

**United Nations  
Commission on  
International  
Trade Law**

**YEARBOOK**

**Volume XV: 1984**



**UNITED NATIONS**

**New York, 1987**

**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.

A/CN.9/SER.A/1984

UNITED NATIONS PUBLICATION  
Sales No. E.86.V.2  
ISBN 92-1-133275-3  
ISSN 0251-4265  
03800P

## CONTENTS

	<i>Page</i>
INTRODUCTION .....	vii

**Part One. Report of the Commission on its annual session; comments and action thereon**

**THE SEVENTEENTH SESSION (1984)**

A. Report of the United Nations Commission on International Trade Law on the work of its seventeenth session (New York, 25 June-10 July 1984) (A/39/17) .....	3
B. United Nations Conference on Trade and Development (UNCTAD): extract from the report of the Trade and Development Board on its twenty-ninth session (TD/B/1026) .....	22
C. General Assembly: report of the Sixth Committee (A/39/698).....	22
D. General Assembly resolution 39/82 of 29 January 1985 .....	23

**Part Two. Studies and reports on specific subjects**

**I. INTERNATIONAL PAYMENTS**

A. International negotiable instruments.....	27
1. Draft Convention on International Bills of Exchange and International Promissory Notes and draft Convention on International Cheques: analytical compilation of comments by Governments and international organizations: report of the Secretary-General (A/CN.9/248) .....	27
2. Draft Convention on International Bills of Exchange and International Promissory Notes and draft Convention on International Cheques: major controversial and other issues: note by the secretariat (A/CN.9/249 and Add.1) 106	106
B. Electronic funds transfers .....	115
Draft legal guide on electronic funds transfers: report of the Secretary-General (A/CN.9/250 and Add.1-4) .....	115

**II. INTERNATIONAL COMMERCIAL ARBITRATION**

A. Sixth session of the Working Group on International Contract Practices (Vienna, 29 August-9 September 1983).....	155
1. Report of the Working Group on the work of its sixth session (A/CN.9/245) 155	155
2. Working papers submitted to the Working Group at its sixth session .....	179
(a) Model law on international commercial arbitration: revised draft articles A to G on adaptation and supplementation of contracts, commencement of arbitral proceedings, minimum contents of statements of claim and defence, language in arbitral proceedings, court assistance in taking evidence, termination of arbitral proceedings and period for enforcement of arbitral award: note by the secretariat (A/CN.9/WG.II/WP.44).....	179
(b) Model law on international commercial arbitration: redrafted articles I to XII on scope of application, general provisions, arbitration agreement and the courts, and composition of arbitral tribunal: note by the secretariat (A/CN.9/WG.II/WP.45) .....	183
(c) Model law on international commercial arbitration: revised draft articles XXV to XXX on recognition and enforcement of arbitral award and recourse against award: note by the secretariat (A/CN.9/WG.II/WP.46) 187	187

B.	Seventh session of the Working Group on International Contract Practices (New York, 6-17 February 1984) .....	189
1.	Report of the Working Group on the work of its seventh session (A/CN.9/246)	189
2.	Draft text of a model law on international commercial arbitration as adopted by the Working Group (A/CN.9/246, Annex) .....	212
3.	Working papers submitted to the Working Group at its seventh session .....	218
(a)	Composite draft text of a model law on international commercial arbitration: note by the secretariat (A/CN.9/WG.II/WP.48) .....	218
(b)	Model law on international commercial arbitration: territorial scope of application and related issues: note by the secretariat (A/CN.9/WG.II/WP.49) .....	227
(c)	Composite draft text of a model law on international commercial arbitration: some comments and suggestions for consideration: note by the secretariat (A/CN.9/WG.II/WP.50) .....	230
<b>III. NEW INTERNATIONAL ECONOMIC ORDER</b>		
A.	Report of the Working Group on the New International Economic Order on the work of its fifth session (New York, 23 January-3 February 1984) (A/CN.9/247)...	235
B.	Working papers submitted to the Working Group on the New International Economic Order at its fifth session .....	247
	Draft legal guide on drawing up international contracts for construction of industrial works: draft chapters: report of the Secretary-General (A/CN.9/WG.V/WP.11 and Add. 1-9) .....	247
<b>IV. INTERNATIONAL TRANSPORT LAW</b>		
A.	Liability of operators of transport terminals: report of the Secretary-General (A/CN.9/252).....	287
	Annex I: selected provision of major international transport Conventions (A/CN.9/252, annex I) .....	295
B.	Text of preliminary draft Convention on Operators of Transport Terminals (A/CN.9/252, annex II) .....	297
C.	Explanatory report on the preliminary draft Convention on the Liability of Operators of Transport Terminals prepared by the secretariat of UNIDROIT: note by the secretariat (A/CN.9/WG.II/WP.52/Add. 1).....	301
<b>V. CO-ORDINATION OF WORK</b>		
A.	Co-ordination of work in general: report of the Secretary-General (A/CN.9/255) 313	313
B.	Uniform customs and practice for documentary credits: report of the Secretary-General (A/CN.9/251) .....	315
	Annex I: Explanatory note submitted by the International Chamber of Commerce to the seventeenth session of the United Nations Commission on International Trade Law on the 1983 revision of uniform customs and practice for documentary credits .....	315
	Annex II: Text of the uniform customs and practice for documentary credits, 1983 revision .....	316
C.	Current activities of international organizations in the field of barter and barter-like transactions: report of the Secretary-General (A/CN.9/253) .....	324
D.	Legal aspects of automatic data processing: report of the Secretary-General (A/CN.9/254).....	328
<b>VI. STATUS OF CONVENTIONS</b>		
	Note by the secretariat (A/CN.9/257) .....	333
<b>VII. TRAINING AND ASSISTANCE</b>		
	Report of the Secretary-General (A/CN.9/256) .....	335

**Part Three. Annexes**

I.	SUMMARY RECORDS OF THE UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW FOR SESSIONS DEVOTED TO THE PREPARATION OF DRAFT LEGAL TEXTS .....	339
	Draft Convention on International Bills of Exchange and International Promissory Notes; draft Convention on International Cheques .....	339
	Summary records of the 286th to 299th and 301st meetings, seventeenth session (New York, 25 June-6 July 1984) (A/CN.9/SR.286-299 and 301) .....	339
II.	BIBLIOGRAPHY OF RECENT WRITINGS RELATED TO THE WORK OF UNCITRAL .....	378
III.	CHECK-LIST OF UNCITRAL DOCUMENTS .....	383

## INTRODUCTION

Since its establishment on 17 December 1966, the United Nations Commission on International Trade Law (UNCITRAL) has devoted its activity to "the promotion of the progressive harmonization and unification of the law of international trade". This *Yearbook*, the fifteenth of the series,<sup>1</sup> is intended to serve this purpose by making the work of the Commission more widely known and more readily available.

This volume covers the actions of the Commission and its subsidiary bodies from the end of its sixteenth session (June 1983) up to and including the seventeenth session (July 1984).

The present volume consists of three parts. Part one contains the Commission's report on the work of its seventeenth session, which was held in New York from 25 June to 10 July 1984. It contains also the actions thereon by the United Nations Conference on Trade and Development (UNCTAD) and by the General Assembly.

In part two the documents considered at the seventeenth session of the Commission are reproduced. Among them are the reports of the Commission's Working Groups dealing respectively with international contract practices and the new international economic order. Also included in this part are reports by the Secretary-General and notes by the secretariat of UNCITRAL which were before the Working Groups.

Part three contains summary records of the seventeenth session, a bibliography of recent writings related to the work of UNCITRAL prepared by the secretariat, and a check-list of UNCITRAL documents.

UNCITRAL secretariat  
Vienna International Centre  
P.O. Box 500, A-1400 Vienna, Austria

<sup>1</sup>To date the following volumes of the *Yearbook* of the United Nations Commission on International Trade Law (abbreviated here as *Yearbook* [year]) have been published.

Volume	Years covered	United Nations publication, Sales No.
I	1968-1970	E.71.V.1
II	1971	E.72.V.4
III	1972	E.73.V.6
Supplement to vol. III	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 SEVENTEENTH SESSION (1984)

### A. Report of the United Nations Commission on International Trade Law on the work of its seventeenth session (New York, 25 June-10 July 1984)<sup>a</sup>

#### CONTENTS

	<i>Paragraphs</i>
INTRODUCTION .....	1-2
<i>Chapter</i>	
I. ORGANIZATION OF THE SESSION .....	3-10
A. Opening .....	3
B. Membership and attendance .....	4-7
C. Election of officers .....	8
D. Agenda .....	9
E. Adoption of the report .....	10
II. INTERNATIONAL PAYMENTS .....	11-93
A. Draft Convention on International Bills of Exchange and International Promissory Notes and draft Convention on International Cheques .....	11-88
B. Electronic funds transfers .....	89-93
III. INTERNATIONAL COMMERCIAL ARBITRATION .....	94-104
A. Draft model law on international commercial arbitration .....	94-101
B. UNCITRAL Arbitration Rules .....	102-104
IV. LIABILITY OF OPERATORS OF TRANSPORT TERMINALS .....	105-113
V. NEW INTERNATIONAL ECONOMIC ORDER: INDUSTRIAL CONTRACTS .....	114-118
VI. CO-ORDINATION OF WORK .....	119-136
A. General co-ordination of activities .....	119-124
B. Revision of the Uniform Customs and Practice for Documentary Credits .....	125-129
C. Current activities of international organizations in the field of barter and barter-like transactions .....	130-132
D. Legal aspects of automatic data processing .....	133-136
VII. TRAINING AND ASSISTANCE .....	137-143
VIII. STATUS OF CONVENTIONS .....	144-147
IX. RELEVANT GENERAL ASSEMBLY RESOLUTIONS, FUTURE WORK AND OTHER BUSINESS .....	148-158
A. Relevant General Assembly resolutions .....	148-150
B. Date and place of the eighteenth session of the Commission .....	151
C. Sessions of the Working Groups .....	152-154
D. Other business .....	155-158

<sup>a</sup>*Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 17 (A/39/17)*  
(hereinafter referred to as "Report").

*Annexes*

	<i>Page</i>
I. UNCITRAL Arbitration Rules .....	22
II. List of documents of the session .....	22

**INTRODUCTION**

1. The present report of the United Nations Commission on International Trade Law covers the Commission's seventeenth session, held in New York, from 25 June to 10 July 1984.
2. Pursuant to General Assembly resolution 2205 (XXI) of 17 December 1966, this report is submitted to the 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 seventeenth session on 25 June 1984. The session was opened on behalf of the Secretary-General by Mr. Carl-August Fleischhauer, Under-Secretary-General, 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:<sup>1</sup> 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,\*\* Senegal,\* Sierra Leone,\* Singapore,\*\* Spain,\*

\*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.

<sup>1</sup>Pursuant 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 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 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.

Kenya,\* Mexico,\*\* Nigeria,\*\* Peru,\* Philippines,\* 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 the Central African Republic, all members of the Commission were represented at the session.

6. The session was also attended by observers from the following States: Argentina, Belgium, Bulgaria, Canada, Chile, Democratic People's Republic of Korea, Dominican Republic, Ecuador, Finland, Greece, Haiti, Holy See, Honduras, Netherlands, Nicaragua, Norway, Oman, People's Democratic Republic of Yemen, Portugal, Republic of Korea, Switzerland, Syrian Arab Republic, Thailand, Venezuela, Zaire and Zambia.

7. The following United Nations organs, specialized agency, intergovernmental organizations and international non-governmental organizations were represented by observers:

**(a) United Nations organs**

United Nations Conference on Trade and Development (UNCTAD)  
United Nations Industrial Development Organization (UNIDO)

**(b) Specialized agency**

International Monetary Fund (IMF)

**(c) Intergovernmental organizations**

Asian-African Legal Consultative Committee (AALCC)  
Commission of the European Communities (CEC)  
Hague Conference on Private International Law  
International Institute for the Unification of Private Law (UNIDROIT)  
Organization of American States (OAS)

**(d) International non-governmental organizations**

European Banking Federation  
International Chamber of Commerce (ICC)  
International Maritime Committee (Comité maritime international, CMI)

\*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.

### C. Election of officers

8. The Commission elected the following officers:<sup>2</sup>

*Chairman:* I. Szasz (Hungary)

*Vice-Chairmen:* J. Barrera Graf (Mexico)

R. K. Dixit (India)

P. K. Mathanjuki (Kenya)

*Rapporteur:* M. Olivencia Ruiz (Spain)

### D. Agenda

9. The agenda of the session, as adopted by the Commission at its 285th meeting on 25 June 1984, was as follows:

1. Opening of the session
2. Election of officers
3. Adoption of the agenda
4. International payments
5. International commercial arbitration
6. New international economic order
7. Operators of transport terminals
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 303rd and 304th meetings, on 10 July 1984, by consensus.

## Chapter II. International payments

### A. Draft Convention on International Bills of Exchange and International Promissory Notes and draft Convention on International Cheques<sup>3</sup>

#### Introduction

11. At its fifteenth session (1982), the Commission decided that the texts of the draft Convention on International Bills of Exchange and International Prom-

<sup>2</sup>The elections took place at the 285th and 293rd meetings, on 25 and 29 June 1984. 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 report of the United Nations Commission on International Trade Law on the work of its first session, *Official Records of the General Assembly, Twenty-third Session, Supplement No. 16* (A/7216), para. 14 (*Yearbook 1968-1970*, part two, I, A, para. 14)).

<sup>3</sup>The Commission considered this subject at its 285th, to 299th meetings on 25 to 29 June and 2, 3 and 5 July 1984. Summary records of these meetings are contained in documents A/CN.9/SR.285-299 (reproduced in this *Yearbook*, part three, I, B).

issory Notes and of the draft Convention on International Cheques, as adopted by its Working Group on International Negotiable Instruments at the close of the eleventh session of the Working Group (August 1981), should be transmitted to Governments and interested international organizations for their comments, together with a commentary. The Commission also requested the Secretary-General to prepare a detailed analytical compilation of those comments.<sup>4</sup>

12. At its sixteenth session, the Commission decided to devote part of its seventeenth session to a substantive discussion of the two draft Conventions. To that end, it requested the secretariat to identify key features and major controversial issues that may be inferred from the comments of Governments and international organizations on the draft Conventions.<sup>5</sup>

13. At its current session, the Commission had before it a report of the Secretary-General containing an analytical compilation of comments by Governments and international organizations (A/CN.9/248—reproduced in this *Yearbook*, part two, I, A, 1), a note by the secretariat identifying major controversial and other issues inferred from those comments (A/CN.9/249—*idem*, part two, I, A, 2), and a note by the secretariat setting forth a summary of the comments of two States which were received after document A/CN.9/249 had been prepared (A/CN.9/249/Add.1—*idem*).

#### Discussion at the session

14. The Commission, at the outset of its discussion, was agreed that it should hold a general discussion on the two draft Conventions and thereafter consider the major and other issues raised by Governments in their observations on the two draft Conventions.

#### 1. General observations on the draft Conventions

15. Opinions were divided on whether further work in the field of negotiable instruments was justified. Representatives who expressed doubts in that regard advanced the following reasons:

(a) The existence of divergent legal systems had not given rise to serious problems in respect of international negotiable instruments used in international payment and financing transactions, as evidenced, for example, by the paucity of relevant case law;

(b) It was feared that the creation of an additional system of negotiable instruments law would lead to serious complications in that different sets of rules would apply to similar types of instruments;

<sup>4</sup>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), para. 50 (*Yearbook 1982*, part one, A).

<sup>5</sup>Report of the United Nations Commission on International Trade Law on the work of its sixteenth session, *Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17* (A/38/17), paras. 80-81 (*Yearbook 1983*, part one, A).

(c) The creation of a special legal régime for international instruments was not the most appropriate way in which to unify the law. In that connection it was stated that unification would truly be served only if it addressed negotiable instruments in both their domestic and international settings. It was also mentioned that the Convention providing a Uniform Law for Bills of Exchange and Promissory Notes, Geneva, 1930 (hereinafter referred to as "the 1930 Geneva Convention") and the Convention providing a Uniform Law for Cheques, Geneva, 1931 (hereinafter referred to as "the 1931 Geneva Convention") were outdated in some respects, and revision of these Conventions would be desirable;

(d) The draft Conventions, though presenting a compromise between competing systems, would not encourage circulation of international negotiable instruments since they did not sufficiently favour the position of the holder of an instrument;

(e) The proposed draft texts were too complex and were often difficult to understand because, for example, provisions frequently contained references to other provisions in the drafts instead of treating an issue in self-contained provisions;

(f) It was deemed unlikely that a convention or conventions would command wide support whether in the form of ratifications by States, or by issuers of negotiable instruments making the convention or conventions applicable.

16. Most of the representatives who expressed some or all of the above reservations distinguished between the draft Convention on International Bills of Exchange and International Promissory Notes and the draft Convention on International Cheques and had less serious objections to the draft Convention on International Bills of Exchange and International Promissory Notes.

17. Representatives supporting further work on the two draft Conventions advanced the following reasons:

(a) The increased use of negotiable instruments in international trade, particularly for purposes of financing export transactions and in lending transactions, justified the unification of law in this field. There is a natural urge on the part of newly independent States to participate in the legislative process in the light of their own interests and views;

(b) The draft Conventions represented an acceptable compromise between common law systems and systems based on the 1930 and 1931 Geneva Conventions, and constituted a good basis for reaching international agreement;

(c) The approach adopted by the two draft Conventions as regards their scope of application was both realistic and acceptable. Although a complete unification of negotiable instruments law covering both international and domestic instruments would no doubt be ideal, such a goal would be difficult to attain, since most countries were not ready to renounce their national legislation. Even a more limited approach, i.e. to draft a law applicable to international instruments having a mandatory character, was unlikely to lead to

many ratifications by States. However, the creation of a new international instrument for optional use could prove to be a valuable first step in the long process of unification and would enable the business community itself to decide whether or not to use such an instrument governed by uniform rules. Furthermore, the establishment of uniform rules for international negotiable instruments would make it possible to accommodate new practices relating to such instruments;

(d) In reply to the objections noted at (a) and (e) of paragraph 15 above, it was noted that, while clarification of certain provisions was desirable and might in fact be needed, any revision aiming at simplification should be undertaken carefully so as not to impair the effectiveness of the texts in dealing with the complex relationships between the parties to an instrument. Furthermore, the paucity of case law relating to international negotiable instruments did not mean that problems did not arise in practice but rather that problems were generally settled between banks.

18. The prevailing view among those representatives who supported further work was that such work should in the first instance focus on the draft Convention on International Bills of Exchange and International Promissory Notes.

19. The question was raised whether countries that had ratified the 1930 and 1931 Geneva Conventions could ratify the proposed draft Conventions without violating their obligations under the former Conventions. It was felt that this question deserved further study at a later stage.

20. In view of the significant degree of support for the unification of negotiable instruments law along the lines agreed to by the Commission at earlier sessions, the Commission agreed that further work on that subject was justified. The Commission decided, however, that such work should concentrate on the draft Convention on International Bills of Exchange and International Promissory Notes, and that the work on the draft Convention on International Cheques should be postponed, and the future work on the draft Convention on International Cheques would be considered after the work on the draft Convention on International Bills of Exchange and International Promissory Notes had been concluded.<sup>6</sup>

## 2. Observations on major controversial issues<sup>7</sup>

### (a) Forged endorsements (articles 14 (1) (b) and 23)

21. There was considerable support in the Commission for the policy underlying article 23, and most represen-

<sup>6</sup>That decision was taken by the Commission after concluding its deliberations on the major controversial issues set forth in paras. 21-38, below. Pursuant to that decision, the Commission did not consider issues specially relating to international cheques.

<sup>7</sup>References to the draft Convention are to the draft Convention on International Bills of Exchange and International Promissory Notes, and references to articles are to those of that draft Convention.

tatives expressed the view that the provisions of article 23 (1) constituted an acceptable compromise between the legal systems of common law and civil law countries.

22. It was noted that under article 23 (1) the liability for damages resulting from a forged endorsement was placed on the forger and on the transferee from the forger. It was suggested that an exception should be made in the case of the endorsee who took the instrument from the forger in good faith. In such a case the endorsee should not be held liable for damages. The rule as proposed in article 23 (1), if retained, would impair the circulation of the proposed international instrument. In that connection other representatives questioned the advisability of introducing into the draft Convention the concept of good faith which was difficult to define and would almost certainly be interpreted in different ways. If an exception were to be made in respect of an endorsee who had no notice of the fact that the endorsement was forged, the exception should be based on the absence of knowledge as defined in article 5.

23. After deliberation, the prevailing view in the Commission was that to make an exception in favour of the transferee in good faith would impair the compromise and therefore the substance of article 23 (1) should be retained.

24. Attention was drawn to the use in article 23 (1) of the word "party". Under the definition of "party" in article 4 (8), the payee was not a party. There was general agreement that the payee and any endorsee whose endorsement was forged should be entitled to recover damages and that therefore article 23 (1) should be modified accordingly.

25. The proposal was made that the amount which may be recovered as compensation under article 23 should be limited to the amount specified in article 66 or 67 of the draft Convention.

26. It was noted that article 23 (2) left to the applicable national law the question whether payment by a party or the drawee of an instrument to the forger would make him liable to pay damages. Since different jurisdictions might deal with this question in different ways, the view was expressed that it would be desirable that the draft Convention should deal with that issue.

27. The possible relationship between articles 23 (2) and 68 was discussed. It was pointed out that although, under article 68, a party may be discharged of liability on the instrument, such party could still be liable off the instrument under article 23 (2) if such liability was left to national law as suggested by the draft Convention. Under one view, that was an acceptable solution since the liability for damages was off the instrument. Under another view, however, the issue was of such importance that it should be settled by the Convention. In that connection, it was suggested that the drawee, the acceptor or the maker who paid, or the endorsee for collection who collected, should be liable

for compensation only if payment was made with knowledge of the forgery.

28. There was a further suggestion that article 23 (2) should be deleted. It was noted, however, that in such a case the drawee who paid the forger would not be liable for damages under article 23 (1) since he was not a person to whom the instrument was transferred by the forger (see article 14). However, the endorsee for collection for whom the instrument was endorsed by the forger was a transferee and could thus be liable under article 23 (1), even if article 23 (2) were deleted. After discussion, the prevailing view in the Commission was that the issue should be reconsidered with a view to revising or deleting article 23 (2).

29. As regards article 23 (3), the question was raised whether it was justified to treat as a forgery the case of endorsement by an agent without authority.

(b) *The concept of holder and protected holder*

30. It was noted that the question as to the circumstances in which the holder of an instrument would be open to claims and defences was one of policy in that a decision had to be made on the degree of protection to be given to the obligor, on the one hand, and the holder, on the other. The draft Convention used the double concept of holder and protected holder and, as a general rule, protected the holder only in cases in which he had the status of a protected holder. Thus, a protected holder could cut off a claim to the instrument as well as most defences to liability. Opinions were divided as to whether the draft Convention achieved a proper balance between the interests of an obligor and of a holder. Under one view, the draft Convention was acceptable in that respect. Under another view, however, the draft Convention was too much in favour of the obligor. The following example was given: C, the payee, obtains by fraud from A, the drawer, a bill drawn on B. C transfers the bill to D and C has a defence against D resulting from the underlying transaction between them. D transfers the bill to E who takes it with knowledge of the defence of C against D but without knowledge of the fraud. Under the draft Convention, E would not be a protected holder and could not cut off a claim by A to the instrument. Several representatives were of the opinion that such a rule was unacceptable and that they would prefer a rule under which E could cut off the claim by A if E had no knowledge of the fraud. Similarly, an obligor should not be entitled to raise a defence against a holder who had no knowledge of such defence.

31. After discussion, the prevailing view in the Commission was that the concept of holder and protected holder should be retained, but that the criteria under which a holder qualified as a protected holder should be reconsidered with a view to shifting the balance more in favour of the creditor. The following views were expressed:

(a) The circumstances in which a holder would take an instrument free of those claims and personal defences of which he had no knowledge should be reconsidered;

(b) The mere fact that a person had taken an incomplete instrument should not prevent him from being protected provided he had completed the instrument in accordance with the authority given;

(c) The requirement that an instrument be regular on its face for the purpose of a person becoming a protected holder was not clear and should be reconsidered;

(d) The question was raised whether the definition of knowledge in the draft Convention was acceptable in view of the fact that a person was deemed to have knowledge if he could not have been unaware of its existence (article 5). The suggestion was made that the definition should be limited to actual knowledge.

32. The suggestion was made that it ought to be considered whether the draft Convention should protect a holder only in those cases in which he took the instrument in good faith, and whether the shelter rule (article 27) should enable a holder to have the rights of a protected holder even though he had taken the instrument in bad faith.

33. It was noted that article 26 (1) (c), concerning real defences that may be set up against a protected holder, referred to the defence based on incapacity and the defence of *non est factum* only. It was not clear whether other real defences available under the applicable national law could be set up against a protected holder and it was suggested that this should be clarified.

34. The general observation was made that the frequent reference to other articles in the draft Convention were not conducive to clarity.

#### *(c) Liability of a transferor by mere delivery*

35. It was noted that article 41 dealt with the liability, off the instrument, of a person who transferred an instrument by mere delivery. Such a person was liable for any damages that a subsequent holder may suffer because of defects in previous signatures, material alterations or other infirmities in the rights of such person to and upon the instrument. It was further noted that such liability did not depend upon whether the transferor by mere delivery knew or did not know of such defects, alterations or infirmities. Finally, such liability ran with the instrument in favour of any subsequent holder who, when he took the instrument, had no knowledge of the defects, alterations or infirmities.

36. Opinions were divided as to whether a rule along the lines of article 41 should be retained in the draft Convention. Under one view, the draft provision should be deleted for the following reasons: the liability regulated in that article was a liability off the instrument, and in view of the principles agreed upon for drafting the proposed Convention such type of liability should not be regulated in the Convention. Furthermore, the liability imposed on a transferor by mere delivery was in many respects greater than the liability incurred by an endorser under the same circumstances.

Also, this liability was too strict in that it was imposed even on a transferor without knowledge of the defect at issue. The opinion was also expressed that the provision was of rather limited practical relevance.

37. Under another view, it was desirable to maintain in the draft Convention a rule along the lines of article 41. It seemed imperative to include in the draft Convention a substantive rule in view of the considerable disparity between existing legal systems with regard to such liability. It was felt, however, that the provision could be modified in the following ways. First, the scope of the provision could be expanded so as to cover also the liability off the instrument of an endorser. Secondly, the scope of the provision could be narrowed by (a) giving a right of action only to the immediate transferee and not to any remote holder, and (b) limiting the instance in which a transferor would incur liability (e.g., only to instances of forgery or unauthorized signature).

38. Despite considerable support for deleting article 41, the Commission decided to retain, for the time being, the draft provision so as to allow further consideration, in particular in the light of the above proposals for modification.

### *3. Observations on additional issues*

39. The Commission considered the additional issues set forth in part III of document A/CN.9/249, and certain other issues.

#### *(a) Article 1 (2) (e): "international elements"*

40. The Commission considered the requirement in article 1 that at least two of the places indicated in article 1 (2) (e) should be situated in different States before a bill of exchange qualified as an international bill of exchange to which the draft Convention applied. Under one view, the scope of application of the draft Convention should be widened by making it applicable to a bill of exchange under the sole condition that the bill contained in the text thereof the words "international bill of exchange (Convention of . . .)"; accordingly, article 1 (2) (e) should be deleted. Under another view, the scope of application should be narrower than that resulting from the present text of article 1 (2) (e), in order to ensure that the draft Convention would only apply to bills that were clearly of an international character. The scope of application might be narrowed, for example, by listing the places noted in article 1 (2) (e) in distinct groupings, and by considering an instrument to be international only if at least one of the places in one group and one of the places in another group were situated in different States. The prevailing view, however, was that the balance struck in article 1 as to the scope of application of the draft Convention was satisfactory and should be maintained.

41. The view was expressed that the draft Convention should only apply if a bill of exchange showed that the place where the bill was drawn and the place of pay-

ment were situated in different States. An indication in the bill of those places was important because they were regarded as essential factors determining the law applicable to issues not covered by the draft Convention. It was decided, however, that an indication of those places should not be a pre-condition to the application of the draft Convention. It was also pointed out that there was a need to revise the criterion contained in article 1 (4) so as to limit the application of the Convention to genuinely international instruments.

42. It was noted that article 1 contained two sets of requirements: the requirements necessary to make an instrument a bill of exchange, and the requirements necessary to give an instrument the international character which would attract the application of the draft Convention. It was suggested that clearer separation of those two sets of requirements was desirable.

(b) *Articles 4 (10) and X: "definition of signature"*

43. Support was expressed for the view that the draft Convention should only permit signatures on bills of exchange to be handwritten, as handwritten signatures gave an assurance of the genuineness of bills of exchange. It was also suggested that in normal commercial practice bills of exchange were not produced in such circumstances (e.g., in sets containing very large numbers of bills) as to make signature by mechanical means essential. The prevailing view, however, was that signatures which were not handwritten should be permitted. Furthermore, bills of exchange were sometimes issued or negotiated in circumstances which made handwritten signatures impractical (e.g., in the case of bank acceptances, or negotiation of bills between banks). In addition, retention of the requirement of handwritten signatures did not assure the genuineness of documents, as such signatures could be forged.

44. It was noted that methods of signature other than those described in article 4 (10) (e.g., by thumb-print) were adopted in some countries, and accordingly it was suggested that the article should permit methods of signature recognized under national laws. It was observed in reply, however, that the present text permitted all methods of signature which were likely to be used on an international bill of exchange. It was also suggested that signatures other than in handwriting (e.g., by symbol) should in some manner identify the signatory.

45. There was general agreement that article X should be retained to accommodate States whose legislation required that a signature on an instrument be handwritten. It was noted, however, that while the idea underlying the article was acceptable, the text itself might need some clarification. In particular, the question was raised as to the effect to be given to a signature which was not handwritten made in a Contracting State which had made a declaration under article X, where the signatory was not a national of that State. The question was also raised as to the effect of a signature which was not handwritten made by a national of that State, if the validity of the signature arose in a State

whose legislation did not require handwritten signatures. It was also suggested that the article might require that the place where a signature was made should be indicated on the bill, as this would assist persons taking the bill to determine the validity of signatures on the bill.

46. It was noted that article 4 (10) included a definition of "forged signature", and it was suggested that, to the extent possible, the articles in the draft Convention dealing with forgery should be grouped together. In addition, doubt was expressed whether it was appropriate to treat a signature made by the unauthorized use of the means indicated in article 4 (10) as a forged signature, in view of the difficulty of ascertaining whether the signature had or had not been authorized.

(c) *Article 4 (11): "definition of money"*

47. It was observed that certain monetary units established by intergovernmental organizations or by intergovernmental agreements (e.g., the Special Drawing Right of the International Monetary Fund, the Transferable Rouble of the International Bank for Economic Co-operation, and the European Currency Unit of the European Economic Community) were currently in use in international commercial transactions. The effect of drawing or making an instrument in such a unit was, however, unclear under most national legislations. The proposed Convention would gain in utility if it were made applicable to instruments drawn or made in and payable in such units, or drawn or made in such units and payable in currency. There was general agreement that the proposed Convention should be applicable in such cases, and that article 4 (11) should be retained and modified to achieve that effect. It was also noted that the retention of article 4 (11) as so modified would result in a need for corresponding modifications to other articles (e.g., article 6). It was also suggested that thought should be given to making the definition of "money" and "currency" include immediately available credit.

(d) *Rate of interest*

48. The Commission considered the requirement that a sum payable must be a definite sum, particularly in connection with the provisions of article 6 which permits the stipulation on an instrument that it is to be paid with interest or by instalments at successive dates.

(i) *Article 6 (a): "rate of interest" and article 7 (4): "rate of interest stipulated"*

49. The prevailing view was that the draft Convention should permit stipulation of interest on international instruments of whatever maturity date.

50. The proposal was made that the draft Convention should allow the issuance of instruments with floating rates. Such instruments were not usually negotiable under current legislations in that they violated the requirement that the sum payable by the instrument be a definite sum. If the draft Convention were to

accommodate current practice in respect of such instruments, it would add to the attractiveness of the proposed Convention. There was considerable support for that proposal. On the other hand, the proposal was opposed on the ground that it would create uncertainty regarding the amount due at maturity and might work to the detriment of the debtor. The view was expressed that instruments with a floating interest rate could clash with the principle that instruments should be certain on their face, and could give rise to legal uncertainty when the rate is left to the full or partial determination of the holder.

(ii) *Article 6(b), (c): "instrument payable by instalments at successive dates"*

51. Opinions were divided on the question whether article 6 (b) and (c) should be retained. Under one view, there was considerable experience in certain countries of the use of such instruments and it would therefore impair the attractiveness of the draft Convention if such use were not accommodated. Under another view, paragraphs (b) and (c) should be deleted. Instruments drawn payable at successive dates would create difficulties as regards presentment for payment, and the commercial need for payment by instalments at successive dates could be met by the drawing or making of separate instruments with successive maturity dates. The Commission agreed that paragraphs (b) and (c) should be retained. After further discussion, the Commission generally agreed that consideration should be given in relation to that issue to making a distinction between bills of exchange and promissory notes taking into account current practices which appeared to draw such a distinction.

52. The Commission did not accept a proposal that the draft Convention should accommodate instruments bearing a clause that if taxes were to be paid the amount of the instrument would be increased proportionally.

(e) *Article 9: "plurality of drawers and payees"*<sup>8</sup>

53. It was stated that a plurality of drawers or payees was not frequently met in practice and that therefore article 9 (1) (b) and (c) and article 9 (2) (b) should be deleted. It was also suggested that the rule of interpretation in article 9 (3) should be reversed. The Commission, after deliberation, agreed to retain article 9 as currently drafted.

(f) *Article 10: "bill drawn by drawer on himself"*

54. The proposal was made that, if a bill was drawn by a drawer on himself, the holder should be entitled to treat it either as a bill of exchange or as a promissory note. It was observed that, while some legislations contained such a provision, other provisions of the draft Convention relating to presentment for payment and to the liability of the drawer would have to be modified. The Commission, after deliberation, did not accept the proposal.

(g) *Article 11: "incomplete instrument"*

55. The Commission did not accept a proposal that article 11 be deleted.

56. The Commission was in agreement with the policy underlying article 11, but also expressed the view that certain aspects regarding completion should be clarified.

(h) *Articles 30, 52, 58 and 63: "legal effects of implied act or omission"*

57. While there was agreement that proceedings such as presentment, protest or notice of dishonour could be waived (articles 52, 58 and 63), there were considerable differences of opinion as to whether such waiver could be made impliedly. Under one view, a waiver should have effect only if it was made expressly on the instrument. Under another view, a waiver should also be given effect if it was made outside the instrument. Under yet another view, the legal effect to be given to a waiver outside an instrument should be left to national law. After deliberation, there was considerable support for the position that the draft Convention should deny legal effect to an implied waiver outside the instrument. It was generally agreed that the words "or by implication" in articles 52, 58 and 63 should be deleted, and that during the reconsideration of these articles the exclusion of implied waivers should be tested on the basis of specific cases.

58. It was also agreed that the words "or impliedly" in article 30 should be deleted, although it was recognized that the implied acceptance of a signature by a person whose signature was forged presented different problems and should accordingly be treated separately.

(i) *Article 34 (2): "exclusion of liability by drawer"*

59. There was general agreement that a drawer of a bill of exchange should be permitted to exclude his liability for non-acceptance of the bill. However, opinions were divided on the question whether the drawer should be permitted to disclaim liability for non-payment of the bill. Under one view, article 34 (2) should not permit such disclaimer, since permitting such disclaimer would make it possible for a bill of exchange to be issued and to circulate without a person being liable on it. Under another view, article 34 (2) was acceptable in that it reflected actual practice and found its counterpart in some legal systems. Under yet another view, the drawer should be permitted to disclaim his liability for non-payment by the drawee or the acceptor in instances where a party other than the drawer was liable on the bill, as in the following cases: (a) where the drawer issued an accepted bill of exchange; (b) where the drawer issued a bill on which a guarantee was given for the drawee (article 43); (c) where the drawer issued a bill on which there was an endorsement; (d) where the drawer issued a bill on which he had disclaimed his liability for non-payment and on which no other party was liable at the time of issuance but where subsequent to the issuance a person became a party, e.g., the bill was endorsed or accepted or guaranteed after its issuance by the drawer.

<sup>8</sup>This issue was set forth in document A/CN.9/249/Add.1 (reproduced in this Yearbook, part two, I, A, 2).

60. The Commission, after deliberation, agreed that the revised draft of article 34 (2) should reflect the policy that the disclaimer by the drawer of his liability for non-payment should have effect only if another party was liable on the bill.

(j) *Article 42: "guarantee"*

61. In respect of the provisions concerning the guarantor the Commission considered the following issues:

(a) *Article 42 (1): "guarantor for the drawee"*. The objection was made that article 42 (1) permitted the guarantee to be given for the drawee although the drawee was not liable on the bill of exchange. Such a rule would seem to indicate that the guarantee for the drawee was in essence a kind of acceptance by a non-drawee. If such were the case the draft Convention should set forth special rules dealing with the liability of the guarantor for the drawee. The Commission, after deliberation, decided to retain a provision permitting a person to guarantee payment by the drawee and noted that the draft Convention in articles 50 (2) (b) and 53 (3) contained special provisions governing the liability of the guarantor for the drawee;

(b) *Article 42 (5): "rule of interpretation"*. It was proposed that the presumption that the guarantee was deemed to have been given for the drawee or the acceptor of a bill, or the maker of a note, in cases where the guarantor had not specified the person for whom he intended to become guarantor, should not be an irrebuttable presumption in cases where the intention of the guarantor was clear from the instrument itself, as where the guarantor's signature appeared beside or under the signature of a party. In such a case the presumption should be that the guarantee was given for such party. The Commission, after deliberation, did not accept this proposal on the ground that the rule as proposed in the draft Convention promoted legal certainty, and that it fell to the guarantor to specify for which person he wished to become guarantor, whether expressly or by implication in reliance on article 42 (5);

(c) *"Guarantee of an incomplete instrument"*. It was noted that the draft Convention permitted the drawee to accept an incomplete instrument (article 38). It was proposed that the draft Convention contain a provision according to which an instrument may be guaranteed before it had been signed by the drawer or the maker or while otherwise incomplete. The Commission, after deliberation, accepted this proposal.

(k) *Articles 48 and 52: "bankruptcy of drawee"*

62. The Commission considered the liability of parties to a bill of exchange in the event of the bankruptcy of the drawee or the acceptor. It was noted that under article 48 presentment for acceptance was dispensed with if the drawee had no longer the power freely to deal with his assets by reason of his insolvency, and that in such a case the holder was entitled to an immediate right of recourse against prior parties (article 50 (1) (b), (2) (a)). However, where the drawee had accepted the bill and had, after such acceptance, but

before maturity, become bankrupt, the draft Convention did not provide for the exercise of a right of recourse by the holder before the date of maturity of the bill (article 54 (1) (b), (2)). It was suggested therefore that the draft Convention should provide for an immediate right of recourse, before maturity, where the holder of an accepted bill learned of the bankruptcy of the acceptor before the date of maturity. After deliberation, the prevailing view in the Commission was against the acceptance of this proposal, which however should not prevent further consideration of this matter.

(l) *Article 58 (2) (d): "dispensation of protest for dishonour"*

63. The view was expressed that the range of cases in which protest was dispensed with under article 58 (2) (d) was excessively wide. For example, paragraph (2) (d) provided that protest was dispensed with in all cases in which presentment for acceptance or for payment was dispensed with. Preference was expressed for a rule according to which protest for dishonour by non-acceptance or non-payment should always be made for the purposes of proving the dishonour, irrespective of whether or not presentment was dispensed with. The Commission, after deliberation, decided to retain article 58 (2) (d) in its present form.

(m) *Article 68 (3): "ius tertii"*

64. The proposal was made that where a third person had asserted a claim to the instrument, article 68 (3) should provide that, if the law of the place of payment permitted payment of the amount of the instrument into court by way of discharge, such arrangement should be effective. The Commission, after deliberation, decided not to accept this proposal.

65. The proposal was made that article 68 (3) should also provide that, if the payer was notified of the claim of a third person to the instrument, such payer could make payment and be validly discharged unless the third person claiming the instrument provided security deemed adequate by the payer. After deliberation, the prevailing view in the Commission was against the acceptance of this proposal, which however should not prevent further consideration of this matter.

(n) *Article 66 (2), (3): "rate of interest recoverable"*

66. The Commission decided to postpone consideration of article 66 (2), (3) of the draft Convention which contains parts placed between brackets.

(o) *Articles 1 (1), (2) and 2: "conflict of laws issues"*<sup>9</sup>

67. There was support for the view that articles 1 and 2 as currently drafted did not resolve conflict of laws problems which might arise in regard to an instrument regulated by the proposed Convention. Under article 1, the Convention applied to an international bill of exchange as defined therein, which at the time of its issue contained in its text the words "international bill

<sup>9</sup>These issues, and the issues discussed below, were not set forth in document A/CN.9/249 (reproduced in this Yearbook, part two, I, A, 2).

of exchange (Convention of . . .)" inserted by the drawer. The idea underlying the Convention was that the instrument would then be regulated by the rules of the Convention, and that the drawer and persons other than the drawer would be bound by the provisions of the Convention by virtue of their signature on the instrument or by taking it up. While a condition for the application of the Convention was that at least two of the places indicated in article 1 (2) (e) be situated in different States, there was no requirement that these States be Contracting States (article 2).

