consider.

39. Ms. VILUS (Yugoslavia) thought it had always been understood that monetary obligations were excluded from the purview of such rules; perhaps it would be as well, therefore, to take up the Japanese representative's suggestion.

The meeting was suspended at 3.50 p.m. and resumed at 4.15 p.m.

40. Mr. SAWADA (Japan) said that he withdrew his suggestion on the understanding that, as mentioned by the representative of Yugoslavia, the general view was that contracts for monetary loans did not fall within the purview of the rules.

41. The CHAIRMAN said that the matter could be reflected in the summary record.

42. Mr. BONELL (Italy) said it was far from certain that such a general view prevailed.

43. Mr. GOH (Singapore) said he understood the concern of the Japanese representative. At the Singapore Financial Centre, many syndicated loans were floated, usually of a transnational nature. Very often, the agreements concerning those loans stipulated that the law of the State of the lending bank would apply. Clearly, bankers benefited from the best professional advice available and his own feeling was that the problem need not trouble the Commission greatly.

44. Mr. ROEHRICH (France) said that he shared the concern of the Italian representative. He would not wish the summary records of the Commission to be construed as reflecting an alleged intention on its part to exclude the questions mentioned by the Japanese representative, including loans subscribed otherwise than by private persons for private needs.

45. There would be no objection to the summary records reflecting the fact that the Japanese representative had drawn attention to the problem. It would of course also be open for that representative, and the Yugoslav representative, to place

on record the views of their own delegations under their own responsibility. The French delegation, however, could not agree to any suggestion that the Commission itself endorsed in any way the Japanese representative's interpretation.

46. Mr. BARRERO STAHL (Mexico) said that he entirely agreed with the Japanese representative: monetary loans fell outside the scope of the model uniform rules under discussion. He therefore supported the idea of stating that exclusion expressly in article C; alternatively, the understanding on that point could be reflected in the summary record or elsewhere.

47. Mr. SONO (Secretary of the Commission) said that all views of members would be reflected in the summary record. His understanding was that the Japanese representative was explaining the reasons for withdrawing his suggestion; that representative wished to place on record his interpretation that the draft uniform rules did not apply to commercial loans. Interpretations on that delicate point did indeed vary considerably.

48. Mr. SAWADA (Japan) said that he was not asking for his own interpretation to be endorsed by the Commission itself.

49. Mr. GUEST (United Kingdom) said that the report of the Commission might well state that the problem raised by the Japanese representative had been "swept under the carpet".

50. Mr. EDWARDS (Australia) said that he was not quite satisfied at the position and believed that a number of other representatives shared his feeling. It was not sufficient to record the interpretation by the Japanese representative, important as the views of one delegation undoubtedly were. What mattered was whether there existed a general understanding regarding the coverage of commercial loans. The Commission should clarify that matter in one way or another. It could not sweep the problem under the carpet, to use the previous speaker's vivid expression.

51. Mr. SONO (Secretary of the Commission) said that he wished to make it clear that, while the summary records would reflect all the views expressed during the discussion, the report of the Commission itself would not contain any reference to the Japanese suggestion.

52. Mr. EDWARDS (Australia) said that it was quite unsatisfactory to defer an important matter like that of commercial borrowing.

53. Mr. SONO (Secretary of the Commission) drew attention to the uncertainty existing at present with regard to the international monetary system. He also pointed out that the courts in a number of countries had already decided that international contracts for loans were not subject to the usury laws. Those laws had been enacted before 1973, i.e. before the floating currency rates system in the capitalist markets. Those laws might have functioned well in the past but were now coming under very close scrutiny in a number of countries because of the floating rates of exchange. Very often, the differences obtained because of variations in exchange rates far exceeded the usury rate.

54. Treatment of that issue by the various countries of the world was not uniform. Some States had already decided not to apply their usury laws to what was a new situation. He felt that the members of the Commission might wish to avoid entering into that delicate issue.

55. Mr. SEKHON (India) supported the Japanese representative. International borrowing was a comparatively new concept which was building up in the international markets, in particular with syndicated loan issues. If the model uniform rules were to be applied to such international borrowing, he feared that unexpected problems would be created.

56. In his experience as representative of India he had had occasion to deal with certain international borrowings and had been able to note the peculiar concepts, peculiar terms and conditions and peculiar situations which applied only to certain particular types of international borrowing.

57. In conclusion, he opposed the idea of leaving the issue vague and urged that article C should expressly state a clear exception in the matter.

58. Mr. SONO (Secretary of the Commission) said that even if the Commission were to reach an agreement on the issue raised by the Japanese representative it would be very difficult to secure its acceptance in the various countries in the light of the new interpretations of usury laws. In some countries, it had been ruled that those laws did not apply to international loans. The position was different elsewhere. The matter was obviously one for domestic law. The best course would be to leave the matter vague.

59. The CHAIRMAN said that, if there were no further comments on that point, he would take it that the Commission took note of the withdrawal of the Japanese representative's suggestion, on the understanding that that representative's interpretation, supported by other representatives, would be mentioned in the summary record of the present meeting. As for the report of the Commission on the present session, it would not deal with the issue at all.

60. *It was so decided.*

61. Mr. DUCHEK (Austria) recalled that the Commission had deferred its decision with regard to the scope of application of the Convention and the reference to private international law in paragraph (1) (b) of article A. He drew attention to the words in that paragraph "where ... the parties have their places of business in different Contracting States".

62. That being so, he wished to know at what stage that matter would be discussed, what body would be responsible for that discussion and who would take a decision in the matter.

63. Mr. SONO (Secretary of the Commission) replied that there was no need to refer to the "Contracting States" in the present uniform rules, which were framed in the form of an annex to a future convention. The question of the extent to which States were bound was a separate matter which belonged to the umbrella part of the convention.

64. Of course, at some point the umbrella convention would have to be prepared if the Commission decided to go ahead on the basis that the text would be included in a convention. In that case, the simplest course would be to adhere to the pattern of the 1980 Vienna Sales Convention in which article 1 referred to "Contracting States" and to the issue of private international law. In that regard, he drew attention also to article 95 of that Convention, which contained a reservations clause with regard to the scope of application of that instrument.