68. It was observed that the following difficulties might arise in the application of the Convention. It was unlikely that the circulation of the instrument would be limited to Contracting States; an action on an instrument might therefore be brought in a forum of a non-contracting State, which would not be bound to apply the Convention. While the drawer had chosen to subject the instrument to the provisions of the Convention, many legal systems did not recognize the principle of party autonomy in the context of negotiable instruments and would thus not permit a person to determine the law governing his rights and liabilities on such instruments. It was also observed that the choice given effect by a conflict of laws system was usually the choice of a national law, and not of a convention independent of a national law. Commercial circles would therefore be reluctant to use such instruments because the legal régime applicable to them would be uncertain. It was suggested that the uncertainty as to the application of the Convention might be reduced if certain further pre-conditions to its application were introduced (for example, that the country of the drawee must be a Contracting State, or that the place of payment must be situated in a Contracting State), as most disputes would probably be litigated in the country of the drawee or at the place of payment.

69. There was opposition to the idea of introducing further pre-conditions to the application of the Convention, on the ground that this would narrow the scope of application of the Convention. While it was recognized that difficulties might arise if a dispute in regard to an instrument to which the Convention applied arose in a non-contracting State, it was observed that this problem would inevitably occur in the process of the adoption of uniform rules until the Convention containing the uniform rules was widely adopted. The proposal was made that the applicability of the rules of the Convention to persons other than the drawer by virtue of their signature on the instrument or by taking it up should be made clearer by a provision in article 1 to that effect. It was agreed that this proposal deserved consideration.

70. It was noted that the Hague Conference on Private International Law (Hague Conference) had on its agenda the revision of the Convention for the Settlement of Certain Conflicts of Laws in connection with Bills of Exchange and Promissory Notes, Geneva, 1930, but that work on this revision had been deferred pending the completion of work by the Commission on the draft Convention. There was wide agreement that

the problems referred to with regard to the applicability of the proposed Convention should be addressed by the Hague Conference in the course of that revision, in co-operation with the Commission.

(p) *Article 1 (2): "written instrument"*

71. It was observed that while article 1 (2) of the draft Convention required an international bill of exchange to be a written instrument, the draft Convention did not contain a definition of writing. It was agreed that the need for such a definition should be considered.

(q) *Article 1 (2) (a): "innovation of the Convention"*

72. There was wide agreement that it should be easily recognizable that the drawer had invoked the application of the Convention by the words "international bill of exchange (Convention of . . .)", and that the Convention was applicable. It was observed that the words invoking the application of the Convention might be in a language unfamiliar to persons to whom the bill was issued or transferred. Suggestions were made in regard to this issue e.g., that the bill should be in a standard form set forth in an annex to the Convention, or should be required to contain the words of invocation in a conspicuous manner or emphasized by a symbol or colour, or should be required to contain the words of invocation in a language widely used in international commerce such as English or French. It was agreed that this issue deserved consideration.

(r) *Article 16: "clauses prohibiting further transfer"*

73. It was noted that article 16 covered two different situations: (a) the drawer or the maker issues an instrument excluding its negotiability, and (b) an endorser makes a restrictive endorsement prohibiting further transfer. Doubts were expressed as to the appropriateness of combining these two situations, as it might lead to confusion and uncertainty about the legal effects of such clauses. It was suggested that the rule on restrictive endorsements should be dealt with separately, for instance in article 20.

74. A concern was expressed that the draft Convention, by introducing a category of instruments of a lower class which were not negotiable, could hamper transactions involving negotiable instruments. On the other hand, there was said to be a practical need in transactions between banks for instruments with restrictions as to further transfer, and the substance of the article should therefore be retained subject to drafting improvements.

75. The Commission concluded that the provision should be reviewed by dealing separately with the two situations and their respective legal effects.

(s) *Article 46: "stipulation by drawer prohibiting presentation for acceptance"*

76. Doubts were expressed as to the appropriateness of the faculty given to the drawer in article 46 to prohibit presentation of a bill for acceptance either generally or before a specified date or event. It was

stated that such faculty was unjustified, and even inconsistent, at least in regard to the cases of mandatory acceptance regulated in article 45 (2). It was observed, for example, that the holder of a time bill may want to know, before maturity, whether the drawee will pay, and that denying this information to the holder would make the bill of less value. Another objection was that to allow the drawer to prohibit presentment "before the occurrence of a specified event" (article 46 (1)) was in conflict with the requirement of "unconditional order" (article 1 (2) (b)).

77. The Commission concluded that the article should be reviewed and revised in order to clarify the legal nature and effects of stipulations prohibiting presentment for acceptance, and that serious consideration should be given to limiting their application to cases of optional acceptance (i.e., article 45 (1)).

(t) *Article 51 (h): "presentment for payment at a clearing-house"*

78. The Commission exchanged views on a proposal to add to article 51 (h) the words "if in conformity with the rules of that clearing-house". It was stated in support of that proposal that, without such amendment, the draft Convention would be potentially disruptive of local clearing arrangements. On the other hand, it was felt that there was no real need for expressing this qualification in view of the non-mandatory wording of paragraph (h), i.e., that an instrument "may be presented" at a clearing-house. It was also observed that the draft Convention need not necessarily yield to existing or future rules imposed by local clearing authorities for domestic instruments.

79. The Commission concluded that this proposal needed further consideration. It was agreed that article 51 (h) was of considerable practical importance and that consideration may be given to making use of the facility of a clearing-house also in other contexts envisaged in the draft Convention (in particular, chapter six, section 1, "Discharge by payment").

(u) *Article 68 (4) (a): "delivery of instrument against payment"*

80. A proposal was made to simplify the text of article 68 (4) (a) by deleting the special rule for the drawee in subparagraph (i). The Commission did not accept this proposal on the ground that the distinction between payment by the drawee and by any other person was justified.

81. It was thought, however, that paragraph (4) should be reviewed as to its appropriateness in cases of instruments payable by instalments on successive dates (article 6 (b)) and in cases of partial payment (article 68 (1)).

(v) *Article 69 (1): "partial payment"*

82. Divergent views were expressed as to the appropriateness of the rule contained in article 69 (1). Under one view, the holder should be obliged to take partial

payment since that would, at least to some extent, be in the interest of prior parties. Under another view, the holder should not be obliged to take partial payment so as to leave it to the holder, who was entitled to full payment, to decide whether or not to accept partial payment in accordance with his interests and assessment of the risks involved. The Commission concluded that this question needed further consideration.

#### 4. Future work

83. The Commission considered the manner in which future work in regard to the draft Convention on International Bills of Exchange and International Promissory Notes might be undertaken. As regards the body within which the work should proceed, the view was expressed that the work might be completed solely within the Commission itself. Such a course might be possible because the Commission already had before it a detailed and well-considered draft Convention prepared by its Working Group. At the present session the Commission had taken certain major policy decisions and other decisions affecting the text, and the Commission could at a future session implement these decisions, perhaps with the assistance of draft texts proposed by the secretariat reflecting these decisions.

84. There was wide agreement, however, that preparatory work had to be undertaken by a working group before the Commission again considered and finalized the draft Convention. Opinions were divided as to the optimum composition of such a working group. There was considerable support for the view that it should consist of all States members of the Commission. Such a composition would facilitate the participation by many States in the process of revision, and lead to a text which was generally acceptable. It was observed that if the revision were made by such a working group, the Commission itself should restrict its review of the revised draft Convention to significant general aspects. A detailed review by the Commission itself would lead to duplication of work.

85. The prevailing view was that the adoption of the draft Convention by the Commission should be preceded by a detailed examination of its provisions by the Commission itself. Adequate representation of State members of the Commission in the process of revision could only be assured at sessions of the Commission, since Governments may be less prepared, because of scarcity of financial resources, to send representatives to sessions of working groups. It followed from this view that the working group should have a limited membership. Its composition need not, however, be identical with that of the present Working Group on International Negotiable Instruments, and some expansion of that Working Group to achieve greater representation of States was desirable. It was also probable that a working group with a limited membership could proceed with the work more expeditiously and efficiently than one with a large membership.

86. There was general agreement that a decision as to the final action to be taken in relation to the draft

Convention (e.g., a recommendation to the General Assembly to convene a Conference of Plenipotentiaries to adopt a convention) should only be taken by the Commission after it had considered the revised draft Convention submitted by the Working Group.

87. It was noted that the Arabic version of the text of the draft Convention was inadequate, in particular as regards the legal terminology used therein, and that it therefore had to be thoroughly revised.

#### *Decision of the Commission*

88. At its 299th and 301st meetings, on 5 and 6 July 1984, the Commission adopted the following decision:

#### *The United Nations Commission on International Trade Law*

##### 1. Decides that:

(a) Further work should be undertaken with a view to improving the draft Convention on International Bills of Exchange and International Promissory Notes;

(b) Such further work is entrusted to the Working Group on International Negotiable Instruments, the composition of which is enlarged to consist of the following members: Australia, Cuba, Czechoslovakia, Egypt, France, India, Japan, Mexico, Nigeria, Sierra Leone, Spain, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland and United States of America;

(c) The mandate of the Working Group is to revise the draft Convention on International Bills of Exchange and International Promissory Notes in the light of decisions and discussion at the present session, and also taking into account those comments of Governments and international organizations in documents A/CN.9/248 and A/CN.9/249/Add.1 which were not discussed at the present session;

(d) Work on the draft Convention on International Cheques is postponed, and that a decision as to further work on this draft Convention will be taken by the Commission after the completion of the work on the draft Convention on International Bills of Exchange and International Promissory Notes;

2. Requests the Working Group to submit a progress report to the eighteenth session of the Commission.

#### **B. Electronic funds transfers<sup>10</sup>**

89. The Commission, at its fifteenth session, had before it a report of the Secretary-General (A/CN.9/221, *Yearbook 1982*, part two, II, C) which considered several legal problems arising out of electronic funds transfers. In the light of those legal problems, the report suggested that, as a first step, the Commission should prepare a guide on the legal problems arising out of

<sup>10</sup>The Commission considered this subject at its 299th meeting, on 5 July 1984.

electronic funds transfers. The guide, it was suggested, should be oriented towards providing guidance for legislators or lawyers preparing the rules governing particular systems for such funds transfers.

90. The Commission accepted this recommendation and requested the secretariat to begin the preparation of a legal guide on electronic funds transfers in co-operation with the UNCITRAL Study Group on International Payments.<sup>11</sup> At the current session the Commission had before it a report of the Secretary-General (A/CN.9/250 and Add.1-4—reproduced in this *Yearbook*, part two, I, B) containing several draft chapters of the legal guide, which had been submitted to the Commission for general observations.

91. The secretariat informed the Commission that an additional chapter on finality of honour of a funds transfer instruction, which was currently in preparation, and a list of legal issues that should be considered in electronic funds transfer systems would be submitted to the Commission at its eighteenth session. The secretariat suggested that the work completed to that point might be submitted to Governments and interested international organizations for their comments, even though further work on other issues might later be undertaken.

92. There was general agreement in the Commission that the draft chapters before the Commission already constituted an excellent beginning to the work in this field and laid the basis for the development of an international common understanding of the legal issues involved. It was noted that it would be premature to attempt to formulate uniform legal rules governing electronic funds transfers before an international common understanding on the subject had been reached. It was noted, however, that the establishment of such a common understanding through the legal guide might make it possible in the future to prepare concrete uniform rules in respect of certain aspects of electronic funds transfers.

93. It was also agreed that the secretariat should be instructed to complete the work on this matter, and that at its eighteenth session the Commission should consider the question of further work on the topic.

#### **Chapter III. International commercial arbitration**

##### **A. Draft model law on international commercial arbitration<sup>12</sup>**

###### *Introduction*

94. The Commission, at its fourteenth session, decided to entrust the Working Group on International Com-

<sup>11</sup>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)*, para. 73 (*Yearbook 1982*, part one, A).

<sup>12</sup>The Commission considered this subject at its 285th meeting, on 25 June 1984.

tract Practices with the task of preparing a draft model law on international commercial arbitration.<sup>13</sup> The Working Group carried out its task at its third, fourth, fifth, sixth and seventh sessions.<sup>14</sup> The Working Group completed its work by adopting the text of a draft model law on international commercial arbitration at the close of its seventh session,<sup>15</sup> after a drafting group had established corresponding language versions in the six languages of the Commission.

95. The Commission had before it the reports of the Working Group on International Contract Practices on the work of its sixth and seventh sessions (A/CN.9/245 and A/CN.9/246—reproduced in this *Yearbook*, part two, A and B).

#### *Discussion at the session*

96. The Commission took note of the reports of the Working Group on International Contract Practices on the work of its sixth and seventh sessions, and expressed its appreciation to the Working Group for having completed its task by preparing a sound and acceptable text for consideration by the Commission.

97. The Commission was in agreement that the draft text of a model law on international commercial arbitration should immediately be sent to all Governments and interested international organizations for their comments. While recognizing the need for extensive consultations on the draft text, the Commission was agreed that any comments should be submitted not later than 30 November 1984. This would allow the secretariat to prepare the required analytical compilation of the comments sufficiently early to enable the compilation to be distributed well in advance of the eighteenth session of the Commission.

98. The Commission agreed that the draft model law on international commercial arbitration should be considered at its eighteenth session with a view to finalizing and adopting the text of a model law on international commercial arbitration. It was felt that for such consideration a period of two to three weeks of that session would be needed, depending on the nature of the comments by Governments and international organizations.

99. The Commission agreed that all matters of substance should be reserved for the eighteenth session, including consideration of proposals made at its present session, to include in a preamble to the model law a

reference to conciliation, and to clarify the territorial criterion for the applicability of the model law.

100. A suggestion was made that the secretariat should prepare a commentary on the draft model law which would assist Governments in preparing their comments on the draft text and later in their considerations as to any legislative action based on the model law. While recognizing the usefulness of a commentary, the Commission agreed that such a commentary could not be prepared in time to be of assistance to Governments in preparing their comments, but was of the view that such a commentary should be submitted to the eighteenth session of the Commission.

#### *Decision of the Commission*

101. At its 285th and 304th meetings, on 25 June and 10 July 1984, the Commission adopted the following decision:

##### *The United Nations Commission on International Trade Law*

1. Expresses its appreciation to its Working Group on International Contract Practices for having completed its task by adopting the draft text of a model law on international commercial arbitration;
2. Requests the Secretary-General to transmit the draft text of a model law on international commercial arbitration to all Governments and interested international organizations for their comments, which should be submitted not later than 30 November 1984;
3. Requests the secretariat to prepare an analytical compilation of the comments received, and to distribute this compilation well in advance of the eighteenth session of the Commission;
4. Requests the secretariat to submit to the eighteenth session of the Commission a commentary on the draft text of a model law on international commercial arbitration;
5. Decides to consider, at its eighteenth session, the draft text of a model law on international commercial arbitration in the light of comments received from Governments and interested international organizations, with a view to finalizing and adopting the text of a model law on international commercial arbitration.

#### **B. UNCITRAL Arbitration Rules<sup>16</sup>**

102. The Commission noted that the UNCITRAL Arbitration Rules, before their adoption at the ninth session of the Commission (1976), had been reviewed by a drafting group only in those languages which then were the official languages of the Commission (i.e., English, French, Russian and Spanish). Although sub-

<sup>13</sup>Report 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, para. 70).

<sup>14</sup>Reports on the work of these sessions are contained in documents A/CN.9/216 (*Yearbook 1982*, part two, III, A), A/CN.9/232 (*Yearbook 1983*, part two, III, A), A/CN.9/233 (*idem*, C), A/CN.9/245 (reproduced in this *Yearbook*, part two, II, A, 1) and A/CN.9/246 (*idem*, B, 1).

<sup>15</sup>The draft text of a model law on international commercial arbitration is contained in the annex to document A/CN.9/246 (reproduced in this *Yearbook*, part two, II, B, 2).

<sup>16</sup>Commission considered this subject at its 285th, 300th and 301st meetings, on 25 June and 5 and 6 July 1984.

sequently translation into the Arabic and Chinese languages, which had become official languages of the General Assembly, were prepared, these translations were found to be in need of revision, in particular as regards the legal terminology used therein.

103. The Commission, at its current session, had before it revised versions of the Arabic and Chinese texts, which had been prepared by the secretariat with the assistance of experts. As regards the Arabic text, it was noted that some minor modifications were desirable. The Commission accordingly entrusted to an *ad hoc* working party composed of States using the Arabic language the task of making these modifications.

#### *Decision of the Commission*

104. The Commission, at its 301st meeting, on 6 July 1984, adopted the Arabic text (as modified by the *ad hoc* working party) and the Chinese text of the UNCITRAL Arbitration Rules. These texts as adopted are set forth in annex I to the Arabic and Chinese versions, respectively, of the present report.

### **Chapter IV. Liability of operators of transport terminals<sup>17</sup>**

#### *Introduction*

105. The Commission, at its sixteenth session (1983), decided to include the topic of liability of operators of transport terminals in its programme of work, to request the International Institute for the Unification of Private Law (UNIDROIT) to transmit its preliminary draft Convention on that subject to the Commission for its consideration, and to assign work on the preparation of uniform rules on that subject to a working group. The Commission deferred to its current session the decision on the composition of the working group.<sup>18</sup>

106. The Commission had before it a report of the Secretary-General on the liability of operators of transport terminals (A/CN.9/252—reproduced in this *Yearbook*, part two, IV, A) which had been requested by the Commission at its sixteenth session.<sup>19</sup> The report discussed some of the major issues which arose from the UNIDROIT preliminary draft Convention and which might merit consideration in the formulation by the Commission of uniform rules on this topic. Annexed to the report was the text of the UNIDROIT preliminary draft Convention (*idem*, B).

<sup>17</sup>The Commission considered this subject at its 300th meeting, on 5 July 1984.

<sup>18</sup>Report of the United Nations Commission on International Trade Law on the work of its sixteenth session, *Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17* (A/38/17), para. 115 (Yearbook 1983, part one, A).

<sup>19</sup>*Ibid.*

#### *Discussion at the session*

107. It was noted that work by the Commission on this topic would be a logical sequence to its work in the field of carriage of goods by sea, which had led to the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg) (the Hamburg Rules).

108. It was generally agreed that the task of formulating uniform legal rules on the liability of operators of transport terminals should be assigned to the Working Group on International Contract Practices, which was composed of all members of the Commission. A suggestion was made that the Working Group should begin its work by considering approaches to be adopted with respect to issues arising in connection with the liability of operators of transport terminals, and then proceed to the drafting of the uniform rules. It was generally agreed, however, that the method of work of the Working Group should be determined by the Working Group itself.

109. Views were expressed concerning certain issues of substance arising from the UNIDROIT preliminary draft Convention. Such views included the following: that the scope of the uniform rules should be limited to the safe-keeping of goods related to international transport and that the rules should define the degree and nature of that relationship; that the uniform rules should not cover the activities of freight forwarders who acted as principals for shippers; that consideration should be given to various types of operations performed by terminal operators in connection with different types of transport; that terminal operators should have a lien over goods taken in charge by them to protect their ability to recover their fees, but that a provision should be included to balance against that protection the rights of parties entitled to receive the goods; that a provision whereby the uniform rules could be applied by a State only against terminal operators agreeing to be bound by the rules would be appropriate for a model law, but not for a convention; that the issuance of a document by a terminal operator should not be compulsory; and that the negotiability of such a document, if issued, should be left to the agreement of the parties.

110. Views were also expressed that the Working Group should consider certain issues not dealt with in the UNIDROIT preliminary draft Convention. Such views included the following: that the Working Group should consider the question of jurisdiction over claims against operators of transport terminals, and the question of whether a carrier should be obligated to notify a terminal operator of loss of or damage to goods handed over to the carrier by the terminal operator; that the Working Group should consider whether the uniform rules should provide for suspension of the limitation period for claims against terminal operators, and whether the uniform rules should deal with obligations of customers toward terminal operators (e.g., to pay their fees, and to inform them as to dangerous goods), as well as the right of terminal operators not to accept dangerous goods.

111. The observer of the United Nations Conference on Trade and Development (UNCTAD) informed the Commission that the Conference, by its resolution 144 (VI), paragraph 9, had requested its Secretary-General to prepare for its Committee on Shipping a study on the rights and duties of container terminal operators and users, and that a copy of that study would be made available to the Working Group of the Commission to which would be assigned the task of preparing uniform rules on the liability of operators of transport terminals. He also stated that the UNCTAD secretariat looked forward to participating actively in the work of the Working Group.

112. The Commission expressed its appreciation of the statement by the representative of UNCTAD. In view of the experience and expertise of UNCTAD in maritime and multimodal transport, port operations and various aspects of containerization, and the relevance of this experience and expertise to issues concerning the proposed uniform rules, the Commission welcomed the prospect of further co-operation between the Commission and UNCTAD in the development of the uniform rules.

#### *Decision of the Commission*

113. The Commission decided to assign to its Working Group on International Contract Practices the task of formulating uniform legal rules on the liability of operators of transport terminals. It further decided that the mandate of the Working Group should be to base its work on document A/CN.9/252 and on the UNIDROIT preliminary draft Convention and the Explanatory Report thereto prepared by UNIDROIT, and that the Working Group should also consider issues not dealt with in the UNIDROIT preliminary draft Convention, as well as any other issues which it considered to be relevant.

### **Chapter V. New international economic order: industrial contracts<sup>20</sup>**

#### *Introduction*

114. The Commission had before it the report of its Working Group on the New International Economic Order on the work of its fifth session (A/CN.9/247—reproduced in this *Yearbook*, part two, III, A). The report set forth the deliberations of the Working Group on the basis of the report of the Secretary-General entitled "Draft legal guide on drawing up contracts for industrial works" (A/CN.9/WG.V/WP.11 and Add.1-9—*idem*, B). The Working Group also had before it a sample draft chapter on "Termination" (A/CN.9/WG.V/WP.9/Add.5; *Yearbook 1983*, part two, IV, B) which had not been considered at the fourth session of the Working Group. The report noted that the Working Group had considered the format of the legal guide (A/CN.9/WG.V/WP.11/Add.9), and draft chapters on "Variation clauses" (A/CN.9/WG.V/WP.11/Add.6).

"Assignment" (A/CN.9/WG.V/WP.11/Add.7), "Suspension of construction" (A/CN.9/WG.V/WP.11/Add.8), "Termination" (A/CN.9/WG.V/WP.9/Add.5), "Inspection and tests" (A/CN.9/WG.V/WP.11/Add.1) and "Failure to perform" (A/CN.9/WG.V/WP.11/Add.1-3). The Working Group had also held an exchange of views on the draft chapter on "Damages" (A/CN.9/WG.V/WP.11/Add.4), and postponed for the next session consideration of the draft chapter on "Liquidated damages and penalty clauses" (A/CN.9/WG.V/WP.11/Add.5).

115. The Working Group was in agreement that, in its final form, the legal guide should be so arranged as to enable a reader readily to identify the parts of the legal guide dealing with a particular issue. It was also agreed that the utility of the legal guide would be enhanced if each chapter were preceded by a summary, and also contained illustrative provisions where necessary as an aid to drafting contract clauses. The Working Group proposed that, in order to expedite the work, two sessions of the Working Group should be held each year, if the course of the work so permitted.

#### *Discussion at the session*

116. The Commission expressed its satisfaction with the work thus far accomplished in regard to the preparation of the legal guide, and expressed its appreciation to the Working Group and its Chairman for their conduct of the work. There was general agreement that, in order to expedite the work, two sessions of the Working Group should be held prior to the eighteenth session of the Commission.

117. The view was expressed that the legal guide should examine the different possible approaches to resolving particular difficulties, and should in its recommended solutions seek to achieve a balance between the interests of the two parties to an international industrial contract. It was also noted that, in order to be of practical help, the legal guide should provide clear solutions, supported where necessary with illustrative provisions which could be used by the parties as a basis for drafting. It was also observed that the legal guide should be of a size and format which would enable its convenient use.

118. There was support for the view that the future work programme of the Working Group needed consideration. It was suggested that the legal aspects of joint ventures or consortia, and contracts for industrial co-operation, might be considered as possible items for such work programme.

### **Chapter VI. Co-ordination of work**

#### *A. General co-ordination of activities<sup>21</sup>*

119. The Commission had before it a report of the Secretary-General which set forth the main activities of

<sup>20</sup>The Commission considered this subject at its 301st meeting, on 6 July 1984.

<sup>21</sup>The Commission considered this subject at its 302nd meeting, on 6 July 1984.

the secretariat for the purpose of co-ordination of work in the field of international trade law since the sixteenth session (A/CN.9/255—reproduced in this *Yearbook*, part two, V). 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.

120. The observer from the Asian-African Legal Consultative Committee referred to the continuous relationship which the Committee had enjoyed with the Commission since 1970. The Committee has recommended that Governments in the Asian-African region should consider ratification or adherence to the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg) (the Hamburg Rules) and the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980). It was noted that the Committee had recommended the use of the UNCITRAL Arbitration Rules and that the regional arbitration centres at Kuala Lumpur and Cairo used the UNCITRAL Arbitration Rules with certain modifications to govern arbitrations conducted by those arbitration centres. The director of the Centre on International Arbitration in Cairo made a statement on the functions of the Centre and on its rules.

121. The observer from UNCTAD noted that, in addition to the co-operation in the field of terminal operations between the secretariats of UNCTAD and the Commission, there was also a continuing contact in the field of legal implications of automatic data processing. He also noted that the UNCTAD secretariat had followed with interest the work of the Commission in the field of industrial contracts.

122. The observer from UNIDROIT reported that its Governing Council had decided to create a Committee of Government Experts to consider the preliminary draft Rules on International Factoring, and a second Committee of Government Experts to consider the preliminary draft Rules on International Financial Leasing. The Governing Council had decided to invite all States members of the Commission, including those which are not members of UNIDROIT, to participate in the work of these Committees of Government Experts. It was also noted that UNIDROIT appreciated the decision of the Commission to undertake work on the liability of operators of transport terminals on the basis of the preliminary draft Convention prepared by UNIDROIT. UNIDROIT would desire to remain associated with the Commission's work on this topic.

123. The observer from the Hague Conference on Private International Law (Hague Conference) reported that the Diplomatic Conference to consider the draft Convention on the Law Applicable to Contracts for the International Sale of Goods would be held from 14 to 30 October 1985. Invitations to the Diplomatic Conference had been sent by the Government of the Netherlands to all States, including States which are not members of the Hague Conference. He also reported that the fifteenth session of the Hague Conference in

October 1984 would consider whether the subject of the law applicable to arbitration clauses should be placed on the agenda of the sixteenth session of the Hague Conference in 1988. In addition, in the light of discussions which had taken place in the Commission's Working Group on International Contract Practices, the Hague Conference will consider whether the Convention on the Taking of Evidence Abroad in Civil or Commercial Matters, the Hague, 1970, could be extended in order to permit arbitrators to forward directly to courts or authorities in a place other than that where the arbitration proceedings are taking place requests for the taking of evidence.

124. The Commission expressed its appreciation for the co-operation shown by the other organizations active in the field of international trade law. During the discussion it was suggested that the Commission urge States to accept the invitations extended by UNIDROIT and the Hague Conference.

#### **B. Revision of the Uniform Customs and Practice for Documentary Credits<sup>22</sup>**

125. The Commission had before it a report of the Secretary-General concerning the 1983 revision of the Uniform Customs and Practice for Documentary Credits (UCP) by the International Chamber of Commerce (ICC) (A/CN.9/251; reproduced in this *Yearbook*, part two, V, B). The report pointed out that the subject of documentary credits had been on the Commission's priority list of topics since 1968 and that the Commission at its second session in 1969 had recommended to Governments the 1962 version of UCP, while at its eighth session in 1975 it had recommended the use of the 1974 version of UCP.

126. The report further pointed out that developments in documentary credit practice since 1974, and especially those brought about by changes in transport technology and documentation and the increased use of stand-by letters of credit, had led to a revision of the 1974 version of UCP by ICC. In order to permit interested circles in countries not represented in ICC to make observations on the operation of UCP so that these could be taken into account in the revision, the Secretary-General, in accordance with past practice on this subject, had addressed to all Governments the same questionnaire as was sent by ICC to its National Committees and had transmitted the replies received to ICC for its consideration. After adoption of the 1983 version of UCP by the Council of ICC on 21 June 1983 with an effective date of 1 October 1984, ICC had forwarded the text to the Commission with a request that the Commission consider recommending its use in international trade, as had been done in respect of the 1962 and 1974 versions.

#### *Discussion at the session*

127. The observer of ICC expressed the appreciation of ICC for the support given by the Commission in the

<sup>22</sup>The Commission considered this subject at its 301st meeting, on 6 July 1984.

past and for the aid in preparing the current revision. After explaining a number of the modifications to UCP contained in the 1983 revision, he indicated the desire of ICC that the Commission should endorse the use of the 1983 version, as it had endorsed the use of the previous versions.

128. It was noted by the Commission that UCP had been one of the most successful efforts in the unification of international trade law. Several delegations reported that the banks in their countries had already decided to apply the 1983 version of UCP when it becomes effective on 1 October 1984. After expressing its appreciation of the continuing co-operation which the Commission had enjoyed with ICC, the Commission was agreed that ICC should be congratulated on its work in adjusting the rules governing documentary credits to the changes taking place in international trade.

#### *Decision of the Commission*

129. At its 301st meeting, on 6 July 1984, the Commission adopted the following decision:

*The United Nations Commission on International Trade Law,*

*Expressing its appreciation to the International Chamber of Commerce for having transmitted to it the revised text of "Uniform Customs and Practice for Documentary Credits", which was approved by the Commission on Banking Technique and Practice of the International Chamber of Commerce and adopted by the Council of the International Chamber of Commerce on 21 June 1983,*

*Congratulating the International Chamber of Commerce on having made a further contribution to the facilitation of international trade by bringing up to date its rules on documentary credit practice to allow for developments in transport technology and changes in commercial practices,*

*Having regard to the fact that, in revising the 1974 text of "Uniform Customs and Practice for Documentary Credits", the International Chamber of Commerce has taken into account the observations made by Governments and banking and trade institutions of countries not represented within it and transmitted to it through the Commission,*

*Noting that "Uniform Customs and Practice for Documentary Credits" constitutes a valuable contribution to the facilitation of international trade,*

*Commends the use of the 1983 revision, as from 1 October 1984, in transactions involving the establishment of a documentary credit.*

#### *C. Current activities of international organizations in the field of barter and barter-like transactions<sup>23</sup>*

130. The Commission, at its twelfth session, requested the secretariat to include in the studies then being

<sup>23</sup>The Commission considered this subject at its 302nd meeting, on 6 July 1984.

conducted in respect of contract practices consideration of clauses of particular importance in barter-like transactions.<sup>24</sup> The Commission also requested the secretariat to approach other organizations within the United Nations engaged in studies on such transactions, and to report to it on the work being undertaken by those organizations.

131. The Commission had before it, at its seventeenth session, a report of the Secretary-General which reported on the activities of other organizations within and outside the United Nations relative to barter-like transactions (A/CN.9/253—reproduced in this *Yearbook*, part two, V, C). The report noted that the Secretariat would continue to monitor developments in this field.

132. There was general agreement that the report was a useful summary of current activities in this field. A number of delegations indicated that they attached great importance to this subject and that further consideration of it would be useful. It was agreed that, in the light of a report to be submitted by the secretariat at a future session on the developments in this field, the Commission may consider whether concrete steps in the field should be undertaken by it.

#### *D. Legal aspects of automatic data processing<sup>25</sup>*

##### *Introduction*

133. The Commission, at its sixteenth session, had before it a note by the secretariat which conveyed in an annex a report on the legal aspects of automatic data processing of the Working Party on Facilitation of International Trade Procedures which is jointly sponsored by the Economic Commission for Europe and the United Nations Conference on Trade and Development (A/CN.9/238, *Yearbook 1983*, part two, V, D). 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 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. The Commission took note of the intention of the secretariat to submit to the seventeenth session a report on this subject.<sup>26</sup>

134. The Commission had before it at the present session a report of the Secretary-General which

<sup>24</sup>Report 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. 23 (*Yearbook 1979*, part one, II, A).

<sup>25</sup>The Commission considered this subject at its 300th meeting on 5 July 1984.

<sup>26</sup>Report of the United Nations Commission on International Trade Law on the work of its sixteenth session, *Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17 (A/38/17)*, para. 118 (*Yearbook 1983*, part one, A).

described several legal problems arising out of the use of automatic data processing in international trade (A/CN.9/254—reproduced in this *Yearbook*, part two, V, D). The report suggested that in the light of these problems, the Commission might wish to place the subject of the legal implications of automatic data processing to the flow of international trade on its programme of work as a priority item.

135. It was noted that automatic data processing is being increasingly used in connection with international trade and that the Commission was likely to encounter legal problems arising out of the use of automatic data processing in many aspects of its future activities. It was suggested that it would be important for the Commission to take leadership in that field.

#### *Decision of the Commission*

136. It was decided to place the subject on the programme of work as a priority item. A decision would be made at the eighteenth session of the Commission whether to refer the subject to a Working Group for the purpose of identifying areas where solutions or the establishment of international common understanding would be desirable.

### **Chapter VII. Training and assistance<sup>27</sup>**

#### *Introduction*

137. At its sixteenth session,<sup>28</sup> the Commission decided that it would be desirable to continue the sponsorship of symposia and seminars on international trade law in collaboration with other organizations. It also affirmed the importance of regional symposia and seminars, both for the purpose of promoting the work of the Commission, and for the purpose of making participants, particularly from developing countries, aware of current legal problems of international trade. The Commission approved the approach taken by the secretariat in organizing symposia and seminars.

138. By its resolution 38/134 of 19 December 1983 on the report of the Commission on the work of its sixteenth session (*Yearbook 1983*, part one, D), the General Assembly reaffirmed the importance, in particular for developing countries, of the work of the Commission concerned with training and assistance in the field of international trade law. It also reaffirmed the desirability for the Commission to sponsor symposia and seminars, in particular those organized on a regional basis, to promote training and assistance in the field of international trade law. The General Assembly also expressed its appreciation to Governments and insti-

tutions for arranging symposia and seminars, and invited Governments, relevant United Nations organs, organizations, institutions and individuals to assist the secretariat in financing and organizing symposia and seminars.

139. The Commission had before it a report of the Secretary-General on training and assistance (A/CN.9/256—reproduced in this *Yearbook*, part two, VII), which described the measures 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 the holding of several regional seminars in developing countries. A workshop on the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980), had been held at the biennial conference of the Law Association for Asia and the Western Pacific (Manila, Philippines, 9-13 September 1983). The secretariat collaborated with the Chamber of Industry of the Ivory Coast, the Economic Community of West Africa and the International Chamber of Commerce in the holding of an international conference (Abidjan, 21-23 November 1983) on the techniques of international commerce. A regional symposium on arbitration had been organized (New Delhi, 12-14 March 1984) by the Asian-African Legal Consultative Committee (AALCC) and the secretariat, in co-operation with the Indian Council of Arbitration.

140. The report noted that on several occasions other than those noted above, the secretariat had participated in symposia and seminars which dealt with the work of the Commission, and that the secretariat intended to keep in touch with Governments and organizations with a view to collaborating with them in organizing symposia and seminars.

#### *Discussion at the session*

141. The Commission expressed its appreciation of the efforts undertaken in this field by the secretariat which were reflected in the report (A/CN.9/256), and approved the general approach taken by the secretariat in this area. There was wide agreement that the sponsorship of regional symposia and seminars on international trade law in general and the activities of the Commission in particular should be continued and strengthened. It was stressed that such symposia and seminars were of very great benefit to lawyers and businessmen in developing countries. In this connection the view was expressed that special efforts should be made to organize such symposia and seminars in Africa in order to disseminate in Africa information on the activities of the Commission.

142. A statement was made by the representative of Australia that an Asian-Pacific Regional Trade Law Seminar would be conducted in Canberra, Australia, from 22 to 27 November 1984, by the Attorney-General's Department of Australia, in association with the UNCITRAL secretariat and the AALCC. The International Institute for the Unification of Private

<sup>27</sup>The Commission considered this subject at its 302nd meeting, on 6 July 1984.

<sup>28</sup>Report of the United Nations Commission on International Trade Law on the work of its sixteenth session, *Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17* (A/38/17), para. 130 (*Yearbook 1983*, part one, A).

Law and the Hague Conference on Private International Law would also participate. The seminar would have as its theme the unification and harmonization of international trade law and practices with particular reference to the work and role of the Commission. The Seminar would be specially designed to contribute to the Commission's programme in training and assistance, and the Government of Australia would provide fellowships for participants from the region.

143. The Commission expressed its deep appreciation for the efforts of the Government of Australia in support of the Commission's training and assistance programme in the Asian-Pacific region, and also expressed its appreciation to all Governments and international organizations which had assisted the secretariat in the organization of regional symposia and seminars.

### **Chapter VIII. Status of conventions<sup>29</sup>**

144. 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) (hereinafter referred to as "the Limitation Convention"); the Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980); the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg) (hereinafter referred to as "the Hamburg Rules"); and the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980) (hereinafter referred to as "the Sales Convention"). The Commission had before it a note by the Secretary-General on the status of these Conventions, which set forth the status of signatures, ratifications and accessions to these Conventions (A/CN.9/257—reproduced in this *Yearbook*, part two, VI).

145. Several States indicated that the question of adhering to the Sales Convention was under active consideration within their Governments and that the prospects of adherence were favourable.

146. The Secretary of the Commission noted the recommendation of the Commission on International Contract Practices of the International Chamber of Commerce (ICC) that the national committees of ICC should approach their respective Governments to encourage their adherence to the Sales Convention. He also noted that a conference of the Law Association for Asia and the Western Pacific held in September 1983 had adopted a resolution urging Governments in the Asian-Pacific region to disseminate information about the Sales Convention with a view to ensuring adherence to the Convention within the shortest possible time. The Secretary of the Commission expressed the hope that the increasing interest in the Sales Convention would generate increased interest in the Limitation Convention.

<sup>29</sup>The Commission considered this subject at its 302nd meeting, on 6 July 1984.

147. With regard to the Hamburg Rules, the Secretary of the Commission expressed the hope that the work of the Commission on the topic of liability of operators of transport terminals would generate increased interest in the Hamburg Rules. The Commission noted with appreciation the statement of the observer of the United Nations Conference on Trade and Development that UNCTAD was prepared to co-operate with the Commission to ensure early ratification and implementation of the Hamburg Rules, for example by organizing regional seminars.

### **Chapter IX. Relevant General Assembly resolutions, future work and other business<sup>30</sup>**

#### **A. Relevant General Assembly resolutions**

##### *1. General Assembly resolution on the work of the Commission*

148. The Commission took note with appreciation of General Assembly resolution 38/134 of 19 December 1983, on the report of the Commission on the work of its sixteenth session (*Yearbook 1983*, part one, D).

##### *2. General Assembly resolution on Uniform Rules on Contract Clauses for an Agreed Sum Due upon Failure of Performance*

149. The Commission took note with appreciation of General Assembly resolution 38/135 of 19 December 1983, on Uniform Rules on Contract Clauses for an Agreed Sum Due upon Failure of Performance (*Yearbook 1983*, part one, D).

##### *3. General Assembly resolution on international economic law*

150. The Commission took note of General Assembly resolution 38/128 of 19 December 1983, on the progressive development of the principles and norms of international law relating to the new international economic order (*Yearbook 1983*, part three, III). 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.

#### **B. Date and place of the eighteenth session of the Commission**

151. It was decided that the Commission would hold its eighteenth session from 3 to 21 June 1985 at Vienna.

#### **C. Sessions of the Working Groups**

152. It was decided that the Working Group on International Contract Practices would hold its eighth session from 3 to 14 December 1984 at Vienna.

<sup>30</sup>The Commission considered this subject at its 301st and 302nd meetings, on 6 July 1984.

153. It was decided that the Working Group on International Negotiable Instruments would hold its thirteenth session from 7 to 18 January 1985 in New York.

154. It was decided that the Working Group on the New International Economic Order would hold its sixth session from 10 to 21 September 1984 at Vienna and its seventh session from 8 to 19 April 1985 in New York.

#### D. Other business

155. A view was expressed that legal texts and other documents emanating from the work of the Commission should receive wider dissemination. In addition, a suggestion was made that means should be explored to disseminate court and arbitral decisions concerning legal texts elaborated by the Commission.

156. The Secretary of the Commission noted that the large bibliography in the *Yearbook* of publications relating to the work of the Commission indicated widespread interest in this work. He also stated that it was expected that preparation of the book on UNCITRAL, which has already been authorized by the Commission, was expected to be completed in 1985. This book would include all legal texts which had been elaborated by the Commission. The Secretary of the Commission also noted that the publication of the *Yearbook* and the book on UNCITRAL would be accommodated within the regular budget.

#### B. United Nations Conference on Trade and Development (UNCTAD): extract from the report of the Trade and Development Board on its twenty-ninth session (TD/B/1026)<sup>a</sup>

*"Progressive development of the law of international trade: seventeenth annual report of the United Nations Commission on International Trade Law (agenda item 8 (b))*

"690. For the consideration of this item, the Board had before it the report of the United Nations Commission on International Trade Law on the

<sup>a</sup>*Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 15 (A/39/15).*

157. The Commission requested that the secretariat attempt to expedite the publication of the *Yearbook*.

158. The view was expressed that in view of the financial difficulties encountered by some States in participating in sessions of the Commission and of its Working Groups the secretariat should explore the most efficient means for the scheduling of sessions and for the utilization of time at the sessions.

#### ANNEX I

##### UNCITRAL Arbitration Rules

Annex not reproduced here. The text of the UNCITRAL Arbitration Rules can be found:

In *Yearbook 1976*, part one, II, A, para. 57;

In the booklet *UNCITRAL Arbitration Rules* (United Nations publication, Sales No. E.77.V.6);

In the Report of the United Nations Commission on International Trade Law on the work of its ninth session, *Official Records of the General Assembly, Thirty-first Session, Supplement No. 17 (A/31/17)* pp. 35-50.

#### ANNEX II

##### List of documents of the session

Annex not reproduced here; see check-list of UNCITRAL documents at the end of this volume.

work of its seventeenth session,<sup>99</sup> distributed under cover of TD/B/1011.

##### "Action by the Board

"691. At its 647th meeting, on 14 September 1984, the Board took note of the report of the United Nations Commission on International Trade Law on its seventeenth session."

<sup>99</sup>*Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 17 (A/39/17).*

#### C. General Assembly: report of the Sixth Committee (A/39/698)<sup>a</sup>

1. On the recommendation of the General Committee, the General Assembly decided at its 3rd plenary meeting, on 21 September 1984, to include in the agenda of its thirty-ninth session the item entitled "Report of the United Nations Commission on International Trade Law on the work of its seventeenth session" and to allocate it to the Sixth Committee.

2. In connection with this item, the Sixth Committee had before it the report in question, which was introduced by the Chairman of the United Nations Commission on International Trade Law at the 3rd meeting of the Committee, on 25 September.<sup>1</sup> In

<sup>1</sup>*Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 17 (A/39/17—reproduced in this Yearbook, part one, A).* The report was submitted pursuant to a decision by the Sixth Committee at its 1096th meeting, on 13 December 1984 (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*).

<sup>a</sup>*Official Records of the General Assembly, Thirty-ninth Session, Annexes, agenda item 127.*

addition to that report, the Committee had before it a note by the Secretary-General (A/C.6/39/L.3) relating to the consideration of the report by the Trade and Development Board of the United Nations Conference on Trade and Development.

3. The Sixth Committee considered the item at its 3rd to 7th meetings, from 25 September to 1 October, and at its 46th meeting, on 14 November 1984. The summary records of those meetings (A/C.6/39/Sr.3-7 and 46) contain the view of representatives who spoke during the consideration of the item.

4. The Committee also had before it draft resolution A/C.6/39/L.5, which was introduced and orally corrected by the representative of Austria at the 46th meeting, on 14 November, sponsored by Argentina, Australia, Austria, Belgium, Brazil, Canada, Chile, Cyprus, Egypt, Finland, France, Germany, Federal

Republic of, Greece, Hungary, Italy, Jamaica, Japan, Kenya, Morocco, the Netherlands, Nigeria, Pakistan, the Philippines, Senegal, Singapore, Spain, Sweden, Thailand, Turkey and Yugoslavia.

5. At its 46th meeting, the Committee adopted draft resolution A/C.6/39/L.5, as orally corrected, by consensus (see para. 6 below).

#### RECOMMENDATION OF THE SIXTH COMMITTEE

6. The Sixth Committee recommends to the General Assembly the adoption of the following draft resolution:

[Text not reproduced in this section. The draft resolution was adopted, with editorial changes, as General Assembly resolution 39/82. See section D, below.]

#### D. General Assembly resolution 39/82 of 29 January 1985

##### 39/82. REPORT OF THE UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW

###### *The General Assembly.*

*Having considered* the report of the United Nations Commission on International Trade Law on the work of its seventeenth session,<sup>1</sup>

*Recalling* that the object of the Commission is the promotion of the progressive harmonization and unification of international trade law,

*Recalling*, in this regard, its resolution 2205 (XXI) of 17 December 1966, as well as all its other resolutions relating to the work of the Commission,

*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 interest 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 value of participation by States at all levels of economic development, including developing countries, in the process of harmonizing and unifying rules of international trade law,

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

2. *Commends* the Commission for the progress made in its work, in particular towards the preparation of a draft convention on international bills of exchange and international promissory notes, a model law on international commercial arbitration, a legal guide on drawing up international contracts for the construction of industrial works and a legal guide on electronic funds transfers, and for having reached decisions by consensus;

3. *Calls upon* the Commission, 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;

4. *Notes* that the Commission has assigned to its Working Group on International Contract Practices the task of preparing uniform legal rules on the liability of operators of transport terminals, and that the Commission has placed in its programme of work as a priority item the topic of legal implications of automatic data processing to the flow of international trade;

5. *Reaffirms* the mandate of the Commission, as the core legal body within the United Nations system in the field of international trade law, to co-ordinate legal activities in the field in order to avoid duplication of effort and to promote efficiency, consistency and coherence in the unification and harmonization of international trade law, and, in this connection, recommends that the Commission should continue to maintain

<sup>1</sup>Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 17 (A/39/17).

## I. INTERNATIONAL PAYMENTS

### A. International negotiable instruments<sup>a</sup>

1. Draft Convention on International Bills of Exchange and International Promissory Notes and Draft Convention on International Cheques: analytical compilation of comments by Governments and international organizations:  
report of the Secretary-General (A/CN.9/248)<sup>b</sup>

### CONTENTS

	<i>Page</i>
INTRODUCTION.....	27
PART I. DRAFT CONVENTION ON INTERNATIONAL BILLS OF EX- CHANGE AND INTERNATIONAL PROMISSORY NOTES.....	28
A. General comments on the draft Convention .....	28
B. Specific comments on individual articles .....	37
PART II. DRAFT CONVENTION ON INTERNATIONAL CHEQUES .....	85
A. General comments on the draft Convention .....	85
B. Specific comments on individuals articles.....	89

### INTRODUCTION

1. In accordance with a decision of the United Nations Commission on International Trade Law taken at its fifteenth session (26 July-7 August 1982),<sup>1</sup> the text of the draft Convention on International Bills of Exchange and International Promissory Notes<sup>2</sup> and of the draft Convention on International Cheques,<sup>3</sup> together with a commentary thereon,<sup>4</sup> was transmitted to Governments and interested international organizations for their comments.

2. In its decision the Commission also requested the Secretary-General to prepare a detailed analytical com-

<sup>a</sup>For consideration by the Commission see Report, chapter II, A (part one, A, above).

<sup>b</sup>Comments by two additional Governments can be found in document A/CN.9/249/Add.1 (reproduced in this Yearbook, part two, I, A, 2).

<sup>1</sup>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), para. 50 (*Yearbook 1982*, part one, A).

<sup>2</sup>A/CN.9/211 (*Yearbook 1982*, part two, II, A, 3).

<sup>3</sup>A/CN.9/212 (*Yearbook 1982*, part two, II, A, 5).

<sup>4</sup>A/CN.9/213: Commentary on the draft Convention on International Bills of Exchange and International Promissory Notes (*Yearbook 1982*, part two, II, A, 4). A/CN.9/214: Commentary on the draft Convention on International Cheques (*Yearbook 1982*, part two, II, A, 6).

pilation of these comments and to distribute it well in advance of the seventeenth session of the Commission to be held in 1984.

3. This report has been prepared in response to that request. It reproduces the comments received by the Secretary-General, as at 31 December 1983, from the following Governments and international organizations: Australia, Austria, Botswana, Canada, China, Cyprus, Czechoslovakia, Denmark, Finland, German Democratic Republic, Germany, Federal Republic of, Hungary, Indonesia, Japan, Mexico, Netherlands, Norway, Spain, Sweden, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland, United States of America, Uruguay, Yugoslavia, and the International Monetary Fund.<sup>5</sup>

<sup>5</sup>The following official languages of the United Nations are the original languages of the comments received:

Chinese: comments by China;

English: comments by Australia, Austria, Botswana, Canada, Cyprus, Czechoslovakia, Denmark, Finland, German Democratic Republic, Germany, Federal Republic of, Hungary, Indonesia, Japan, Netherlands, Norway, Sweden, United Kingdom of Great Britain and Northern Ireland, United States of America, Yugoslavia and the International Monetary Fund;

Russian: comments by the Union of Soviet Socialist Republics;

Spanish: comments by Mexico, Spain and Uruguay.

4. Part I of this report reproduces the comments on the draft Convention on International Bills of Exchange and International Promissory Notes and Part II the comments on the draft Convention on International Cheques.

5. An in-depth analysis, identifying the key features and major controversial issues that may be inferred from the comments reproduced in this report, is contained in document A/CN.9/249.<sup>c</sup>

#### **Part I. Draft Convention on International Bills of Exchange and International Promissory Notes**

##### *A. General comments on the draft Convention*

###### *Australia*

The Australian Government generally supports the draft Bills and Notes Convention and the draft Cheques Convention as a uniform optional scheme in respect of international negotiable instruments and sees the Conventions as a reasonably workable compromise between two basically different legal systems—civil law and common law.

The draft Conventions embody certain legal principles that are characteristic of civil law systems such as the continental concept of a guarantee (*the aval*) and rules relating to forged endorsements and material alterations and the protest and dishonour of negotiable instruments. While these concepts may create some difficulties in adapting the draft Conventions to Australian commercial and legal practice, these difficulties are not seen as major obstacles to the acceptance by the Australian legal and commercial community of the underlying scheme of the draft Conventions.

The draft Conventions do not significantly weaken the rights and obligations of parties to international negotiable instruments and Australian banking practice should be capable of adapting readily the handling of international negotiable instruments under the Conventions which generally simplify the issue, negotiation and payment of such instruments.

The following comments are not intended as an exhaustive analysis of the two draft Conventions, but rather provide a discussion of the main areas of concern to the Australian business, banking and legal communities that are raised by the draft Conventions.

###### *Conflict of laws:*

The choice of law governing the formal validity of a bill of exchange is governed in Australia by s. 77 (a) of the Bills of Exchange Act 1909 (BEA) which also applies to cheques and promissory notes. This section provides that the validity of a bill as regards requisites of form is determined by the law of the place of issue, and the formal validity of supervening contracts by the law of the place where they are made. Section 77 (b)

provides that "the interpretation of the drawing, endorsement, acceptance, or acceptance *supra* protest of a bill" is determined by the law of the place where the contract is made. Under Australian law, the law of the place where such contract is made is the law of the place where the last act necessary to render a party liable took place—in the case of a bill of exchange, normally delivery. Accordingly, each contract on the bill may have to be interpreted according to the law of the place where the bill was delivered.

The duties of a holder of a bill with respect to such matters as presentment, protest, notice of dishonour, are governed by the law of the place "where the act is done or the bill is dishonoured" (s. 77 (c)). This itself may present some problems of interpretation. Where a bill is drawn in one country but is payable in another, the due date of payment is determined according to the law of the place where it is payable.

Australian conflicts rules, supplemented by the provisions of the BEA, can, therefore, require Australian traders and financers to have a familiarity with the negotiable instrument laws of many jurisdictions, as well as dexterity in the application of the conflicts rules.

The approach of the draft Conventions to notice of dishonour and protest are entirely different from the BEA scheme. The rules under the draft Conventions are intended to apply universally—there is no question of the need to search out and apply the rules of the national laws of individual countries. Australia generally supports the scheme under the draft Conventions in this respect and mentions that an amendment of s. 77 of the BEA would be necessary to take account of the rules under that scheme.

###### *Austria*

Efforts to reach a compromise between the main bill of exchange laws and to promote in such a way international business transactions by a unification of laws are welcomed by Austria. The draft Convention is a remarkable attempt toward such a unification. Apart from certain exceptions which will be discussed in detail later on, the result brought about by the draft Convention may be considered a viable compromise. The envisaged convention, however, will fulfill its purpose only if it is internationally accepted and applied which, in turn, will be the case only if the regulations are clear, unambiguous and distinct. This is the only way to secure that the Convention will be applied in practice. This point of view may even be more important than certain legal policy considerations, e.g. whether and how a person who lost a bill of exchange has to be given particular protection.

Unfortunately, the draft Convention does, in general, not meet these requirements. The structure of the regulations is very complicated, the multitude of their interactions is not clearly distinguishable (the Geneva Convention shows that complicated regulations and a complicated system need not necessarily be the result of

<sup>c</sup>Reproduced in this Yearbook, part two, I, A, 2.

the complexity of the matter to be regulated). Therefore, it is not difficult to foresee that the business circles involved will have little ambition to subject themselves to such a system.

If one is aware of the fact that even conventions which are clear and distinct in their contents and the quality of which has been generally recognized, like the United Nations Convention on Contracts for the International Sale of Goods for instance, are being ratified only with reluctance and enter into force only after many difficulties have been overcome, the chances of success of a convention having the mentioned drawbacks must be rated very low. Therefore, it should be a consideration of principle whether it is reasonable to draw up a convention which—in the form currently proposed—has hardly any chances to ever enter into force.

#### *Botswana*

We have carefully studied the document and we have nothing useful and original to say about it.

#### *Canada*

Canada generally approves the draft Convention on International Bills of Exchange and International Promissory Notes and the draft Convention on International Cheques and is of the view that appropriately revised, they should be adopted as multilateral treaties.

With the exception of the points addressed subsequently, Canada finds that the texts of the draft Conventions are, in terms of organization, detail, relevance to modern business practices and clarity of expression, a distinct improvement upon the Geneva Convention on International Bills of Exchange and Promissory Notes that the new drafts will replace.

Matters not addressed by the Conventions: Questions may arise concerning the selection of the appropriate domestic law from among those which might claim to govern the obligations contained in the instrument by providing the supporting subsystem of law required to resolve collateral issues that are not covered by the Convention. Canada believes, without making any specific recommendations as to substance or form, that a provision similar in purpose to subsection 97(2) of the United Kingdom Bills of Exchange Act or Section 10 of the Canadian Bills of Exchange Act would enhance the draft Conventions.

#### Section 10 of the Canadian Act reads:

"10. The rules of the common law of England, including the law merchant, save in so far as they are inconsistent with the express provisions of this Act, apply to bills of exchange, promissory notes and cheques."

#### *China*

With the steady growth of world trade, bills and notes have been used increasingly as means of payment in international settlement. They are circulated internationally on an extensive scale, which has long transcended national boundaries, as is determined by their nature and functions. In order to safeguard their use and circulation and settle international disputes arising from the differences in national negotiable instruments laws and from the invocation of different laws by the parties to an instrument to interpret their rights and liabilities or as the basis of their actions, it is imperative and necessary to make a uniform, universally accepted law on negotiable instruments.

The two drafts as they now stand are the products of nine years' efforts and 11 Working Group meetings, starting from 1973. They have paid attention to the characteristics and customs of both the Anglo-American system of law and that of continental Europe, summed up the views of different quarters, and adopted a new and realistic course of action. While taking into consideration the difference in national laws on negotiable instruments, they have endeavoured to seek common ground and reserve the differences for further study. Therefore, the two drafts are suited to present conditions and have a certain mass basis.

But they have shortcomings too, which are manifested mainly in the following aspects:

1. Considering the many new circumstances, experiences and problems that have emerged in the circulation of international instruments since the war we recommend as a guiding principle for drawing up the two drafts that they should be "fair and reasonable, clear-cut in defining the rights and liabilities, and easy to apply". While maintaining a certain continuity by assimilating the essence of the two major systems of law and discarding what has become outmoded in them, it is necessary to sum up the new experiences in the circulation of international instruments and fill up deficiencies scientifically and appropriately to ensure greater accuracy and perfection of the two drafts and make them easier to apply.

2. Some of the articles and paragraphs in the two drafts are rather redundant, some are incomplete, and some lack clear-cut stipulations. In the draft Convention and International Bills of Exchange and International Promissory Notes, for example, the provisions governing endorsement are scattered in chapter two ("Interpretation"), chapter three ("Transfer") and chapter four ("Rights and liabilities"), making it inconvenient to invoke them; on the other hand, some of the questions relating to endorsement are left out, e.g., the effect of alteration, obliteration and forgery of an endorsement on an instrument, and the liability of the alterer, obliterator and forger. Another example is the interpretation of terms, such as "holder", "protected holder", "a holder who is not a protected holder", "qualifying as a holder" etc. These terms are used at different places in the draft, but are not interpreted one by one in chapter two ("Interpretation"), which has

thus failed of its purpose as a chapter specially devoted to interpretation. In addition, some of the terms that have been left without interpretation may cause a divergence of view in the course of application. Moreover, there should be explicit provisions in chapter four ("Rights and liabilities") about the rights, obligations and liabilities relating to an instrument at each stage of the whole process from drawing, circulation to payment, so as to avoid or reduce disputes in the course of application and enable the instrument to play its due role. But the provisions about liabilities in that chapter are incomplete. For example, there are no provisions about the liability of the holder or the endorsee (the collecting bank or the paying bank) arising from a forged endorsement on an instrument, thus failing to give due protection to the banks either as collecting banks or as paying banks.

3. Some of the articles and paragraphs in the two drafts are highly elastic and leave quite a few gaps in them. It is hardly avoidable that such elasticity would lead to increased disputes and differences in their application and affect the solution of problems; and the many gaps are liable to induce parties to invoke their own national negotiable instruments laws and thus create more conflicts of laws, even leading to such disputes as have developed around the application of municipal law in private international law. All this would have an adverse effect on the circulation of international instruments.

#### *Cyprus*

In Cyprus the Bills of Exchange Law, Cap. 262, deals with Bills of Exchange and Promissory Notes. As with the draft Convention on International Cheques so here, in case the Convention is adopted by Cyprus, the existence of two different sets of rules, the one applicable to international bills and international promissory notes and the other to all other bills and promissory notes might lead to confusion. To avoid this, adequate publicity must be given to the Convention and the domestic law as well as the draft Convention if possible must be changed as regards a number of their provisions.

#### *Czechoslovakia*

The draft Convention on International Bills and Notes can be considered as a suitable basis for discussion on uniform rules intended for universal international use.

#### *Finland*

International unification has been notably successful in the field of international payments. The objective of the present drafts is to bridge divergences between the 1930 Geneva Conventions and Anglo-American law.

This is clearly a useful objective. The draft Convention on International Bills of Exchange seems to form a good basis for the envisaged unification.

On the other hand, it is doubtful whether there is a genuine need for a convention on international cheques based on the assumption that the cheque as a document is transmitted from one country to another. It would seem that the need to regulate such international cheques is diminishing and that future efforts should be directed towards electronic transfer of funds.

#### *German Democratic Republic*

The Government of the German Democratic Republic welcomes the elaboration of the draft Convention on International Bills of Exchange and International Promissory Notes and the draft Convention on International Cheques. By the elaboration of these two draft Conventions two important steps have been initiated towards the further unification of bill and cheque law. The Government of the German Democratic Republic supports such further unification, because it may facilitate and simplify the use of bills of exchange/promissory notes and cheques in international economic relations. Bills of exchange/promissory notes and cheques have considerable significance in handling and securing payments in international transactions. Therefore, it seems necessary to establish, as far as possible, uniform and simple juridical bases for the practical use of bills of exchange/promissory notes and cheques. The Government of the German Democratic Republic considers it an advantage of the two draft Conventions submitted that it has been possible to combine two different conceptions of bill and cheque law: the conception reflected in the Geneva Convention providing a Uniform Law for Bills of Exchange and Promissory Notes dated 7 June 1930 and in the Geneva Convention providing a Uniform Law for Cheques dated 19 March 1931, as well as the conception based on Common Law. In the view of the Government of the German Democratic Republic, the compromise found in the two drafts offers acceptable, fair and practicable solutions to all states which intend to become parties to the Conventions.

The Government of the German Democratic Republic considers the elaboration of conventions containing a coherent set of direct regulations and to which States may become parties, to be an adequate approach. It can be expected that in this way the effect of the envisaged unification is greater than would be the case if a convention, accompanied by a model law, would be recommended to States to regulate the matters in question at the national level. Taking into consideration the different economic and legal nature of bills of exchange/promissory notes and cheques, it was in its opinion indispensable to take as a basis in the drafting process the option of two separate conventions to which States may become parties. It is advantageous in the interest of achieving maximum universality for both Conventions, if both of them have the same structure

and if the provisions on bills of exchange/promissory notes and cheques are as uniform as possible, while making allowance for their different functions.

In both Conventions the effort is obvious to adapt the structure of the Conventions to the practical sequence of steps in dealings using bills of exchange/promissory notes and cheques which may prove to be favourable for the practical application of the two Conventions. The two Conventions are based on the conception that all legal problems related to bills of exchange/promissory notes and cheques shall be regulated as far as possible by the texts of the Convention themselves. This obviously explains why no reference has been made to subsidiary applicable law. However, the intention of avoiding reference to subsidiary applicable law should, under no circumstance, lead to a further expansion of the draft provisions. The present volume is completely sufficient for covering the legal aspects of all typical processes related to bills of exchange/promissory notes and cheques. Besides, the pertinent commentary will be an important aid in the practical use of bills of exchange/promissory notes and cheques as well as in future jurisdiction.

#### *Germany, Federal Republic of*

The UNCITRAL draft Convention on International Bills of Exchange and International Promissory Notes provides for the creation of a new law on bills of exchange which is to be applied exclusively to international transactions.

The Geneva Conventions have already brought about a far-reaching unification of the law on bills of exchange which has proved good for more than half a century. However, groups of important States have kept aloof from these Conventions. It would be desirable to include these States in the unification, even if no significant difficulties have arisen up to now in international commercial transactions because of the different systems of law on bills of exchange.

The solution offered by the draft to create an international bill of exchange as an alternative to the commercial papers already existing cannot serve the objective of promoting global unification as to the law on bills of exchange. It would, on the contrary, rather bring about the danger of impairing the uniformity achieved. In practice, the system proposed would for a long time entail considerable legal uncertainty and difficulties which, in the opinion of all groups concerned in the Federal Republic of Germany, would not be balanced by substantial advantages.

UNCITRAL's effort towards further unification of the law on bills of exchange should therefore not be directed towards introducing a new legal system beside the old one, but should strive towards making the Geneva Conventions acceptable to the Anglo-American legal systems as well as towards further developing them in accordance with the requirements of modern transactions, if necessary. For this purpose, it should first be

clarified which provisions of the Geneva Conventions are in need of amendment.

#### *Hungary*

According to the opinion of the Government of the Hungarian People's Republic the draft Conventions on International Bills of Exchange and International Promissory Notes as well as on International Cheques reach the purpose of unification that have been aimed at by UNCITRAL in the sphere of negotiable instruments.

The draft Conventions are acceptable and satisfying as regards their contents, structures and forms. The Hungarian Government agrees with the facultative methods of the regulations and with the system that on the international negotiable instruments not only one, but two separate Conventions should be established namely one on Bills of Exchange and Promissory Notes and another one on Cheques. The drafts contain a successful compromise between the Geneva and English Bill of Exchange system; the drafts apply a solution convenient to practice regarding the divergence between the conceptual views of the two systems. The Bill of Exchange and Cheque systems established by the drafts are sovereign and independent.

The draft Conventions are basically suitable to solve the well-known problems, arising from the difference between English and Geneva systems. According to the conviction of the Hungarian Government they are apt to the unification in the field of bills and cheques in such a manner as is achieved in the area of documentary credit.

In Hungary there is no theoretical and practical obstacle to the widespread application of the Convention on International Bills of Exchange and Promissory Notes as well as International Cheques.

#### *Indonesia*

The Indonesian Commercial Code covers the law on Bills of Exchange, Promissory Notes and Cheques, which are derived from the Uniform Law for Bills of Exchange and Promissory Notes (ULB) and the Uniform Law for Cheques (ULC) adopted by the Geneva International Conventions of 1930 and 1931.

The ULB and ULC came into force in the Netherlands and, based upon the principle of concordance, were adopted through the Netherlands Indies, which became Indonesia in 1945. They came into force as of January 1, 1936, for Bills of Exchange and Promissory Notes (State Gazette 1934/562 and 1935/351), as of January 1, 1936, for Cheques (State Gazette 1935/77) and 562). The draft Convention on International Bills of Exchange and Promissory Notes, and the draft Convention on International Cheques are not merely based upon the ULC and the ULB but also upon the Bills of Exchange Act of 1882 (BEA) and the Uniform Commercial Code (UCC).

The two draft Conventions cover materials originating from two different systems of laws namely the civil law and the common law system. Therefore these two drafts contain a broader substance than the Indonesian Commercial Code.

Considering that the two draft Conventions which provide rules for settling problems concerning international payments are in line with the Indonesian Commercial Code (subject to a reservation concerning provisions on "signature"), they are acceptable and would be taken into consideration by the Government of the Republic of Indonesia.

#### *Japan*

It will be very meaningful to create, in addition to the existing negotiable instruments governed by convention and domestic laws, a new bill of exchange or promissory note to be issued only for international transactions. The Japanese Government supports the idea of adopting a new multilateral convention creating such an instrument. The present texts of the draft Convention on International Bills of Exchange and International Promissory Notes, the product of discussion in the Working Group on International Negotiable Instruments of UNCITRAL, provide an excellent basis for achieving a good compromise between the Anglo-American and Geneva systems, and the Japanese Government (and Japanese banking and trading circles) finds the basic principles on which the texts are drafted acceptable.

#### *Netherlands*

The Netherlands expresses its appreciation to the UNCITRAL Working Group on International Negotiable Instruments for having finalized two draft Conventions designed to establish uniform provisions governing international bills of exchange and international promissory notes, and international cheques. Though the draft Conventions in certain respects fundamentally change basic rules of the civil law system of negotiable instruments, as indeed also of the common law system, it is realized that the proposed uniform provisions are the outcome of carefully worked out compromises. The Netherlands, therefore, is in favour of continuing work on the basis of the draft Conventions if there were sufficient support among member States of UNCITRAL for the adoption of uniform provisions in the form of either a convention or a model law.

Though the Netherlands thus expresses its willingness to co-operate actively with other Governments, it must at the same time express its doubts whether the establishment of a third system of negotiable instruments law would add measurably to legal certainty in the area under discussion. The fact that the two major systems of negotiable instruments law differ in important aspects has not, to any significant extent, impeded the use of negotiable instruments in settling

international payments. Having regard to the large volume of payment transactions by means of such instruments, one cannot help but note the paucity of court decisions. It is arguable that an untried third system, because of the unfamiliarity of many of its provisions and the absence, at least initially, of their uniform interpretation, might well have a detrimental effect on the degree of legal certainty that currently exists.

Since bills of exchange and promissory notes are more widely used in international transactions than are cheques, the Netherlands would prefer that further work be focused on the draft Convention on International Bills of Exchange and International Promissory Notes and that, consequently, work on international cheques be deferred if not abandoned. For this reason, the comments of the Netherlands are largely directed to that draft Convention though they apply equally to the draft Convention on International Cheques to the extent that the provisions of the two draft Conventions are similar.

The Netherlands, at this stage does not pronounce itself on the question whether uniformity of law would better be achieved through the adoption of a convention or a model law. In this respect it notes that the large measure of uniformity found in the legislation of civil law countries is the result not so much of ratification by States of the Geneva Conventions of 1930 and 1931, as of the use by States of these Conventions as models for domestic legislation.

#### *Norway*

1. The Government of Norway approves of the proposal for two separate, independent conventions on international bills of exchange and international promissory notes and on international cheques.

We acknowledge the high quality of the UNCITRAL draft Convention on International Bills of Exchange and International Promissory Notes. We also approve of the thoroughness of the draft Convention and its systematic structure. The UNCITRAL Working Group has reached good compromises between civil and common law and has, from a practical point of view, proposed a sound and workable regulation.

2. The Norwegian Government supports the adoption of the draft Convention as a binding multilateral treaty. The draft ought not to be adopted only as a model for enactment. This approach would invite deviations from the Convention during the different national enactment processes.

3. It seems to us that the Contracting States to the Convention providing a uniform law for bills of exchange and promissory notes, Geneva June 7th 1930 (Norway included), will not be able to ratify an UNCITRAL Convention without denouncing the Geneva Convention. Norway will support proposals for

an amendment to the Geneva Convention allowing the Contracting States to ratify the UNCITRAL Convention and make it applicable to international bills of exchange and international promissory notes.

4. From a practical point of view, it is obviously a complicating disadvantage at the same time to have two different sets of rules regulating in essence the same kind of negotiable instruments for international purposes. From our point of view, there seems to be nothing in the draft itself that makes it unacceptable as a general regulation common to all kinds of international bills of exchange and promissory notes. If the UNCITRAL draft Convention meets with a wide approval, the Norwegian Government is therefore inclined to support a revision of the Geneva Convention by the States parties to that Convention and with a view to harmonize it with the UNCITRAL Convention.

5. We emphasize that the draft Convention does not prohibit the application of the Convention to bills of exchange and promissory notes (instruments) outside its own scope of application as defined in articles 1 and 2. Without contradicting the Convention, a Contracting State may thus in its own legislation prescribe for the application of the Convention notwithstanding the fact that the words "international bill of exchange (Convention of...)" or "international promissory note (Convention of...)" are missing in the text of the instrument and notwithstanding that all the places listed in article 1 (2) (e) or (3) (e) are situated in the same country. In the future, these possibilities might be exploited for the purpose of harmonizing different national laws.

6. A higher degree of correspondence between the articles of the two draft Conventions would have been an advantage, in particular as regards the more general rules and principles of the first parts of the drafts. Full correspondence between articles 1 to 33 inclusive of the draft on bills of exchange and promissory notes and articles 1 to 35 inclusive of the draft on cheques could easily be achieved:

i. Articles 3 and 4 of the draft on cheques could either be included in article 1 or 6, or be totally deleted. As the articles now read, they seem superfluous, and the Working Group has not found it necessary to propose similar rules in the draft on bills and notes.

ii. Articles 8 and 9 of the draft on cheques correspond to article 8 of the draft on bills and notes and are easily combined in one article.

iii. Articles 9 and 10 of the draft on bills and notes correspond to article 12 of the draft on cheques. The rules in article 10 of the draft on bills and notes are conveniently transferred to article 9 as a new paragraph (4).

7. The comments and examples to the draft Convention have been most useful. We recommend that a similar thorough commentary accompany the final Convention.

### Spain

Our initial position in making these remarks on the draft Convention on International Bills of Exchange and International Promissory Notes, submitted for comment, is one of praise and approval for the idea on which it is based, for the objective sought and for the steps taken to date towards that objective within the United Nations Commission on International Trade Law (hereafter UNCITRAL).

It is unquestionably desirable that there should be suitable instruments for documenting international economic operations and that there should be uniform regulations governing these instruments.

To further the purpose of making international economic, commercial and financial exchanges possible, the law must provide appropriate legal means for making these international economic relations possible and ensuring their security.

Instruments such as the bills of exchange and promissory notes discussed here are traditional instruments for the exchange of goods and services. They are used to document economic operations, which are basically contractual, and facilitate the fulfilment of the obligations deriving from them.

However, these instruments are at present governed by differing sets of regulations. Supranational uniformity has been achieved in some areas, but in any case there are still two major systems which are quite different, the Anglo-American system and that established under the Geneva Convention. Spain is a signatory to that Convention but it has not incorporated the Uniform Law into Spanish law; the legislation in force, with minor amendments in this area, is the Commercial Code of 1885.

The fact that there is no uniform legislation governing the above instruments hinders their use in international trade, not merely because of differences in the principles implemented, but also because of ignorance and consequent mistrust of the relevant legislation in other countries.

It is therefore a praiseworthy endeavour to overcome these difficulties by establishing a uniform set of regulations for these international instruments; accordingly, the main objective of the regulation should be to achieve consistency in the formulation, interpretation and implementation of the rules. The idea of providing potential users with an instrument they may use optionally, if they see fit, is also a good one. The issuer can choose to have the instrument governed by the Convention by referring to it explicitly, or choose not to. However, even within these optional regulations, the Convention will make it possible to set up a uniform system that overcomes the existing divergences. Its ultimate success will depend on the degree of acceptance it achieves. To achieve the maximum possible acceptance, solutions must be sought that make a compromise between the systems currently in force. Each country will

have to relinquish part of what it considers characteristic in its legal code. The present draft Convention is examined in this spirit, recognizing both the desirability and the difficulty of the task.

It should be noted before reading these comments that the Spanish Government submitted the draft Convention for examination and comments by organizations associated with the circles concerned by the proposals. The present document contains quotations from the opinions given by the Consejo Superior Bancario (Higher Council on Banking; hereafter CSB) and the Consejo Superior de Cámaras de Comercio de España (Higher Council of Spanish Chambers of Commerce; hereafter CSCC).

As stated above, the main concern is to work towards consistency in the formulation, interpretation and implementation of regulations. In view of this objective, we would make a very general initial remark applying to the draft Convention as a whole, a remark which may appear superficial but which is of extreme importance. It concerns the drafting, terminology and syntax used in the draft, which, in the Spanish version at least, give cause for serious reservations. It is paradoxical that the Commentary annexed to the draft Convention (A/CN.9/213, hereafter Commentary), which is a translation from an English original, should be more correctly written than the original Spanish version of the draft Convention. This is not the place for a detailed analysis of this aspect of the draft Convention; the purpose of our comment is simply to stress the importance of this matter and to suggest that the draft should be completely revised, in consultation with all countries having Spanish as an official language.

Other characteristics of the draft Convention, which may also be considered "formal" but do not constitute drafting defects in one specific version, also make these provisions difficult to read and understand. We refer to the excessive use of definitions, which often bring confusion rather than clarity (see for example the remarks in article 4) and to the continual qualifications and cross-references (some of which will be pointed out below) which, as the CSCC states in its opinion, make the text exceptionally difficult to read.

In view of the international scope of the draft Convention, great care is necessary to avoid all such defects, which are obstacles to its interpretation. Similarly, because the Convention is to be implemented in different countries by people whose legal conceptions are different, it is especially important to avoid using any vague concepts or subjective or ambiguous interpretation criteria.

At this point we shall merely endorse the opinion given to this effect by the CSB, and point out the danger that phrases, concepts and criteria may be interpreted in different ways. Specific references to this will be made further on.

#### *Conclusions*

ONE. The Spanish Government approves of UNCITRAL's draft Convention on International Bills

of Exchange and International Promissory Notes, which is an important stage in UNCITRAL's work on standardizing international trade laws.

The use of these instruments in international trade has a long history, but it is impeded at the present time by the diversity of the legal systems. The attempt to overcome these differences by means of an optional, uniform set of regulations, based on a compromise between the two great legal systems now predominant in the world, deserves our praise and support, because it represents an endeavour to remove existing obstacles to the normal use of such instruments in international trade.

TWO. In a spirit of co-operation to promote this initiative, the Spanish Government considers it appropriate to make use of the comments procedure in order to put forward some views aimed at improving the draft Convention and ensuring its future acceptance. They are proposed subject to any subsequent developments that the Spanish delegation to UNCITRAL may make at later stages in the drafting or at the diplomatic conference on the draft Convention, if convened.

THREE. The Spanish Government's first general comment is that the present Spanish version of the draft Convention requires thorough revision to correct not only the technical terminology relating to bills and notes but also the actual grammatical drafting. The "Spanish original" displays serious defects which indicate that it was originally a translation from a text drafted in another language. The Spanish Government attaches great importance to this issue; it considers that these shortcomings should be remedied by means of a revision carried out by a group within UNCITRAL, to include representatives of all delegations having Spanish as an official language, and it offers to make Spanish representatives available as of now for participation in this task.

FOUR. Another general comment relates to the method of presentation: the Spanish Government suggests that it would be desirable to simplify the text of the draft Convention so that it is easier to read and understand, and ultimately to interpret and implement. The technical difficulties inherent in so complex a subject are recognized, but it is desirable to have a clearer presentation with, if possible, fewer definitions and cross-references than in the present version. Similarly, it would be desirable, to ensure wider acceptance of the future international instruments, for the text to be more specific and avoid the use of imprecise or ambiguous legal concepts.

FIVE. The Spanish Government notes the omission from the draft Convention of two fundamental issues on which, in view of their importance, basic provisions should be expressly formulated:

1. The procedural treatment of recourse on bills and notes; the practical success of these instruments depends to a great extent on such regulation.

2. The connection between the instruments and the underlying transactions. As this is not regulated, the isolated reference to a specific theme, the assignment of funds made available for payment, appears strange and incongruous.

#### *Sweden*

1. The Working Group has had as its aim to harmonize the Anglo-Saxon Common Law System and the European Civil Law system—the latter represented by the Geneva Convention providing uniform laws for bills of exchange and promissory notes. It is the opinion of the Swedish Government that the draft Convention on International Bills of Exchange and Promissory Notes is well elaborated and that it represents a workable compromise between the two legal systems.

2. However, the Working Group has confined the Convention to be applicable only to negotiable instruments of an international character. Consequently, the Convention is not intended to replace the national legislation in this field. This could imply that States Parties to the intended Convention would have double legislations for bills of exchange and promissory notes. For several reasons, such a situation could not be deemed to be very appropriate, at least not as far as Sweden is concerned.

3. Apart from the inevitable complications in having two parallel systems with differing provisions, it may be observed that there would still exist bills of exchange of an international character which would not be covered by the draft Convention. This is the case regarding e.g. bills which are drawn and payable in the country where both the drawer and the drawee have their residence but which are later endorsed to a person in another country.

4. For the reasons mentioned, the need for conventions concerning only international negotiable instruments may be questioned. In the view of the Swedish Government it must be deemed more important to strive for harmonizing the legislations concerning national negotiable instruments. If such a harmonization is achieved, this would also solve the problems as regards international payments.

5. The Geneva Convention has to a considerable extent meant a harmonization of the national legislations in this field. However, many States have chosen not to become Party to this Convention. Besides, development has made some of its provisions unsuitable or at least impractical.

In a document elaborated for the attention of the Council of Europe the Swedish Government has raised the question whether time has not come to make a general revision of the Geneva Convention. As stated in the said document, such a revision should be undertaken on a universal basis. In the view then expressed by the Swedish Government, some organ within the United Nations, e.g. UNCITRAL, would be the appropriate forum.

6. A revision of the Geneva Convention would of course not be required if the work already undertaken by UNCITRAL should result in uniform laws for both international and national instruments. Thus, an alternative to revising the Geneva Convention could be to enlarge the scope of the present draft Convention.

7. The present draft Convention is now to be discussed at the seventeenth session of the UNCITRAL. It has been decided that this discussion should concern key features and major controversial issues. The Swedish Government proposes that this discussion include the question of amending the present draft Convention in such a way as to make the Convention acceptable also as regards national instruments. It is obvious that such a revision would strongly benefit from the work which has already been carried out in the UNCITRAL Working Group.

8. Considering its principal attitude as regards the present draft Convention the Swedish Government does not at present wish to make detailed comments on the particular articles. It may be noted, however, that the draft texts apparently solve all the problems pointed out in the document that Sweden presented to the Council of Europe, as far as international instruments are concerned. This is satisfactory. In comparison to the Geneva Convention, the present draft Convention is more flexible as regards the proceedings for recourse. This also seems expedient.

9. On the other hand, the Swedish Government would like to express its doubts as to the rules in the present draft concerning the rights of the holder of an instrument and the defences of a party against the holder, especially when it comes to the effects of forged signatures or other unauthorized acts.

The proposed rules, apparently motivated by the concept that a party should know his endorser, may have certain disadvantages. For instance, they would probably make people less inclined to receive endorsed instruments, especially in commercial relations. However, the Swedish Government is aware of the fact that the proposed rules are part of the compromise between the two legal systems. Applied on international instruments only, the provisions seem acceptable from a Swedish point of view.

#### *Union of Soviet Socialist Republics*

From the point of view of their content, structure and form the draft Conventions are, on the whole, satisfactory and acceptable, as is the method of presentation, i.e. regulation of international bills and notes and of international cheques in two separate documents.

#### *United Kingdom of Great Britain and Northern Ireland*

The general observation that Her Majesty's Government would like to make in respect of the above draft Convention is that to be effective such a Convention

has to be mandatory. The only other general point is that this branch of the law is becoming less important and that real interest is shown in the law relating to international payments made by electronic transfer of funds.

#### *United States of America*

The United States generally approves the draft Convention on International Bills of Exchange and International Promissory Notes. The United States supports the proposal that the Convention be adopted as a multilateral treaty, but is doubtful of the utility of adopting these provisions as a model law. The United States regards this draft Convention as a workable compromise between two fundamentally different legal systems. Therefore, these comments are directed primarily toward implementing the compromise policy decisions of the Working Group rather than toward reopening them.

The draft Convention on International Bills of Exchange and International Promissory Notes is an attempt to establish a settled body of law to govern items of international commercial paper that are expressly designated on their face as controlled by the Convention. These items would not be subject to the uncertainties of conflict of law decisions. The draft Convention proposed by the Working Group does not, therefore, attempt to reform the laws applicable to domestic paper, or even the laws applicable to all international commercial paper. Rather, the draft Convention provides rules for a restricted category of international paper—rules which are certain and which are adapted to the practices of the commercial community in States with different legal systems. To accomplish this goal, the Working Group had to reach a compromise between fundamentally different sets of legal rules concerning commercial paper. The United States believes that the draft Convention has successfully achieved such a compromise and that the rules established are adaptable to commercial practices in the United States. The United States thus supports the draft Convention as a means of furthering certainty in the rules applicable to international commercial transactions.

The United States believes that the proper use of the draft rules to further certainty in international commercial transactions is through the adoption by States of a convention applicable to designated international commercial paper. The use of this draft as a "model" for enactment by States would invite its amendment during the enactment process, detracting from uniformity and creating uncertainty. Parties to instruments would still feel a need to learn foreign law and consult foreign counsel, and the major potential benefits of the Convention would be lost. Use as a model law would also retain all the present problems and perhaps even exacerbate them by adding yet another system of rules to be considered. Furthermore, promulgation as a model would be perceived as the weakest possible endorsement of the draft.

The current draft Convention is a compromise between two basically different systems of domestic law on commercial paper: civilian and common law. Each of these systems now has several variations as implemented in different States. In many respects, the compromise in the draft Convention is fundamentally different from current United States law on commercial paper. Examples include omission of the entire concept of "negotiation" in article 12; giving the status of "holder" to a person in possession of an instrument through a necessary, but forged, endorsement in article 14; and relieving of liability a payor who pays an instrument bearing a forged necessary endorsement in article 23. Other examples include creating in articles 42 and 43 the concept of a "guarantor" who has characteristics of both the civil law *avaliste* and the common law guarantor and accommodation party; and requiring protest as a condition precedent to liability of secondary parties in article 55, while not requiring notice of dishonour as a condition precedent to liability of secondary parties in articles 60 and 64. These differences will create difficulty in adapting the draft Convention to our commercial practices in the United States. However, these rules seem adaptable to United States commercial practices. Thus, in the spirit of compromise, the United States is favourably disposed to the present draft, even though some difficulties can be anticipated.

The article-by-article comments of the United States are directed primarily to improving the drafting of the Working Group and carrying out its decisions, rather than seeking to overturn or reopen the compromises struck. Although the comments make some important proposals, the proposals seek to clarify the draft and to eliminate problems which would otherwise arise in common law courts.