65. Since the Commission was at present working on the basis that the text would constitute an annex to a convention,

the question of drawing up an umbrella convention could be left to the secretariat, except for some key issues which the Commission itself would have to decide and with respect to which a document had been submitted to it (A/CN.9/XVI/CRP.4) containing two draft provisions on reservations, namely a "contracting-in" clause and a provision on the writing requirement.

66. Mr. MAGNUSSON (Sweden) asked what was the position with regard to paragraph (1 *bis*) of article A of the revised draft, which did not appear in the text of article A in document A/CN.9/XVI/CRP.3.

67. Mr. SONO (Secretary of the Commission) drew attention to note 11 in document A/CN.9/235. Paragraph (1 *bis*) stated explicitly the understanding implicit in the previous draft. The draft rules did not deal with the validity of the contract as such. Insofar, however, as the rules provided that a penalty which was invalid under the general provisions of the law was nonetheless recoverable, the uniform rules did deal with a limited issue of validity.

68. The secretariat had dropped paragraph (1 *bis*) from article A because it was likely to create confusion. It might seem to cast doubts on the fact that the draft rules did not deal with validity in general. It had been intended to reserve only a small point with regard to which the draft rules did touch on the issue of validity. Since that reservation might create misunderstandings, it had been felt preferable to eliminate it.

Suggestion by the secretariat: contracting-in clause—writing requirement (A/CN.9/XVI/CRP.4)

69. Mr. SONO (Secretary of the Commission), introducing document A/CN.9/XVI/CRP.4, said that it had been prepared on the understanding that the draft rules would take the form of an annex to a convention. Accordingly, an umbrella convention would be required. As far as the ordinary clauses of that convention were concerned, it could be taken that they would follow the usual pattern of UNCITRAL conventions. There remained, however, two points to be dealt with at the present stage and which formed the subject of the documents he was introducing. They were two key points which were closely related to the rules contained in the annex.

70. The first of those points was that of the reservation on the contracting-in clause, a matter which had been mentioned in paragraph 17 of the report on the previous session. On the understanding expressed in that passage of the report, the secretariat had prepared the draft clause he was now submitting.

71. Turning to the writing requirement, he explained that the secretariat had drawn up a reservation clause enabling States to make a declaration on the subject if they wished to impose the writing requirement. That suggestion followed closely the formula of the 1980 Vienna Sales Convention.

72. Paragraph 2 of the document dealt with the question of the rules of private international law in relation to the scope of application of the model rules, and indicated that the approach of articles 1 and 95 of the Vienna Sales Convention might be used but suggested that the issue should not be settled at the present session.

73. Lastly, paragraph 3 stated that, even if the model rules were to take the form of a model law, the question of the two reservations and the issue of private international law—which

would in any case not be dealt with in the annex itself—should be brought to the attention of legislatures in an appropriate form.

74. Mr. SEKHON (India) drew attention to the fact that article 1 of the Vienna Sales Convention referred to the "Contracting States". In his own country, there were many public sector undertakings which engaged in international borrowing and he wished to know whether the term "Contracting State" would embrace a public sector undertaking which was not the State as such.

75. Mr. SONO (Secretary of the Commission) explained that, where article 1 of the Vienna Sales Convention referred to two States as being "Contracting States", it was referring to those States which became parties to the Convention itself. The provisions of the Vienna Sales Convention applied to all transactions between parties having their places of business in different States even if a party concerned was a State agency.

76. The CHAIRMAN said that, if there were no further comments, he would take it that the Commission agreed to refer the contents of document A/CN.9/XVI/CRP.4 to the drafting group.

77. *It was so decided.*

Proposal by the secretariat on the form of the draft

78. Mr. SONO (Secretary of the Commission) recalled that the Commission had been working on the understanding that, tentatively, the draft rules would serve as an annex to a convention. The question as to whether that tentative approach would become final was still pending. In the light of the background against which the rules had been produced, it would not seem advisable to consider recommending to the General Assembly the convening of a diplomatic conference at the present stage.

79. The purpose of the tentative decision to prepare the rules in such a form that they could serve as an annex to a convention had been based on the belief that that form could serve to accommodate both the model law approach and the convention approach.

80. That being so, the secretariat now proposed that the Commission should inform the Sixth Committee that the project had been completed by it and explain the reason why the annex approach had been adopted. The Commission would request the Sixth Committee to consider the possibility of adopting the Convention through that Committee itself, if feasible, and, in the contrary event, recommended to the General Assembly that it consider the possibility of a diplomatic conference if practicable in its opinion, or consider any other adequate means of formulating a convention.

81. The Sixth Committee would of course have before it the report of the Commission, which would explain the background of the Commission's understanding in the matter. In that connection, he recalled that in the voting on the last General Assembly resolution on the subject there had been ten States in favour of a model law and eight States in favour of a convention.

82. After examining the report of the Commission, the Sixth Committee might perhaps postpone its decision in the matter until a later session. Should that occur, the draft rules would remain as a draft convention of UNCITRAL and it

was conceivable that the Sixth Committee would recommend the annex to be used as a model law by national legislatures. That recommendation would be incorporated in a General Assembly resolution to be adopted on the proposal of the Sixth Committee. In due course, there might be a State wishing to host a diplomatic conference on the subject.

83. It was the feeling of the secretariat that the Sixth Committee was a more adequate place to seek an assessment of the situation in the matter. In that connection, the Commission might wish to request the secretariat to prepare in the inter-sessional period the remaining draft provisions of an umbrella convention, on the pattern of the relevant provisions of the Vienna Sales Convention, and submit them together with the draft rules in an annex form. Of course, those parts which would be prepared by the secretariat would

be clearly marked as such, in accordance with the past practice established in relation with the three previous UNCITRAL Conventions.⁶⁶

84. The essence of his proposal was to adopt the rules as an annex to a convention and leave the final decision to the Sixth Committee. Even if that Committee were to postpone its decision to a future session, the rules would still remain as a draft that could be used as a model. In conclusion, he stressed that all the efforts made and all the studies carried out by the Commission with a view to the formulation of the uniform rules would in any event be reflected in the legal guide for drawing up contracts for the supply and construction of large industrial works.

The meeting rose at 5 p.m.

282nd meeting

Wednesday, 1 June 1983, at 2 p.m.
Chairman: Mr. CHAFIK (Egypt)

[A/CN.9/SR.282]

The discussion covered in the summary record began at 3.05 p.m.

INTERNATIONAL CONTRACT PRACTICES: DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES AND PENALTY CLAUSES (*continued*) (A/CN.9/XVI/CRP.5 and Add.1, CRP.6)

1. Mr. SONO (Secretary of the Commission), introducing the uniform rules on liquidated damages and penalty clauses submitted by the drafting group (A/CN.9/XVI/CRP.6), explained that in article A the last phrase, whether as a penalty or as compensation, was designed to qualify the scope of application. The drafting group had preferred it to other more specific alternatives because the latter might lead to unnecessary complications.

2. Articles A *bis*, B and C were the same as the corresponding articles in the United Nations Convention on Contracts for the International Sale of Goods (Vienna Sales Convention).

3. The negative form had been retained for article D because the question of the burden of proof which the Commission had been trying to avoid might have been raised by a positive wording.

4. In article E, the word "if" had been substituted for "where" in order to follow the Vienna Sales Convention. The word "require" had been deleted to improve the drafting. In paragraph (2), references to non-performance and defect had been avoided and the phrase "a failure of performance other than delay" inserted in the second line. The second sentence contained several phrases between square brackets; a choice needed to be taken between the first and second alternatives and between the third and fourth. There had been no consensus in the drafting group on the alternatives and the decision had been left to the Commission.

5. The text of article F was based on the alternative for which the indicative voting had shown a preference. The word

"substantially" had been preferred to "grossly" or "manifestly" because the last two words could have different shades of meaning in different languages. The last sentence had been changed to the positive form.

6. For article G, the two paragraphs of the revised draft had been combined as requested by the Commission. The word "substantially" had again been used in order to conform to article F. The extent of the reduction was not stated; it was left to the discretion of the court. The reference to a limit had been deleted in order to accommodate to some extent those who had wished for some special rule in case the contract provided that the sum was payable even if the obligor was not liable. A phrase such as "to a reasonable extent" had been considered but that had been felt to be implicit in the text.

7. The words "by agreement" had been deleted in article X in line with the Vienna Sales Convention and to avoid the issue of whether the agreement should be explicit or implicit. The word "only" had also been deleted because it was no longer necessary since article X had been placed at the end of part two.

8. When article Y had been discussed in the Commission, the hope had been expressed that it could be eliminated if certain improvements were made to article E. However, after extensive discussion, the drafting group had decided to retain the article but include it as an article VI *bis* in the umbrella convention (A/CN.9/XVI/CRP.5/Add.1) if the rules became an annex to a convention.

9. He wished to assure the Commission that the drafting group had paid careful attention to the various views expressed in the discussions and had tried to accommodate as many as possible.

10. The CHAIRMAN invited the Commission first to consider part one of the document as a whole.

⁶⁶Convention on the Limitation Period in the International Sale of Goods (1974) and amending Protocol (1980); Convention on the Carriage of Goods by Sea (1978); Convention on Contracts for the International Sale of Goods (1980); see Status of Conventions in this volume, part two, VI.

11. Mr. ROEHRICH (France) said that the phrase "*défaut d'exécution*" should be substituted for "*inexécution*" in the French text of article A, line 2, to bring it in line with the English.

12. Mr. SEKHON (India) said that in the drafting group he had drawn attention to a provision in the Indian Constitution that all contracts must be in writing. Such a provision had been included in article 96 of the Vienna Sales Convention and he had understood that the same would be done in the uniform rules.

13. Mr. SONO (Secretary of the Commission) said that that provision had been included in article IV of the draft convention proposed by the secretariat (A/CN.9/XVI/CRP.5).

14. Mr. LEBEDEV (Union of Soviet Socialist Republics) said that he did not consider it adequate to include the reference to contracts being in writing merely in article IV of the umbrella convention. In the Vienna Sales Convention, the matter was referred to in article 11 as well as article 96.

15. Mr. SONO (Secretary of the Commission) said that the secretariat would give further explanations when the Commission discussed its proposal for the draft convention.

16. Mr. SAMI (Iraq) said that he considered the reference to the place of business in article B (a) to be ambiguous and would prefer the place of business to be defined simply as the place which had the closest relationship to the contract and its performance. That matter had already been discussed at a preceding session.

17. The CHAIRMAN recalled that article B was taken from the Vienna Sales Convention.

18. There being no further comments on part one, he invited the Commission to discuss part two, article by article.

Article D

19. Mr. ROEHRICH (France) said that the words "*défaut d'exécution*" should be substituted for "*inexécution*" in the French version, as in article A.

20. The CHAIRMAN said that the correction would be made in both cases.

Article E, paragraph (1)

21. Mr. VOLKEN (Observer for Switzerland) recalled that his delegation had proposed that a reference to failure to deliver goods at the agreed place should be inserted in addition to delay.

22. Mr. SONO (Secretary of the Commission) said that the drafting group had not been able to accommodate all the views expressed in the Commission. In any case, paragraphs (1) and (2) could be invoked together.

23. The CHAIRMAN said that there had been no majority for that suggestion during the discussion.

Article E, paragraph (2)

24. Mr. ROEHRICH (France) proposed that the various alternatives should be voted upon immediately since they had

been amply discussed in both the Commission and the drafting group.

25. The CHAIRMAN invited the Commission to proceed to an informal indicative vote on the four alternatives in article E, paragraph (2), on the understanding that the choice was between alternatives 1 and 2 and between alternatives 3 and 4.