The United States strongly urges that a commentary accompany the final text. The existing commentary has been prepared at the request of the Secretariat and has thus far accompanied the draft Convention as an explanation of its provisions. It has proved most helpful to bank counsel, practitioners and law professors in the United States who have studied the draft Convention. A commentary on the Convention finally adopted would facilitate efforts to have the Convention accepted by States. As the draft Convention contains a number of concepts which are unknown in common law systems, a commentary would be of special importance to a common law country such as the United States.

The United States proposals have been prepared with considerable restraint. In view of the limited time for consideration of the draft Convention at a diplomatic conference, the already long period of work on the draft by the experts on UNCITRAL's Working Group, and the complexity of the subject matter, it seems desirable that the number of proposals made to UNCITRAL at this stage and ultimately at a diplomatic conference be kept to a minimum.

### *Uruguay*

The draft Convention under consideration creates new types of negotiable instruments, the international bill of exchange and the international promissory note, which are suitable and appropriate instruments for international trade and are governed by an international trade convention. This Convention will obviate conflicts of interpretation regarding the applicable law and will therefore facilitate trade.

The text of the draft Convention on International Bills of Exchange and International Promissory Notes does not give rise to any general objection. On the contrary, it appears to offer an excellent and appropriate set of rules suitable for application in different countries, notwithstanding differences in their international legislation.

Some of the solutions adopted in the draft Convention differ from those adopted in our internal law, but they are not incompatible to the extent of their approval being inadvisable.

### *Yugoslavia*

1. Yugoslavia commends the results of the Working Group on International Negotiable Instruments of the United Nations Commission on International Trade Law (UNCITRAL) and considers it to be a considerable effort toward the unification of the existing legal rules of the common law system and the system based on the Geneva conventions in the field of the bills of exchange and cheques.

The draft Conventions take more account of the needs of contemporary financial transactions than the laws and practices existing in the world today. The general impression is however that both draft Conventions pay attention to the interests of the creditors rather than those of the debtors, which is not in the interest of developing countries.

2. Although the draft took note of the solutions offered by the two legal systems in the world, there prevail, nevertheless, concessions to the common law system, a difficulty which the jurists and businessmen of the so-called system of Geneva conventions will have to encounter. This general impression can be illustrated by the fact that, under the draft Convention, a bill is linked to the underlying transaction (which is the attitude of the common law States), turning thus from an abstract to a causal transaction.

3. The decision to include promissory notes in the draft Convention on International Bills of Exchange was a good one. Promissory notes are not only more frequently used in the world today but they are more effective (there is no need for acceptance or protest, etc.) and they ensure greater legal security. In this respect, the draft Convention marks a progress in comparison with the instruments which have not given this type of a bill due attention.

4. The texts of the draft Conventions on International Bills of Exchange and Promissory Notes and on International Cheques are very similar, even in cases when a distinction should have been made between them. International transactions in recent years have offered ample proof of the important differences between the two negotiable instruments (a bill is a form of credit and a cheque a form of payment). Therefore, it was expected that the two drafts would differ much more. The application of the provisions relating to bills of exchange to cheques can have adverse effects in practice. Consequently, it is necessary that the draft Convention on International Cheques be thoroughly reviewed, having in mind the purpose of the cheque in international transactions.

5. Despite the intention of the draft Conventions to deal with international bills of exchange and international cheques in a comprehensive manner, it is hard to imagine that they have managed to settle all the problems which may arise as a result of the use of these instruments in international transactions. Hence, it would be advisable either to amend the draft Conventions so as to include the provisions concerning the conflict of laws, or to prepare another draft convention to regulate the matters pertaining to International Private Law.

### *B. Specific comments on individual articles*

#### **CHAPTER ONE. SPHERE OF APPLICATION AND FORM OF THE INSTRUMENT**

##### *Spain*

The chapter heading seems unfortunate; the first phrase applies to the Convention and the second applies to the two instruments which it regulates.

#### **ARTICLE I**

##### *Spain*

Sphere of application of the Convention: there are two separate provisions applying to this, article 1, paragraph (1), and article 2; these might be rewritten.

An essential characteristic of the Convention is its optional nature. It applies to those bills and notes called international only if the drawers or makers decide that they shall be subject to the Convention.

Therefore, although the Commentary on the draft Convention states that paragraphs (2) and (3) of article 1 make this optional nature clear, it would seem advisable for it to be made explicit in the provision defining the Convention's sphere of application. As it stands, article 1 (1) merely states that "This Convention applies to international bills of exchange and international promissory notes"; paragraphs (2) and (3) establish what international bills of exchange and promissory notes are by listing the requirements, the

first of which is that the text should include the words "international bill of exchange. Convention of . . .", by which the issuer opts to make the instrument subject to the Convention. Thus, the adjective "international" is reserved exclusively for bills and notes that are subject to the Convention. In view of the fact that the Convention is optional and, consequently, that not all international bills and notes will be within its sphere of application, it would be preferable for paragraph (1) to refer explicitly to its optional nature, and for paragraphs (2) and (3) to establish the requirements that instruments have to meet in order to be considered international and to be covered by the Convention, instead of attempting a comprehensive definition of "international" instruments ("An international bill of exchange/promissory note is a written instrument which: . . .").

#### *United States of America*

For common law nations there is an important problem if they become a party to the Convention on International Bills of Exchange and International Promissory Notes but not to the Convention on International Cheques. In the common law system a cheque is considered a particular type of bill of exchange and therefore the Convention on International Bills of Exchange and International Promissory Notes could be regarded as applicable to cheques if no other convention applies, unless the Convention on International Bills of Exchange and International Promissory Notes provides that it does not apply to international cheques. The United States therefore recommends that article 1 include a provision to the effect that the Convention does not apply to international cheques.

#### *Article 1 (2)*

#### *Spain*

**Form of the instrument:** The parts of the definition contained in paragraphs (2) and (3) are the formal requirements for the instrument. The list should reflect this, and not be formulated in the definition style used in the present draft.

#### *United States of America*

Paragraphs (2) and (3) of article 1 state that a qualifying bill or note must be a "written instrument". The term "written" is not defined in the Convention, and comment 4 indicates that the draftsmen deliberately omitted such a definition. The United States proposes that such a definition be added to article 1. In particular, the definition should require that any "Signed writing" meets several tests, including that the writing be permanent and capable of physical transmission between parties, that it be signed in a manner which prevents tampering, and that it contain the signature of the issuer.

#### *Article 1 (2) (a)*

##### *Canada*

**Words of invocation:** In the opinion of Canada, each of the Conventions might be deficient in stipulating that instruments be governed by its text if the text contains certain words invoking the Convention. We note, for example, that the Convention will be enacted in Chinese and Russian as well as English, French and Spanish. There may be simple human problems of recognizing instruments that are to be governed by the international Convention if the key phrase appears in Chinese or cyrillic text. It would be desirable if some symbol, or abbreviation that is readily reproducible by normal typewriters could be devised or adopted to aid the process of recognition of the instruments requiring special treatment under the Conventions.

##### *China*

**Paragraph (2) (a) of article 1:** "Contains, in the text thereof, the words 'international bills of exchange (Convention . . .)'".

**Recommendation:** This be changed into "Contains, in the text thereof, the words 'international bill of exchange (Convention of . . .)', or 'bill of exchange' if the places indicated on the bill show that it is an international bill of exchange".

##### *Czechoslovakia*

The important question arises whether the drawer of a bill (or the maker of a note) when using the words "International Bills of Exchange" or "International Promissory Note (Convention of . . .)" has thereby indicated either a choice of law or a choice of the legal regime of the bill (note) in compliance with the Convention. The effects of such a choice should be specified in the text of the Convention, as follows: article 1 (2) (a) should be amended to the effect that this designation by the drawer (maker) constitutes also an indication of the legal régime of the Convention; at some proper place, the Convention should specify that clauses according to article 1 (2) (a) or (3) (a) inserted in the bill (note) by the drawer (maker) subject the instrument to the regime of the Convention and bind all holders who took it, and all subsequent parties.

It would be expedient to specify that the words mentioned in paragraph (2), letter "a" and in paragraph (3), letter "a", and any bill (note) on the whole may be filled in any language (in more languages also), i.e. that the mentioned expressions may be written in corresponding expressions of different languages.

##### *Japan*

In view of the fact that a bill of exchange or promissory note covered by the draft Convention would be issued for optional use in international transactions, it is essential to ensure that the bill or note

shall be clearly distinguishable from other existing instruments as an international bill of exchange or promissory note governed by the Convention. The ideal solution would be to require persons choosing to issue an instrument subject to the Convention to use a universally standard form for the bill or note, which may be attached to the Convention as an annex. Limiting the languages which may be used in the text of the bill or note might be another useful solution. If these ideas are judged to be impractical, it would be worth considering requiring that the words contained in article 1 (2) (a) or (3) (a) be written in certain specified languages, say, English or the United Nations official languages, in addition to the original language.

#### *Norway*

According to subparagraphs (2) (a) and (3) (a) the words "international bill of exchange (Convention of . . .)" or "international promissory note (Convention of . . .)" must appear in the text of the instrument. In the practical handling of the instruments it is important that these words are easily recognized. The Convention ought to require that the words are conspicuous in the text. The maker or the drawer can ensure that the requirement is met. One should also consider to require the use of a conspicuous short-title in the text of the instrument, e.g. "UNCITRAL Convention" or the like. Furthermore, it should be considered to work out a standard form to be annexed to the Convention.

#### *United States of America*

Paragraphs (2) (a) and (3) (a) of article 1 state that the words "international bill of exchange (Convention of . . .)" or "international promissory note (Convention of . . .)" must appear in the text of the instrument. This provision is intended to make it difficult subsequently to alter the instrument by adding the required language. However, the required language may be buried in a mass of printed terms and may not be conspicuous. Thus, a bank employee might not recognize the instrument as subject to the Convention and requiring special handling. The United States submits that the language required by article 1 (2) (a) and (3) (a) also be "conspicuous".

#### *Article I (2) (b)*

#### *Czechoslovakia*

This provision should state specifically that a "definite sum of money" includes an amount expressed in two or more currencies with their conversion rates.

#### *Article I (2) (c)*

#### *Mexico*

The expression "at a definite time" is inadequate; all obligations must be met at a definite time. It is more

consistent with legal usage to speak of a bill being payable on demand or on a specific day.

Suggested wording: "Is payable on demand or on a specific day."

#### *Spain*

It seems inaccurate to use the phrase "at a definite time", which is intended to include both maturity "on a stated date" and maturity "by instalments at successive dates", or any other method given in article 8. It would be sufficient for subparagraph (c) to say "maturity" which is defined in article 4 with a cross-reference to article 8. Such is the wording of the French version of the draft ("échéance").

#### *Article I (2) (e)*

#### *Czechoslovakia*

Paragraph (2) and paragraph (3) contain, apparently, necessary requisites of an instrument even in the absence of an express provision that the instrument is not an international instrument when a requisite is missing. The position under the provisions under letter "e" is still more indistinct. To set up the international character of the instrument the drawer or maker is required to situate two specified elements of his written declaration into two different States, but there is not any provision whether all these elements must be included, at one same time, in the bill (the note); in other words it is not clear if the place of drawing, the address of the drawee, the address of the payee, the place of payment are the indispensable requisites of the bill (note). We are observing that the address of the drawer has not been mentioned usually. Perhaps the address of the drawer and the place of payment are not indispensable requisites of a bill (note), if article 51, letter "b" of the draft Convention is taken into respect. Article 11 which explains the above said indistinctness, to some degree, might be included into article 1.

#### *Japan*

In (2) (e), a bill of exchange covered by the Convention is required to show that at least two of the places listed in 2 (e) are situated in different States. It is questionable whether a bill should qualify as an international bill of exchange merely because it shows that the place indicated next to the name of the drawee and the place of payment are situated in different States. The Japanese Government proposes that the places listed in (2) (e) be grouped (e.g. (i) and (ii); (iii) and (v); (iv)) and that (2) (e) should provide that an international bill of exchange governed by the Convention shall show that at least one of the places in one group and one of the places in another group are situated in different States.

In order to determine whether places shown on the instrument are situated in different States, it would be

necessary to require that the instrument indicate the names of the States in which the places are situated. The text of the Convention should state this clearly.

According to article 1 (2) (e) or (3) (e), an instrument showing that only two of the places listed there are situated in different States shall qualify as an international bill of exchange or promissory note governed by the Convention. Thus, an instrument which shows neither the place where it is drawn or made nor the place of payment can qualify as such under article 1. However, these two places are regarded as essential factors determining the law applicable to issues that are not covered by the Convention. Therefore, the Japanese Government proposes requiring that these two places be stated in the text of the instrument as indispensable requisites.

#### *Spain*

One of the "requirements" stands out because it is more a substantive than a formal one; it determines when an instrument is international and may be subject to the Convention. It is dealt with in the subparagraphs (e) under paragraphs (2) and (3), and it would seem to be out of place among the other requirements. This provision states that a bill of exchange/promissory note is an instrument which "shows that . . . two of the following places are situated in different States", but it does not specify the form in which this information must be shown.

The statement of these requirements should be stricter, and it should also explain the form in which the different places are described: whether the State alone is sufficient—as stated in the Commentary—or whether, where appropriate, the city, domicile or street address must be specified. As it stands, article 1 does not say what "places" or domiciles have to be shown on an instrument for it to be complete, and this is critical in view of the distinction in article 4 between a protected holder and an unprotected holder.

Once the mandatory data and the form in which they are to be shown have been specified, it will be possible to establish that an instrument is international by reference to places located in different States.

#### *Article 1 (2) (f)*

#### *Spain*

As regards the formal requisite of the signature, see the comments on article 4.

#### *Article 1 (3) (a)*

#### *China*

Paragraph (3) (a) of article 1: "Contains, in the text thereof, the words 'international promissory note (Convention of . . .)'".

Recommendation: This be changed into "Contains, in the text thereof, the words 'international promissory note (Convention of . . .)', or 'promissory note' if the places indicated on the note show that it is an international promissory note".

#### *Article 1 (4) and article 2*

#### *Spain*

Two qualifications relating to the internationality of instruments are contained in article 1 (4) and article 2.

The former provision carries the formal aspect too far as a test of the internationality of an instrument; it leaves room for the Convention to apply even when it is untrue that the places shown on the instrument are in different States. This has been pointed out by the CSCC, which claims that the drawer is thus enabled to escape regulation by the national law of his State, on his sole initiative, merely by falsifying the fact of internationality. It would be desirable for the Convention to specify more strictly the exact consequences of false statements regarding places, and of an instrument having no real international character.

Article 2 introduces another qualification relating to "internationality", namely that the Convention applies even when the States shown on the instrument are not Contracting States. This provision could have been made directly in the previous article, after the reference to different States, thus making article 2 unnecessary. Although the Commentary gives a detailed discussion of the matter, arguing that the solution in the draft Convention is the most appropriate one for developing the use of such instruments, the problems of conflict of law raised by this formulation should not be passed over; for this reason, the CSB has suggested that a fuller treatment of this issue would be advisable.

## ARTICLE 2

#### *Finland*

According to this article the Convention would be applicable without regard to whether the places indicated on an international bill of exchange are situated in Contracting States. Obviously, this would not cause difficulties insofar as cases concerning such bills of exchange are brought before the courts of a Contracting State. One may assume that a State ratifying the new Convention would not apply the 1930 Convention to a document called an "international bill of exchange" although the title of the document would also correspond to the prescription of a bill of exchange under the 1930 Convention. One might ask, however, what happens if such a case is brought to a court in a non-Contracting State bound by the 1930 Geneva Convention. The document could then satisfy the requirements of the Geneva Convention in employing the term "bill of exchange", even if also containing further language, i.e. the word "international". If the court

applied the Geneva Convention or corresponding legislation, this would imply an alteration in the legal effects of the document. As a whole, however, such changes would seem to be of a fairly minor importance.

## CHAPTER TWO. INTERPRETATION

### ARTICLE 3

#### *Denmark*

This provision seems malapropos and could be used to explain away provisions of the Convention. Similar provisions are not found in other conventions and should therefore be deleted.

#### *Spain*

Article 3 reaffirms a principle already expressed in other UNCITRAL conventions, and one which should be maintained. However, this provision concerns more the objectives to guide interpretation than the criteria to govern it.

### ARTICLE 4

(The comments relating to paragraph (7) of this article (definition of a "protected holder") are set forth under articles 24, 25 and 26, under the heading "holder and protected holder".)

#### *Australia*

Article 1 of the Bills and Notes Convention and the Cheques Convention specifies certain conditions that need to be satisfied before a negotiable instrument can be regarded as an international bill, note or cheque, as the case may be. However, the draft Conventions do not define all of the terms so specified, e.g., 'unconditional order' and 'unconditional promise'. While the BEA similarly does not define such terms for the purposes of Australian law, problems that have arisen over the years in Australia as to the meaning of those terms in the BEA could be overcome in the context of the draft Conventions if the draft Conventions contained appropriate definitions. Australia, therefore, sees merit in having terms such as those defined in the draft Conventions to avoid, as far as possible, problems of interpretation.

#### *Spain*

Article 4 gives a long list of definitions. The procedure is not usual in Spanish statutes, but must be accepted in the case of an international convention. However, some of the definitions appear obvious and unnecessary (e.g. Nos. 1, 2 and 9, the content of which is obvious from other articles in the draft Convention—articles 1 and 8 for example).

#### *United Kingdom of Great Britain and Northern Ireland*

It is strongly felt that the list of definitions should be extended to include for example all parties and relevant terms such as "drawer", "endorser", "endorsee", "guarantor", "acceptor", "visa", "endorsement", "acceptance", "delivery".

#### *United States of America*

Although article 1 requires that an international bill of exchange and an international promissory note contain an unconditional promise or order to pay, article 4 does not define these terms. There are many standard problems in this area which have been resolved by statutes and case law, and they should not be subject to re-opening through the omission of such a definition. A minimum definition of unconditional promise or order to pay should have two elements. One is the exclusion of promises or orders to pay only from a particular fund; the other is the exclusion of instruments which are "subject to" other documents (though not of instruments that merely refer to other documents). The United States proposes that article 4 be amended to add such a definition of "unconditional promise or order".

The draft Condition uses the term "person" throughout, but there is no definition of the term. The United States proposes that article 4 be amended to add a definition of "person" which would include individuals, corporations and other juridical entities, and instrumentalities of a State.

#### *Uruguay*

Article 4 contains definitions of certain terms. We note that it omits to define the drawer of the bill of exchange and the signatory of the promissory note. We suggest that the following definitions be included: "'Drawer' means the drawer of an international bill of exchange", "'Maker' means the signatory of an international promissory note".

#### *Article 4 (6)*

#### *Mexico*

The reference to article 14 appears to imply that anyone receiving an instrument legitimately through a means other than endorsement could not be regarded as the holder, which is an inadmissible position. Consider, among others, the case of transfer *mortis causa*.

#### *Article 4 (10) and article (X)*

#### *Canada*

**Reservations:** There are two very significant provisions in the drafts that Canada considers give unjustifiable scope for variation of the text of the

Convention by domestic law. In article (X) in the Bills of Exchange Convention and article 36 in the Cheques Convention very dangerous scope is provided for local variation. The former would vary the effect of unwritten signatures appearing in some printed, stamped, embossed or mechanical medium; the latter would vary the legal effect of a certification of an international cheque. It appears to us that the considerable advantages of uniformity of international legislation would be very significantly eroded if signatory States were permitted to vary the legal significance of unwritten signatures and certified cheques by local law. Both provisions are of unquestionable importance to the validity and practical value of instruments affected. The scope of the power that the drafts presently propose to give to Contracting States and the significance of the Conventions' provisions dealing with these two points appear to Canada to run strongly contrary to the principle that reservations of ratifying or acceding States may not destroy fundamental obligations of a treaty. Therefore Canada strongly objects to the introduction of those provisions in the draft Conventions and calls for their removal or, in the event that these powers must, in the interest of compromise, be maintained, that they be sharply curtailed.

#### Czechoslovakia

Though we are in favour of retaining paragraph (10), we recommend to place the word "also" after the word "includes" in the first line so as to make clear that the manual signature is to be regarded as the signature of preference.

#### Denmark

For reasons of safety it does not seem reassuring that signatures on cheques and bills of exchange can be affixed either by a stamp or other mechanical means.

#### German Democratic Republic

It is considered appropriate to formulate article (X) proposed in connection with paragraph (10) along the same lines as those followed in article 12 of the United Nations Convention on Contracts for the International Sale of Goods (*Yearbook 1980*, part three, I, B).

#### Germany, Federal Republic of

On account of the increased dangers of forging signatures no substitute of signature should be permitted beside facsimile signatures. To permit other substitutes of signatures could also lead to difficulties in business life because each kind of signature of a person liable on a bill of exchange would have to be examined as to its validity.

#### Hungary

The Hungarian Government is of the opinion that article (X) should harmonize with article 12 of the United Nations Convention on Contracts for the International Sale of Goods (*Yearbook 1980*, part three, I, B).

#### Indonesia

Article 4, paragraph (10) of the draft Convention on International Bills of Exchange and International Promissory Notes lays down the meaning of "signature" which includes a signature by stamp, symbol, facsimile, perforation or other mechanical means.

In this connection, a reservation is entered to the above mentioned article to the effect that a signature placed on an international bill of exchange or a promissory note in Indonesia must be handwritten.

#### Japan

Article 4 (10) is acceptable, but it is not clear what will be the consequences of the application of article (X). What would be the consequences if a signature were affixed on an instrument by some means other than handwriting in the territory of a Contracting State which had made the declaration in accordance with article (X)? Is it only that the signature would not impose any liability on the person who affixed the signature (see article 29 (1)) or that any subsequent party who received the instrument could not become a holder since the instrument would not show an uninterrupted series of endorsements (see article 14 (1) (b))?

#### Mexico

The definition of "forged signature" is confusing in its reference to "wrongful or unauthorized use".

In principle, wrongful use means illegal use. If what is understood is the lack of legal authorization to make use of mechanical means, the situation is one of no signature, not of a forged signature. If the person who signed (used the mechanical means) was not empowered to do so, which appears to be the premise of "unauthorized use", it would seem to be excessive that a forgery of this kind should affect third parties in good faith. Anyone having the facilities and the legal entitlement to sign using mechanical means must be responsible for safeguarding these facilities and must bear the corresponding risk.

#### Norway

The concept of "forged signature" is dealt with both in article 4 (10) and in article 23 (3). We suggest article 23 (3) be deleted and the rule be transferred to article 4 (10).

We will at this stage neither support nor oppose the inclusion of article (X) in the final text. However, we call attention to the difficulties which may arise from reservations according to the article.

#### *Spain*

The definition of "signature" gives cause for concern. We are obliged to state our serious reservations about a provision under which a statement of will used to establish such rigorous legal effects of obligation and liability as those relating to bills of exchange may be expressed by the means specified in article 4 (10). This was the opinion submitted by the CSB. Although article (X) of the Convention, resorting to the reservation mechanism, does provide that States may require the signature to be handwritten, that option does not circumvent the problem. The uncommon variety of the methods of signing gives added importance to the issue of forgery. The term "forged signature" is also defined in paragraph (10). In regulating endorsement (article 23), the draft Convention relates the issue of forgery to that of an agent or representative acting without authorization, and there is also reference to this area in articles 30 and 32. It would be desirable for the definition of a forged signature and for the applicable regulations to be revised jointly.

#### *Union of Soviet Socialist Republics*

Article (X) proposed in connection with paragraph (10) would enable those States under whose legislation the validity of a contract requires a handwritten signature on the instrument, or where the word "signature" traditionally implies handwriting, to participate in the Convention. For the purpose of securing recognition by other Contracting States of the declaration provided for in this article, it would be desirable to include in the draft an article similar in sense to article 12 of the United Nations Convention on Contracts for the International Sale of Goods (*Yearbook 1980*, part three, I, B). It might also be necessary to introduce into the text of article (X) clarifications in respect of the signatures to which the declaration will refer.

#### *United States of America*

There are definitions of "forged signature" in both article 4 (10) and article 23 (3). The definition in article 23 (3) is illustrative only and incomplete. It seems to be both correct and of general applicability, but is limited by its terms to "the purposes of this article"—a limitation which the United States finds unnecessary and confusing. The limitation suggests that this definition is inaccurate in other contexts. The United States therefore proposes that article 4 be amended to provide a complete definition of "forged signature", which would include both unauthorized signatures and those beyond the scope of an agent's authority, and would be used consistently throughout the Convention. Such a

definition should include the concepts from articles 4 (10) and 23 (3) and make their separate provisions unnecessary.

#### *Yugoslavia*

The answer to the question whether a bill should insist on a handwritten signature or should it be interpreted, as in article 4 (10), in broader terms, is not a simple one. This is all the more so, since it is difficult to prove, by virtue of article 23 (3), that an unauthorized person has signed the instrument if facsimile is used instead of signature.

#### *Article 4 (11)*

#### *Czechoslovakia*

We would agree to this provision, provided that the notion of fictitious currency established by intergovernmental institutions or intergovernmental treaties will be specified with greater precision.

#### *Denmark*

We support the inclusion of article 4 (11) in the final text.

#### *Finland*

This provision is considered useful and its retention is therefore supported.

#### *German Democratic Republic*

The proposal to add a new paragraph (11) concerning the inclusion of a monetary unit of account in the terms "money" or "currency" is acceptable. If such a provision is adopted, it will be necessary, however, to refer to a monetary unit of account also in article 71.

#### *Union of Soviet Socialist Republics*

It appears that acceptance of paragraph (11) would extend the scope of use of international instruments by making it possible to draw instruments in transferable roubles and other units of account. The use of a unit of account to express the sum payable by an instrument or the currency of payment does not in principle conflict with the other provisions of the draft Convention pertaining to the sum payable by an instrument (articles 6, 7 and 71).

#### *United States of America*

The article includes only a partial definition of "money" and "currency"—one relating only to SDRs.

The partial definition does not make clear whether it refers only to official physical currency of a State (such as dollar bills), but in article 71 on payment it seems to be used in a broader sense so as to include immediately available credit. The United States therefore proposes that article 4 (11) be amended to include in the definition of "money" and "currency" both official physical currency and immediately available credit.

The United States supports the inclusion in the final draft of the Convention of the language of article 4 (11) which is now in brackets.

#### *International Monetary Fund*

We note that article 4 (11) of the bills and notes convention and article 6 (9) of the cheques convention contain a proposed definition of "money" or "currency" which reads:

"'Money' or 'currency' includes a monetary unit of account which is established by an intergovernmental institution even if intended by it to be transferable only in its records and between it and persons designated by it or between such persons."

It occurs to us that this definition might be improved. For this purpose we would suggest:

"'Money' or 'currency' includes a monetary unit of account which is established by an intergovernmental institution and which is transferable among the members of this institution or other entities as the institution may prescribe."

An important effect of this provision would be to make it clear that instruments could be drawn or made subject to the conventions that call for payment in a specified currency while being denominated in special drawing rights. It would also permit participants in the Fund's Special Drawing Rights Department and other holders prescribed by the Fund to avail themselves of the rules of the conventions, should they find this to be of advantage, in respect of instruments that they might issue that are both denominated and payable in special drawing rights. These effects are explained in the commentary at paragraphs 24 and 25.

We note that the proposed definition of "money" or "currency" is still tentative. We would urge that it be adopted substantially in the form that we have suggested and that consequential amendments to the conventions be made accordingly.

#### **ARTICLE 5**

##### *Denmark*

According to this provision a person is also in bad faith if he could not have been unaware of the existence of a fact. In English, the correct term for this concept is "constructive knowledge" the implication of which would seem to be that a person wilfully seeks not to

acquire knowledge of some specific issue. A person should also be seen as acting in bad faith if he ought to have acquired a special knowledge.

#### *Germany, Federal Republic of*

According to this provision, "knowledge" is considered to be present not only in the case of positive knowledge but also in the case, in which a person could not have been unaware of the existence of a fact. According to the Commentary, this wording implies a presumed knowledge. This might lead to the objectionable conclusion that the person concerned has the burden to prove his ignorance. Moreover, this definition does not make quite clear whether it corresponds to "gross negligence" under article 16, paragraph 2 of the Geneva Law on Bills of Exchange or to "knowingly acting" under article 17 of the Geneva Law on Bills of Exchange. It is to be feared that with that unprecise clause the courts in the various States would arrive at completely different requirements as to the element of the knowledge of a fact.

#### *Spain*

The "general provisions" on interpretation end with article 5, which interprets what is understood by having knowledge of a fact. The first part of the provision is unnecessary; there is no need to say that "a person is considered to have knowledge of a fact if he has actual knowledge of that fact". The second part of the article establishes a presumption: a person is considered to have knowledge of a fact if he could not have been unaware of its existence. In view of the great importance that knowledge or unawareness of a fact will in many cases assume under the draft Convention, this presumption should clearly be more carefully refined and regulated. The CSCC made this point and recommended greater clarity as to the meaning of the presumption.

It must be borne in mind that the holder's protection will fundamentally depend both on the instrument's being complete and on the knowledge we are discussing here. This system is in conflict with the Spanish one, which is based on the presumption of "*bona fides*".

#### **ARTICLE 6**

##### *Article 6 (a)*

##### *Czechoslovakia*

We recommend that this provision should include the provision set forth in article 7 (4) according to which it is necessary to indicate in the instrument the rate of interest, and that otherwise the interest clause is to be regarded as not written.

*Spain*

Articles 6 and 7 establish, at some length, the provision that instruments may be paid with interest. Such provision does not exist in Spanish law. It does in the Geneva system, but in a more restricted form. This is a laudable innovation, but the regulations are not entirely satisfactory.

*United States of America*

Article 6 provides that an instrument is deemed to be payable for a definite sum even though it is to be paid with interest. There is significant statutory and case law in the United States that the interest rate must be stated, though the modern commercial tendency is to issue "floating rate" notes in which no fixed rate is stated. This tendency is reflected in the recent modification of UCC section 3-106 in Louisiana to permit "floating rate" notes to be negotiable. The United States therefore suggests that article 6 (a) be amended to clarify whether interest rates must be fixed or not and suggests that the amendment permit "floating rate" to be negotiable. Such an amendment would ensure wider application and greater use of the Convention.

*Article 6 (b) and (c)**Spain*

The provision in article 6 for instruments with successive instalment dates appears to us to raise serious problems. This provision may prove to be well-inspired, but it requires greater development in the Convention of specific requirements regarding acceptance, payment, regularity of payment, etc. For example, article 69, which states that the holder is not obliged to take partial payment, should provide an exception for instruments with successive instalments. In any case, we believe that the provision for instalments, combined with that for two or more jointly and severally liable parties, could make the discharge mechanism for bills of exchange exceptionally complicated.

*Yugoslavia*

An instrument payable by instalments is not provided for under the Geneva Conventions, and is contrary to the notion of the instrument as an abstract transaction. If this draft article is accepted, an instrument payable by instalments will create problems with respect to protest and presentment for payment.

**ARTICLE 7***Article 7 (1)**China*

Paragraph (1) of article 7: "If there is a discrepancy between the amount of the instrument expressed in

words and the amount expressed in figures, the amount of the instrument is the amount expressed in words."

**Recommendation:** This be supplemented by adding "... in case there is a mistake in the amount expressed in words, too, the instrument should be dishonoured."

**The reason:** It is impossible to deal with an instrument in which the amount expressed in figures is 500,000 and the amount expressed in words is "five hundred and five hundred", with the word "thousand" missing.

*Czechoslovakia*

We recommend that this provision specify that the lowest amount be retained in those cases where the amount is expressed several times in words or several times in figures and there is a discrepancy between them.

*Article 7 (2)**Czechoslovakia*

It should be clarified whether the sum payable by an instrument is a "definite sum of money" for the purposes of article 1 (2) (b) in those cases where the currency indicated has the same description in different States but is not the currency of the place of payment (e.g. payment is to be made in Switzerland in dollars).

*Article 7 (4)**China*

Paragraph (4) of article 7: "A stipulation stating that the sum is to be paid with interest is deemed not to have been written on the instrument unless it indicates the rate at which interest is to be paid."

**Recommendation:** This be supplemented by adding "... or indicates that interest is to be paid at international market rate at a definite time and place".

**The reason:** Considering the constant changes in international market rates, it is hardly possible to fix the interest rate for a time-bill in advance; sometimes the interest rate is to be calculated at a floating rate, i.e., according to the international market rate on the day of payment.

*Norway*

According to paragraph (4), a stipulation in the instrument stating that the sum is to be paid with interest, is without effect unless it indicates the rate at which interest is to be paid. It is unclear whether a reference to a rate of interest extrinsic to the instrument (for example to a certain rate in a certain market) will

be recognized. We suggest that paragraph (4) be drafted in the same way as article 6 (d) according to which the instrument may refer to an extrinsic rate of exchange.

#### *Spain*

Regarding article 7 (4), under which the interest clause is deemed not to have been written unless it indicates the rate of interest, we feel it would be preferable to establish a presumption, rather than giving scope for inadequate statement by the drawer.

#### *Yugoslavia*

Under articles 6 and 7, all instruments, not only those payable at sight, bear interest. If such a broad conception is accepted, there may be difficulties in case of the failure to indicate the date of the instrument or the date of payment. Therefore, it is not clear how the interest on such instruments will be calculated.

### ARTICLE 8

#### *Japan*

Article 8 is generally acceptable. However, in view of the following points, it needs further study.

(1) Article 8 (2) is not sufficiently clear as regards the endorser. It is unclear whether or not this provision imposes a secondary liability on an endorser making an endorsement after maturity.

(2) The Convention should provide in its text rules on the calculation of time and the treatment of holidays additional to article 8 (8).

#### *Article 8 (1)*

#### *China*

Paragraph (1) of article 8: "An instrument is deemed to be payable on demand: . . . (b) If no time of payment is expressed."

Recommendation: There should be an express stipulation on how to determine the period of its circulation or validity (i.e., prescription).

#### *Denmark*

We find it undesirable, as these rules are international, that according to paragraph (1) (a) it is sufficient that the bill of exchange contains ". . . words of similar import . . .". It seems most practical to use a uniform terminology on the time for payment. The said provision might therefore appropriately conclude with the words ". . . at sight or on demand or on presentment".

#### *Article 8 (2)*

#### *Canada*

Canada believes the words "acting after maturity" should be added to the end of the section as presently drafted to ensure that the instrument is only regarded as being payable on demand as regards those persons who become parties to it by their signature after maturity.

#### *Article 8 (3)*

#### *Mexico*

See comments on article 1 (2) (c) regarding the expression "at a definite time".

#### *Article 8 (4)*

#### *China*

To be amended as follows: "The time of payment of an instrument payable at a fixed period after date starts at the date of the instrument and ends at the date when payment becomes due."

#### *Article 8 (5)*

#### *Mexico*

The text should state that the maturity of a bill payable at a fixed period after sight is determined by the date of its presentation for acceptance. What happens if the instrument is not accepted?

Suggested wording: "The maturity of a bill payable at a fixed period after sight is determined by the date on which it is presented for acceptance."

#### *Article 8 (7)*

#### *Mexico*

The date of presentation should be indicated on the note. It is suggested that this paragraph be brought into line with the solution given in connection with article 38, paragraph (3).

### ARTICLE 9

#### *Article 9 (1) and (2)*

#### *Denmark*

The provisions of paragraph (2) (b), allowing payment to be made to two or more payees, may prove impractical where the addresses of all payees are not

known, except where in the alternative the instrument is payable to any of them.

#### *Indonesia*

The Indonesian Commercial Code does not contain a provision whereby a bill or note may be drawn or made by two or more drawers or makers or may be payable to two or more payees.

It is to be noted that if the drawers/makers or payees are regarded as a unity, it is not contrary to the civil law system which considers the issuance of a bill or note as an underlying transaction between the drawer and the payee.

#### *Uruguay*

We suggest an improvement in the drafting so that the text would read as follows:

(1) "A bill may:

"(a) Designate two or more payees"  
"..."

(2) "A note may:

"..."  
"(b) Designate two or more payees."

#### *Article 9 (3)*

#### *Czechoslovakia*

The final sentence is not clear. Payment to all holders to be made at the same time will be difficult from the technical point of view unless divisible payment would be split in equal portions among all holders.

#### *Spain*

Article 9 raises an interesting problem by providing that, when there are two or more payees, they must exercise their rights jointly unless they are designated in the alternative. It would seem that the rule should be the reverse, as suggested by the CSCC. Similarly, it would be desirable to indicate that the parties are jointly and severally liable when, for example, there are two or more drawers.

That the parties are jointly and severally liable is clear from article 65, but problems may arise between this and the requirement for holders to exercise their rights jointly. Thought should be given to the case of a co-payee-endorser, with joint and several liability, who makes payment to a subsequent holder and who later, when he wishes to recover from those liable to him under article 67, is unable to do so without co-operation from the other co-payees; or again, the case of two or more drawers of whom one makes payment to redeem the instrument and has later to recover from the acceptor.

#### *Uruguay*

The rule in article 9, paragraph (3) is clear, but is perhaps lacking in that it does not refer to the case where the instrument is drawn in favour of A and/or B, as mentioned in the commentary (paragraph 6).

We suggest that the following text be added:

"If it is indicated on the instrument that it is payable to alternative or joint payees, it shall be understood to be payable to all those designated."

### ARTICLE 10

#### *Article 10 (a)*

#### *China*

Article 10: "A bill may: (a) Be drawn by the drawer on himself;"

Recommendation: This be supplemented by adding "and regarded by the holder as an international promissory note;"

The reason: A bill drawn by the drawer on himself is by nature a promissory note, so the holder may treat it in pursuance of the regulations governing international promissory notes.

#### *Article 10 (b)*

#### *Canada*

This paragraph may only be properly construed if read in conjunction with paragraph (a) on the same article. On the principle that independent provisions of a statute should stand alone, paragraph (b) should be amended to read "be drawn payable to the drawer's order".

### ARTICLE 11

#### *China*

Paragraph (1) of article 11: "An incomplete instrument which satisfies the requirements set out in subparagraphs (a) and (f) of paragraph (2) . . . may be completed and the instrument so completed is effective as a bill or a note."

Recommendation: The article be deleted.

The reason: According to article 1, an international bill of exchange and an international promissory note are written instruments which must satisfy the requirements set out in subparagraphs (a), (b), (c), (d), (e) and (f) respectively of paragraphs (2) and (3). The stipulation that a written instrument which satisfies only the requirements set out in two of the six subparagraphs is an "incomplete instrument" which may be completed contradicts the spirit of article 3. At the same time, by

accommodating itself to unreasonable circumstances, thus reducing the quality of an international instrument, and by failing to specify who is to complete an "incomplete instrument", the article may give rise to unnecessary disputes.

#### Czechoslovakia

We suggest that it be specified whether the completion of an instrument is effective "*ex tunc*" or "*ex nunc*". Solution of this question may often be of importance in practice.

#### Yugoslavia

An incomplete instrument is often used in international transactions, therefore it is commendable that the provisions relating to such an instrument were included in the draft Convention. Here, it is proposed that the draft provisions concerning such instruments be amended. In order to ensure legal security, it is necessary to specify, in addition to the requirements set out in article 11, that an incomplete instrument should bear the signatures of the drawer and the acceptor or the endorser. In other words, the Convention should provide that only certain persons may complete an incomplete instrument.

A distinction between an incomplete instrument and an ineffective instrument is not clear. The Convention should stipulate that in the case of an incomplete instrument one or more essential elements are "deliberately" omitted so that they may be completed later on by an authorized person (indicating the authorized persons).

Under the draft Convention, the holder of an incomplete instrument is not a protected holder, which means that defences based on the underlying transaction may be set up against him. This solution is not advisable as it may slow down the circulation of an instrument.

### CHAPTER THREE. TRANSFER

#### Spain

We propose that the chapter heading in the Spanish version be changed to "*Transmisión*", which is the more correct legal term when referring to bills of exchange.

### ARTICLE 12

#### Mexico

The transfer of instruments other than by endorsement is not regulated. This omission suggests the impossibility of transferring the instrument by means other than through negotiation, which is inadmissible. It is suggested, therefore, that the opening phrase read:

"For the purposes of this Convention, an instrument is transferred:".

#### Uruguay

We should like to see added to article 12 a provision establishing clearly that the instrument is transferred by endorsement even if it does not contain the words "to order".

The absence of a requirement that these words be entered on the instrument is due to the context and is explained in the commentary thereon (especially the commentary on article 16), but the clarification would in our view be desirable.

### ARTICLE 13

#### Spain

The most important point to make about this chapter, regulating endorsement, is that it enables the instrument to be converted into a bearer instrument. Although the payee has to be specified in person when the instrument is issued, the endorsement provided for in the Convention not only makes it possible, but apparently normal practice, to transfer the instrument to bearer; article 13 provides that an endorsement may be special, in which case the endorsee is identified, or in blank. The usual endorsement would thus appear to be in blank; it may indicate that the instrument is payable to any person in possession (article 13), but if there is no indication the signature is sufficient to make the person in possession a legitimate holder (article 14). Thus endorsed, an instrument functions as a bearer instrument and may be retransferred "by mere delivery" to a new transferee (article 12). Moreover, since a bill may be drawn to the drawer's own order (article 10), it can be established as a bearer instrument by the drawer himself.

The ease with which instruments can be transferred and transferees legitimated under these provisions might prove excessive. The facility for these instruments to be issued and transferred as bearer instruments may cause them to be regarded with greater mistrust. For example, the danger which Italian law attempts to meet by the prohibition in article 2004 of the *Codice Civile* might prove a more serious one in the sphere of banking; banks would be provided with a valuable tool which could be used, for example, for collecting funds through branches or subsidiaries abroad by issuing bearer instruments, and this could be seriously detrimental to the financial system of a particular State.

The facilities provided for in this chapter are in conflict with the present legislation on bills of exchange in Spain, which does not allow bills to be made payable to bearer; blank endorsement is provided for and the "bearer" of a bill may retransfer the instrument but he may not exercise the rights conveyed unless the endorsee's name is specified.

Other brief comments will now be made on this chapter.

The provision that endorsement and mere delivery should be means of transfer omits any reference to the possibility that an instrument may be transferable by other means provided for in national legislations, although such transfers place the transferee in a similar position to the transferor.

As the CSCC has pointed out, it would be desirable for article 13 to require the date of endorsement to be specified; it could be relevant in establishing the protected holder's status and it would also clarify the time at which a mere signature on an instrument becomes effective as a blank endorsement. Although this requirement is stated later with respect to the guarantee, the right place for it to be stated is here.

#### *Article 13 (2) (a)*

##### *Czechoslovakia*

We recommend an amendment to this provision to the effect that an endorsement in blank consisting of a mere signature must be written on the back of the instrument, or on its *allonge*.

#### **ARTICLE 14**

(The comments relating to article 14 (1) (b) are reproduced under article 23.)

#### *Article 14 (1) and (2)*

##### *Czechoslovakia*

This provision proceeds from the difference between "holder" and "protected holder". It would be possible to employ its paragraphs (1) and (2) for a formulation of who is to be considered as a protected holder, provided that such holder did not obtain the instrument in the manner indicated in paragraph (3). In addition, the provision of paragraph (3) as now drafted appears unsuitable, since article 15 grants certain rights also to a person who did not obtain the instrument in such manner.

#### *Article 14 (3)*

##### *China*

Paragraph (3) of article 14: "A person is not prevented from being a holder by the fact that the instrument was obtained under circumstances, including incapacity or fraud, duress or mistake of any kind, that would give rise to a claim to, or to a defence upon, the instrument."

Recommendation: This be changed into "A person who obtained the instrument *bona fide* is not prevented

from being a holder by the fact that the instrument was obtained under circumstances, of which he had no knowledge, including incapacity or fraud, . . ."

The reason: A holder must be a person who obtained the instrument *bona fide* and who had nothing to do with those circumstances.

##### *Mexico*

The proposed wording is pedestrian. The following text is suggested in its place: "A person does not lose his status as a holder even when he has obtained the instrument under circumstances that would give rise to a claim to, or to a defence upon, the instrument, including incapacity or fraud, duress or mistake of any kind."

#### **ARTICLE 16**

##### *Czechoslovakia*

It should be specified that the type of clause referred to in article 16 makes further transfer impossible. Since the transferee is placed in the position of a mere collection agent, the clauses are improperly confused with collection endorsements under article 20.

##### *Denmark*

From the point of view of Danish law the proposed provisions of the Conventions would seem to hamper transactions involving bills of exchange and cheques by introducing some kind of "second-class" bills of exchange and cheques which are non-negotiable but more or less simple claims. The rule has broader scope than its Danish equivalents as we bypass the rules on simple claims. The rule appears to be practical, however, seeing that it is part of an international code.

##### *Netherlands*

Where the drawer or the maker indicates on the instrument that it is "not transferable", "not negotiable", "not to order" etc., the instrument is, under article 1 (2) or (3) of the draft Convention, apparently still a negotiable instrument. If this interpretation is correct, the rule in article 16, that the transferee does not become a holder, is acceptable. To the words "except for purposes of collection" should be added the words "if the instrument has been so endorsed to him".

The consequences of the prohibition of further transfer by an endorser are, under Dutch law (article 114 K) and the ULB (article 15), different from those obtaining under article 16. When the endorser prohibits further transfer, the instrument may be further negotiated, but the endorser does not then guarantee acceptance or payment to persons to whom the instrument is endorsed subsequently. In other words, an endorsement prohibiting further transfer

does not destroy negotiability, but the endorser excludes his own liability to persons subsequent to his endorsee.

It is suggested that this kind of restrictive endorsement, if retained in the draft Convention, should be dealt with separately, e.g. in article 40 (2).

The endorsement which prohibits further transfer with the effect that the transferee does not become a holder except for purposes of collection belongs more properly in article 20 and should therefore not be dealt with in article 16.

#### *Norway*

The article deals with two somewhat different situations: on the one hand a restrictive statement included into the instrument by the maker or the drawer and on the other hand a restrictive endorsement. We question the convenience of combining the two situations and suggest that restrictive endorsements are entirely dealt with in article 20.

The payee of an instrument into which the drawer or the maker has inserted a restrictive statement, may not further transfer the instrument, not even with the effects of an ordinary assignment. This is different under the Geneva Convention (cf. ULB article 11). We are not convinced that the solution of the draft Convention is the best one.

#### *Spain*

Article 16 raises two issues: first, there is no reason why the person holding a document which is not to be transferred should not still be known as the holder, even if he is subject to that prohibition; second, the non-transferability clause should have different effects according to whether the person who stipulates it is the drawer (or maker) or an endorser, since this affects the position of any person to whom the instrument is transferred in spite of the prohibition (if the clause has been added by an endorser, a holder in that position must retain all his rights against previous endorsers and against the drawer).

#### *United States of America*

This article provides that words prohibiting negotiation prevent a transferee from becoming a holder "except for purposes of collection," whether these words are added by the drawer at issuance of the instrument or by the endorser later. The Convention thus combines and confuses two situations: (1) that in which the drawer or maker issues an instrument which does not have the normal transfer characteristics of negotiability, and (2) that in which an endorser makes a restrictive endorsement. The United States thus proposes that the article be amended to delete any reference to words added by an endorser (delete "or an endorser in his endorsement") and limit the article to words originally

placed on the instrument by the issuer. If necessary, the deleted language can be transferred to article 20.

#### *Uruguay*

The intent of article 16 is not clear.

In the situation referred to in the provision, we understand that collection by the holder is not allowed unless the latter can prove that he is authorized by the drawee or by a banking or financial institution the latter has designated for purposes of collection or unless the instrument has been endorsed for collection in the manner provided for in article 20.

We believe that the wording would be improved by a reference to article 20, even if only in brackets.

### ARTICLE 17

#### *Canada*

By providing that an endorsement must be unconditional, this provision appears to us capable of bearing the interpretation that a conditional endorsement is no endorsement at all. Canada supports the policy of the amendment as far as it is explained in paragraph 191 of UNCITRAL document A/CN.9/210 of 12 February 1982 (*Yearbook 1982*, part two, II, A, 1). But we believe the policy could be better implemented if a provision in the terms of United Kingdom Bills of Exchange Act, section 33 (Canadian Bills of Exchange Act, section 66) were substituted.

Section 66 of the Canadian Act reads as follows:

"66. Where a bill purports to be endorsed conditionally, the condition may be disregarded by the payer and payment to the endorsee is valid, whether the condition has been fulfilled or not."

#### *China*

Article 17: "(1) An endorsement must be unconditional. (2) A conditional endorsement transfers the instrument whether or not the condition is fulfilled."

Recommendation: The two paragraphs seem to be contradictory. If an endorsement must be unconditional, it is essential to state clearly whether or not a conditional endorsement is binding on the parties to the instrument when the endorsement is made and the instrument transferred.

#### *Hungary*

According to paragraph (2)—at first sight surprisingly—the conditional endorsement transfers the bill of exchange whether the condition is fulfilled or not. Examining more thoroughly the reason of this rule, it is probable that it has the same meaning as expressed by the Geneva Convention, that the endorsement can be

considered as non-written. It appears to be an ambiguous drafting.

#### Norway

Article 17 (2) deals with the conditional endorsement. With reference to paragraph 2 of the commentary to article 17, we call attention to the concept of the "protected holder", cf. articles 4 (7) and 5, and the requirement of the holder having no knowledge of claims to or defences upon the instrument. The inclusion of the condition into the endorsement may prevent a holder from qualifying as a protected holder.

#### Spain

A condition attached to an endorsement is ineffective but it does not invalidate the endorsement. This provision in article 17 would appear debatable and in conflict with article 18, which makes ineffective an endorsement in respect of part of the sum.

## ARTICLE 18

#### Mexico

The solution proposed in this article is inadmissible: one party is the material holder of the instrument, and the other party is the one authorized to exercise the rights which derive from the instrument; if there is a partial endorsement and the instrument is transferred, since the endorsement is ineffective the holder cannot exercise his rights, and the endorser, for his part, is similarly unable to do anything, since he has parted with the instrument.

Suggested wording: "Partial endorsement coupled with the transfer of the instrument has the same effect as full endorsement; otherwise the endorsement is regarded as not having been placed on the instrument."

#### Spain

In view of the prohibition of partial endorsement, it should be remembered that the draft Convention makes provision, firstly, for instruments to mature by successive instalments (article 6) and, secondly, for them to be endorsed after maturity (article 22) and, *a fortiori*, after any of the instalment dates. Presumably, endorsement in respect of part of the sum is permissible when it applies to the total of the outstanding instalments. In any case, this provision might be clarified.

#### United Kingdom of Great Britain and Northern Ireland

A minor criticism in relation to the commentary in respect of partial endorsement is that what does or does not create a partial endorsement does seem to be somewhat excessively refined.

## ARTICLE 20

#### Czechoslovakia

It should be specified that a case where a court authorizes recovery on an instrument is covered by this provision.

#### United States of America

This article does not clearly require that the endorsement of a collection endorsee be a collection endorsement, i.e., one that contains the words mentioned in the first paragraph. It now simply says that the purpose must be "for purposes of collection" and this can be done without using the form of a collection endorsement. The United States therefore proposes that the article be amended to clarify the requirement that any taker after a collection endorsement is bound thereby, regardless of intervening ordinary endorsements, by deleting the words "purposes of" from article 20 (1) (a).

#### Yugoslavia

Under article 20 (1) (b), the endorsee "may exercise all the rights arising out of the instrument" which is a broadly based authorization, in particular when an instrument is transferred to the endorsee by an endorsement "through an agent".

## ARTICLE 21

#### China

Article 21: "... qualifying as a holder..."

Recommendation: The term "qualifying as a holder" should be defined or revised.

The reason: A legal term has a definite meaning and should be used uniformly in the two drafts. Terms that are not the same should be defined clearly to avoid confusion.

#### Czechoslovakia

The draft Convention does not contain a general provision on cancelling endorsements and on the effects of such cancellation.

#### Spain

The method and effects of transferring an instrument to a prior party or to the drawee requires more detailed treatment than it is given in article 21. In any case, mere delivery hardly seems adequate. For this reason the CSCC invoked the principle of literality and advised that endorsement should be required for transfer to a prior party.

## ARTICLE 22

### *Denmark*

The provision is vague on whether transfer after maturity is invalid.

### *Netherlands*

This provision deals with the transfer of an instrument after maturity: an overdue instrument may be transferred in accordance with article 12. Article 22 does not state the effects of such a transfer. One must therefore look to other provisions of the draft Convention, in particular article 4 (7) (b). That provision denies protected holder status to a holder who takes the instrument after the time-limit provided by article 51 for presentment for payment has expired.

It follows that the taker of an overdue instrument, being a holder, takes it subject to the claims and defences specified in article 25 except where his transferor is a protected holder (cf. shelter rule of article 27 (1)). The policy underlying such a result is presumably that the fact that the instrument is overdue is evident from the face of the instrument and that consequently the taker is put on notice.

The above interpretation depends on whether the words "after maturity" (used in article 22) mean the same as the words "after the time-limit for presentment for payment has expired" (used in article 4 (7) (b)).

(a) In respect of instruments not payable on demand the "time-limit for presentment for payment" is the date of "maturity" or the business day which follows (article 51 (e)). "Maturity", according to article 4 (9), "means the date of payment referred to in article 8". Article 8 specifies the "time of payment" of an instrument payable at a fixed period after date, the "maturity" of a bill payable at a fixed period after sight and the "maturity" of a note payable at a fixed period after sight.

It may be assumed that in respect of instruments not payable on demand and for the purposes of article 4 (7) (b) and article 22, the "time-limit for presentment for payment" coincides with "maturity", except for the business day which follows maturity. The inconsistency, as noted, could be removed by the use of one term only.

(b) In respect of instruments payable on demand the "time-limit for presentment for payment" is up to one year from the date of the instrument (article 51 (f)). The "maturity" of such instruments is the date on which they are presented for payment (article 8 (6)). The draft Convention does not state clearly whether the holder of a demand instrument must effect protest of non-payment when the instrument is dishonoured upon first presentment, on pain of losing his right of recourse against secondary parties, or whether he is entitled to re-present it for payment, provided he does so within one year of its date.

In the first eventuality the "maturity" of a demand instrument which is presented for payment before the expiry of the time-limit of one year does obviously not coincide with the "expiration of the time-limit for presentment for payment" to which article 4 (7) (b) refers. In such a case, can the holder who takes after maturity but before the expiration of the one year period qualify as a protected holder? It is arguable that, if the holder took the instrument without notice of the fact that he took it after maturity (and of the fact that it was dishonoured by non-payment) he is, if he otherwise complies with article 4 (7), a protected holder. This would appear to be the approach of Section 3-302 (1) (c) of the UCC.

In the second eventuality the "maturity" of a demand instrument, under the current definition of article 8 (6), would correspond to the date on which the time-limit for presentment for payment expired only if the date of presentment for payment coincides with the last day of the time-limit of one year.

It is suggested, therefore:

- (i) that the issue of the transfer of a demand instrument after "maturity" be re-examined;
- (ii) that the use in the draft Convention of the terms "expiration of the time-limit for presentment for payment", "maturity", "time of payment" be reviewed;
- (iii) that the rights of a taker of overdue instruments be specified in article 22.

It may be noted that the issue of presentment for payment of a demand instrument within the time-limit of one year of its date also arose at the Conference which adopted the Geneva Uniform Laws. The issue was resolved in favour of the rule (not reflected in the uniform law) that renewed presentment and timely protest for non-payment may be made during the one-year period. The Conference approved the interpretation given by the Netherlands delegation in a written observation, as follows (C.360.M.151, 1930.II, p. 284)

### "Article 19"\*

"Article 19 regards an endorsement after the expiration of the time-limit fixed for drawing up the protest as a cession.

"Let us suppose that payment has been demanded without success on a sight bill, that protest has not been made, that the time-limit laid down in article 33 has not yet expired and that the bill of exchange is then endorsed.

"When the endorsee presents the bill for payment, can the plea be advanced against him that the endorsement was made 'after expiration of the limit of time fixed for drawing up' the protest and that

\*Article 19, now article 20 ULB, reads as follows:

"An endorsement after maturity has the same effects as an endorsement before maturity. Nevertheless, an endorsement after protest for non-payment, or after the expiration of the limit of time fixed for drawing up the protest, operates only as an ordinary assignment . . ."

consequently the rigorous provisions of article 19 are applicable to it. If so, the endorsee would be the victim of circumstances which he could not have known from the bill of exchange. Nevertheless, a decree by the Egyptian Mixed Tribunal, published in the *Journal des Tribunaux mixtes d'Egypte* on February 5th/6th, 1930, adopted this unfortunate conclusion in a similar case.

"The Netherlands delegation is of the opinion that such an interpretation is contrary to that of the Uniform Regulation. It considers that when a sight bill has been presented for payment and when, on refusal of payment, protest has not been made, the time-limit fixed for drawing up the protest has not expired within the meaning of article 19.

"If this is the Conference's opinion on these matters, the Netherlands delegation will propose no amendment."

#### *Uruguay*

Article 22 allows transfer by endorsement after maturity. We feel that this is not desirable because it implies the circulation of an instrument after its maturity. It also implies a solution that is in conflict with our internal system.

We suggest that, after maturity, endorsement should be allowed only for judicial or extra-judicial collection.

### FORGED ENDORSEMENTS

#### ARTICLE 23

(and references to article 14 (1) (b))

#### *Australia*

A legal principle of general application is that a person whose signature is forged on a negotiable instrument is not liable on the instrument. The draft Conventions confirm this principle (article 30 (Bills and Notes Convention), article 32 (Cheques Convention)). However the draft Conventions, and the BEA differ in relation to the effect of a forged endorsement on the liability of other parties on the instrument.

The BEA renders a forged endorsement wholly inoperative and no rights may be obtained through or under it. Under the Act, a holder or a holder in due course has no rights against persons who signed before the forgery and payment of the holder of the instrument will not discharge the payer if the holder claims through a forged endorsement.

Under the draft Conventions, however, a person who acquires an instrument after a forgery is nevertheless a holder and has all the rights conferred on holders by the Conventions (article 14 (1) (b) (Bills and Notes Convention), article 16 (1) (c) (Cheques Convention)).

Such a person will be able to sue all parties to the bill, whether they became parties before or after the forgery (article 68 (Bills and Notes Convention), article 61 (Cheques Convention)). However, the draft Conventions provide a statutory right to compensation in favour of any party for damages that the party may have suffered because of the forgery (article 23 and 25 respectively). In short the *bona fide* holder is protected and may sue any party to the instrument notwithstanding the forgery.

Although the principles relating to the consequences of taking a forged instrument differ under the draft Conventions, Australia does not see the Convention provisions as posing any major barrier to the acceptance of the scheme contained in the Conventions. The problem of forged endorsements arises only rarely in relation to trade bills, which, in most cases, pass directly from the drawer to the collecting bank and there is generally an absence of intervening parties.

#### *Denmark*

It should be clearly specified whether the right to recover compensation for any damage suffered because of forgery shall be upheld against other endorsers, cf. the principle laid down in section 10 of the Danish Cheques Act and section 7 of the Danish Bills of Exchange Act.

#### *Indonesia*

This article, as does the Indonesian Commercial Code, lays down the legal effect of a forged endorsement on a bill or note. The two legal systems are in disagreement as to the legal consequence of such forged endorsement.

In this connection we are in agreement with the conclusion of the Working Group, set forth in the commentary, which establishes a compromise between the two legal systems:

(a) A forged endorsement or an endorsement signed without authority is effective as an endorsement if it is part of an uninterrupted series of endorsements.

(b) Any party who suffered damages because of the forgery has a right to damages against the forger and the person to whom the forger directly transferred the instrument.

#### *Japan*

The formulation of article 23, which would certainly be one of the essential provisions of the Convention, is acceptable as a compromise between the two different systems. However, it needs further study, in view of the following problems:

(1) Under paragraph (1), those having the right to recover compensation are limited to the parties. Thus, this right is not conferred upon a person from whom the

instrument was stolen and whose signature was later forged since he is not a party (see article 4 (8)). However, this is not a sound approach. Such a person should also be entitled to recover compensation under this provision. Therefore, the Japanese Government proposes that the words "and any person whose endorsement is forged" be added after the words "any party" in article 23 (1).

(2) The present text sets no limit for the amount of compensation for damages recoverable under article 23. However, in view of the limit set for the amount recoverable under articles 41 (2), 64 and 75 (3) of the draft Convention, the amount recoverable under article 23 (1) from a person to whom the instrument was directly transferred by the forger should be limited to the amounts stipulated in article 66 and article 67.

#### Norway

The Norwegian Government is satisfied with the compromise of article 23 between civil law and common law.

The person who acquires the instrument from the forger may qualify as a protected holder although he is liable to any party for the loss caused by the forgery, cf. article 4 (7) and example H in the commentary to article 14. This construction is somewhat surprising. It is unclear whether the liability may be set up as defence against the protected holder, cf. article 26 (1) (b). The answer might be that the claim for compensation were to be regarded as a counter-claim and not as a defence. The implications of such a construction would ultimately depend upon the applicable national law. Anyway, as a natural consequence of the compromise in article 23, we suggest that article 26 (1) in a new subparagraph (d) state that a claim for compensation under article 23 may be set up against a protected holder as a defence to his claim on the instrument.

Paragraph 24 of the commentary says that article 23 (1) does not apply in cases where the person whose signature is forged, is liable on the instrument according to article 30. We suggest that this be explicitly stated in article 23.

Article 23 (1) leaves several questions to the applicable national law, cf. paragraph 25 of the commentary. We understand that the liability under article 23 (1) is a strict liability and that it is not left to national law to decide whether negligence is a condition.

Under Norwegian law, however, the employer may in some circumstances be liable for damage caused by his employees by forgery. This may more generally be the case if an employee exceeds his authority, cf. article 23 (3). We presume that such application of national law on vicarious liability will not be contrary to the Convention.

Regarding article 23 (3), we refer to our comment to article 4 (10).

#### Spain

With respect to article 23, we have already mentioned in our comments on article 4 the desirability of attempting a unified treatment of the issue of forgery. Furthermore, it seems unsuitable to bring together the issue of forgery and that of unlawful conduct by an agent, acting without authority or exceeding his authority. This was the opinion of the CSCC.

The identification of the person liable for compensation also raises some doubts. Under article 23, the person to whom the instrument was directly transferred by the forger is liable for payment of compensation, even if he is unaware of the fact of forgery (he is liable even without guilt, or else the guilt is presumed "*juris et de jure*"). On the other hand, the direct transferee is not liable if he is an endorsee for collection (against whom there would be an even easier presumption of "*consilium fraudis*"), even if he has knowledge of the forgery (paragraph 2), and nor is a subsequent transferee with knowledge of the forgery.

In short, the risk of forgery has to be borne by the person who acquires the instrument (in accordance with Anglo-American law) and not by the person whose signature is forged or whose instrument is stolen.

#### United States of America

This article embodies an important compromise and the United States supports paragraphs (1) and (2) as they are now drafted.

#### Article 23 (1)

#### Finland

Under this provision a person acquiring a bill of exchange has to ascertain the endorsement not to be a forged one. If he fails to do so, he runs the risk of facing—together with the forger—claims of compensation for the damages suffered by any party because of the forgery.

The proposed solution would, in the first place, mean that a person acquiring a bill of exchange is required to ensure himself of the identity of the endorser. This would seem to be a generally acceptable requirement. Only in the case where he has made an effort to this effect but has been misled, would he be exempted from responsibility for damage arising from the forgery. Although it is felt that the rules of the 1930 Convention would better serve commercial needs, the proposed rule might be acceptable as a reasonable compromise.

#### Mexico

The person receiving the instrument should not be liable, unless he has acted in bad faith.

Suggested wording: "If an endorsement is forged, any party has against the forger, and against the person who, in bad faith, received the instrument directly from the forger, the right to recover compensation . . ."

#### *Article 23 (1) and (2)*

##### *Czechoslovakia*

Paragraph (1) should provide that the drawee or the endorsee "by procuration" are liable because of a forged endorsement only in the case that they knew of the forgery.

In our view the provision in the second paragraph is of declaratory significance only.

#### *Article 23 (2)*

##### *Austria*

Article 23 (2) says that the liability of a party or of the drawer who pays, or of an endorsee for collection who collects, an instrument on which there is a forged endorsement is not regulated by the Convention. This means that such liability must be judged according to the specific applicable national law.

(a) This, as such, is in contravention of the idea of law unification. The draft Convention creates another sphere which remains reserved to the national law. This criticism has all the more significance as it relates to an important question.

(b) Moreover, the provision is not clear and gives rise to many questions. It is not easy to see what kind of liability it could be, in respect of whom and what for. This would in any case have to be stated.

(c) The provision also raises doubt with regard to the effect of a forged endorsement as referred to in the draft Convention. The question arises whether the regulation is not in contravention of the principle that a forged endorsement does not prevent a valid transfer of the instrument (article 14 (1) (b)). Because the provision of article 23 (2) seems to be meaningful only if it has a scope of application, i.e. if liability within the meaning of the provision is conceivable. Such liability, however, can only be based on the fact—as, for instance, under U.S. law—that due to a forged endorsement the holders succeeding the forger derived no rights from the instrument, since a bill of exchange bearing a forged endorsement is not transferable. It is only then that the predecessor of the forger can still derive rights from the instrument and may demand payment; in such case it is meaningful to make every party liable to its successor for the authenticity of the signatures, i.e. to let it assume the liability for a forged signature.

If, however, it is possible to make a valid transfer of the bill of exchange despite a forged endorsement, the person which had derived rights from the bill of exchange before it was forged can no longer raise claims based on the instrument. The bill debt is

discharged by payment. Given this situation, it is hard to see why a party which paid the bill of exchange can be liable on ground of a forged endorsement.

(d) If one starts from the assumption, however, that liability as referred to in article 23 (2) is conceivable within the framework of the draft Convention, the difficulties—apart from the fact that the effect of the forged endorsement does not seem to be clarified—in international business transactions caused by the different bills of exchange laws would be prolonged: the U.S. banks collecting an instrument drawn in favour of an American would continue to demand guarantees from the European bank tendering the bill in respect of a possible liability because under American law they themselves are not authorized to collect the instrument in the event of a forged endorsement due to the lack of authority of the endorser for collection and thus would have to compensate the authorized person or the person having indemnified such other person for the collected amount. The guarantee demanded from the European banks tendering the bill because they are not subject under the Geneva system to liability corresponding to that of the American law on bills of exchange could be advanced within the American period of limitation of six years although a recourse by the European bank tendering the bill against its customer may be subject to a considerable shorter period of limitation due to the relevant national law.

##### *Canada*

We have previously referred to the desirability of amending the Conventions to provide, in the fashion of subsection 97 (2) of the United Kingdom Bills of Exchange Act (section 10 of the Canadian Bills of Exchange Act) that issues affecting bills, cheques and notes that are not resolvable by the application or construction of the text of the Act shall be determined in accordance with the principles of the common law including the law merchant. Article 23 (2) is an example of a type of section demonstrating the importance of the point and the value of such an express invocation of supplementary sources of law available for the resolution of disputes. It does not appear to Canada to be an adequate discharge of the functions of the Convention merely to state that the liability of a party in particular circumstances "is not regulated by the Convention", without going forward to provide an indication of the source of law by which that liability may be determined. Even if it were intended by the draftsmen that such liabilities would be determined in accordance with generally accepted international principles of conflicts of law, a statement to that effect would be of assistance, e.g., in curbing the perhaps unjustified application of peculiar domestic rules of conflicts sponsored by individual domestic tribunals.

##### *Hungary*

This Convention might regulate the consequences arising from payment of an instrument which contains a forged signature by providing a rule under which the

drawee who pays an instrument to the person who forged the endorsement or the endorsee for collection who collects such an instrument is only liable for damages in case he knew of the forgery.

#### *Mexico*

It is not clear why the Convention does not regulate the liability of the drawee who pays an instrument on which there is a forged endorsement. The circulation of bills of exchange is based on the principle that exempts the drawee from the obligation (indeed, even denies him the authority) to establish the legitimacy of the endorsements.

Suggested wording: "The party paying an instrument is not obliged to establish the authenticity of the endorsements, nor does he have the power to require that the authenticity be verified; he must, on the other hand, authenticate the identity of the person presenting the instrument as the last holder, and also the continuity of the endorsements thereon."

#### *Union of Soviet Socialist Republics*

In paragraph (2) it would be desirable to regulate the question of consequences arising from payment of an instrument by the drawee directly to a person who has forged an endorsement, or from the taking by the endorsee for collection (usually by a bank) of an instrument from such a person, by establishing a rule under which a drawee who pays on an instrument to a person who has forged an endorsement, or an endorsee for collection who collects such an instrument, is liable for damages only if he was aware of the forgery.

#### *Article 23 (3)*

#### *Mexico*

The first line of the Spanish version should read "*estampado en un título*" instead of "*estampado en un instrumento*".

#### *United States of America*

Article 23 (3) provides a definition of "forged endorsement" which seems to be both correct and of general applicability. However, as was mentioned earlier in connection with the article 4 (10), that definition is expressly limited to "the purposes of this article," a limitation which the United States finds unnecessary and confusing. The limitation suggests that this definition is inaccurate in other contexts. The United States therefore proposes that article 4 be amended to provide a complete definition of "forged signature", which would include both unauthorized signatures and those beyond the scope of an agent's authority, and would be used consistently throughout the Convention. Such a definition should include the concepts of articles 4 (10)

and 23 (3) and make their separate provisions unnecessary.

The Convention makes no exception to general rules applicable to forged endorsements in situations where the instrument is issued as part of a fraudulent scheme by an employee of the drawer, who causes the instrument to be issued in the name of some person, real or fictitious, with the intention of signing that person's endorsement. Since such fraud can best be prevented, and insured against, by the drawer, the United States proposes that article 23 be amended to place the loss on the drawer and not on the person who takes from the forger in such a case.

### CHAPTER FOUR. RIGHTS AND LIABILITIES

#### *Holder—Protected holder*

#### ARTICLES 4 (7), 24, 25 and 26

#### *Australia*

#### *Articles 25 and 26*

A fundamental concept in any law on negotiable instruments is the protection that is given to a person who acquires a negotiable instrument in the ordinary course of business, in good faith and without notice of any defects in title of the person from whom the instrument was acquired.

Like the position under the BEA, the draft Conventions distinguish between a 'holder' and a 'protected holder' of a negotiable instrument. However, while the definition of a holder in the BEA and the draft Conventions (article 14 (Bills and Notes Convention), article 16 (Cheques Convention)) is similar, the concept of a 'holder in due course' (under the BEA) and that of a 'protected holder' (the draft Conventions) are not identical.

In s. 34 of the BEA, a holder in due course is defined as a holder who has taken a bill, complete and regular on the face of it, if he became a holder before it was overdue and without notice that it had been previously dishonoured, and if he took it in good faith and for value and without notice at the time it was negotiated to him of any defect in the title of the person who negotiated it. Once a bill has come into the hands of a holder in due course, any subsequent holder is entitled to the same protection as the holder in due course even though he himself was not a holder in due course, unless the subsequent holder was party to any fraud or illegality affecting the bill.

Under the draft Conventions, the protected holder is defined as a holder of an instrument that was complete and regular on its face when he became a holder if he was at that time without knowledge of any claim or defence to the instrument that would be valid under the Conventions against ordinary holders (article 26 (Bills

and Notes Convention), article 27 (Cheques Convention) or of the fact that the instrument had been dishonoured by non-payment, and if the time limit for presentation of the instrument had not expired.

It appears that the holder in due course and the protected holder differ in two respects. Firstly, there is no requirement under the draft Conventions as there is under the BEA that a protected holder must take a bill for value. Secondly, whilst a holder in due course is required to be 'without notice' of previous dishonour of defects in title, the protected holder is required to be 'without knowledge' of previous dishonour or claims. The draft Conventions appear to introduce an element of constructive knowledge (Bills and Notes Convention (article 5), Cheques Convention (article 7)). Under the BEA, however, 'notice' means actual notice and there is no room for the operation of the doctrine of constructive notice. Insofar as a bank may be a protected holder in many cases, the question is raised of the extent of knowledge that can or should be attributed to a bank.

So far as the privileged position of the holder in due course and the protected holder is concerned, a protected holder may in fact be in a slightly weaker position than the holder in due course. Under s. 43 (1) (d) of the BEA, a holder in due course holds a bill free from any defect of title of prior parties, as well as from mere personal defences available to prior parties among themselves, and is entitled to enforce payment against all parties liable on the bill. On the other hand, under article 26 of the Bills and Notes Convention and article 27 of the Cheques Convention, certain specific defences can be raised against the protected holder e.g. that the instrument was unsigned, that the signature was forged or unauthorized, that there had been a material alteration, that there had been a lack of presentation, that time limits had elapsed, that the party lacked capacity to incur liability on the instrument or the plea of *non est factum*.

Moreover, a party may raise against the protected holder defences based on the underlying transaction between himself and that holder or arising from any fraudulent act on the part of that protected holder in obtaining the signature of that party on the instrument.

It may be possible, therefore, in comparing the legal position of the holder in due course and the protected holder, to provide examples of where the holder in due course would take an unqualified title to the bill whilst the protected holder would not. Australia intends to give this matter further consideration.

#### Austria

##### Articles 25 and 26

(a) One of the main reasons for the lack of clarity and the complexity of the system is the differentiation between holder and protected holder because this differentiation has the result that there are two different groups of defences.

Article 27 makes the system even more unclear, by providing that a holder may, under certain conditions, assume the legal position of his predecessor who had been a protected holder. Although, in general, this may be welcomed because it strengthens the formalism of the bill of exchange and thus the legal position of the holder, the manner in which this is achieved seems to be much too complicated.

Another major drawback is that the draft Convention offers no regulation for the question of claims to the instrument against the holder, so that for solving this problem the applicable national laws have to be used. Because of this, the difficulties generally arising in connection with questions of international private law and the application of foreign law will remain in this field as well.

(b) On the other hand, the complexity of the system is not offset by an improved protection against the formalization of the bill of exchange or against its misuse.

It is unfair, for instance, that a defence based on the underlying transaction (legal relationship between predecessors) cannot be set up against a protected holder or a holder put on the same footing as a protected holder under article 27, even if such holder acted deliberately to the disadvantage of the debtor when acquiring the instrument (cf. article 17 of the Uniform Law on Bills of Exchange and Promissory Notes). It is equally unfair that no defence based on an underlying transaction may be set up against the protected holder (or a holder of equal footing under article 27), even if such holder had acquired the bill of exchange in bad faith or may be blamed of gross negligence when acquiring the instrument (cf. article 16 para. 2 of the ULB).

While this provides strong protection for the protected holder (or holder of equal footing), protection of the holder seems to be unduly weak. A defence based on the underlying transaction may even be set up against such holder if he neither knew of such defence nor was obliged to know and did not act to the disadvantage of the debtor when acquiring the instrument.

This shows that the generalizing differentiation between holder and protected holder is not suited for arriving at just solutions in this respect. It would be different if—like in the Geneva system—the defence and/or the claim to the instrument against the respective holder were made dependent on his good faith (bad faith) *vis-à-vis* the debtor and/or in relation to the title of the predecessor.

(c) It serves business transactions best if the rights from a bill of exchange can be realized rapidly. The system of the draft Convention, however, gives rise to the concern that the realization of rights will meet with particular difficulties in practice and that delays will therefore occur.

The point is that it will not be possible to judge, on the basis of the instrument alone, what rights are vested

in the respective holder and what defences may be set up against him; rather, the question will have to be solved first whether the holder is just a holder or a protected holder (or a holder of equal footing). For this purpose it may still be easy to ascertain whether the time limit for presentment of the instrument had already expired when the instrument was acquired by the holder; it will be more difficult, though, to determine whether the holder knew of a defence under article 25 or a claim to the instrument when acquiring the bill of exchange.

In practice, there will also be the negative effect that the defences which may be set up against a holder are not enumerated in a final list as in the case of the protected holder (article 26), but that article 25 contains—apart from some explicitly mentioned defences—only a general reference to “any defence available under this Convention”.

#### *Canada*

##### *Article 26 (2)*

Canada does not see the utility of the phrase “to an instrument” that has been introduced in the first line of this subsection. It appears to us that the intent of the section is that no right of a protected holder shall be qualified in the manner described in the section. By making reference “to an instrument” the section raises a doubt whether rights of action derived from the instrument or “under the instrument” are impliedly excepted. If the subsection referred only to “rights of a protected holder” this ambiguity would not arise.

#### *China*

##### *Article 25 (1)*

Article 25: “... a holder who is not a protected holder ...”

Recommendation: The term be defined.

The reason: The article affirms the legal rights to be exercised by a party to an instrument against “a holder who is not a protected holder”, while limiting the legal rights of “a holder who is not a protected holder”. Therefore, the term should be clearly defined to facilitate its application.

#### *Czechoslovakia*

##### *Articles 4 (7) and 25*

Article 25 is included because of the difference between “holder” and “protected holder”. In our view it contains a needlessly complicated formulation and we recommend adoption of the more simple regulation of the Geneva Uniform Law which is based upon the premise that any holder of an instrument who evidences

his right in the way regulated by the Geneva Uniform Law is not obliged to hand over the instrument to a person who lost it, unless the holder obtained the instrument in bad faith or was guilty of gross negligence in obtaining it. The fundamental provision upon which the importance of a negotiable instrument must be founded should be constituted by the principle that he who is sued on an instrument may not set up against the holder defences that are based upon his own relations with the drawer or with prior holders unless the suing holder when obtaining the instrument knowingly acted to the detriment of the debtor. This formulation is simple and corresponds better to the economic function of the bill or note. On the other hand, the definition of “protected holder” in article 4 (7) is cumbersome and complex in view of its reference to article 25, and it specifies certain requirements the non-fulfilment of which cannot be regarded as obtaining an instrument in bad faith or to the detriment of the debtor.

#### *Denmark*

##### *Article 26 (1) (b) and (c)*

It seems a rather drastic step that a person as a defence may invoke the acts referred to under (1) (b) in both Conventions. In Danish law this would be equivalent to elimination of part of the negotiability of cheques and bills of exchange.

At the same time it appears odd that a person’s statement to the effect that he was unaware of signing a cheque/bill of exchange, cf. (1) (c) in both Conventions, is admissible evidence.

#### *Finland*

##### *Articles 4 (7) and 26 (1)*

Under article 4 (7) a holder of an instrument is not a “protected holder” if the instrument was incomplete at the time of his becoming a holder, even if the instrument had since been completed in accordance with an agreement, as envisaged in article 11. This would also apply to features of the instrument other than the one introduced later on. Such a solution would seem to interfere with the present practices and is not supported. It would mean that the holder would not be protected against any defence based on the underlying transaction even if not related to the feature left incomplete in the bill of exchange, *vide* article 25 (1).

Under subparagraph (c) of article 26 (1) a party may set up defences against a protected holder if based on his incapacity to incur liability on the instrument or on the fact that he has signed the document without knowledge that his signature had made him a party to the instrument and provided that such absence of knowledge was not due to his negligence. Whilst the former defence seems to be reasonable, it is feared that the latter might give rise to conflicts. The “example H”, referred to in paragraph 6 of the Commentary to this provision, rather

strengthens these fears. It is therefore proposed that the latter part of the provision be deleted (starting with "or on the fact . . .").

*Germany, Federal Republic of*

*Articles 25 and 26*

According to the rules suggested, in practice all imaginable defences may be invoked against the holder of a bill of exchange who is no protected holder. A protected holder, however, becomes a holder who is not protected if only he did not have knowledge of a defence due to gross negligence. That restriction of trade protection as opposed to the Geneva system will most likely impair the negotiability of the international bill of exchange substantially; it is therefore doubtful if such a commercial paper would attain practical importance.

*Japan*

*Article 4 (7)*

The definition of "protected holder" as set out in article 4 (7) is not sufficiently comprehensive. Particularly, the factor of regularity as referred to in the definition is confusing. According to the example given in paragraph 13 of the commentary (A/CN.9/213, *Yearbook 1982*, part two, II, A, 4), a bill shall not be regular when the name of the first endorser does not correspond to the name of the payee. However, a person who was in possession of such a bill would not even be a 'holder', since he was not in possession of a bill on which there appears an uninterrupted series of endorsements (see article 14 (1)). Consequently, the definition as set out in article 4 (7) needs further study.

*Netherlands*

*Articles 25 and 26*

The draft Convention, in chapter four, section 1, deals with the central question of negotiable instruments law: in what circumstances should the person in possession of an instrument be protected against a claim to the instrument and be able to cut off defences raised by prior parties, and which defences?

The legislative technique employed in the draft Convention, by the use of the concepts of holder and protected holder and the so-called shelter rule, is inspired by the Anglo-American systems.

Like the English and American statutes which protect only the "holder in due course", the draft Convention protects only the protected holder and adopts the single concept of "protected holder" for the purpose of protecting such holder against both claims and defences.

Dutch law on the other hand, in accordance with articles 16 and 17 of the ULB, differentiates between protection against claims and protection against

defences. In order to cut off claims of ownership, the holder must be free from bad faith and gross negligence (article 115K, article 16 ULB) and in order to cut off defences he must not, in acquiring the instrument, have acted to the detriment of the obligor (article 116K, article 17 ULB).

Like the English and American statutes, the draft Convention denies the status of protected holder to a holder who, when he became a holder, knew (article 4 (7)) or ought to have known (article 5) of "a claim or a defence affecting the instrument" (cf. Commentary, para. 14, *Yearbook 1982*, part two, II, A, 4).

The treatment of defences under the draft Convention is complex and leads to results that are different from those obtaining under Dutch law and the Geneva Conventions.

The differences may be illustrated by using the example discussed at the Geneva Conference in 1930 (C.360.M.151, 1930, II, p. 292) and also used during the deliberations of the UNCITRAL Working Group (see A/CN.9/77, para. 81 (b), *Yearbook 1973*, part two, II, 1).

The purchaser of goods accepts a bill of exchange drawn on him by the seller to his (seller's) order. Seller subsequently delivers defective goods. The acceptor-purchaser may therefore, in an action against him by the drawer-seller, set up as a defence the fact that the goods were defective. Suppose the bill is endorsed to A who takes it with knowledge of the defence which the acceptor may set up against the drawer.

Under the draft Convention, A is not a protected holder: when he took the bill, he had knowledge of a defence referred to in article 25. Under article 25 (1) (b), the acceptor may set up the defence (based upon the underlying transaction between himself and the drawer) against A.

Under Dutch law, A will cut off the defence raised by the acceptor if, in acquiring the bill, he did not knowingly act to the detriment of the acceptor. Mere knowledge by the holder of existence of a personal defence available to the obligor does not therefore impair the protection a holder enjoys under Dutch law (article 116K) or the ULB (article 17).

In respect of personal defences the Geneva Uniform Law would thus give greater protection to the holder since he may be protected against personal defences even when he had notice of them.

It is however relevant to note that the courts of Contracting parties to the Geneva Convention have given divergent interpretations of article 17 ULB. Some courts have held that knowledge of a personal defence available to the obligor amounts to acting knowingly to the detriment of the obligor.

In the Netherlands, the doctrinal view is generally that the transferee of an instrument who knew or ought

to have known of the obligor's defence does not deserve the protection which article 17 of the ULB, on a strict interpretation, grants him, even though he did not knowingly act to the detriment of the obligor.