26. *The results of the informal indicative vote on the alternative proposals in article E, paragraph (2), were: alternative 1, 27 votes in favour, 3 against and 4 abstentions; alternative 2, 7 votes in favour; alternative 3, 6 votes in favour, 23 against and 1 abstention; alternative 4, 25 votes in favour.*

27. The CHAIRMAN noted that alternatives 1 and 4 commanded the greatest support. He suggested that those versions should be adopted.

28. *It was so agreed.*

Article F

29. Mr. SAWADA (Japan) said that, although his delegation had no objection to the replacement of the words "grossly" and "manifestly" in both articles F and G by "substantially", he hoped that the intention had not been to make the provisions less stringent.

30. Mr. SONO (Secretary of the Commission) reminded the Commission that some delegations had considered the word "grossly" too vague. The word "substantially" was the only one on which there had been agreement in all languages. There was no intention to modify the stringency of the rule.

31. Mr. BOGGIANO (Observer for Argentina) pointed out that, in the Spanish text, different translations were used for "substantially" in article F and in article G.

32. Mr. OLIVENCIA RUIZ (Spain) suggested that the Spanish-speaking delegations should discuss the matter and submit their solution to the secretariat.

33. *It was so agreed.*

Article G

34. Mr. MUCHUI (Kenya) said that the text of article G could be improved by replacing "unless the agreed sum" by "unless it". There could be no doubt that the reference was in fact to the agreed sum.

35. Mr. SONO (Secretary of the Commission) said that the suggestion made by the representative of Kenya did indeed improve the draft. The drafting group had initially favoured "unless such sum", but later restored "unless the agreed sum" in order to follow the wording of the Vienna Sales Convention. It was also felt that the text should be made as explicit as possible for the benefit of those whose native language was not English.

36. The CHAIRMAN said that, if he heard no objection, he would assume that the Commission wished to adopt article G, on the understanding that the Kenyan representative's suggestion would be considered in consultation with the secretariat.

37. *It was so decided.*

Article X

38. The CHAIRMAN said that, if he heard no objection, he would assume that the Commission wished to adopt article X.

39. *It was so decided.*

The meeting was suspended at 4 p.m. and resumed at 4.35 p.m.

Point raised by the United Kingdom delegation

40. Mr. GUEST (United Kingdom) said that, since the Commission's report would presumably state that the Commission had approved parts one and two of the draft, and since the question might come up in the Sixth Committee and other bodies, his delegation would like to have the following statement incorporated in the report: "One representative, however, stated that, notwithstanding considerable efforts made by the Commission and the spirit of accommodation shown by all delegations in the course of the work, he remained to be convinced that the topic of liquidated damages and penalty clauses was, by virtue of its intrinsic nature, an appropriate subject for unification."

41. Mr. FARNSWORTH (United States of America) said that his delegation might wish to associate itself with the statement just made by the representative of the United Kingdom, but would reserve its position until the question of the title had been decided.

42. Mr. LEBEDEV (Union of Soviet Socialist Republics) said that over the years the Commission had discussed the important question of whether the draft should take the form of rules, a model law or a convention. It was to be noted that the existing title invoked two juridical concepts which were not common to all legal systems. It might therefore be better to give a neutral, descriptive title to the draft, and he suggested that the following wording might serve as a basis for the title: "Uniform rules on contract clauses for an agreed sum due upon a failure of performance".^{bb} That was not perhaps an ideal version, but it had at least the merit of being easily translatable into other languages. In that connection, he pointed out that the term "liquidated damages" was very difficult to translate into Russian.

43. Mr. MUCHUI (Kenya) said that this suggestion did not at first sight appeal to his delegation. Article A referred to a "penalty" and to "compensation", and the latter term was understood to mean liquidated damages.

44. Mr. OLIVENCIA RUIZ (Spain) said that the title suggested by the representative of the Union of Soviet Socialist Republics was satisfactory in that it provided a neutral and descriptive formulation in the absence of an agreed terminology which would cover the concepts involved.

45. Mr. BONELL (Italy) said that the suggestion of the representative of the Union of Soviet Socialist Republics was an interesting one, and he agreed that the existing title gave rise to considerable difficulties from the standpoint of translation. In Italian, for example, the term *clausula penale* covered what would elsewhere be understood by the term "liquidated damages", and it was thus difficult to arrive at Italian equivalents for penalty clauses and liquidated damages as discrete concepts.

46. Mr. ROEHRICH (France) said that it was rather late to try to settle the question, and that the best solution might be to adopt the formulation suggested by the representative of the Union of Soviet Socialist Republics but retain the footnote on page 1 of document A/CN.9/XVI/CRP.6.

47. Ms. VILUS (Yugoslavia) said that it was indeed strange to have a title which referred to liquidated damages and penalty clauses when those terms were not employed in the body of the text, and she therefore supported the version proposed by the Union of Soviet Socialist Republics.

48. Mr. WAGNER (German Democratic Republic) and Mr. MORALES (Cuba) said that their delegations favoured the wording suggested by the representative of the Union of Soviet Socialist Republics.

49. Mr. MAGNUSSON (Sweden) said that his delegation had no strong feelings about retaining the original title or accepting the neutral formulation suggested by the Soviet delegation.

50. Mr. TOLENTINO (Philippines) said that the existing title would not be incompatible with his country's legal system, but he noted that in articles F and G drafting changes had been introduced which altered the principles of liquidated damages, and he accordingly found the proposed Soviet title an acceptable alternative, albeit a rather lengthy one. A possible solution might be to refer to "contractual indemnity clauses".

51. Mr. FELICIO (Brazil) said he could support the change proposed by the representative of the Philippines; he would also prefer the word "uniform" in the title suggested by the Soviet delegation to be deleted.

52. The CHAIRMAN said that there seemed to be general agreement that the existing title was unsatisfactory, and a large measure of support for the Soviet delegation's suggestion. He would therefore assume that the Commission wished to adopt the wording of the title suggested by the delegation of the Union of Soviet Socialist Republics, while retaining the footnote indicating that the title was a tentative one until the drafting exercise was completed.