Professor Molengraaf, a Netherlands delegate to the 1930 Geneva Conference, was opposed to article 17 ULB. He said the following (C.300, M.151, 1930, II, p. 292):

"The text now proposed, while requiring that the holder should have knowingly acted to the detriment of the debtor, involved the protection of a holder in bad faith. In other words, it protected a person who, in acquiring the bill of exchange, knew that the previous claimant was liable to be met by a defence which could be set up by the person sued by the holder. That principle was contrary to the law of bills of exchange . . . This law was based on the protection of the rights of third parties "in good faith". It did not sanction the possibility of a bill of exchange becoming an instrument for the unfair enrichment of a person who had acquired it in bad faith. Such enrichment would, however, be encouraged if the debtor of the bill of exchange were refused the right to set up the defence of bad faith, and if the burden of proof were put on him that there was an intention to defraud him to his detriment."

It is suggested, therefore, that article 25, in this particular respect, is acceptable.

The meaning of article 25 (1) is less clear. Whereas article 26 sets out, by cross references to other provisions, the defences that may be raised against a protected holder, article 25 (1) merely refers to "defences available under this Convention". The provision would gain in clarity if it specified which defences are referred to.

It is true that, under the draft Convention, the situation of a mere holder is akin to that of an assignee. However, under article 28, a holder is presumed to be a protected holder. Consequently, the burden of proof that the holder, when taking the instrument, had knowledge or constructive knowledge of a defence, falls on the obligor. This presumption and the shelter rule set forth in article 27 (1), though not known in civil law jurisdictions, should ensure that the conditions pertaining to the circulation of an international instrument are not less favourable than those obtaining under the Geneva system.

#### *Article 26*

Article 26 (1) (c) lists the defences of incapacity and *non est factum* as defences that may be raised against a protected holder. It is suggested that the issue of defences based on circumstances which render the obligation of a party null and void be either spelled out in article 26 or be left to the applicable national law.

The current listing of only two such defences might be interpreted as an exhaustive listing. Yet, obligations that are illegal or undertaken on the instrument as a result of a physical duress (*vis absoluta*) may not be enforceable

on grounds similar to those obtaining in respect of incapacity or *non est factum*.

Preference is expressed for leaving the matter of what constitutes real defences to the applicable national law.

#### *Norway*

##### *Article 4 (7)*

1. The concept of "protected holder" is defined in article 4 (7). The definition requires i.a. that the instrument was complete when the holder acquired it. Even if the instrument is later completed in accordance with article 11, the holder will not qualify as a protected holder in respect of the features in which the instrument was complete upon delivery. We suggest that paragraph (7) be amended in order to avoid the consequence.

2. An essential part of the definition of "the protected holder" is the requirement that the holder upon delivery had no knowledge of a claim to or a defence upon the instrument. A holder who knows of any one claim or any one defence and therefore is not protected against it, will neither be a "protected holder" in respect of claims and defences of which he had no knowledge, cf. paragraph 14 of the commentary to the article. We would prefer the solution that knowledge of one claim or one defence did not preclude the holder from protection against other claims and defences.

#### *Articles 25 and 26*

1. The articles deal with i.a. the defences which may be set up against a holder and a protected holder.

2. With reference to our comment to article 23, we suggest that there be inserted in article 26 (1) a new subparagraph (d) stating that a protected holder's liability according to article 23 may be set up against him as a defence to his claim on the instrument.

3. Article 26 (1) (b) contains two alternatives, "defences based on the underlying transaction . . ." and "(defences) arising from any fraudulent act . . .". If it is agreed that the second alternative only is a subcategory of the first one, the former might be deleted.

4. With exception to these few comments, the Norwegian Government is satisfied with articles 25 and 26.

However, the Norwegian Civil Proceedings Act provides for some special arrangements in cases where the plaintiff relies on a bill of exchange or a promissory note. The defendant is precluded from invoking several kinds of defences at the first stage of the trial. The court may order him to pay although he has a valid defence. The defence may be tried in a second stage of the trial or in a new case. The court may then reverse the original order or order the plaintiff to pay back if he has already received payment. We presume that this procedural arrangement will not be contrary to the Convention.

### Spain

#### *Holder—protected holder: general observations*

The issue of the position of the holder in relation to the defences available to the various parties constitutes the "cornerstone of the draft Convention", as the CSCC puts it. However, serious reservations may be expressed as to the method by which this aspect should be regulated. The draft Convention makes an initial distinction between a holder and a protected holder, which is explained in the definitions of these terms. The difference between the two is based, among other criteria, on "knowledge" of certain facts, that is to say on a criterion which is subjective and uncertain. In order to simplify it, presumptions are used which may in some cases have the reverse effect (cf. articles 5 and 28). The defences available are listed by means of cross-references, and we shall return to this later on.

The complexity of the system is the result of its initial tenet, the distinction between a protected holder and an unprotected holder. To start with, the terminology seems inappropriate; a person cannot be qualified as unworthy of legal protection. On the other hand, if the system is to be based on the above distinction, both concepts must be clearly specified; a reading of article 4 reveals that this has not been done (see the comments to this article). The concept of a protected holder is defined basically by one objective criterion—inaccurately formulated—and, more especially, by his unawareness of certain facts. This means that the qualification of holders as protected holders must be pronounced on a case-to-case basis and cannot be pronounced before the event. It would appear a simpler solution to establish how the knowledge of certain specified acts affects the system of available defences, removing the need to set up any initial distinction. These thoughts must suffice for this section.

In short, the subject of grounds for dishonour should be regulated with much greater clarity and simplicity. The system proposed in the draft Convention is very different from the Geneva system, provided for under article 17 of the Uniform Law; but, far from being a step forward, it introduces imperfections which suggest that the advisability of staying closer to the Geneva model should be considered.

#### *Article 4 (7)*

The definition of most consequence is, no doubt, that of a "protected holder", a concept which it is absolutely necessary to define since, as we stated above, one of the cornerstones of the Convention rests on the distinction between a protected and an unprotected holder. However, the definition is not satisfactory. The basic definition, that of a holder in subparagraph (6), consists of a reference to article 14, and then an unprotected holder is defined in an excessively imprecise, complicated and ambiguous manner, although the subject calls for the greatest clarity and objectivity.

First of all, the definition speaks of the "*tenedor de un título que a simple vista parecía completo y en regla . . .*". The expression "*a simple vista*" ("at first sight" or "at a glance") is unacceptable. Happier expressions are used in the English version ("on its face") and in the French version ("*d'après son contenu*"). The explanation in the Commentary (paragraph 13), "*según lo indicado en el cuerpo de éste*" (English: "on the face of it" (the instrument)), is also better than the phrase used in the text of the draft. The reference should be to the literal content of the document.

It is also unclear what is understood by an instrument which is complete. It should presumably be one that meets all the requirements in article 1; however, the subparagraphs (e) under paragraphs (2) and (3) mention five different places of which two must be in different States. They do not explicitly require that for the title to be complete all five must be shown, nor do they state clearly the manner in which these entries are to be made.

Also, as the CSCC has pointed out, there is no clear reason why a person receiving an incomplete bill should not be a protected holder if he completes it in accordance with the relevant agreement. Furthermore, it may be difficult to establish whether an instrument was completed before or after a person became the holder. Besides, provision is made for the omission of one requirement: if the date is missing, the Convention provides that the instrument shall be considered payable on demand. It makes no sense for its holder to be "protected".

Some negative "conditions" also attach to the status of a "protected holder". One is that he must be "without knowledge"—a subjective, negative condition complicated by a set of presumptions—of certain specified facts:

First of all, those referred to in article 25; that is to say, we have another complicated reference making the provision still harder to understand, since article 25 refers to "any defence available under this Convention".

Secondly, the fact that the instrument has been dishonoured by non-acceptance or non-payment. It is hard to understand why a holder who knows that an instrument has been dishonoured by non-acceptance should not be a protected holder. It is also hard to understand why knowledge of dishonouring by non-payment should affect qualification of the holder, since, as provided by the following subparagraph (b), he may on no account be a protected holder if the time-limit has expired for presentation of the instrument for payment. As the CSCC has pointed out, the importance of distinguishing clearly between the concepts of a "protected" and an "unprotected" holder within the system in the draft Convention makes its comprehension and delimitation difficulties the more serious.

### *Articles 24, 25 and 26*

Section 1, entitled "The rights of a holder and of a protected holder", contains one of the essential cornerstones of this draft: regulation of the defences available against a holder.

An initial distinction is made in this area between a protected holder and an unprotected holder; in our general remarks on the draft Convention we outlined our serious doubts and reservations about a system which appears imprecise and ambiguous.

We shall now make a few more specific comments. First of all, it seems somewhat inappropriate to place these provisions in this section. True, the holder's rights are affected by the defences described, but the main emphasis is on the right of liable persons to use such defences against his claims.

Article 24, the first in the section, makes reference to the rights of a holder. Paragraph (1) establishes his rights by means of a comprehensive cross-reference ("those conferred on him by this Convention") and by reference to the persons against whom his rights may be exercised: "the parties to the instrument". It must be remembered that there are parties without liability (articles 34 (2) and 40 (2)) and liable persons who are not parties to the instrument (article 4). Paragraph (2) indicates the right of transfer by means of another cross-reference, this time to article 12.

After this purely introductory article, we come to the issue of defences; article 25 concerns those available against an unprotected holder and article 26 those against a protected holder. Before commenting on substantive issues, and whether or not the proposed system is acceptable, it would be advisable, most particularly in this context, to avoid a number of defects to which general reference has been made above.

An example of the poor drafting in the Spanish version is to be found in article 25 (1) (b). Also, the continual use of cross-references makes understanding of the provisions over-complicated. Article 25 starts with a general cross-reference and article 26 with a reference to a specific list of articles and paragraphs.

As pointed out by the CSCC, it might be better to reverse the order of these two provisions; in other words, it would be preferable to establish first of all the defences available against any holder and then those that may be invoked only against an "unprotected" holder.

It might also be desirable to deal separately with defences and with claims on an instrument; these issues are intermingled in articles 25 and 26 of the draft ("rights" and "claims" on an instrument).

### *United States of America*

#### *Article 4 (7)*

A "protected holder" is a holder who takes an instrument complete and regular on its face and not overdue without knowledge of a claim or defence "referred to in article 25". Knowledge of a defence not referred to in article 25 (such as known defects in the transaction which caused the issuance of the instrument) will not prevent a subsequent transferee from becoming a protected holder. This limitation on the knowledge requirement of article 4 (7) (a) is not clear, nor is it sound policy. It does not seem that knowledge of a defence under article 25 (1) (b) or (1) (c) would ever be significant, since both of those provisions refer to transactions "between himself" (presumably the person acquiring the instrument) and another party. If this is so, however, a person can attain the status of a protected holder even though he knew of breach of contract defences or fraud in the inducement in the transaction underlying the original issuance of the instrument. The United States believes that protected holder status should not be extended to parties who know of defences, except under the shelter provisions of article 27. The definition of "protected holder" should therefore be amended by deleting the phrase "referred to in article 25" from the present knowledge requirement in article 4 (7) (a).

#### *Article 25*

Under article 25 (1) (a), a holder is subject to any defence available under the Convention. Under the comparable provision for protected holders—article 26 (1) (a)—there are specific cross references to articles furnishing such defences. The United States suggests that these two paragraphs in articles 25 and 26 be conformed, preferably by adding to the text of article 25 (1) (a) a list of specific cross references to other articles furnishing such defences.

### *Yugoslavia*

#### *Article 4 (7)*

Article 4 (7) defines the term "protected holder" which is quite distinct from the term "legal" holder of an instrument or a holder in "good faith" under Yugoslav law. The institute of the "protected holder" sets more requirements than is required in the case of a "holder in good faith". The application of this institute may pose problems in practice, especially in the case of an incomplete instrument (article 38).

The requirements enumerated in article 25 and more specifically defining those set out in article 4 (7) in respect of claims and defences will be a serious obstacle to a speedier circulation of an instrument, primarily because of the fact that a bill is based on an underlying transaction.

**Articles 25 and 26**

These articles are an illustration of the aforementioned statement that the Working Group has viewed a bill as a causal transaction, which is unacceptable because it does not meet the needs of the present transactions and will not facilitate the circulation of an instrument. Namely, article 25 (1) (b) and article 26 (1) (b) stipulate that a party may set up against a holder who is not a protected holder "any defence based on an underlying transaction".

**ARTICLE 27***Czechoslovakia*

The provision of paragraph (1), because of its wording "by a protected holder", leads to the interpretation that for the purpose of a person to be a "protected holder" it is not sufficient if he complies with the terms of article 4, paragraph (7), but that in addition, his predecessor must be a "protected holder".

*Norway*

The implications of "the shelter rule" in article 27 are explained in several examples. We strongly oppose the solution outlined in example C. There are no good reasons why the person C in the example should obtain the rights of a protected holder. We suggest that article 27 be amended in order to avoid the consequence.

*Spain*

Article 27 makes the system even more complicated; it is an obstacle to understanding the characteristics of a protected holder and the already complex definition of him in article 4.

*Article 27 (2)**Denmark*

According to the provisions of paragraph (2) a party who pays an instrument and the instrument is transferred to him, such transfer does not vest in that party the rights to and upon the instrument which any previous protected holder had. The situations envisaged in this context are not easily understandable.

**ARTICLE 28***Spain*

Article 28 has further resort to presumptions. These are used, in principle, to facilitate the implementation of legislation, but in this case the conflicting effects of articles 5 and 28 may increase the complexity of the system.

**ARTICLE 29***Norway*

A reference to articles 30 and 32 seems to be equally relevant to paragraph (2) as to paragraph (1), cf. our comment to article 23. The final text may read:

*Article 29*

Subject to the provisions of articles 30 and 32:

- (a) A person is not . . .
- (b) A person who signs . . .

*Spain*

Section 2, on the liability of the parties, contains some general provisions which, curiously, start with a negative formulation (article 29 (1)), whereas it would be more logical to have a positive one specifying when a person is liable on an instrument, to whom he is liable and the nature of his liability.

**ARTICLE 30***Czechoslovakia*

For the purpose of legal certainty we recommend to delete the implied approval of the forged endorsement.

*German Democratic Republic*

This article introduces the notion of "implication". An implication is "a state of mind or facts which is deduced".

In view of the special nature of bills of exchange/promissory notes as negotiable instruments, the contents of which should be fully comprehensible for everybody and presented with clarity, use must be made, as a matter of principle, of explicit statements only. Otherwise, dealings using bills of exchange/promissory notes may involve some uncertainty and their negotiability may be considerably limited or affected. These remarks also apply to the use of the term "implication" in articles 52, 58 and 63.

*Japan*

Article 30 provides that a person whose signature was forged is liable where he has represented that the signature is his own. However, according to paragraph 2 of the commentary (A/CN.9/213, *Yearbook 1982*, part two, II, A, 4), he is not liable if the person to whom the affirmative representation was made knew of the forgery. However, it would be inappropriate to provide that the person who has represented that the

signature was his own is not liable at all to any subsequent holder if the person to whom the affirmative representation was made knew of the forgery. If, however, the Commission decides to adopt such a principle, the text of the Convention should state such rule expressly.

#### *Norway*

The word "represented" in article 30 is to be interpreted according to Anglo-American tradition, c.f. paragraph 2 of the commentary. Preserving the rule, article 30 ought to be drafted in a way more open to a direct translation into the languages of non-common-law countries.

#### *Union of Soviet Socialist Republics*

The reference to the possibility of an "implied" acceptance by the person whose signature was forged on the instrument to be bound by such a signature should be deleted from the text of this article in view of the vagueness of the term and of the fact that it is known only to one legal system (Anglo-American law).

#### *United States of America*

Article 30 provides that a forged signature does not impose liability on the person whose signature was forged, unless "he has, expressly or impliedly, accepted to be bound by the signature" or represented it to be his own. The concepts of express adoption and misrepresentation cause no problems. However, the concept of implicit "acceptance to be bound" is not clear, although it seems to suggest that the person whose signature was forged is precluded from asserting the forgery. The United States proposes that this concept be expressly stated in article 30, to make it clear that if a person's failure to exercise due care substantially contributes to the making of a forgery of his signature, he will be precluded from asserting the fact of the forgery.

## ARTICLE 31

#### *Australia*

A further divergence between the BEA and the draft Conventions concerns the effect of material alterations to an instrument. Under the draft Conventions, while parties who sign an instrument subsequent to any alteration will be liable on the instrument as altered, parties who sign before the alterations will be liable only according to its original terms (article 31 (Bills and Notes Convention), article 33 (Cheques Convention)). However under s.69 of the BEA, where a bill is "materially" altered the parties who signed it prior to the making of the alteration are discharged from liability on the bill except to a holder in due course for

the original amount, and then only if the alteration is not apparent. Australia accepts the Convention provisions despite the differences with the position under the BEA.

#### *Norway*

An instrument may be altered more than once. We suggest article 31 be amended to take account of the possibility.

#### *United Kingdom of Great Britain and Northern Ireland*

A major point is made that this article does not say whether there is to be any difference between the treatment of alterations which are apparent and those which are not, as provided by the Bills of Exchange Act 1882, s.64. It is felt that a material alteration should not be apparent for the provisions of the article to apply. On the other hand it is felt that a person who knowingly takes a materially altered bill should not be able to enforce it against any prior holder or the alterer.

#### *Article 31 (1)*

#### *Denmark*

While the provisions of paragraph (1) (b), first sentence do match the rules of section 13 of the Danish Cheque Act and section 10 of the Danish Bills of Exchange Act it might be expedient to insert a clause that the holder of the instrument must be in good faith if he is to repudiate the objections of a party who has signed the instrument.

#### *Finland*

In subparagraph (b) of this provision a situation is envisaged where the instrument in question has been once altered. It is understood that where a bill of exchange has been altered twice, reference should be made to the terms of the text as it was when the party concerned first signed the bill of exchange, even if that were not the original text.

#### *Article 31 (2)*

#### *Yugoslavia*

Paragraph (2) of article 31 may create difficulties in practice and prevent the circulation of an instrument. A strict application of the provision of paragraph (2) of this article would mean that all parties would be liable even for an obvious error in material alteration. Therefore, one may wonder whether the parties who have signed the instrument shall also be liable for any subsequent alteration.

## ARTICLE 32

*Uruguay*

Article 32 lacks a rule concerning signature by juridical persons, especially commercial corporations. It would be desirable to include a provision on this matter.

*Article 32 (4)**Norway*

Paragraph 6 of the commentary suggests that paragraph (4) of the article will be overriding articles 25(1)(c) and 26(1)(b) in a conflict between the agent or the principal and his immediate transferee. However, there seems to be no need for such a deviation from the main principles of articles 25 and 26. We propose that either paragraph (4) of article 32 be deleted or a reservation be included regarding the immediate transferee of the agent. As far as subsequent protected holders are concerned, article 32 (4) is superfluous in addition to article 26, cf. article 32 (3).

## ARTICLE 33

*Canada*

Canada does not see the utility of the verb "made" in the last complete line of this article. It appears to direct attention rather too pointedly to funds that may have been specifically deposited with the drawee. We consider that the intent of the article extends to all funds in the hand of the drawee for the account of the drawer and this meaning would be clarified if the verb "made" were deleted.

*Denmark*

Presumably the rules of article 35 of the Cheques Convention and article 33 of the Bills and Notes Convention shall be taken to mean that a bank may refuse to pay without specifying the grounds for the refusal, even though there may be sufficient funds in the account. This is not considered sufficiently clearly formulated for the Cheques Convention and its commentary on article 35. By contrast, the problem seems to have been solved in article 33 where a parenthesis in the commentary contains the passage "unless the drawee has accepted". A similar parenthesis or passage ought to be inserted in the Cheques Convention.

*Spain*

This section ends with a provision, in article 33, which appears out of place in the system proposed in the draft Convention; the draft contains no general regulations concerning the relations between the instrument and the underlying transactions. This isolated reference to the assignment of funds made available for payment therefore seems strange.

## ARTICLE 34

*Article 34 (1)**Canada*

Canada does not see the utility of the word "subsequent" in the third line of this section. It is difficult to give it a sensible meaning. Every party is a subsequent party to the drawer; no party is a subsequent party to the holder who is paid. The United Kingdom and Canadian statutes refer to holder or any subsequent endorser, but article 34 (1) would be satisfactory to us if the word "subsequent" were simply deleted.

*Article 34 (2)**Denmark*

The provision in paragraph (2) differs radically from the Danish provision in section 9 of the Bills of Exchange Act if it is to be inferred from paragraph (2) that the drawer may also limit his liability to pay the bill. This makes the Bills of Exchange system highly recondite for those using the system. A stringent rule corresponding to that in subsection 2 of section 9 of the Danish Bills of Exchange Act (and article 35 of the Convention) is preferable.

*Spain*

The provision that the drawer may exclude or limit his liability invites comment. The CSCC could not see the purpose of this provision and recommended its deletion, since the possibility of excluding liability is not made subject to the existence of other liable parties. The maker of a promissory note may not exclude or limit his own liability (article 35). This difference between bills of exchange and promissory notes clearly rests on the fact that, in the latter case, the maker's liability is primary (as explained in the Commentary). In any case, for the sake of consistency, the existence of a party with primary liability (the acceptor's signature) should be a prerequisite for allowing the drawer to exclude or limit his liability.

*Uruguay*

Article 34, paragraph (2), is in complete conflict with our internal law and we see no international need for it. Traditionally, a bill must be paid by the drawer in the event of non-acceptance or non-payment by the drawee. If the drawer is to be allowed to be exempted, this would allow the circulation of an instrument lacking any debtor or person liable for payment.

*Yugoslavia*

It is not clear why the provision of paragraph (2) of article 34 stipulating that the drawer may exclude or

limit his own liability by an express stipulation on the bill has been included in the draft Convention. The assumption is that the Working Group meant only a bill since such a stipulation of paragraph (2) would be absurd in the case of promissory notes under which the maker undertakes to pay a definite sum. Or how can he guarantee to pay a definite sum (which is the purpose of a note) if he excludes or limits his own liability (article 34 (2)). Paragraph (2) of article 34 indicates that the Working Group probably had a bill in mind but the wording implies all instruments. Therefore, it should be reworded for the sake of clarity.

#### ARTICLE 35

*Articles 35 (2) and 36 (2)*

##### *Hungary*

It is logical, that the maker of a promissory note can not exclude his obligation, since he promises his own payment. But, if it seems necessary to put it in express wording, then why is it not declared regarding the acceptor, too, in article 36 (2). It might be believed by an erroneous "*a contrario*" conclusion, that the acceptor may exclude his responsibility.

*Article 36 (1)*

##### *Mexico*

In the Spanish version, the use of the word "*hasta*" is clearly incorrect. The Spanish text should read: "*El librador no quedará obligado por la letra entre tanto no la acepte.*"

#### ARTICLE 37

*Article 37 (b)*

##### *Germany, Federal Republic of*

No convincing reason can be ascertained for evaluating the mere signature by the drawee on the reverse side of the bill of exchange as a declaration of acceptance. That rule may result in confusions with respect to endorsements and seems to be particularly dangerous in those cases in which a bill of exchange is endorsed in blank before the name of the drawee is inserted.

##### *Hungary*

It has not been specified that the mere signature of the drawee has to be on the face of the bill of exchange. This becomes only evident from article 42 (4) (b) (in chapter F: The "guarantor"). This is unfortunate because everybody would look for it logically in chapter D: "The drawee and acceptor".

#### ARTICLE 38

*Article 38 (3)*

##### *Mexico*

A broader formulation should be used. Any holder must be able to insert the date of acceptance. It is undesirable that this right should be reserved solely to the drawer, who is not a suitable person for presenting the bill for acceptance. Moreover, how is a third party to know who inserted the date of acceptance?

Suggested wording: "When a bill drawn payable at a fixed date after sight, . . .; failing such indication by the acceptor, the holder may insert the date of acceptance."

#### ARTICLE 39

##### *Spain*

As regards the acceptor's liability, article 39 requires that this be unconditional or "unqualified". "Qualified" acceptance is considered to be "non-acceptance", but the drawee is nevertheless bound according to the terms of his "acceptance". The principle defined here appears sound, aside from drafting considerations, but it is not in line with the principle applied to conditional endorsement, mentioned above (article 17; the endorsement is valid and the condition ineffective). Here, too, greater consistency would seem to be required.

*Article 39 (1)*

##### *China*

Paragraph (1) of article 39: "An acceptance must be unqualified. An acceptance is qualified if it is conditional or varies the terms of the bill."

Recommendation: This be changed into "An acceptance ought to be unqualified, but allowances are made for conditional acceptance."

##### *Czechoslovakia*

We recommend that the notion "variation of the terms" of the instrument be clarified, especially how it differs e.g. from the notion "material alteration" as used in article 31.

*Article 39 (3)*

##### *Canada*

This article introduces a concept which is both intricate and impractical. We are aware that many bills of exchange acts in force in the world today contemplate a partial acceptance. We are, however, not aware of any practical significance to these provisions.

Furthermore, statutes such as the Canadian Bills of Exchange Act, in making provision for such rare possibilities, go a great deal further than the draft Conventions in working through the implications for the parties of a partial acceptance. If article 39 (3) were to be accepted, it would be necessary to give further consideration to articles such as article 55 which at present refers only to dishonour by non-acceptance and perhaps would require an amendment to refer to partial dishonour by partial acceptance. If the point were of any practical significance we would undertake that exercise and suggest the appropriate amendments.

However, we consider that partial acceptance is a rare and undesirable phenomenon which should not be condoned or promoted by the draft Convention. Canada objects to the introduction of this concept in a final draft of the Convention and strongly requests its deletion since there is now not the time or the business purpose for taking the effort to assimilate it properly within the text of the draft Convention.

#### *Mexico*

Partial acceptance must be regarded as non-acceptance. This is not the traditional solution; see, for example, article 99 of our law LTOC and article 26 of the Geneva Uniform Law. But under that solution how can the non-accepted part of the bill be protested or returned?

Suggested wording: "Partial acceptance is regarded as refusal of acceptance."

## ARTICLE 40

#### *United States of America*

The United States suggests that this article be clarified by an amendment which would expressly state that an endorser does not have to be in the chain of title and that an anomalous signer has the liability of an endorser.

#### *Article 40 (2)*

#### *Mexico*

The limitation of liability to a part of the amount of the instrument raises the following question: How, with respect to the exercise of the rights of both, is the instrument to be divided by the endorser who pays partially and the holder from whom part of the payment is withheld?

On the other hand, the stipulation remains valid since it is authorized by the Convention. It is improper to say that it has effect only with respect to that endorser.

Suggested wording: "The endorser may exclude his own liability by an express stipulation on the instrument. Such stipulation has effect only with respect to the endorser who placed it."

## ARTICLE 41

#### *Czechoslovakia*

In our view this provision is needlessly complicated. For example it is not quite clear why the holder of an instrument in these cases, irrespective of his good faith, should be responsible for the fact that some signature on the instrument was forged. Apparently, it would be sufficient and would comply with trade intercourse that the holder who does not sign the instrument and transfers it by mere delivery is not liable according to the Convention on the instrument, but according to general provisions of the applicable law; i.e. he would be responsible to the person who took the instrument, on the basis of their relationship, possibly not even contractually, including his responsibility towards subsequent acquirers of the instrument, provided that he acted intentionally or negligently to their detriment.

#### *Denmark*

Presumably the provision refers to a person transferring an instrument on which his name has not been written. In view especially of the fact that we are dealing with international rules it will be complicated to apply this rule in practice. The Danish Government therefore recommends deletion of the said provision.

#### *Finland*

Under this provision any person who transfers an instrument by mere delivery is liable to any holder for damages. Liability is thus not limited to those transferors whose names appear on the bill of exchange. It may be doubted whether this is a technically sound solution, even if one may assume that the burden of proving that a certain person has transferred the bill of exchange rests on the party claiming liability on this ground.

#### *Germany, Federal Republic of*

Article 41 imposes upon the person who transfers a bill of exchange by mere delivery an extensive liability towards all subsequent holders with regard to defects in preceding signatures, material alterations or other defects in the bill of exchange. This provision seems to go too far and will most likely not promote the negotiability of international bills of exchange.

#### *Japan*

The liability which is imposed under article 41 on a person who transfers an instrument by mere delivery is liability off the instrument. It is questionable whether rules on such liability should be included in the Convention.

If, however, the Commission decides to include such rules in the Convention, the requirements for such liability should be carefully reexamined. According to the present text, a holder is entitled to claim damages from the person who transfers an instrument by mere delivery without the presentment and protest which are stipulated as necessary conditions for liability when the holder makes a claim against an endorser under article 40 (cf. articles 49, 53 and 55). There seems to be a lack of consistency here. Furthermore, it is not clear whether a holder making a claim under article 41 is considered theoretically to receive damages when he is able to make a claim against another party or parties on whom primary or secondary liability is imposed.

#### *Netherlands*

According to article 41, a person who transfers an instrument by delivery alone is liable to any subsequent holder for damages such holder suffered because of the fact that prior to such transfer there was a forged or unauthorized signature or a material alteration, or a claim or defence may be set up against him, or the instrument was dishonoured by non-acceptance or non-payment.

The Netherlands would prefer to see this provision deleted. It has no counterpart, neither in Dutch law nor in the Geneva Uniform Laws. Nor does the provision quite square with the warranty provisions of the UCC which apparently inspired the provision of article 41: according to section 3-417 (2), the warranty given by a transferee who transfers the instrument by delivery alone runs only to his immediate transferee.

It is submitted that article 41, if retained, would impair the circulation of international instruments and run counter to the fundamental principle, laid down in article 29 (1), that a person is not liable on an instrument unless he signs it. The fact that the commentary to article 41 states that the liability under the article is "off the instrument" is not convincing. Moreover, the provision as currently drafted would seem to impose greater liability on transferors by mere delivery than on transferors by endorsement and delivery. Whereas presentment and protest are conditions precedent to the liability of endorsers, the liability of transferors by delivery alone "materializes the moment the instrument is transferred, regardless of its date of maturity" (cf. Commentary, para. 2; *Yearbook 1982*, part two, II, A, 4). Furthermore, whereas under article 40 (2), the endorser may exclude or limit his own liability by an express stipulation on the instrument, the transferor by delivery alone has no such faculty.

If deletion of article 41 were not acceptable, the provision should be reexamined with a view to extending the liability contemplated in article 41 to both types of transferor.

#### *Norway*

1. An endorser has liability only under article 40, a transferor by mere delivery only under article 41. The liability of an endorser is thus in several respects less

than that of a transferor by mere delivery. This is an anomaly. We suggest article 41 be amended to apply to all transferors, both endorsers and transferors by mere delivery.

2. Article 41 (1) (a) interferes with the compromise of article 23 (1) in respect of forged or unauthorized endorsements. The deviation from the compromise seems unjustified. We suggest that subparagraph (a) of article 41 (1) be restricted to the forged signature of, or the unauthorized signature on behalf of, the drawer or the maker.

#### *Spain*

Concerning the liability of the endorser, it is surprising that, under article 41, liability is assigned to a person who transfers an instrument by mere delivery; that is, without his being an endorser and without his signature appearing on the instrument. He is liable for compensation to any person who has suffered damages as a result of events in which he had no hand, and of which he may even be unaware (see the comments above to article 23).

#### *United States of America*

This article applies only to those who transfer by "mere delivery" (i.e., without endorsing). An endorser has liability only under article 40. Therefore, the liability of an endorser is less, in many circumstances, than the liability of a transferor by mere delivery. The endorser could escape all liability on the instrument if the instrument is not correctly protested, regardless of forgery, alteration, etc. The United States proposes that article 41 be amended to apply to all transferors by deleting the words "by mere delivery" from the first line of article 41.

The purpose of such an amendment would be to make article 41 liability applicable to both endorsers and nonendorsers. (This warranty liability applies primarily in situations involving alterations and forged signatures of a drawer or maker. Under article 23 it seems not to apply in forged endorsement cases, for no damages result.) The proposed amendment would clarify the position of the anomalous endorser and of the transferor who adds an endorsement after a prior blank endorsement. Under the current language their liability appears to be determined by article 40 and not by article 41. If so, the current language allows them to escape liability for forgery, alteration, and valid defenses against them if the instrument is mistakenly paid or even if it is dishonoured and not duly protested. The United States believes that liability for damages caused by forgeries of an issuer's signature and material alterations should be imposed on both endorsers and nonendorsers, at least if not disclaimed.

## ARTICLE 42

#### *Japan*

(1) No provision of the present draft Convention makes clear whether an incomplete instrument may be

guaranteed or not, while it is clearly provided that an incomplete instrument satisfying the requirements set out in article 1 (2) (a) or (3) (a) may be accepted by the drawee (see article 38 (1)). It is, however, difficult to see any reason why guarantee should be treated in a manner different from acceptance. The Japanese Government proposes that a provision be added stating that such an instrument may be guaranteed before it has been signed by the drawer or maker, or while otherwise incomplete.

(2) With the present text of article 42 (4), it is not clear what the effect of the drawee's signature alone on the back of the instrument is considered to be. Additional rules would appear to be necessary.

#### *Article 42 (1)*

##### *Mexico*

The objections raised against the possibility of partial liability for an instrument apply here also. Again, in the case of partial performance, how are the parties to divide the instrument?

Suggested wording: "Payment of an instrument may be guaranteed for the account of any party. A guarantee may be given by any person who may or may not already be a party."

##### *Yugoslavia*

Under article 42 (1) "A guarantee may be given by any person who may or may not already be a party". Such a broadly formulated provision is unacceptable since *aval*, as is known, cannot be given by the primary parties of an instrument (acceptor of a bill or the maker of a note), because they are already bound to all parties who have signed the instrument.

#### *Article 42 (4) (a)*

##### *Mexico*

Our law LTOC (article 111) contains a more logical solution, which is recommended and according to which whenever a signature cannot be given another meaning, that signature constitutes a guarantee.

#### *Article 42 (4) (b)*

##### *Mexico*

This provision should be brought into line with article 37, subparagraph (b).

#### *Article 42 (4) (c)*

##### *Mexico*

This may lead to absurd solutions. If on the back of the instrument there is a signature which is not that of

the drawee and the latter has not been the legitimate holder of the instrument, how can it be considered an endorsement? It is suggested that this subparagraph be deleted.

#### *Article 42 (5)*

##### *Germany, Federal Republic of*

The irrefutable presumption that the guarantee for a bill is deemed to have been given for the drawee or the acceptor if the guarantor made his declaration of guarantee by his mere signature on the bill is very often not in conformity with the true will of the parties. This will is usually expressed by the fact that the guarantor's signature is right beside that of the person for whom the guarantee is given.

##### *Spain*

The provisions regulating the guarantee call for a comment on a substantive issue: the nature of this legal transaction. The guarantee is presented as applying to payment of the instrument (article 42 (1)), and it may or may not specify the person for whom it is given. If it does not, there is a presumption that the guarantee is given for the acceptor or the drawee (the maker in the case of a promissory note). Although the Commentary states that in respect of the liability of a guarantor the Convention follows in substance the provisions of the Geneva Uniform Law, this provision allows the guarantee to be given for the drawee, who is not liable on bills (cf. article 36 (1)). What is more, if nothing is specified and if the bill is not accepted, the presumption is that the guarantee is for the drawee, whereas the presumption in the Geneva Uniform Law is that it is for the drawer. It would appear that the characteristics of a guarantor for the drawee are different from those of any other guarantor, and he is therefore not subject to the same regulations. For example, the provision in article 43 (1)—that a guarantor is liable to the same extent as the party for whom he has become guarantor—does not apply to a guarantor for the drawee (cf. article 43 (2)). This seems to indicate that the concept of a guarantor for the drawee bears more resemblance to that of an acceptor than to that of a true guarantor. His liability is that of an acceptor who is not the drawee, who is not specified in the instrument as an alternate acceptor and who is not the acceptor by intervention who comes forward after a protest.

## ARTICLE 43

#### *Article 43 (1)*

##### *Denmark*

It seems odd that under this article a guarantor may limit his liability to something other than part of the amount of the bill.

## ARTICLE 44

### *United Kingdom of Great Britain and Northern Ireland*

A minor criticism is that it appears that the special right of the guarantor is not sufficiently specified.

## CHAPTER FIVE. PRESENTMENT, DISHONOUR BY NON-ACCEPTANCE OR NON-PAYMENT, AND RE COURSE

## ARTICLE 45

### *Netherlands*

Though a bill payable on demand is not usually presented for acceptance, article 45 (1) permits presentment for acceptance of such a bill and, according to article 47 (e), presentment is then to be made within one year of the date of the bill.

Article 45 (2) (c) states that a bill drawn payable elsewhere than at the residence or place of business of the drawee must be presented for acceptance, but makes an exception in respect of the demand bill. It is noted that paragraph 6 of the commentary of article 45 sets forth an explanation (see *Yearbook 1982*, part two, II, A, 4). However, the reason why a domiciled bill payable at a definite time must be presented for acceptance is equally valid in respect of a bill payable on demand.

## ARTICLE 46

### *Indonesia*

The stipulation on a bill whereby the drawer prohibits presentment for acceptance, permitted by this article, is also set forth in the Indonesian Commercial Code.

However, the draft Convention provides for the possibility that such a bill is presented for acceptance, notwithstanding the prohibition of such a presentment, and regulates its legal consequences.

The Indonesia Commercial Code does not regulate such possibility nor does it regulate the legal consequences. We would therefore consider that the provision stated in the draft Convention corresponds to the needs of international payments.

### *Article 46 (1)*

### *China*

Paragraph (1) of article 46: "Notwithstanding the provisions of article 45 the drawer may stipulate on the bill that it must not be presented for acceptance or that

it must not be so presented before a specified date or before the occurrence of a specified event."

**Recommendation:** This be supplemented by adding "But this article does not apply to the presentment for payment".

**The reason:** In actual business operation, presentment for acceptance "not . . . before the occurrence of a specified event" is sometimes mixed up with presentment for payment. For example, in documentary-payment/demand collection, the payment should be made immediately when the bill is presented and the document should be handed over to the payer. But, if a payer says that the bill must be presented for payment after the occurrence of a specified event (e.g., arrival of a ship or goods), this would delay the payment. Since a bill of exchange is an unconditional order to pay, the conditions required of presentment for acceptance are not applicable to presentment for payment.

### *Hungary*

For clearer drafting it is suggested to begin paragraph (1) of article 46 instead of the words "Notwithstanding the provisions of article 45" by the wording "in case of paragraph (1) of article 45".

### *Spain*

The provision in article 46 that the drawer may "stipulate on the bill that it must not be presented for acceptance" seems badly worded. To begin with, it is not strictly speaking a matter of "stipulation" (*estipular* in Spanish). Moreover, the apparent intention of article 46 is not to prohibit the presentment of the bill for acceptance, since acceptance is effective if granted, but to provide for all liable persons to be freed from any liability that might result from dishonour by non-acceptance. The provision would be better stated thus. It is a logical provision for the Convention to make, since it allows total exclusion of liability on the part of the drawer and endorsers.

### *Union of Soviet Socialist Republics*

The provision of paragraph (1) may, in practice, cause difficulties in that it gives the drawer the right to prohibit presentation of a bill for acceptance in those cases where, according to article 45 (2), a bill must be presented for acceptance.

This is especially evident if we take the example of a bill of exchange drawn payable at a fixed period after sight and with the drawer's stipulation prohibiting presentation of the bill for acceptance. If such a bill is not presented for acceptance or the drawee refuses to accept it, it would be impossible to determine the date of payment on the bill and, thus, the time when the party's liability on the bill arises. The objective of this rule is, apparently, to deprive the holder of the right to

immediate recourse, i.e. to recourse before the date of payment, if the bill is dishonoured by non-acceptance (article 46 (2)). However, this objective can be achieved in a simpler way that has already been provided for in the Draft Convention, by the drawer's stipulation on the bill of exchange excluding his own liability for acceptance (article 34 (2)).

We accordingly believe that the drawer's right to prohibit presentment of a bill of exchange for acceptance provided for in article 46 (1) should apply only to paragraph (1) of article 45.

#### *United States of America*

This article permits drawers to stipulate that a bill of exchange may not be presented for acceptance. Especially as to time bills of exchange, the holder may need to know whether the drawee will pay the instrument before the payment date. Denying this information to the holder may make the instrument of less value. The United States proposes that this article be deleted.

### ARTICLE 47

#### *Hungary*

Without modifying the text of article 47 it would be suggested to insert in the commentary an explanation to the effect that the holder of a bill may present it to the acceptor by proxy without endorsing the bill to this person.

#### *Spain*

The rules governing presentment for acceptance contain no reference to place, such as that given in article 51 relating to presentment for payment. Although this omission is justified in the Commentary (para. 3 under article 47; *Yearbook 1982*, part two, II, A, 4), it might be preferable for the place to be indicated.

#### *United States of America*

Although article 51 on presentment for payment has several paragraphs on where presentment must be made, article 47 on presentment for acceptance has no such paragraphs. The omission could be confusing, and these two articles should be conformed. Therefore, the United States proposes that article 47 be amended to add two new paragraphs modeled on article 51 (g) and (h).

#### *Article 47 (a)*

#### *Finland*

The expressions "business day" and "reasonable hour" both appear rather imprecise. It is proposed to

replace them by "banking day" and "banking hour" or by adding a provision according to which a State may in its national legislation determine the appropriate time for a bill's presentation.

#### *Norway*

1. The terms "business day" and "reasonable hour" are imprecise. We suggest that the Convention authorize the Contracting States to define these terms more precisely in their national legislation.

2. The bill must be presented for acceptance to the drawee or his agent at the place where they are at the moment, cf. subparagraph (a) and paragraph 3 of the commentary. Presentment for payment is "local". The bill may thus have to travel a long distance in a short time if the drawee is not resident in the place of payment. The holder may easily go astray. We suggest that the bill may be presented for acceptance at the places designated in article 51 (g) for presentment for payment. If the drawee or his agent cannot be found at that place, the bill is considered to be dishonoured by non-acceptance.

#### *Union of Soviet Socialist Republics*

Subparagraph (a) provides that for a bill to be duly presented for acceptance it must specifically be presented by the holder. Since in today's international practice bills are presented for acceptance by banks, which are not holders within the meaning of the law on bills of exchange, since they act in accordance with a general civil contract of agency and not on the basis of some special endorsement, a provision should be added to this subparagraph specifying that bills can also be presented for acceptance on behalf of the holder. The rule would, in principle, be in keeping with the basic Geneva and Anglo-American system of the law on bills of exchange.