53. *It was so decided.*

Secretariat proposal (A/CN.9/XVI/CRP.5 and Add.1)

54. Mr. SONO (Secretary of the Commission), introducing the secretariat proposal for a draft United Nations convention on liquidated damages and penalty clauses (A/CN.9/XVI/CRP.5 and Add.1), said that the secretariat's proposal should be viewed in the nature of a sample format for the guidance and information of the Commission should it decide to pursue the option of an umbrella convention with uniform rules attached. Most of the provisions were modelled closely on the Vienna Sales Convention, the exceptions being article IV, article V and article VI *bis*, which had formerly been article Y and was contained in A/CN.9/XVI/CRP.5/Add.1.

55. In the case of the Vienna Sales Convention, the secretariat had been requested to prepare a draft for consideration at the stage of the plenipotentiary conference. In the present case, however, the secretariat had felt it would assist the Commission in reaching a decision to have an idea of the structure that a convention could take. Since the uniform rules had been prepared for use either as a model or

^{bb}See in this volume part three, IV, A.

as an annex, the various reservation clauses were not included; reservations by States on points permitted should be reflected in domestic legislation in an appropriate manner. That had been the approach taken in the 1964 Uniform Law on the International Sale of Goods (ULIS).

56. The Commission had just reached tentative agreement on the title for the uniform rules, but if it were to decide on the form that the rules should take it should also make a firm decision as to their title.

57. The three courses of action open to the Commission were: to recommend to the Sixth Committee the model law approach; to pursue the option of an umbrella convention with uniform rules attached thereto; and a third alternative which had been put forward earlier as the secretariat proposal. That solution would consist of giving the Sixth Committee a full report on the Commission's proceedings, indicating clearly the divergence of views among its members, and explaining that the annex approach had been followed as a compromise, although a majority of members had been in favour of the model law option. The Commission would further state that in the light of the divergent views, it was not in a position to propose the convening of a diplomatic conference. Given, however, the desirability of promoting uniformity in the field in question, the Commission could inform the Sixth Committee that it recommended the adoption of a convention through the Sixth Committee itself. There was of course always the possibility that the Sixth Committee would not find such an approach feasible and would decide either to hold a diplomatic conference or to recommend the annex as a model for domestic legislation.

58. In any event, a decision by UNCITRAL was necessary if the Commission wished to complete the project at its current session.

59. Mr. EDWARDS (Australia) said that most delegations appeared to be in favour of the model law approach. His delegation had difficulty with the idea of the Commission putting forward as the primary option a proposal to the Sixth Committee which was at variance with the view of the majority of its members. Could it not instead recommend to the Sixth Committee the adoption of the uniform rules as a model for domestic legislation, stating that that had been the majority view of the Commission? At the same time, the Sixth Committee could be informed that some delegations had favoured the adoption of a convention; the proposals in A/CN.9/XVI/CRP.5 and Add.1 could be annexed as a secondary document, for use in the event that the Sixth Committee did not agree with the Commission's recommendation.

60. The final decision would in any event rest with the Sixth Committee, but the central thrust of the Commission's recommendation should tally with the view of most of its members.

61. Mr. ROEHRICH (France) said that the main difference between the Australian representative's suggestion and the third alternative advanced by the Secretary was that the former would require the Commission to take a definite position, whereas the latter would amount to a neutral submission to the Sixth Committee. It was unlikely that the Sixth Committee would turn down a firm recommendation by the Commission. He felt that the matter should be given further thought, since it was a question of orientation and policy, as well as of the way in which the case was presented.

62. Mr. DIXIT (India) said that the Commission should endeavour to reach consensus on the matter. It was important to take an objective approach in reporting to the Sixth Committee, and it should moreover be borne in mind that the Commission members accounted for no more than one-third of the member States represented in the General Assembly. On that basis his delegation would favour the alternative put forward by the Secretary.

63. Mr. FARNSWORTH (United States of America) pointed out that UNCITRAL, which was an expert body, had devoted considerable time and effort to the subject. He felt that the Commission owed it to the Sixth Committee to provide clear guidance on the matter. One option would be to maintain the initial compromise agreed to by the Commission. If that course of action were taken, delegations which wished to do so could enter a reservation. Alternatively, the Commission could go along with the Australian representative's suggestion, which his delegation felt was more straightforward.

64. Whatever course of action the Commission agreed to, it should be remembered that the only decision the Commission had taken was to proceed with the drafting of the uniform rules, giving a fair hearing to the idea of their being annexed to a convention; his delegation's understanding had been that the Commission would return to the question of the form that the rules would actually take.

65. Mr. SONO (Secretary of the Commission) said that the Commission had tentatively agreed to prepare the uniform rules as a possible annex to a convention, since the annex approach could accommodate the views of all concerned.

66. Mr. LEBEDEV (Union of Soviet Socialist Republics) agreed with the United States representative that the Commission had agreed to revert to the matter of the form for the rules. His delegation believed that the best course of action would be for the Commission to give a full report to the Sixth Committee on the way in which the Commission's proceedings had actually developed. There had in fact been three schools of thought: some delegations had felt that the uniform rules should be used as general provisions, others were in favour of a model law, while still others preferred a convention. During the discussion, a formula had been proposed as a possible compromise based on the proposal in paragraph 17 of the Commission's report on its fifteenth session (A/37/17). The Commission could at the same time submit the proposals in A/CN.9/XVI/CRP.5 and Add.1 as a possible structure for a future convention.

67. He agreed with what had been said by the representative of India; UNCITRAL had a responsibility to all member States represented in the General Assembly, not only those who were members of the Commission.

68. Mr. HERBER (Federal Republic of Germany) agreed that a full and clear report to the Sixth Committee was essential. So far as substance was concerned, however, his delegation saw no wisdom in the Commission recommending a course of action to which it had not itself agreed.

69. The Australian proposal reflected the situation as it now stood; since there appeared to be a large majority in favour of the uniform rules, those should be submitted to the Sixth Committee. The question of whether or not they should be annexed to a convention should be left open, since there was no agreement on that point.

283rd meeting

Thursday, 2 June 1983, at 9.30 a.m.

Chairman: Mr. CHAFIK (Egypt)

[A/CN.9/SR.283]

*The meeting was called to order at 9.50 a.m.***INTERNATIONAL CONTRACT PRACTICES:
DRAFT UNIFORM RULES ON LIQUIDATED DAMAGES
AND PENALTY CLAUSES (continued)**

(A/CN.9/218, A/CN.9/219 and Add.1 and A/CN.9/235)

1. The Chairman said that there were two proposals before the Commission. One, submitted by the representative of Australia, was based on the majority view noted at the outset of the discussions in favour of a model law. The other, submitted by the representative of the Union of Soviet Socialist Republics, was based on the form of an umbrella convention to which uniform rules would be annexed. He suggested that the sponsors of the two proposals should hold informal consultations with a view to producing a compromise proposal, which the Commission could approve by consensus for submission to the Sixth Committee of the General Assembly.

2. *It was so agreed.*

The meeting was suspended at 9.55 a.m. and resumed at 10.40 a.m.

3. Mr. SONO (Secretary of the Commission) said that, as a result of a compromise arrived at during the informal consultations, the report on the Commission's sixteenth session would indicate that the Commission had completed its work on the draft uniform rules; rules A to X would appear as an addendum to the report.

4. The report would reflect the fact that three main approaches—model law, convention and general conditions—had been discussed, as well as a fourth approach, based on the form of a convention with substantive rules annexed to it. The draft text of an umbrella convention, prepared by the secretariat, would appear as a second addendum to the report.

5. The report would note that, whilst there had been considerable support for the form of a convention with rules annexed, the model law approach seemed to have had the greatest support. Since, however, the Commission had been unable to arrive at a consensus on the form to be adopted, the report would refer the final decision on the matter to the Sixth Committee.

6. Mr. SAMI (Iraq) said that the fact that there had been a majority in favour of a model law should be clearly reflected in the report—particularly since the majority had been considerable, and even those who preferred the form of a convention had indicated their willingness to accept the majority view.

7. The CHAIRMAN said that the majority at the end of the discussion had been much smaller than at the outset. The purpose of the proposal now being made was to enable the Commission to proceed on its traditional basis of consensus. However, the report would reflect the point made by the representative of Iraq.

8. Mr. SONO (Secretary of the Commission) said that since a number of delegations had changed their viewpoints during the debate, and since no indicative vote had been taken on the matter at any stage, it might be difficult to state in the report that there had been a majority in favour of the model law formula.

9. Mr. DUCHEK (Austria) said that he shared the view of the representative of Iraq. The Sixth Committee should not be left to settle a matter on which a majority view had been expressed in the Commission.

10. As could be seen from the summary records of the Commission's fifteenth session, it was the Austrian delegation which had suggested the formula based on an umbrella convention accompanied by an annex, as a compromise between the convention and model law approaches. The summary records of the current session's earlier meetings had revealed some support for that formula; his delegation still preferred it, since the only possible solution seemed to be one embodying the convention approach. However, as it had stated throughout, his delegation would not object to the model law formula if that was the only way to obtain approval for the draft uniform rules. The Commission ought to try and reach a consensus on the matter.

11. The CHAIRMAN said that, if there was no formal objection, he would take it that the Commission adopted the compromise described by the Secretary.

12. *It was so decided.*

13. The CHAIRMAN said that the Commission had thus concluded its consideration of agenda item 4.

The discussion covered in the summary record ended at 11 a.m.

II. TEXTS ON LIQUIDATED DAMAGES AND PENALTY CLAUSES^a

A. Uniform Rules on Contract Clauses for an Agreed Sum Due upon Failure of Performance (A/38/17, annex I) (A/CN.9/243, annex I)^b

B. Draft United Nations Convention on Contract Clauses for an Agreed Sum Due upon Failure of Performance (A/38/17, annex II) (A/CN.9/243, annex II)^c

[A/CN.9/243, annex I]

Article 4

A. Uniform Rules on Contract Clauses for an Agreed Sum Due upon Failure of Performance¹

PART ONE: SCOPE OF APPLICATION

Article 1²

These Rules apply to international contracts in which the parties have agreed that, upon a failure of performance by one party (the obligor), the other party (the obligee) is entitled to an agreed sum from the obligor, whether as a penalty or as compensation.

Article 2

For the purposes of these Rules:

- (a) A contract shall be considered international if, at the time of the conclusion of the contract, the parties have their places of business in different States;
- (b) The fact that the parties have their places of business in different States is to be disregarded whenever this fact does not appear either from the contract or from any dealings between, or from information disclosed by, the parties at any time before or at the conclusion of the contract;
- (c) Neither the nationality of the parties nor the civil or commercial character of the parties or of the contract is to be taken into consideration in determining the application of these Rules.

Article 3

For the purposes of these Rules:

- (a) If a party has more than one place of business, his 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;
- (b) If a party does not have a place of business, reference is to be made to his habitual residence.

^aFor consideration by the Commission see Report, chapter II (part one, A). See also in this volume part two, I.

^b29 June 1983. Referred to in Report, para. 76.

^c29 June 1983. Referred to in Report, para. 77.

¹The text of the Rules was adopted by the Commission in paragraph 76 of the report. The title was provisionally adopted by the Commission in paragraph 75 of the report.

²See table of correspondence between articles as numbered in the Rules as adopted, and the Rules as discussed in the Commission.

These Rules do not apply to contracts concerning goods, other property or services which are to be supplied for the personal, family or household purposes of a party, unless the other party, at any time before or at the conclusion of the contract, neither knew nor ought to have known that the contract was concluded for such purposes.

PART TWO: SUBSTANTIVE PROVISIONS

Article 5

The obligee is not entitled to the agreed sum if the obligor is not liable for the failure of performance.