#### *Article 47 (c)*

#### *Canada*

Canada considers that a rule which would validate an acceptance by a person and in a name other than that of the drawee is likely to create confusion and foster uncertainty. We are uncertain what entities might properly be described as "authorities" within the meaning of the subsection, but even if situations exist in individual contracting states where official, semi-official or governmental agencies have authority to accept bills of exchange drawn on resident nationals of the contracting state, it would be preferable, in our view, for the Convention to require the acceptance to be in the name of the drawee even though some additional text may be added to show that it is by the authority of the intervening agency.

*Article 47 (e)**Czechoslovakia*

Seen through the needs of trade, it appears necessary to extend the one year period mentioned.

**ARTICLE 48***Norway*

We suggest the expression "reasonable diligence" be worked out in some detail in the proposed commentary to the final text.

*Spain*

Article 48 raises problems. An optional presentment of a bill for acceptance cannot be said to be "*dispensada*" (i.e. "excused" or "not required"), since it was never a requirement. What is intended in the Convention is that in some cases, although the bill has never even been presented for acceptance, dishonour by non-acceptance should produce the effects described in article 50 (2) and render liable the persons referred to in article 48. The content of this article might be incorporated in article 50 (1) (b).

*United States of America*

This article establishes conditions under which presentment for acceptance can be excused but does not provide for delay in presentment for acceptance, even in circumstances involving *vis major*. In this omission, article 48 is at variance with articles 52, 58 and 63, which deal with delays in presentment for payment, protest, and notice of dishonour. The United States proposes that article 48 be amended to add a new paragraph, modeled on article 52 (1), which would allow delay in presentment for acceptance on the ground of *vis major*.

*Articles 48 and 50**German Democratic Republic*

Regrettably, no provision has been made for the holder to exercise, prior to maturity, his right of recourse against the parties liable upon such recourse, if the drawee is bankrupt or has suspended payments. There is no reason to regulate the case of bankruptcy or suspension of payments in a different way from that of a juridical person in liquidation as regards their effects on recourse. Practically, it is not acceptable for the holder of a bill of exchange/promissory note that he should have the right of recourse before maturity, if the drawee has no longer the power freely to deal with his assets by reason of his insolvency. The present version needs to be revised in order to provide also those possibilities for exercising the right of recourse before

maturity which are based on the Geneva Convention and have proved their practical effectiveness in many countries.

*Union of Soviet Socialist Republics*

The general approach of the draft Convention is that immediate recourse on a bill can be obtained only in cases where a bill is dishonoured by non-acceptance. In contrast to the Geneva Convention (ULB, article 43) the present draft Convention does not envisage the possibility of claiming against all the parties liable on the bill (drawer, endorsers and their guarantors; or against the acceptor and his guarantor) before maturity in the event of the drawee's insolvency or in the event of a suspension of payments on his part or where execution has been levied against his goods without result. This approach infringes substantially on the interests of the holder, who should in these circumstances be entitled to expect immediate satisfaction of all his demands, in particular from the guarantor of the acceptor or drawee, who in the case of international payments is normally a bank. It would thus be useful to provide for the holder's right to immediate recourse in the event that the drawee or the acceptor goes bankrupt or suspends payments.

*Articles 48 and 52**Japan*

Articles 48 and 52 set out the cases where presentment may be dispensed with. The Japanese Government suggests that the text should state clearly that any stoppage of payment on the part of the drawee is included in the grounds listed in articles 48 (a) and 52 (2) (d), instead of using the term "insolvency".

*Articles 48, 52, 58 and 63**United States of America*

There is no general provision in the Convention concerning the ability of the parties to vary the provisions or waive the requirements of the Convention by agreed-upon terms. The resulting ambiguity is particularly troubling in relation to waivers of presentment, notice of dishonour, and protest, which are commonly used in the United States. It would be desirable to amend articles 48, 52, 58, and 63 (which deal with dispensation of presentment, notice of dishonor, and protest) to allow waivers.

**ARTICLE 49***Norway*

The article sets out due presentment for acceptance of a bill as a condition precedent to the liability on the bill of the drawer, the endorsers and their guarantors.

According to article 53, due presentment for payment of an instrument is a condition. If the instrument is not duly protested, the drawer, the endorsers and their guarantors are no longer liable thereon, cf. article 59. If the holder loses his right of recourse on the instrument according to these articles, a drawer or an endorser may make an inequitable gain. The right of recourse being a right on the instrument, it seems unclear whether it will be contrary to the Convention if national law would furnish the holder with a claim off the instrument to such an inequitable gain. Anyway, the Convention ought to state explicitly that the contracting States are free to furnish the holder with such a claim, cf. the Geneva Convention, annex II, article 15.

#### *Articles 49 and 50*

##### *Hungary*

It would be desirable to provide for the holder's right to immediate recourse in the event the drawee or the acceptor goes bankrupt or stops payment—as is provided for by the Geneva Convention, article 43.

#### **ARTICLE 50**

##### *Hungary*

See comments by Hungary under article 49.

##### *Norway*

1. The alternative "acceptance cannot be obtained with reasonable diligence" in subparagraph (a) of paragraph (1) is superfluous in addition to subparagraph (b) and should be deleted.

2. The alternative "when the holder cannot obtain the acceptance to which he is entitled under this Convention" ought to include a reference to article 39.

##### *Spain*

The range of cases classed as dishonour by non-acceptance seems too wide; this makes the position of prior parties insecure (cf. article 50 (1) (a), to which drafting amendments should also be made).

#### *Article 50 (1)*

##### *United States of America*

Article 50 (1) states that dishonour occurs when "acceptance cannot be obtained with reasonable diligence" and when "the holder cannot obtain the acceptance to which he is entitled". Neither of these specifications is clear. If the latter specification refers to qualified acceptances, it is merely repetitive but would need a reference to article 39 to limit it properly. If the

former specification includes, in addition to the situation where the drawee hides, the situation where the drawee is available but the holder is delayed beyond the time limit by "*vis major*", it is objectionable. It would be improper to give the holder recourse against the drawer or an endorser because the holder failed to perform (even if due to impossibility), when the drawee was willing to perform. The United States therefore suggests that article 50 (1) be redrafted for greater clarity, with commentary to explain the purpose of different specifications.

#### **ARTICLE 51**

##### *Indonesia*

Presentment of an instrument for payment, as provided in this article, is also covered in the Indonesian Commercial Code. However the provision of the draft Convention is broader, i.e.:

- (1) Presentment for payment of a bill drawn upon or accepted by two or more drawees or of a note signed by two or more makers;
- (2) Presentment for payment in case the drawee or the acceptor or the maker is dead;
- (3) Presentment for payment to a person or authority, other than the drawee, the acceptor or the maker, entitled under the applicable law to pay the instrument.

The provisions mentioned above give the holder more advantages in solving problems relating to presentment for payment.

##### *Spain*

Section 2, "Presentment for payment and dishonour by non-payment", seems to provide too wide an area in which presentment for payment is dispensed with (article 52), for in many cases the parties will become liable for the dishonour by non-payment of an instrument which has not even been presented for payment (article 54). This is the same comment as was made above to article 50.

Specifically, it seems strange that article 51 should make presentment of the instrument an obligation when the drawee, acceptor or maker is dead, while article 52 dispenses with that obligation if the same persons lose the power freely to deal with their assets by reason of insolvency. The reference to the drawee's being "a corporation, partnership, association or other legal entity which has ceased to exist" also seems inappropriate. Similarly, it is hard to see why presentment for payment loses relevance when a bill has been protested for dishonour by non-acceptance.

##### *United States of America*

This article is similar to article 47 on time of presentment for acceptance, but there are several

unexplained differences from article 47. These differences appear in paragraphs (c), (g), and (h). The United States proposes that article 47 conform to article 51, and in particular that paragraphs modeled on article 51 (g) and (h) be added to article 47.

#### *Article 51 (a)*

##### *Czechoslovakia*

It is suggested that presentment for payment is due presentment if it is made within the two business days that follow the date of maturity.

##### *Hungary*

Under article 51 (a), a bill of exchange is to be presented for payment on a business day. Under paragraph (e) a bill of exchange expiring on a fixed day must be presented either on the date of the maturity or on the business day which follows. From the comparison of these two paragraphs and even considering article 8, it is ambiguous what the situation is if the maturity day is not a business day. Does paragraph (e) concern this very case? It is contradicted by the fact that paragraph (e) does not limit the utilization of the one day extension in the case where the maturity day is not a business day. But it has been nowhere declared that the generally accepted rule is that, if the maturity of any fixed day is not a business day, then the expiry date is the next following business day and not the previous one.

##### *Norway*

Regarding the terms "business day" and "reasonable hour" in paragraph (a), we refer to our comment to article 47.

#### *Article 51 (c)*

##### *Norway*

According to paragraph (c), if the drawee, the acceptor or the maker is dead, the instrument must be presented to his heirs or to somebody entitled to administer his estate. The different national arrangements for succession upon death varying widely, we fear that paragraph (c) will be open to a plurality of questions of interpretation and of application in the different national contexts. A better solution would perhaps be to entirely dispense with presentment for payment in these cases.

#### *Article 51 (e)*

##### *Denmark*

In view of the fact that these are international rules and that many of the provisions on limitation in both Conventions often stipulate considerably longer time

limits than those found in the corresponding Danish legislation it seems incongruous to note that (e) allows only one day for presentment for payment where the equivalent Danish provision (subsection 1 of section 38 of the Danish Bills of Exchange Act) allows a limit of two days.

##### *Japan*

Article 51 (e) provides that an instrument which is not payable on demand must be presented for payment on the date of maturity or on the business day which follows. The Japanese Government proposes that the words "on the business day which follows" be replaced by the words "on one of the two business days which follow", since the latter would be more appropriate if due consideration is given to the provisions of the draft Convention regarding protest for dishonour (article 57) and notice of dishonour (article 62) and to the relevant provision of the Geneva Uniform Law (article 38 (1)).

##### *Norway*

As we understand paragraph (e), the holder may choose between the date of maturity, provided that this day is a business day, and the following business day. Thus, if the instrument matures on a Friday, Saturdays and Sundays not being business days at the place of presentment, the holder may present the instrument either on the Friday or on the following Monday. If the instrument matures on a Saturday or a Sunday, the holder has only the following Monday at his disposal. The last implication seems to be too demanding. We suggest that, the day of maturity not being a business day, the holder has the two following business days at his disposal. Anyway, the proposed commentary to the final text ought to explain paragraph (e) in some detail.

#### *Article 51 (g)*

##### *Yugoslavia*

It is unclear whether the place of payment specified on the instrument is an essential element or not. Under most European systems, for instance, if the place of payment is not specified on the instrument, the instrument is presented for payment at the address of the drawee. If no place of payment is specified and the address of the drawee or the acceptor or the maker is not indicated, the instrument is deemed to be ineffective since it lacks an essential element. Furthermore, there is an impression that article 51 (g) does not fully conform to article 1 of the draft Convention.

#### *Article 51 (h)*

##### *Canada*

Canada believes that the amendments to permit presentment of international instruments at clearing houses are an improvement to the draft Conventions.

However, in both cases it may be necessary for the Conventions to include provisions in order to preserve and give paramountcy to the local rules of the clearing house. In other words, international instruments should only be presentable through domestic clearing facilities if they comply with the technical or legal requirements imposed by the clearing authorities for domestic instruments. Rules to the opposite effect in the Convention would be potentially disruptive of local clearing arrangements. We suggest that article 51 (h) be amended by adding at the end thereof the words "if in conformity with the rules of that clearing house".

#### *United Kingdom of Great Britain and Northern Ireland*

It is felt that the position as to presentment to a clearing house should be clarified because article 51 (g) and article 51 (h) appear to be at variance. It is suggested that this position could be clarified by amending article 51 (h) to read as follows:

"Notwithstanding article 51 (g), an instrument may be presented for payment to the representative or authorised agent of the drawee or the acceptor or the maker at a clearing house."

Presentment for payment at a clearing house has not been taken into account in articles 68 (4) (a); article 70; article 71 (2) (b) (i), (2) (b) (ii) and (4), and article 72 (2) (a).

### ARTICLE 52

#### *United States of America*

See comment by the United States under article 48.

#### *Article 52 (1)*

#### *Canada*

This article excuses delay when caused by circumstances which are beyond the control of the holder. The resources of large international banks are considerable. The obstacles which they could overcome by the full application of those resources might include many that it would not be commercially reasonable for anyone to expect them to avoid or overcome on behalf of a customer in a purely routine transaction. In commercial agreements entered into by Canadian banks it is customary to refer to circumstances which are not reasonably within the control of the party to avoid or overcome. We consider that this terminology introduces a test which is sensitive to the costs and benefits to be obtained from action. Canada recommends that the Convention be amended to reflect this more lenient test.

#### *Article 52 (2) (a)*

#### *Hungary*

There should be excluded from paragraph (2) (a) the possibility that the drawer and endorser or guarantor may waive presentment of the instrument for payment

by "implication". It is suggested that the waiver must be expressed.

#### *Union of Soviet Socialist Republics*

For the reasons set forth in the remark on article 30, it would be desirable to delete the reference in paragraph (2) (a) to the possibility that the drawer, an endorser or guarantor may waive presentment of the instrument for payment "by implication". Besides it is not clear how a waiver "by implication" can be made on the instrument (the Commentary does not cite a relevant example). From a practical point of view it would be sufficient if the Convention, in addition to providing for a waiver made expressly on the instrument, also provided for a waiver made expressly outside the instrument.

#### *Article 52 (2) (c)*

#### *Canada*

The combined effect of this paragraph and paragraph (f) of article 51 will be that instruments payable on demand may validly be presented to the drawee or acceptor one year and thirty days after their date of issue. Of course, the drawee will not have any way of ascertaining whether presentment for payment was validly extended by *vis major*. As a result, it will be difficult for the drawee to ascertain its duty with respect to the instrument. Canada considers that it would be preferable for the one year time limit established in paragraph 51 (f) to be a maximum, not extendable by any circumstances.

### ARTICLE 53

#### *Norway*

See comment by Norway under article 49.

#### *Article 53 (3)*

#### *Denmark*

Apparently failure to protest and present for payment has the effect of wiping out all claims except those on the parties listed under paragraph (3). From a Danish legal point of view there should be recourse to file a claim under the doctrine of unjustified enrichment, as specified in Danish Cheques Act sections 57 and 74, compare draft Convention on International Cheques articles 45 and 52.

### ARTICLE 54

#### *Denmark*

As we are dealing with international rules it would seem appropriate to lay down rules specifying when non-payment has taken place.

*Article 54 (2)**Canada*

Canada is aware of the distinction in some legal systems between rights of action on bills of exchange and rights of recourse on the same instruments, but the distinction is not so well established that we can satisfy ourselves that this section might not be open to misinterpretation. We think that no ambiguity in drafting ought to create a risk that the obligations of the acceptor in article 36 (2) and of any guarantor for the acceptor in article 43 (2) are in any way qualified by article 54 (2). Canada therefore suggests that the section be revised to refer to an "immediate right of action against the acceptor and any guarantor for him, and rights of recourse against the drawer, the endorsers and their guarantors".

*Article 54 (2) and (3)**Mexico*

It would be better to speak of exercising the appropriate rights rather than a right of recourse.

Suggested wording: "if a bill is dishonoured . . . , the appropriate rights against the endorsers and their guarantors".

*Spain*

Paragraphs (2) and (3) of article 54 should provide for the holder to exercise a right of recourse against all the parties, including the acceptor and the maker, who are omitted in the present text.

**ARTICLE 55***Czechoslovakia*

The article should be completed by giving the holder a right of immediate recourse in cases where the drawee, acceptor or maker declares bankruptcy or ceases payment, or where bankruptcy or liquidation proceedings upon the property of these debtors are opened. This right of immediate recourse should not depend on observance of the provisions of articles 48 to 50.

*Denmark*

It is a cumbersome procedure that one's rights of recourse can be exercised and the instrument be protested only after it has been dishonoured in conformity with the provisions of article 54.

*Mexico*

On the grounds put forward in commenting on the previous article, the following wording is suggested: "If

an instrument has been dishonoured by non-acceptance or by non-payment, the holder may exercise the appropriate rights only after the instrument has been duly protested for dishonour in accordance with the provisions of articles 56 to 58."

*Spain*

Section 3, "Recourse", begins by regulating protest. The categorical statement in article 55, ". . . the holder may exercise a right of recourse only after the instrument has been duly protested . . .", is not in complete accordance with the rest of the regulations on protest. It is in conflict, particularly, with article 56 (3) which allows the protest to be replaced by a declaration written on the instrument, unless there is a stipulation to the contrary. True, sub-paragraph (4) removes the inconsistency by providing that a declaration of this kind is deemed to be a protest. But it would, in any case, be desirable to amend article 55, which also conflicts with the wide range of cases in which protest is dispensed with under article 58, although this range itself seems excessively wide. For example, subparagraph (2) (d) provides that protest is dispensed with in all cases where presentation of the instrument is also dispensed with. This increases still further the insecurity of liable persons whose liability becomes effective, as mentioned above. The reasons for the dispensation in all these cases are really not clear, for the protest could serve to prove dishonour regardless of whether or not the instrument was presented.

On the other hand, the flexibility characterizing the protest regulations, and specifically the provision for the protest to be replaced by the declaration mentioned above, deserves approval. The CSB welcomed this provision, "since there can be no better evidence of the refusal to accept or to pay than a declaration by the liable persons themselves". This declaration may not be made in a separate document, but it should perhaps be allowed on a sheet attached to the instrument.

*Uruguay*

We suggest that it be explained in the draft text that the recourse allowed by the instrument is executory, using appropriate wording to indicate that it allows summary enforcement proceedings.

**ARTICLE 56***Article 56 (1)**Norway*

Under paragraph (1) a protest may be made in the form of a statement by a "person authorized in that respect by the law of that place". We presume that it will not be contrary to the Convention to authorize other than public bodies, e.g. banks to certify dishonour.

*Article 56 (2)**United States of America*

Article 56 (2) allows a protest to be made on the instrument itself, on an affixed slip ("allonge") or on a separate document. Article 56 (3) allows replacement of protest by a signed, dated declaration of dishonour by the drawee, acceptor or maker, but requires that this declaration be written on the instrument itself. As it is doing with respect to article 49 of the draft Convention on International Cheques, the United States proposes that article 56 (3) be amended to allow the drawee bank's declaration of dishonour to be written "either on the instrument itself or on a slip affixed thereto ('allonge')". Such an amendment would be in accordance with banking practices and would give the banks greater flexibility.

*Article 56 (2) (b)**Mexico*

The instrument itself should bear an indication of the fact that it was protested.

*Article 56 (3)**Norway*

According to paragraph (3), if a protest is replaced by a declaration of non-acceptance or non-payment, the declaration must be written on the instrument. We suggest the alternatives (a) and (b) of paragraph (2) also be allowed to achieve greater flexibility.

**ARTICLE 57***Hungary*

In order to determine clearly the time-limits for making protest it seems to be more appropriate to include a provision similar to article 44 of the Geneva Convention.

*Indonesia*

The time limits within which an instrument must be protested for dishonour, provided in this article, are also found in the Indonesian Commercial Code.

The draft Convention stipulates a shorter time limit within which the instrument must be protested so as to enable the holder to execute his right of recourse against the parties liable. Therefore the draft Convention gives legal assurance to the holder.

*Union of Soviet Socialist Republics*

This article relates the time-limits for making protest to the time when the bill was dishonoured by non-acceptance or non-payment. However, these times

cannot be determined exactly in all cases, especially in the case of bills payable on demand or payable at a fixed period after sight, and this may cause disputes between the parties and thereby in itself delay the bill recourse. Therefore, in determining the time limits for making protest for non-acceptance or non-payment it would seem more acceptable to include a provision corresponding to the Geneva Convention (ULB article 44), viz.:

"1. Protest for dishonour of a bill of non-acceptance must be made within the time-limits fixed for presentation for acceptance (article 47 (d), (e) or (f)) and if presentment for acceptance is made on the last day of the time allowed, protest must be made on one of the two business days following it.

"2. Protest for dishonour on a bill by non-payment must be made within the time-limits fixed for presentment for payment in accordance with article 51 (e) or (f) or on one of the two business days following it and if a bill payable on demand is presented on the last day of the time allowed under article 51 (f), protest must be made on the first business day following it."

**ARTICLE 58***United States*

See comment of the United States under article 48.

*Article 58 (2) (a)**Czechoslovakia*

Implied waiver of protest may give rise to considerable trouble in practice and in the interpretation of the draft Convention.

A similar problem may occur with articles 30 and 52.

*Hungary*

As a consequence of our comments to article 52 (2) (a) above it is suggested to delete the reference to waiver by implication.

*Union of Soviet Socialist Republics*

For the reasons set forth above it would be desirable to delete from this article the reference to a waiver by implication.

*Article 58 (2) (f)**Canada*

In earlier drafts, an article 61 (f) was included at the end of what is now article 58 (2) which provided:

"If the person claiming under article 80 (the old article dealing with lost instruments) cannot effect

protest by reason of his inability to satisfy the requirements of article 83."

We cannot locate a similar ground for dispensing with protest for dishonour by non-acceptance or non-payment in the current draft. We consider that the holder of a lost instrument should not be prejudiced by failing to protest a lost instrument. The United Kingdom and Canadian Bills of Exchange Acts provide that where a bill is lost or destroyed or wrongly detained or accidentally retained in a place other than where it is payable, protest may be made on a copy or written particulars of the bill. Canada recommends that consideration be given to an express provision of this nature in the draft Convention.

#### ARTICLE 59

*Norway*

See comment of Norway under article 49.

#### ARTICLE 60

*Germany, Federal Republic of*

The suggested extension of the duties to give notice which is different from the Geneva system seems hardly to be practicable: on the one hand, it may lead to all persons concerned being given notice by all others; on the other hand, the persons party to a bill of exchange often only know their immediate previous holder.

*Mexico*

Although it may be thought that, with the provisions of article 63, this is enough, it would be useful to specify that the obligation to give notice only exists when the domicile of the persons to be notified appears on the instrument, or when the holder knows the domicile.

It is suggested that a paragraph (5) be added with the following wording: "In the case of a person whose domicile is not indicated on the instrument there is no obligation to give this notice, unless the person who is to give it knows the said domicile."

*Norway*

With reference to paragraph (3) and the example in the commentary, we mention that according to the language of paragraph (3), the person B in the example must give notice of dishonour to A when he is notified by C.

*Spain*

With regard to the regulations on notice of dishonour, the following points must be made: first, notice

is not dispensed with, as is protest, whenever the requirement to present the instrument for acceptance or payment is dispensed with; second, the combination of requirements for notice in paragraphs (1) and (3) of article 60 may be excessive (to the CSCC, the relationship between these two paragraphs was unclear); third, too much freedom is allowed as to the form of notice, for even oral notice would meet the requirement of article 61 (CSB opinion); fourth, failure to meet the requirements for notice does not "impair" the instrument, but merely makes the party who failed to give notice liable for the damages resulting from such failure.

#### ARTICLE 63

*Article 63 (2) (b)*

*Hungary*

See comment of Hungary under article 58 (2) (a).

*Union of Soviet Socialist Republics*

See comment of the USSR under article 52.

#### ARTICLE 64

*Yugoslavia*

Articles 64 and 66 provide for strict sanctions against the holder of an instrument who fails to give notice of dishonour. If he fails to give such notice, he shall be liable for any damages which a party who is entitled to receive that notice may suffer from such failure, including the amount of the instrument. If this paragraph is retained, then a party who has a right of recourse may be unjustly enriched. This is obviously a question of direct and indirect damages. The draft Convention should adopt a stand that failure to give a notice renders a person who is required to give such notice liable only for direct damages.

#### ARTICLE 65

*Spain*

Article 65, which directly concerns the general issue of recourse, seems out of place in section 4. Reference has been made in our general remarks to the fact that there is no specification of the nature of the claims, and to the procedural problems to which they might give rise. It must also be pointed out, with reference to article 65, that the joint and several nature of the parties' liability is not established, and that the provision for the holder to proceed simultaneously against various liable persons may cause difficulties with regard to subsequent claims for final settlement of rights on a bill or note.

## ARTICLE 66

*Article 66 (1) (b)**Spain*

The last section in this chapter is section 4, "amount payable", which contains a set of requirements of great practical importance, regarding the method of establishing that amount in every case. Doubts will always arise as to whether the specified rates of interest are those most appropriate. With respect to the expenses referred to in article 66 (1) (b), the CSCC recommends that bank and collection costs be explicitly included.

*Article 66 (1) (b) (ii)**Norway*

1. No. (ii) of subparagraph (b) of paragraph (1) specifies the rate at which interest is to be paid after maturity. Even if the instrument stipulates for a rate of interest to the date of maturity which is higher than the rate provided for in paragraph (2), the rate of paragraph (2) seems to apply after maturity. We suggest that if the rate of interest stipulated in the instrument is higher than the rate of paragraph (2), the rate of the instrument shall continue to apply.

2. In several countries, the general rate of delay interest is higher than the rate provided for in paragraph (2). In Norway, the general rate for the time being is 15 per cent per annum, and the rate according to paragraph (2) would have been about 10 per cent today. This seems too low and in any case anomalous. We suggest that paragraph (2) refer primarily to the general rate of delay interest in the country where the instrument is payable.

*Article 66 (1) (b) and (c) and article 67 (c)**Mexico*

There is no mention of the right to recover the costs incurred in collecting the instrument. Could this have been an oversight?

*Article 66 (2)**Finland*

This provision would have the effect that the rate of interest on delayed payments would differ from the rate of interest on other obligations. It would seem more appropriate to refer in this paragraph first to the rate applied for interest on sums in arrears in (the main centre of) the country where the instrument is payable.

*German Democratic Republic*

The rate of interest to be fixed in the last sentence of paragraph (2) should be such as not to constitute an incentive for the party liable to default at maturity. Taking into consideration the development of rates of interest for the main currencies, a rate of 9.0 per cent is proposed.

*United Kingdom of Great Britain and Northern Ireland*

As the United Kingdom has no official rate of interest a suitable formula would have to be provided to deal with this omission.

*Article 66 (2) and (3)**Czechoslovakia*

We recommend to fix, in a subsidiary way, the interest at the rate of 8 per cent, at the minimum.

*United States of America*

The numbers in brackets in paragraphs (2) and (3) are too low. The United States proposes that these figures be raised to the range of "[5]" or "[6]".

## CHAPTER SIX. DISCHARGE

*Section 1. Discharge by payment**Australia*

Discharge by payment is dealt with in the draft Conventions in considerably more detail and particularity than in the BEA. However, it does not appear that the Convention provisions will give rise to any difficulty and may even have the advantage of answering a number of questions that arise under the BEA system.

## ARTICLE 68

*Article 68 (3)**Norway*

Paragraph (3) deals with the problem of "*ius tertii*". The position of a party liable on the instrument may be rather delicate if a third party asserts a claim to it. The problem is not confined to bills of exchange and promissory notes and is in several countries dealt with by specific rules on discharge by paying the amount due into court or by other similar procedures. We suggest that paragraph (3) refer to the national law of the place of payment regarding such arrangements.

*Spain*

Section 1 of this short chapter entitled "Discharge" starts with the essential issue of the discharging effects of payment. The regulations on this issue revert to the distinction, commented on above, between a "protected holder" and an "unprotected holder", which again raises serious problems in connection with the discharging effects of payment. Particularly controversial is the assumption that the party liable for payment is aware that the holder has knowledge of certain facts and is therefore not "protected". The party may invoke this "knowledge" by the holder as a defence against the latter's claims.

*United States of America*

Article 68 (3) is the Convention's attempt to deal with the *ius tertii* problem. The Convention protects any payor who pays a protected holder and any payor who pays a non-protected holder, so long as the payor does not know of a third party's claim, etc. The only situation in which the payor is not discharged is that in which he both pays a non-protected holder and knows of the third party claim, etc. However, a third party claimant should be permitted to delay payment long enough to seek court resolution of competing claims if the claimant both notifies the payor and provides sufficient indemnity. The Working Group omitted the indemnity mechanism in article 68, apparently deliberately, but used it extensively in articles 74-79 on lost instruments. The United States proposes that article 68 be amended to make an exception to discharge of the payor where the third party claimant both notifies the payor of its claim and provides security deemed adequate by the payor before the instrument has been paid by the payor.

*Article 68 (4)**Czechoslovakia*

We recommend the following formulation: "A person receiving payment of an instrument must, unless agreed otherwise, deliver to any person making such payment, the instrument, a receipted account, and any protest."

**ARTICLE 69***Indonesia*

Partial payment, regulated by this article, is also covered in the Indonesian Commercial Code.

Article 69 provides for the possibility that the holder takes or refuses partial payment and regulates the legal consequences, whereas the Indonesian Commercial Code prohibits such refusal and does not regulate the legal consequences.

The draft Convention's concepts are described in more detail and would solve the problems that may arise.

*Yugoslavia*

The wording that "The holder is not obliged to take partial payment" is too narrow and renders the position of the parties liable more difficult. A paragraph stipulating that "The holder cannot refuse partial payment" would be more acceptable since it will (even partially) help attain the goal for which the instrument was drawn, and thus reduce the expenses of protest and of notices.

**ARTICLE 70***Indonesia*

This article provides that the holder may refuse an offer that the instrument be paid in a place other than the proper place for due presentment for payment. If the holder refuses, the instrument is considered to be dishonoured by non-payment. The Indonesian Commercial Code does not contain such a rule. This provision has the advantage of enabling the holder to refuse or accept such an offer.

*Spain*

The provisions of article 70 are too severe and should perhaps be qualified somewhat.

**ARTICLE 71***Netherlands*

Article 71 is concerned with instruments drawn or made in a currency other than the currency of the place of payment. The proposed rule is that such instruments are to be paid in the currency in which the amount of the instrument is expressed. In this respect article 71 constitutes a departure from Dutch law (article 140 K) and the Geneva Uniform Law (article 41) which, in such a case, allow payment in local currency.

It is recognized that the rule proposed by article 71 has the advantage of minimizing the risk of loss inherent in fluctuations in exchange rates. As such it would deserve support. But it is doubtful whether the rule is practicable: the foreign currency in which the amount is expressed may not be available in the place of payment or payment in the foreign currency may violate the exchange control regulations of the State in which the place of payment is situated.

Most of the concerns which legitimately occupied the UNCITRAL Working Group could probably be met by allowing conversion of the foreign currency into local currency (unless there is a stipulation on the instrument for effective payment in the foreign currency) and to specify along the lines of article 72 at what rate and on what date such conversion is to be made.

*Yugoslavia*

Too detailed provisions of this article may be more confusing than simple general principles. It is suggested therefore that they be simplified and clarified, because the question of the currency in which an instrument may (the word "must" should be deleted) be paid is extremely important for the parties.

*International Monetary Fund*

Our final observation concerns the references to rates of exchange (article 71 of the bills and notes convention, article 64 of the cheques convention) and to rates of interest (article 66 of the bills and notes convention). Each of the Contracting States to the conventions should be advised to assure itself, as well as UNCITRAL, that these references are sufficiently clear and appropriate to be readily ascertainable.

*Article 71 (2)**Mexico*

The reference to the drawer or maker is incorrect; it should be the acceptor. The drawer may make this indication only after the instrument has been presented to him, and in this case he must accept or refuse the instrument. In any event, if the drawer is accorded this right, it is not clear why it should not also be given to the acceptor.

On the other hand, it seems unjust to require the holder to accept a currency other than that specified on the instrument, since the alternative currency may be a weak one or subject to various taxes or to exchange control as is currently the case in Mexico.

*Articles 71 and 72**Spain*

Articles 71 and 72 contain provisions of the highest practical importance, in particular for international instruments.

This issue should be dealt with in conjunction with article 4 (11) whose content, as we have seen, is still under consideration.

**ARTICLE 72***Indonesia*

Payment in a currency which is not that of the place of payment is subject to exchange control regulations.

Such provision is not regulated by the Indonesian Commercial Code. However, this provision is in line with the Indonesian exchange control regulations.

*International Monetary Fund*

One important effect of this provision is to make clear the priority of members' obligations under article VIII, Section 2 (b) of the Fund's articles of Agreement over other possibly conflicting obligations that might be undertaken by a Contracting State under the UNCITRAL conventions. We are glad to note the explanation of the commentary of this provision which reads in part:

"... The regulatory provisions referred to in this article are not only those of the Contracting State itself but include those which the Contracting State is bound to enforce by virtue of international agreements to which it is a party. An example of the latter type of regulatory provisions is article VIII, section 2 (b), of the articles of Agreement of the International Monetary Fund according to which 'exchange contracts which involve the currency of any member and which are contrary to the exchange control regulations of that member maintained or imposed consistently with [the Fund] Agreement shall be unenforceable in the territories of any member.'"

*Article 72 (2)**Canada*

Canada notes and supports the amendment to this article by which the holder is permitted to elect between the rate of exchange at the date of breach and at the date of payment. But we consider that some provision should be added limiting the time available to the holder in which to make his election. It would be obviously unjust to the defaulting party to permit the holder to conduct a prolonged foreign exchange currency speculation at his expense. The Convention ought to provide that the election ought to be made within a specified time or a "reasonable time".

**ARTICLE 73***Spain*

Section 2 is inappropriately entitled "Discharge of a prior party". The section consists of a single article (article 73). The first paragraph refers in far too general terms to "any party who has a right of recourse". The second paragraph should mention not only the drawee, but also the acceptor, since the two are usually mentioned separately by the draft Convention, and the guarantor for the drawee, in order to be consistent with the provisions relating to this curious concept.

**CHAPTER SEVEN. LOST INSTRUMENTS****ARTICLE 74***Czechoslovakia*

With respect to the possibility that the obligation on an instrument is paid in instalments, it will be useful in

practice that duplicates and copies of an instrument may be drawn or made. Therefore it would be convenient if the draft Convention regulates these questions.

#### *Denmark*

Both the Danish Cheques Act and Bills of Exchange Act contain provisions on cancellation, but the rules set out in article 74 are material and in conformity with banking practice.

#### *Indonesia*

This article is conform to the Indonesian Commercial Code: the ex-holder retains his rights to payment of the instrument. In order to obtain payment, the Indonesian Commercial Code requires that the ex-holder is under the obligation to give security to the person from whom he claims payment for a period of 30 years. On the other hand, to exercise such rights, the draft Convention requires the holder:

1. To give security, of which the nature and the terms are determined by an agreement between the holder and the payor;
2. To submit a written statement concerning the elements and the facts of the lost instrument.

#### *Japan*

The provisions of the draft Convention referring to lost instruments are modelled on the Anglo-American system, but the Japanese Government is prepared to accept them in the spirit of compromise. However, the following suggestions for improvement might be made.

Article 76 (1) provides that a person losing an instrument has, subject to the provision of paragraph (2), the same right to payment which he would have had if he had been in possession of the instrument. On the other hand, (2) (b) of the same article provides that a party from whom payment is claimed under a lost instrument may require the claimant to give security. It is not made clear by these provisions whether or not the party from whom payment under a lost instrument is claimed has to pay interest after maturity before the security is given in response to the request made under article 74 (2) (b). If clarity is desirable here, an additional provision would appear to be necessary.

#### *Norway*

1. We generally approve of the provisions on lost instruments. However, there will be cases where the ex-holder cannot comply with the requirements of subparagraph (a) of paragraph (2). For example, the ex-holder has forgotten the series of uninterrupted endorsements or the date of the instrument. In these cases, we presume it will not be contrary to the

Convention to apply national law on cancellation of negotiable instruments.

2. As we understand subparagraphs (b), (c) and (d) of article 74 (2) and article 78, the ex-holder will not be personally liable to the payer in addition to the payer's access to the security or to the amount deposited. We would prefer that the ex-holder also were personally liable.

#### *Articles 74 to 79*

#### *Netherlands*

The approach to lost instruments in articles 74 to 79 of the draft Convention is similar to that followed by Dutch law (article 167a and b K) in that the person who lost the instrument and thus cannot exhibit it when demanding payment may nevertheless claim payment though he may be required to give security to the party paying.

The provisions on lost instruments, it would appear, are drafted on the assumption that the instrument is lost before it becomes payable. They do not deal with the situation where the instrument has become due and was protested for non-acceptance or non-payment. In the latter event, article 74 (2) should require that the person claiming payment of the lost instrument must also produce the protest, if it was made in a separate document, or, if made on the instrument itself, the elements of the declaration of protest on the instrument.

The provisions on lost instruments are also drafted on the assumption that the drawee will not pay a lost instrument since he is under no obligation to pay. The assumption is probably correct and it is probably not necessary to provide for the rare instance where the drawee does pay, though Dutch law (article 167a K) envisages this possibility.

#### *Spain*

Under article 74, a person who loses an instrument maintains the same rights as if it had stayed in his possession, provided that he states in writing the data listed in subparagraph (2) (a). Article 79 establishes a similar provision for a party who has paid a lost instrument. In the latter case, however, the only explicit requirement is that he must be in possession of "the received written statement" (an unfortunate expression, in any case). It would appear that the written statement with the data specified in article 74 (2) (a) (referred to also in article 78) is likewise required. The connection between articles 74 and 79 is not clear from the draft.

#### *Yugoslavia*

These articles introduce new rules applicable in cases when an instrument is lost, whether by destruction,

theft or otherwise. It is not in the interest of the bill to delete the rules governing cancellation and instead to introduce these rules.

## ARTICLE 75

### *Indonesia*

This article deals with "notification" which is not regulated by the Indonesian Commercial Code. The purpose of the notification is to enable the ex-holder to assert a claim against a subsequent holder.

The provision would benefit any holder who lost his instrument.

### *Article 75 (1)*

### *Mexico*

The party who has paid may not know the domicile of the person he paid.

Suggested wording: "A party who has paid a lost instrument and to whom the instrument is subsequently presented for payment by another person must notify the person whom he paid of such presentation, unless he is ignorant of his domicile."

### *Article 75 (2)*

### *Mexico*

The procedure for giving notification is very briefly described, especially if compared with the text of article 61, although notification would seem more important in the latter case.

Suggested wording: "Such notification must be given in the manner prescribed in article 61."

## ARTICLE 76

### *Norway*

We refer to our second comment to article 74.

Paragraph (2) of article 74 deals with release of the security. We suggest a parallel provision on release to the ex-holder of an amount deposited.

### *Spain*

A safety system is established for the case where a "party" is forced to make payment twice (article 76 (1), first part). The system seems adequate as far as the deposit is concerned, but inadequate as regards "security", if there has been no agreement on this and the "party" has to accept such security as the judge may determine, even if it is not "to his satisfaction".

Article 76 also recognizes the right of a party "who by reason of the loss of the instrument, then loses his right to recover from any party . . ." to realize the security or to reclaim the amount deposited. This article is also hard to understand and suffers, as does the whole chapter, from a lack of clarity and precision.

### *Article 76 (2)*

### *Japan*

Article 76 (2) provides that where security is given in accordance with article 74 (2) (b), the person who has given security is entitled to obtain release of the security when the party for whose benefit the security was given is no longer at risk to suffer loss because of the fact that the instrument is lost. The Japanese Government suggests that a corresponding right be given under the same circumstances to the party for whom a deposit has been made in accordance with an order made under article 74 (2) (d).

## ARTICLE 77

### *Norway*

The alternative of dishonour by non-acceptance is left out by mistake, cf. paragraph 1 of the commentary.

## ARTICLE 79

### *Indonesia*

This article lays down a provision regarding payment to the ex-holder of a lost instrument in accordance with article 74. Such party may acquire such rights of recourse against prior parties as the ex-holder would have had if he had been in possession of the instrument. In this connection the Indonesian Commercial Code sets forth the same rules, except for the right of recourse against the endorser.

### *Norway*

Paragraph (2) seems too severe on the payer of a lost instrument. He ought to have an opportunity, parallel to article 74, of replacing the statement he received by a new written statement.

### *United States of America*

Article 79 (1) provides a payer of a lost instrument with the rights of a payer in possession of a paid instrument, but paragraph (2) requires such a party to be in possession of the receipted writing referred to in article 78 in order to obtain these rights. There is no explanation as to why the Convention requires actual possession of a particular piece of paper, rather than mere proof by the payer of his payment of a lost

instrument. This imposes too harsh a penalty on the payor who loses the received writing. The United States therefore proposes that article 79 (2) be amended to require only that the payor of a lost instrument prove his payment in order to have the rights of a payor, and that possession of the received writing be presumptive proof of such payment.

## CHAPTER EIGHT. LIMITATION (PRESCRIPTION)

### ARTICLE 80

#### *Australia*

The draft Conventions introduce special rules governing the period of time within which an action on the instrument must be brought and the point of time from which that period starts to run. The Conventions introduce a general period of limitation of four years for actions against any party, whether primarily or secondarily liable, subject to extensions where an action may be brought by a party secondarily liable against a party liable to him. This period of limitation is shorter than the general period specified for civil actions under the legislation of the Australian States (6 years). However, it is not felt that the reduction in the limitation period will cause any real difficulties for the Australian business community.

#### *Denmark*

As we are dealing with international rules the period of limitation should reasonably exceed the six-month period of limitation stipulated in section 52 of the Danish Cheque Act. However, a four-year period of limitation, as laid down in the draft Conventions, seems entirely out of proportion.

#### *Finland*

It might be useful to add a provision to this article on possible interruption of the period of limitation.

#### *Indonesia*

This article sets forth special rules in respect of the period of time within which an action arising on the instrument must be brought and the point of time from which such period starts to run. This provision is also contained in the Indonesian Commercial Code.

However, the draft Convention does not discriminate between the parties against whom recourse action is exercised, and stipulates a longer period of time.

The period of time provided by the draft Convention is brought about by the international character of the instrument which involved many places in different countries.