Article 6

- (1) If the contract provides that the obligee is entitled to the agreed sum upon delay in performance, he is entitled to both performance of the obligation and the agreed sum.
- (2) If the contract provides that the obligee is entitled to the agreed sum upon a failure of performance other than delay, he is entitled either to performance or to the agreed sum. If, however, the agreed sum cannot reasonably be regarded as compensation for that failure of performance, the obligee is entitled to both performance of the obligation and the agreed sum.

Article 7

If the obligee is entitled to the agreed sum, he may not claim damages to the extent of the loss covered by the agreed sum. Nevertheless, he may claim damages to the extent of the loss not covered by the agreed sum if the loss substantially exceeds the agreed sum.

Article 8

The agreed sum shall not be reduced by a court or arbitral tribunal unless the agreed sum is substantially disproportionate in relation to the loss that has been suffered by the obligee.

Article 9

The parties may derogate from or vary the effect of articles 5, 6 and 7 of these Rules.

Table of correspondence

Article as adopted	Article before the Commission
1	A
2	A bis
3	B
4	C
5	D
6	E
7	F
8	G
9	X

[A/CN.9/243, annex II]**B. Draft United Nations Convention on Contract Clauses for an Agreed Sum Due upon Failure of Performance¹***Article I (Vienna Sales Convention, art. 1)²*

Each Contracting State shall apply the Uniform Rules on Contract Clauses for an Agreed Sum due upon a Failure of Performance (hereinafter referred to as "the Uniform Rules") contained in the annex to this Convention to the contracts described in article 1 of the Uniform Rules

(a) When, at the time of the conclusion of the contract, the parties have their places of business, as described in articles 2 and 3 of the Uniform Rules, in different Contracting States; or

(b) When the rules of private international law lead to the application of the law of a contracting State.

Article II (Vienna Sales Convention, art. 90)

The Uniform Rules do not prevail over any international agreement which has already been or may be entered into and which contains provisions concerning the matters governed by the Uniform Rules, provided that the parties to the contract have their places of business in States parties to such agreement.

Article III (Vienna Sales Convention, art. 95)

Any State may declare at the time of signature, ratification, acceptance, approval or accession that it will not be bound by subparagraph (b) of article I.

Article IV (Vienna Sales Convention, art. 96)³

A Contracting State whose legislation requires contracts to be concluded in or evidenced by writing may at any time

¹The draft Convention was prepared by the secretariat in the eventuality that it was decided to annex the Rules to a convention. See paragraphs 77 and 78 of the report.

²The source used as a model for article I was the United Nations Convention on Contracts for the International Sale of Goods, hereafter referred to as the Vienna Sales Convention, article 1 (Yearbook ... 1980, part three, I, B) (A/CONF.97/18, annex I).

³The Commission agreed to the substance of articles IV and V in the eventuality that a convention was prepared. See paragraph 67 of the report.

make a declaration that it will apply the Uniform Rules only to a contract concluded in or evidenced by writing where any party has his place of business in that State.

Article V (ULIS, art. V)⁴

Any State may declare at the time of signature, ratification, acceptance, approval or accession to this Convention that it will apply the Uniform Rules only to a contract in which the parties to the contract have agreed that the Uniform Rules be applied thereto.

Article VI (Vienna Sales Convention, art. 94)

(1) Two or more Contracting States which have the same or closely related legal rules on matters governed by the Uniform Rules may at any time declare that the Uniform Rules are not to apply to a contract where the parties thereto have their places of business in those States. Such declarations may be made jointly or by reciprocal unilateral declarations.

(2) A Contracting State which has the same or closely related legal rules on matters governed by the Uniform Rules as one or more non-contracting States may at any time declare that the Uniform Rules are not to apply to contracts where the parties have their places of business in those States.

(3) If a State which is the object of a declaration under the preceding paragraph subsequently becomes a Contracting State, the declaration made will, as from the date on which this Convention enters into force in respect of the new Contracting State, have the effect of a declaration made under paragraph (1), provided that the new contracting State joins in such declaration or makes a reciprocal unilateral declaration.

Article VII (Vienna Sales Convention, art. 28)⁵

If, in accordance with the provisions of the Uniform Rules the obligee is entitled to performance of an obligation, a court is not bound to enter a judgment for specific performance unless the court would do so in respect of similar contracts not governed by the Uniform Rules.

Article VIII (Vienna Sales Convention, art. 89)

The Secretary-General of the United Nations is hereby designated as the depository for this Convention.

Article IX (Vienna Sales Convention, art. 91)

(1) This Convention is open for signature by all States at the Headquarters of the United Nations in New York until

(2) This Convention is subject to ratification, acceptance or approval by the Signatory States.

(3) This Convention is open for accession by all States which are not Signatory States as from the date it is open for signature.

⁴The source used as a model for article V was article V of the Convention relating to a Uniform Law on the International Sale of Goods (The Hague, 1964) (United Nations, *Treaty Series*, vol. 834, No. 11929, p. 107).

⁵The Commission considered article VII in the context of the substance of the Rules. See paragraphs 43, 44 and 73 of the report.

(4) Instruments of ratification, acceptance, approval and accession are to be deposited with the Secretary-General of the United Nations.

Article X (Vienna Sales Convention, art. 93)

(1) If a Contracting State has two or more territorial units in which, according to its constitution, different systems of law are applicable in relation to the matters dealt with in the Uniform Rules, it may, at the time of signature, ratification, acceptance, approval or accession, declare that this Convention is to extend to all its territorial units or only to one or more of them, and may amend its declaration by submitting another declaration at any time.

(2) These declarations are to be notified to the depositary and are to state expressly the territorial units to which the Convention extends.

(3) If, by virtue of a declaration under this article, this Convention extends to one or more but not all of the territorial units of a Contracting State, and if the place of business of a party is located in that State, this place of business, for the purposes of this Convention, is considered not to be in a Contracting State, unless it is in a territorial unit to which the Convention extends.

(4) If a Contracting State makes no declaration under paragraph (1) of this article, the Convention is to extend to all territorial units of that State.

Article XI (Vienna Sales Convention, art. 97)

(1) Declarations made under this Convention at the time of signature are subject to a confirmation upon ratification, acceptance or approval.

(2) Declarations and confirmations of declarations are to be made in writing and be formally notified to the depositary.

(3) A declaration takes effect simultaneously with entry into force of this Convention in respect of the State concerned. However, a declaration of which the depositary receives formal notification after such entry into force takes effect on the first day of the month following the expiration of six months after the date of its receipt by the depositary. Reciprocal unilateral declarations under article VI take effect on the first day of the month following the expiration of six months after the receipt of the latest declaration by the depositary.

(4) Any State which makes a declaration under this Convention may withdraw it at any time by a formal notification in writing addressed to the depositary. Such withdrawal is to take effect on the first day of the month following the

expiration of six months after the date of the receipt of the notification by the depositary.

(5) A withdrawal of a declaration made under article VI renders inoperative, as from the date on which the withdrawal takes effect, any reciprocal declaration made by another State under that article.

Article XII (Vienna Sales Convention, art. 98)

No reservations are permitted except those expressly authorized in this Convention.

Article XIII (Vienna Sales Convention, art. 99)

(1) This Convention enters into force on the first day of the month following the expiration of twelve months after the date of deposit of the [fifth] instrument of ratification, acceptance, approval or accession.

(2) When a State ratifies, accepts, approves or accedes to this Convention after the deposit of the [fifth] instrument of ratification, acceptance, approval or accession, this Convention enters into force in respect of that State on the first day of the month following the expiration of twelve months after the date of the deposit of its instrument of ratification, acceptance, approval or accession.

Article XIV (Vienna Sales Convention, art. 100)

This Convention applies only to contracts concluded on or after the date when the Convention enters into force in respect of the Contracting States referred to in subparagraph (a) or the Contracting State referred to in subparagraph (b) of article I.

Article XV (Vienna Sales Convention, art. 101)

(1) A Contracting State may denounce this Convention by a formal notification in writing addressed to the depositary.

(2) The denunciation takes effect on the first day of the month following the expiration of twelve months after the notification is received by the depositary. Where a longer period for the denunciation to take effect is specified in the notification, the denunciation takes effect upon the expiration of such longer period after the notification is received by the depositary.

Done at this day of

in a single original, of which the Arabic, Chinese, English, French, Russian and Spanish texts are equally authentic.

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V. CHECK LIST OF UNCITRAL DOCUMENTS

List of documents before the Commission at its sixteenth session

<i>Title or description</i>	<i>Document symbol</i>	<i>Location in present volume</i>
A. General series		
Provisional agenda, annotations thereto and tentative schedule of meetings; note by the Secretary-General	A/CN.9/231	Not reproduced
Report of the Working Group on International Contract Practices on the work of its fourth session (Vienna, 4-15 October 1982)	A/CN.9/232	Part two, III, A
Report of the Working Group on International Contract Practices on the work of its fifth session (New York, 22 February—4 March 1983)	A/CN.9/233	Part two, III, D
Report of the Working Group on the New International Economic Order on the work of its fourth session (Vienna, 16-20 May 1983)	A/CN.9/234	Part two, IV, A
Revised text of draft uniform rules on liquidated damages and penalty clauses	A/CN.9/235	Part two, I
Co-ordination of work: some recent developments in the field of international transport of goods	A/CN.9/236	Part two, V, C
Current activities of international organizations related to the harmonization and unification of international trade law	A/CN.9/237 and Add.1 to 3 and Add.1/Corr.1 (English only)	Part two, V, B
Co-ordination of work: legal aspects of automatic data processing	A/CN.9/238	Part two, V, D
Co-ordination of work in general	A/CN.9/239	Part two, V, A
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Status of conventions	A/CN.9/241	Part two, VI
Electronic funds transfers: progress report	A/CN.9/242	Part two, II
Report of the United Nations Commission on International Trade Law on the work of its sixteenth session (Vienna, 24 May—3 June 1983)	A/CN.9/243	Part one, A
B. Restricted series		
Communication of information on developments relevant to the work of the Commission	A/CN.9/XVI/R.1	Not reproduced
Draft report of the United Nations Commission on International Trade Law on the work of its sixteenth session (24 May—3 June 1983)	A/CN.9/XVI/CRP.1 and Add.1 to 12	Not reproduced
Alternative proposals on article F	A/CN.9/XVI/CRP.2	Not reproduced
Draft uniform rules on liquidated damages and penalty clauses (Part I: scope of application and general provisions)	A/CN.9/XVI/CRP.3	Not reproduced
Suggestion by the secretariat	A/CN.9/XVI/CRP.4	Not reproduced
Draft United Nations Convention on Liquidated Damages and Penalty Clauses: secretariat proposal	A/CN.9/XVI/CRP.5 and Add.1	Not reproduced
Uniform Rules on Liquidated Damages and Penalty Clauses: submission of the Drafting Group	A/CN.9/XVI/CRP.6	Not reproduced
C. Information series		
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Summary records of the 255th to 261st meetings of the United Nations Commission on international Trade Law related to international contract practices: Draft Uniform Rules on Liquidated Damages and Penalty Clauses	A/CN.9/SR.255-261,	Part three, I, B, 2
SIXTEENTH SESSION		
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Working Group on International Contract Practices, fourth and fifth sessions

A. Working papers

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Model Law on International Commercial Arbitration: draft articles 1 to 24 on scope of application, arbitration agreement, arbitrators, and arbitral procedure: note by the secretariat	A/CN.9/WG.II/WP.37	Part two, III, B, 1
Model Law on International Commercial Arbitration: draft articles 25 to 36 on award: note by the secretariat	A/CN.9/WG.II/WP.38	Part two, III, B, 2

FIFTH SESSION

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Model Law on International Commercial Arbitration: revised draft articles I to XXVI: note by the secretariat	A/CN.9/WG.II/WP.40	Part two, III, D, 1
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Working Group on the New International Economic Order, fourth session**A. Working papers**

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