#### *Japan*

The principle underlying article 80 is acceptable. According to Example B, paragraph 2 of the commentary (A/CN.9/213, *Yearbook 1982*, part two, II, A, 4), where a party who has paid within a year before the expiration of the period prescribed in article 80 (1) exercises the right of recourse against a prior party in accordance with paragraph (2) of the same article, the prior party is given a full year from the date on which he paid the party exercising the right of recourse within which to bring an action against a party prior to him. However, the text itself does not make this clear. The Japanese Government suggests that the text state the rule expressly.

#### *Mexico*

No limitation is foreseen on the right of action against the guarantor of the drawee.

#### *Norway*

The Norwegian Government favours a limitation period of three years.

#### *Spain*

The draft Convention ends with a chapter on "Limitation", consisting of a single article on which a few very specific remarks will suffice.

First of all, some comments on the terminology: the expression with which the provision begins is incorrect ("el derecho de acción derivado de un título no podrá ejercerse . . ."); subparagraphs (1) (a) and (1) (b) speak [in the Spanish version] of the "firmante" (party) where the reference should be to the "maker" of a promissory note and not just to any "party" to an instrument. This terminology leads to confusion and should be carefully revised.

Secondly, no reference is made to the limitation or prescription of an action against the guarantor for the drawee.

Lastly, the reference to the date of dishonour in subparagraph (d) of paragraph (1) seems to be incomplete in the Spanish version; non-acceptance ("falta de aceptación") alone is mentioned, and a reference to non-payment would seem to be required also.

#### *Uruguay*

We suggest a wording on the following lines:

"A right arising on an instrument shall cease to exist after four years have elapsed . . ."

With the existing wording it may be understood that the passage of time terminates only the right to bring a claim.

*Yugoslavia*

A period of four years for the holder of an instrument to exercise his right of action against the acceptor or the maker or the drawer or an endorser or their guarantor, or a period of one year for a party who has paid the instrument to exercise his right of action against a party liable to him is too long. Such long periods of limitation are contrary to the nature and purpose of an instrument designed to ensure a prompt and safe transaction, on the one hand, and to make the payments due and repay the debts incurred on an instrument as soon as possible, on the other.

**Part II. Draft Convention on International Cheques***A. General comments on the draft Convention**Australia*

See the general comments of Australia in part I, A, *supra*.

*Austria*

The draft Convention is based on the assumption that a unification of the law on international cheques will further international business transactions. The question, however, remains whether such an activity is really required because it is doubtful whether international cheques will be used in business transactions in the future at all. The point is that conditions have essentially changed since the start of UNCITRAL's work because of the introduction of electronic means of transfer.

Apart from this objection and concentrating on the contents of the draft Convention one finds that the special function of the cheque has not properly been taken into account. While a bill of exchange is also a credit instrument, the cheque is only a means of payment. This difference in function must also be reflected in the legal regulation, which, however, is not the case. Under article 43 (b), for instance, the cheque must be presented for payment within the long period of 120 days; article 47, moreover, provides that a cheque presented before its stated day will be due only after the stated day.

The function of a cheque as a means of payment furthermore gives rise to the necessity that a cheque law must contain particularly clear regulations which are easy to apply. The draft Convention, however, has been modelled mainly on the draft Convention on International Bills of Exchange. The essential criticism of the Bills of Exchange Convention therefore also applies to a particularly high degree to the draft Convention on Cheques.

Because of the aforementioned reasons, this draft cannot be considered as a suitable basis for further activities in this field.

*Canada*

See the general comments of Canada in part I, A, *supra*.

*Cyprus*

See the general comments of Cyprus in part I, A, *supra*.

*Czechoslovakia*

The draft Convention on International Cheques can be considered a suitable basis for consideration of uniform rules intended for universal international use.

*Finland*

See the general comments of Finland in part I, A, *supra*.

*German Democratic Republic*

See the general comments of the German Democratic Republic in part I, A, *supra*.

*Germany, Federal Republic of*

The UNCITRAL draft Convention on International Cheques provides for the creation of a new law on cheques which is to be valid exclusively for international transactions.

The Geneva Conventions have already brought about a far-reaching unification of the law on cheques which has proved good for more than half of a century. However, groups of important states have kept aloof from these Conventions. It would be desirable to include these states in the unification, even if no significant difficulties have arisen up to now in international commercial transactions because of the different systems of law on cheques.

The solution offered by the draft to create an international cheque as an alternative to the commercial papers already existing cannot serve the objective of promoting global unification as to the law on cheques. It would, on the contrary, rather bring about the danger of impairing the uniformity achieved. In practice, the system proposed would for a long time entail considerable legal uncertainty and difficulties which, in the opinion of all groups concerned in the Federal Republic of Germany, would not be balanced by substantial advantages.

UNCITRAL's efforts towards further unification of the law on cheques should therefore not be directed towards introducing a new legal system beside the old one, but should strive towards making the Geneva

Conventions acceptable to the Anglo-American legal systems as well as towards further developing them in accordance with the requirements of modern transactions, if necessary. For this purpose, it should first be clarified which provisions of the Geneva Conventions are in need of amendment.

#### *Hungary*

See the general comments of Hungary in part I, A, *supra*.

#### *Japan*

It will be very meaningful to create, in addition to the existing cheques governed by conventions or domestic laws, a new cheque to be issued only for international transactions. The Japanese Government supports the idea of creating such a cheque by adopting a new multilateral convention separate from the proposed convention governing an international bill of exchange or promissory note. The present texts of the draft Convention on International Cheques, the product of discussions in the Working Group on International Negotiable Instruments of UNCITRAL, provide an excellent basis for achieving a good compromise between the Anglo-American and Geneva Systems, and the Japanese Government (and Japanese banking and trading circles) find the fundamental principles on the basis of which the texts are drafted acceptable.

However, where the draft Convention on International Cheques adopts the same institutions as are adopted in the draft Convention on International Bills of Exchange and International Promissory Notes, the comments made with regard to the latter draft Convention apply.

#### *Netherlands*

See the general comments of the Netherlands in part I, A, *supra*.

#### *Norway*

1. The Government of Norway approves of the proposal for two separate, independent conventions on international cheques and on international bills of exchange and promissory notes.

We acknowledge the high quality of the UNCITRAL draft Convention on International Cheques. We also approve of the thoroughness of the draft Convention and its systematic structure. The UNCITRAL Working Group has reached good compromises between civil and common law and has, from a practical point of view, proposed a sound and workable regulation.

2. We are not convinced of the need for a convention on international cheques. Secondly, while bills of exchange and promissory notes typically are being

employed by the business community, the law on cheques also has an important consumer protection aspect. We have been unable to scrutinize the draft in this respect. Thirdly, as far as we know the draft Convention on International Cheques has been received with some hesitation. Wide acceptance ought to be a precondition for adoption of the draft Convention as a multilateral treaty. For the time being, the Norwegian Government will therefore not commit itself to support the draft. Nevertheless, we want to make comments upon it.

3. The draft ought not to be adopted only as a model for enactment. This approach would invite deviations from the Convention during the different national enactment processes.

4. It seems to us that the Contracting States to the Convention providing a uniform law for cheques, Geneva 19 March 1931 (Norway included), will not be able to ratify an UNCITRAL Convention without denouncing the Geneva Convention. Norway is inclined to support proposals for an amendment to the Geneva Convention allowing the contracting States to ratify the UNCITRAL Convention and make it applicable to international cheques. A revision of the Geneva Convention itself might be undertaken as a separate activity.

5. There is in Norway a great confidence in the cheque as an instrument of payment. It seems to be somewhat different elsewhere. The high degree of confidence is partly achieved through a criminal legislation which has some bearing on a few of the articles of the draft. Even though a cheque drawn against insufficient funds is recognized as valid, it is a criminal offence to draw such a cheque, cf. article 3 of the draft Convention. It is also a criminal offence for the drawer without due reason, to withdraw his funds with the drawee or to countermand the cheque, to the detriment of the holder, cf. article 66. Application of these provisions of criminal law in respect of international cheques will not be contrary to the Convention. Maintenance of the high confidence in cheques is of great importance to us.

6. A higher degree of correspondence between the articles of the two draft Conventions would have been an advantage, in particular as regards the more general rules and principles of the first parts of the drafts. Full correspondence between articles 1 to 33 inclusive of the draft on bills of exchange and promissory notes and articles 1 to 35 inclusive of the draft on cheques could easily be achieved:

i. Articles 3 and 4 of the draft on cheques could either be included in articles 1 or 6, or be totally deleted. As the articles now read, they seem superfluous, and the Working Group has not found it necessary to propose similar rules in the draft on bills and notes.

ii. Articles 8 and 9 of the draft on cheques correspond to article 6 of the draft on bills and notes and are easily combined to one article.

iii. Articles 9 and 10 of the draft on bills and notes correspond to article 12 of the draft on cheques. The rules in article 10 of the draft on bills and notes are conveniently transferred to article 9 as a new paragraph (4).

7. There is in our opinion one serious weak point in the draft as there is in the Geneva Convention (ULC): the draft only confusingly deals with the problem of under what circumstances and to what extent a drawee who pays a cheque is discharged of his debt to the drawer. This is an important question, and an UNCITRAL Convention ought to establish beyond doubt which questions are settled under the Convention and which are referred to national law. The answers of those questions that are to be regarded as settled under the Convention ought to be reflected in the final text.

The problem is touched upon in article 25 and the commentary to that article. According to paragraphs 18 (last section) and 21 of the commentary, the drawee is discharged of his debt to the drawer upon payment of the cheque even if there is a forged endorsement on it. However, this solution is reflected in none of the articles of the draft. According to article 25 (2), cf. paragraph 28 of the commentary, the draft Convention does not deal with the liability of a drawee who pays a cheque upon which there is a forged endorsement. This is confusing.

Article 25 (2) refers to articles 70 and 72 as exceptions to the general principle. Why does it not refer to article 66 too?

Article 66 rests on the underlying presumption that payment of the cheque by the drawee discharges him of a corresponding part of his debt to the drawer. To this principle, article 66 makes an exception as regards cheques which the drawer has countermanded. However, the general principle is not reflected in section 1 "Discharge by payment" of chapter six "Discharge". It seems unclear to what extent this general principle is meant to be subject to the qualifications of articles 61 following. Anyway, discharge of a party to the cheque, cf. article 6 (7), of his liability on the instrument and discharge of the drawee *vis-à-vis* the drawer are two quite different kinds of discharge.

We strongly recommend that a new section 3, dealing with these questions, be included in chapter six of the draft Convention. We do not refer to the problem in our article-by-article comments.

8. The comments and examples to the draft Convention have been most useful. We recommend that a similar thorough commentary accompany the final Convention.

#### *Spain*

The main point which will be noted on reading the draft Convention on International Cheques is that instrument's extraordinary similarity to the draft Convention on International Bills of Exchange and Inter-

national Promissory Notes. The similarity is such that the major part of the text is a literal repetition of the other draft Convention.

The fact that the rules proposed are basically identical might lead one to believe that the preparation of two separate texts serves no useful purpose. The wording of the two drafts is such that there is no more difference between the rules governing cheques and those governing bills of exchange and those governing promissory notes. It might therefore be said that there are no reasons for regulating the last two types of instrument together and regulating international cheques separately and that it would be preferable to have a single regulation for all these instruments, subject to the establishment of special and specific rules for each one. This would avoid possibly excessive repetition.

The commentary on the draft Convention on International Bills of Exchange and Promissory Notes (*Yearbook 1982*, part two, II, A, 4) justifies the preparation of a separate draft Convention on International Cheques by indicating that it is a concession to the continental system embodied in the Geneva Laws which regulate these instruments separately. This does not, however, appear to be the main reason for the procedure adopted.

Although there are no reasons of legislative method which would justify preparation of two separate drafts, there are others of a pragmatic nature which make this advisable. The aim of achieving the maximum degree of uniformity and the greatest possible measure of acceptance of the draft juridical rules makes desirable this division of the subject under which each text is independent in itself, so that each one may be accepted and implemented independently. Thus, those States which wish to ratify or accede to one of the texts can do so and refusal to accept one of the sets of rules does not necessarily involve rejection of the other.

In any case, although the desire to achieve the greatest possible degree of unification justifies regulation of the matter of cheques in a separate instrument, it does not seem necessary or desirable that the two drafts should form separate conventions, since the Contracting States, on ratifying or acceding to one convention, can exclude a part of its content. The reason for the submission of two separate texts is therefore understandable, but it is recommended that there be only a single convention, divided however into parts.

Since the draft Convention on International Cheques is very similar to—and largely identical with—the draft concerning bills of exchange and promissory notes it gives rise to substantially the same comments. The present report therefore can refer to the report on the draft Convention on International Bills of Exchange and Promissory Notes. The general comments made therein are fully applicable to the draft Convention on International Cheques. These include comments on deficiencies of drafting, terminology or syntax; on the excessive number of definitions, distinctions and

references, on the danger of vague concepts and ambiguous and subjective interpretation criteria; the basic question of valid grounds for dishonour and the distinction between protected holders and non-protected holders; and the absence of a rule to resolve problems of a procedural nature and of a provision concerning the effects of the instrument on the transactions to which it applies.

Virtually all the specific comments made concerning the text of the draft Convention on International Bills of Exchange and Promissory Notes apply also to the draft Convention on International Cheques. Consequently, in order to avoid unnecessary repetition, it has been considered sufficient simply to refer to those comments.

#### *Sweden*

In a separate document, the Swedish Government has submitted its comments on the Working Group draft Convention on International Bills of Exchange and Promissory Notes. These comments are relevant also as regards the present draft Convention on International Cheques.

For reasons mentioned in the said document, the need for conventions concerning only international negotiable instruments may be questioned. The Swedish Government wishes to add that cheques apparently are becoming less frequent in international relations. Consequently, the need for a Convention on International Cheques is less accentuated also from this point of view.

#### *Union of Soviet Socialist Republics*

See the general comments of the USSR in part I, A, *supra*.

#### *United Kingdom of Great Britain and Northern Ireland*

The general observation in respect of the Convention on International Cheques is that there is a wide-spread lack of interest in it.

#### *United States of America*

The draft Convention on International Cheques is an attempt both to provide a settled body of law for designated international cheques and to establish rules which are adaptable to the banking and commercial practices in many states. The United States would have greater difficulty adapting its banking and commercial practices to the Convention on Cheques as currently drafted, than it will to the Convention on Bills and Notes. First, the draft Convention on International Cheques has no provisions to require the orderly, speedy and efficient handling of cheques, such as those contained in article 4 of the Uniform Commercial

Code. Such provisions are necessary for processing large numbers of cheques and should be added to the Convention. Second, the use of crossed cheques and cheques payable in account is unknown in the United States, and the introduction of these specialized types of instruments would have disadvantages that would not be outweighed by their advantages.

The draft Convention on International Cheques is an attempt to establish a settled body of law to govern cheques used in international commerce that are expressly designated on their face as controlled by the Convention. The draft Convention proposed by the Working Group does not, therefore, attempt to reform the laws applicable to domestic cheques, or even the laws applicable to all international cheques. Instead, the draft Convention provides rules for a restricted category of international cheques—rules which are certain and are adapted to the practices of the commercial community in many states. These states have both different legal systems and different commercial practices in the use and handling of cheques.

Unlike other types of commercial paper, in the United States cheques are processed in bulk by machines. To accommodate these new cheque-handling processes, prior rules from a hand-processing age involving fewer pieces of paper have been expanded and modified in article 4 of the Uniform Commercial Code. There is no equivalent expansion and modification of rules in the draft Convention on International Cheques. Thus, United States support of this draft Convention depends in good part on the adaptability of the Convention to present commercial practices of cheque processing by banks in the United States.

The rules set forth in UCC article 4 provide for efficient processing of cheques by limiting the time during which collecting banks may send cheques forward to the drawee, or remit proceeds or notice of dishonour to prior parties. The rules also limit the time period for drawees to decide to pay or dishonour cheques and then to remit proceeds or notice of dishonour to prior parties. The draft Convention on International Cheques contains no such time limits for actions by drawees, and contains no time limits for collecting banks, except the requirement in article 50 that a dishonoured cheque must be protested within two business days after dishonour. That time period, however, commences with dishonour and not with receipt of notice of dishonour. Thus, that requirement is not particularly useful to efficient processing of cheques under practices in the United States. It is possible that Federal Reserve regulations may be able to provide sufficient control of those cheques which enter its system so as to provide useful time limits, but it would be preferable to incorporate the relevant rules in the draft Convention itself.

A second, and more important problem, concerns the specialized types of cheques created by Chapter Seven of the draft Convention—crossed cheques and cheques payable in account. These specialized types of cheques are unknown in the United States. It is questionable

whether persons in the United States would know how to handle these cheques properly. It is possible that bank employees who handle cheques in bulk could be educated to identify these unusual items and to refer them to knowledgeable superiors. However, that would still not protect members of the general public, who also handle cheques regularly but would not be aware of the specialized rules concerning these unusual items. Thus, crossed cheques would confuse an unsuspecting public if they were introduced into the United States.

Further, even proper use of crossed cheques or cheques payable in account would not provide in the United States the protection expected by the foreign drawer, because the bank-customer relationship is quite different in the United States than may be the case in countries where such instruments are in general use. Banks in the United States do not usually investigate the past history of deposit account customers, and some banks do not even investigate their identity, as long as collected funds are involved. Thus, the thief who steals a crossed cheque or a cheque payable in account in the United States would probably be able to establish an account and realize on the cheque. And, if he stole such a cheque before it reached the payee, the loss would fall on the foreign drawer who expected to be protected.

For these reasons, the use in the United States of crossed cheques and cheques payable in account would not protect parties and might even create new avenues for potential fraud. Favourable consideration by the United States of the draft Cheque Convention will therefore depend in some degree on whether a solution can be found to this problem. One possible approach to this problem might be to allow adopting states to treat Chapter Seven as optional, and to declare that it does not apply, while allowing them to adopt the balance of the Convention.

Many of the article-by-article comments of the United States on the draft Convention on International Cheques are adapted from the comments on the draft Convention on International Bills of Exchange and International Promissory Notes. They are directed primarily to improving the drafting of the Working Group and carrying out its decisions, rather than seeking to overturn or re-open the compromises struck. Although the comments make some important proposals, the proposals seek to clarify the draft and to eliminate problems which would arise in common law courts.

Two of the comments, however, are peculiar to the draft Convention on International Cheques. These are the comments on article 49 and articles 68-72. One relates to the problems of processing cheques in bulk, and the other to the specialized type cheques currently unknown in the United States. Both of these comments are important to the acceptability of the Convention to the United States.

The United States strongly urges that a commentary accompany the final text. The existing commentary has been prepared at the request of the Secretariat and thus

far has accompanied the draft as an explanation of its provisions. It has proved most helpful to practitioners and others in the United States who have studied the draft Convention. It can be expected that a commentary on the Convention finally adopted would facilitate efforts to have the resulting Convention accepted by States. Since the draft Convention contains a number of concepts which are unknown in common law systems, a commentary would be of special importance to a common law country such as the United States.

The following comments and proposals have been prepared with considerable restraint. In view of the limited time for consideration of the draft Convention at a diplomatic conference, the already long period of work on the draft by the experts on UNCITRAL's Working Group, and the complexity of the subject matter, it seems desirable that the number of proposals made to UNCITRAL at this stage and ultimately at a diplomatic conference be kept to a minimum.

#### *Uruguay*

With respect to this draft Convention we would repeat the general comments made concerning the draft Convention on Bills and Notes, because it does not give rise to any major objection and will certainly be a most useful instrument which will facilitate international trade.

#### *Yugoslavia*

Most of the observations expressed with respect to the draft Convention on International Bills of Exchange and Promissory Notes *mutatis mutandis* apply also to the draft Convention on International Cheques.

#### B. Specific comments on individual articles

##### CHAPTER ONE. SPHERE OF APPLICATION AND FORM OF THE CHEQUE

###### ARTICLE 1

###### *Spain*

The first basic difference between the rules governing bills of exchange and promissory notes and those governing cheques is that cheques may be issued, when drawn, as bearer instruments. This is clear from the definition of a cheque contained in article 1, paragraph (2) (b): "... Order... to pay... a sum... to the payee or to his order or to bearer" (in the Spanish text of the draft Convention the reference to the bearer is missing, probably through a typographical error, as it appears in the English and French versions and in the commentary on the draft). The possibility of drawing an international cheque to bearer is consistent with article 14 which specifies the manner in which such a

cheque may be transferred, and with article 16, paragraph (1), which lists the characteristics of a holder. There is therefore no difference as regards the naming of the payee. All these instruments may be drawn in favour of the payee or to order and are subject to the same rules concerning transfer (articles 14 *et seq.*) and in each case there is the same possibility of using a "non-transferability" clause (article 18). There is consequently no distinction between instruments drawn to order and instruments specifically naming the payee.

According to article 1, paragraph (2) (c), a cheque may be drawn only against a banker. This follows the widespread practice which makes cheques purely banking instruments.

#### *Article 1 (2)*

##### *Japan*

See the comment of Japan in part I, B, *supra* under article 1 (2) (a) and (e).

##### *United States of America*

Paragraph (2) of article 1 states that a qualifying cheque must be a "written instrument". The term "written" is not defined in the Convention and the United States proposes that such a definition be added to article 1. Comment 4 indicates that the draftsmen deliberately omitted such a definition, but then states that the term would include "any mode of representing or producing words in visible form, such as handwritten, typed or printed". This comment definition could include some electronically reproduced "writings" since they are not excluded, and the commentary definition is only inclusive. The United States therefore proposes that a definition be added to the text of article 1. This definition should require that any "signed writing" must meet several tests, including that the writing be permanent and capable of physical transmission between the parties, that it be signed in a manner which prevents tampering, and that it contain the signature of the issuer.

#### *Article 1 (2) (a)*

##### *Czechoslovakia*

The important question arises whether the drawer of a cheque when using the words "International Cheque (Convention of . . .)" has thereby indicated either a choice of law or a choice of the legal régime of the cheque in compliance with the Convention. The effects of such a choice should be specified in the text of the Convention, as follows: Article 1 (2) (a) should be amended to the effect that this designation by the drawer constitutes also an indication of the legal régime of the Convention; at some appropriate place, the Convention should specify that the clause according to article 1 (2) (a) makes the cheque subject to the régime of the Convention and binds any holder who took the cheque, and all subsequent parties.

##### *Norway*

See the comment of Norway in part I, B, *supra* under article 1 (2) (a).

##### *United States of America*

See the comment of the United States in part I, B, *supra* under article 1 (2) (a).

#### *Article 1 (2) (b)*

##### *Czechoslovakia*

See the comment of Czechoslovakia in part I, B, *supra* under article 1 (2) (b).

#### *Article 1 (2) (e)*

##### *Czechoslovakia*

Paragraph (2) contains, apparently, necessary requisites of a cheque even in the absence of an express provision that the instrument is not an international cheque if a requisite is missing. The provision of paragraph (2) (e) requires, in order to establish the international character of the cheque, that at least two of the specified places are situated in different States, but there is no provision indicating that all these elements must be included in the cheque; in other words it is not clear whether the place of drawing, the address of the drawer, the address of the drawee and the address of the payee, the place of payment are indispensable formal requisites of the cheque. We also note that the address of the drawer is usually not mentioned. Perhaps the address of the drawer and the place of payment are not indispensable formal requisites of a cheque.

## CHAPTER TWO. INTERPRETATION

### ARTICLE 3

##### *Spain*

Under article 3 a cheque is considered valid even if it is drawn against insufficient funds. It would seem that the same solution should be adopted even for the case where funds are totally lacking. Article 66 provides that where a cheque is countermanded "the drawee is under a duty not to pay". These two rules relate to what is known as the "cheque contract" or international cheque law, but they do not affect the law on cheques as instruments of exchange and do not affect the situation of the holder of the cheque. It could therefore be decided to make no reference to these matters of internal relations between the persons involved in the cheque, because they do not affect the system of exchange obligations arising from the instrument. Alternatively, they could be included in the proposed rules, but in that case it would seem necessary to have a more comprehensive regulation than is contained in the present list.

## ARTICLE 4

*Spain*

Article 4 allows a cheque to bear a date other than the true date of drawing and article 47 draws attention to a specific consequence of this; but here again the question of pre-dated and post-dated cheques deserves more comprehensive treatment.

*Uruguay*

The substance of this article conflicts with our internal public law. To enter a date other than the date on which the cheque is drawn amounts to a false declaration which to make is a criminal offence.

Should the draft Convention be adopted without modification of this provision, appropriate reservations would have to be made if the Republic of Uruguay decided to accede to the instrument.

*Yugoslavia*

The wording of draft article 4 is unsatisfactory since the date on which the cheque was drawn has not only a procedural but also a substantive effect on the rights and duties of the parties. Consequently, a rule should be established that a cheque must bear a date and that without such date it cannot be valid as a cheque.

## ARTICLE 5

*Denmark*

See the comment of Denmark in part I, B, *supra* under article 3.

## ARTICLE 6

(The comments relating to paragraph (6) of this article (definition of a "protected holder") are set forth under articles 27 and 28, under the heading "holder and protected holder".)

*United Kingdom of Great Britain and Northern Ireland*

See the comment of the United Kingdom in part I, B, *supra* under article 4.

*United States of America*

See the comment of the United States in part I, B, *supra* under article 4.

*Uruguay*

A number of terms used in the Convention are defined in this article, but it fails to define the term "drawer". We suggest that the following definition be included:

"'Drawer' means the person who draws an international cheque."

## Article 6 (3)

*Canada*

The draft Convention seems to presuppose that a cheque is by definition drawn on a bank. This is no longer the case in Canada where cheques may also be drawn on trust companies, loan companies or credit unions. Canadian legislation relating to cheques on a bank includes in the definition of a "bank" any person or institution which "accepts deposits transferable by order to a third party". We are concerned that the definition of a "banker" in article 6 (3) of this draft Convention might be held not to include all persons or institutions in Canada which may legally issue cheques because the wording "assimilated to" in the definition does not appear to have any very precisely defined meaning in either a legal or financial context. Canada therefore strongly recommends that article 6 (3) be amended to read as follows:

"'Banker' includes any person or institution that accepts deposits transferable by order to a third party."

*Denmark*

Paragraph (3) of the Convention on Cheques provides a somewhat muddled definition of a bank ("banker"), and a more precise definition of the concept would be desirable.

*Norway*

Of the definitions in article 6, the definition of "banker" in paragraph (3) is the only one which refers to the applicable national law, cf. paragraph 3 of the commentary to the article. We suggest that paragraph (3) explicitly refer to national law.

*Spain*

Article 6, paragraph (3), may complicate the determination of the possible drawees of a cheque as it allows cheques to be drawn against "any person or institution assimilated to a banker". Here it will be for the national law to establish such assimilation.

*United Kingdom of Great Britain and Northern Ireland*

It is strongly felt that the definition of banker is unsatisfactory. A better definition is that in section 2 of the Bills of Exchange Act 1882 namely "banker" includes a body of persons whether incorporated or not who carry on the business of banking.

## Article 6 (4)

*German Democratic Republic*

The remarks made on article 4 of the Convention on International Bills of Exchange and International Prom-

issory Notes also apply to this article. In addition, it is recommendable for the sake of greater clarity to add in paragraph (4) of article 6 that the cheque may be drawn payable to order or to bearer. Otherwise, the possibility of drawing a cheque payable to bearer could only be deduced from article 14.

#### *Article 6 (5)*

##### *Japan*

See the comment of Japan in part I, B, *supra* under article 4 (7).

#### *Article 6 (8)*

##### *Denmark*

See the comment of Denmark in part I, B, *supra* under article 4 (10).

##### *Germany, Federal Republic of*

See the comment of the Federal Republic of Germany in part I, B, *supra* under article 4 (10).

##### *Hungary*

See the comment of Hungary in part I, B, *supra* under article 4 (10).

#### *Article 6 (8) and (9)*

##### *Czechoslovakia*

See the comment of Czechoslovakia in part I, B, *supra* under article 4 (10).

#### *Article 6 (8) and Article (X)*

##### *Japan*

See the comment of Japan in part I, B, *supra* under article 4 (10) and article (X).

##### *Norway*

We will at this stage neither support nor oppose the inclusion of article (X) in the final text. However, we call attention to the difficulties which may arise from reservations according to the article.

##### *Union of Soviet Socialist Republics*

See the comment of the USSR in part I, B, *supra* under article 4 (10) and article (X).

#### *Article 6 (9)*

##### *Union of Soviet Socialist Republics*

See the comment of the USSR in part I, B, *supra* under article 4 (11).

## ARTICLE 7

##### *Denmark*

See the comment of Denmark in part I, B, *supra* under article 5.

##### *Germany, Federal Republic of*

See the comment of the Federal Republic of Germany in part I, B, *supra* under article 5.

## ARTICLE 8

##### *Spain*

Articles 8 *et seq.*, in prohibiting (ineffectively) the payment of interest, show a difference between the cheque, on the one hand, and the bill of exchange and the promissory note, on the other. This prohibition is understandable and seems appropriate since the cheque, in principle, is an instrument of payment and not a credit instrument and therefore matures immediately on sight. These features are not consistent, however, with the long period allowed for presentment for payment under article 43 (120 days).

## ARTICLE 9

##### *Australia*

The provision concerning stipulation of interest on cheques differs from that contained in the Bills and Notes Convention (article 6). Article 6 provides that a sum is deemed to be a definite sum even though it is to be paid with interest. This corresponds with section 14 of the BEA which also applies to cheques. However, article 9 of the Cheques Convention provides that a stipulation on a cheque that it is to be paid with interest is deemed not to have been written and, therefore, is of no effect without affecting the validity of the cheque. The explanatory note to the article makes it clear that the rationale of this provision is that a cheque is a payment instrument, providing for payment on demand, and that such a stipulation of interest might lead to undesired late presentment. Having regard to the fact that this provision will apply only to international cheques which are deliberately brought within the Convention, it means that parties and their bankers in Australia will need to be made aware that such a provision for interest on an international cheque is of no effect.

*Canada*

Canada agrees with the policy in the Convention that cheques ought not to bear interest and that any provision apparently encouraging such practice should be expunged.

**ARTICLE 10***Article 10 (2)**Czechoslovakia*

See the comment of Czechoslovakia in part I, B, *supra* under article 7 (2).

**ARTICLE 11***Uruguay*

We feel that the wording of this article could be improved, as paragraph (1), subparagraph (b), seems to conflict with paragraph (2).

We suggest that the text be reworded as follows:

"A cheque is always payable on demand. Any stipulation to the contrary is deemed not to have been written."

*Article 11 (1)**Spain*

Article 11, as it appears in the Spanish text submitted for comment, is incomplete. Paragraph (1) is missing. This is the provision to the effect that a cheque is payable on sight. As it appears in the commentary and in the French and English versions, the text is satisfactory.

*Article 11 (2)**United Kingdom of Great Britain and Northern Ireland*

Article 11 (2) is criticised because it appears to conflict in respect of post-dating cheques with article 47. It is suggested that article 11 (2) should be deleted.

**ARTICLE 12***Cyprus*

A new paragraph to be added to take care of fictitious or non-existing payees. (See Section 7 (3) of Cap. 262). If an international cheque is payable to a fictitious or non-existing person, it may be arguable whether the cheque is an international one or not.

*Indonesia*

The Indonesian Commercial Code does not contain a provision whereby a cheque may be drawn by two or more drawers or may be payable to two or more payees.

However it is commonly found in payment transactions that a cheque is drawn jointly by two or more persons or jointly drawn by two or more persons on behalf of an entity, as a drawer.

It is to be noted that if the drawers or payees are regarded as a unity, it is not contrary to the civil law system which considers the issuance of a cheque as an underlying transaction between the drawer and the payee.

*Norway*

1. According to article 12 (1) (a), a cheque may be drawn by the drawer "... payable to his order". A more precise wording would have been "... payable to himself", cf. paragraph 9 of the commentary to article 1.

2. According to article 12 (1) (a), a cheque may be drawn by the drawer on himself, i.e. a cheque drawn by a banker on himself, cf. article 1 (2) (c). This implication would have been easier to understand if subparagraph (a) were split into two subparagraphs which might have read, cf. also our comment no. 1:

(1) A cheque may:

- (a) Be drawn by the drawer payable to himself;
- (b) Be drawn by a banker on himself;

...

3. In most States, a central bank or a national reserve system has a monopoly to issue bank-notes which are legal tender. Even though cheques drawn by an ordinary banker on himself will not be legal tender, issuance of such bank-notes may be detrimental to public interests, especially if they are payable to bearer and issued in great numbers. Under the Geneva Convention, the principal rule is that a banker cannot draw a cheque on himself, cf. Annex I (ULC) article 6 and also annex II, articles 8 and 9. Some similar provisions in the draft Convention may be necessary to ensure wide acceptance of the draft. Without committing ourselves, we put forward for discussion the suggestion that the Convention state that a Contracting State is free:

(i) To restrict issuance of cheques drawn by a banker on himself within its own territory, at least if they are drawn in its own currency;

(ii) To restrict importation of such cheques into its own territory;

(iii) To decide that such cheques issued or imported under violation of such restrictions will not be recognized in its territory;

(iv) To decide that cheques drawn in its own currency by a foreign banker on himself will not be recognized.

4. The interpretation of paragraph (2) outlined in paragraph 5 of the commentary is confusing. We suggest that either paragraph 5 is deleted in the proposed commentary to the final text and the question left to the courts to decide or the interpretation outlined in paragraph 5 is stated in the final text of the Convention. Otherwise the interpretation outlined in the commentary will serve as a trap for the readers of the Convention.

### *Spain*

Article 12 re-casts articles 9 and 10 of the draft Convention on bills of exchange and promissory notes, but does not provide for a plurality of drawees. There may be grounds for this but, in principle, there does not seem to be any reason why the possibility of a cheque being drawn against several banks should be excluded. If it is possible within one State for several banks to issue cheque-books jointly, it is *a fortiori* desirable in international practice to allow cheques to be drawn on a number of banks situated in different States.

### *Union of Soviet Socialist Republics*

It would be desirable either to add to this article a paragraph in line with the provision contained in the Geneva Convention (ULC, article 5), viz.: "a cheque made payable to a specified person with the words 'or to bearer', or any equivalent words is deemed to be a cheque to 'bearer'" or to include this provision in the draft as an independent article.

### *Uruguay*

We suggest the following wording:

"A cheque may:

...

(c) Designate two or more payees."

The rule in article 12, paragraph (2), is clear but is perhaps lacking in that it does not refer to the case where a cheque is drawn in favour of A and/or B, as mentioned in the commentary (paragraph 5).

We suggest the addition of the following:

"If it is indicated on the instrument that it is payable to alternative or joint payees, it shall be understood to be payable to all those designated."

### *Article 12 (1)*

### *Czechoslovakia*

We suggest that it should be mentioned expressly that an international cheque may be drawn payable also to bearer.

### *Article 12 (1) (a)*

#### *Germany, Federal Republic of*

It can be deduced from this provision read in conjunction with article 6, para. (2), that banks shall be entitled to draw international cheques on themselves. This would be a doubtful practice in point of view of currency policy because money may thus be created. Moreover, there is no sufficient practical need for admitting such cheques.

### *Article 12 (2)*

#### *Czechoslovakia*

See the comment of Czechoslovakia in part I, B, *supra* under article 9 (3).

## ARTICLE 13

#### *Czechoslovakia*

See the comment of Czechoslovakia in part I, B, *supra* under article II (1).

### *Article 13 (1)*

#### *Norway*

The date of the cheque, cf. article 1 (2) (d), is left out in the enumeration of paragraph 1 of the commentary to article 13.

#### *Yugoslavia*

Article 13 (1) provides for the completion of an incomplete cheque, thus accepting the theory of omission. Although the completion of such a cheque is permitted by some laws, since so-called essential elements are presumed, it will not benefit international payments. If a cheque is an instrument of payment, then it should be as close to a banknote as possible.

## CHAPTER THREE. TRANSFER

## ARTICLE 14

### *Spain*

The chapter on "Transfer" is almost identical with the corresponding chapter in the draft Convention on International Bills of Exchange and Promissory Notes. There is one important difference, however, which should not be underestimated. This is the system for the transfer of cheques which are drawn payable "to bearer". Article 14 provides that such cheques are

transferred by mere delivery. Endorsement does not seem to be an appropriate method of transfer for such instruments. However, article 40, paragraph (4) (b), makes the general statement that "A signature alone on the back of the cheque is an endorsement". It goes on to state that "A special endorsement of a cheque made payable to bearer does not convert the cheque into an order instrument". The meaning of endorsement of a cheque to bearer and of a signature alone on the back of the cheque should be dealt with more fully and made more clear.

#### *Yugoslavia*

The two subparagraphs of article 14 regulate not only two totally different cases but they are regulated in a way which is likely to have undesirable effects.

### ARTICLE 15

#### *Canada*

For the same reason that we advocate no change in article 9, we do question the wisdom of the policy promoted in article 15. In the experience of the Canadian banks, it is almost never necessary for a cheque to be endorsed so often that the holder is required to affix an *allonge*. Canada does not consider a cheque to be a credit instrument and we object to this apparent sanction by the Convention to its use as such. Undue delay in presentment for payment is a likely consequence. See our comment on article 43 (b), *infra*. This provision appears to Canada to be retrogressive rather than progressive since it does not assist in the task of modernizing the law to reflect current business practices.

#### *Czechoslovakia*

See the comment of Czechoslovakia in part I, B, *supra* under article 13 (2) (a).

#### *Uruguay*

We should like to see added to this article a provision establishing clearly that the instrument is transferred by endorsement even if it does not contain the words "to order".

The absence of a requirement that these words be entered on the instrument is due to the context and is explained in the commentary thereon, but the clarification would, in our view, be desirable.

### ARTICLE 18

#### *Czechoslovakia*

See the comment of Czechoslovakia in part I, B, *supra* under article 16.

#### *Denmark*

See the comment of Denmark in part I, B, *supra* under article 16.

#### *Norway*

The article deals with two somewhat different situations: on the one hand a restrictive statement included into the cheque by the drawer and on the other hand a restrictive endorsement. We question the convenience of combining the two situations and suggest that restrictive endorsements are entirely dealt with in article 22.

#### *United States of America*

See the comment of the United States in part I, B, *supra* under article 16.

### ARTICLE 19

#### *Article 19 (2)*

#### *Norway*

Article 19 (2) deals with the conditional endorsement. With reference to paragraph 2 of the commentary to article 17, we call attention to the concept of "the protected holder", cf. articles 6 (6) and 7, and the requirement of the holder having no knowledge of claims to or defences upon the instrument. The inclusion of the condition into the endorsement may prevent a holder from qualifying as a protected holder.

### ARTICLE 22

#### *Czechoslovakia*

See the comment of Czechoslovakia in part I, B, *supra* under article 20.

#### *Norway*

We refer to our comments to article 18.

#### *United States of America*

See the comment of the United States in part I, B, *supra* under article 20.

### ARTICLE 23

#### *Czechoslovakia*

See the comment of Czechoslovakia in part I, B, *supra* under article 21.

*Article 23 (2)**Spain*

Article 23, paragraph (2), gives rise to serious doubts, not only because of the way it indicates the effects of endorsement in favour of the drawee, but mainly because of the exception in the last phrase, whose meaning is not at all clear and because, in any event, it raises the question of the definition of "establishments".

**ARTICLE 24***Uruguay*

This provision allows a cheque to be transferred after the expiration of the period of time for presentment. We believe that this formula does not suit the interests of trade.

Under Uruguayan law, a cheque loses its intrinsic validity after the expiration of the time allowed for presentment. We feel that this is a satisfactory solution for the security of trade.

**ARTICLE 25***Denmark*

See the comment of Denmark in part I, B, *supra* under article 23.

*Hungary*

See the comment of Hungary in part I, B, *supra* under article 23 (2).

*Indonesia*

This article deals with forged endorsements which is also dealt with in the Indonesian Commercial Code. However, this article is concerned with the right of any party who suffered damages to recover compensation from the forger or any person who directly takes from the forger, whereas the Indonesian Commercial Code lays down that only the drawee has the right to recover compensation. Therefore this article allows all parties concerned to recover compensation for damages.

*Japan*

See the comment of Japan in part I, B, *supra* under article 23.

*Norway*

See the comment of Norway in part I, B, *supra* under article 23.

*Union of Soviet Socialist Republics*

See the comment of the USSR in part I, B, *supra* under article 23.

*Article 25 (1)**Cyprus*

If an endorsement is forged, any party who suffers damages should have the right to recover compensation from the forger, from the person to whom the cheque was directly transferred by the forger and from any person or persons who received the cheque with knowledge of the forgery. It is considered correct that the person or persons who was/were aware of the forgery should not be allowed to escape liability. Cases may come to light where such a person or persons had some sort of involvement with the forger or the person to whom the cheque was directly transferred.

*Czechoslovakia*

See the comment of Czechoslovakia in part I, B, *supra* under article 23 (1).

**CHAPTER FOUR. RIGHTS AND LIABILITIES***Holder—Protected holder***ARTICLES 6 (6), 27 AND 28***Czechoslovakia**Articles 6 (6) and 27*

See the comment of Czechoslovakia in part I, B, *supra* under articles 4 (7) and 25.

*Denmark**Article 28*

See the comment of Denmark in part I, B, *supra* under article 26.

*Germany, Federal Republic of**Articles 27 and 28*

See the comment of the Federal Republic of Germany in part I, B, *supra* under articles 25 and 26.

*Norway**Article 6 (6)*

See the comment of Norway in part I, B, *supra* under article 4 (7).

*Articles 27 and 28*

See the comment of Norway in part I, B, *supra* under articles 25 and 26.

*United States of America**Article 6 (6)*

See the comment of the United States in part I, B, *supra* under article 4 (7):

*Article 27*

See the comment of the United States in part I, B, *supra* under article 25.

*Yugoslavia**Articles 27 and 28*

The provisions stipulating that a party may set up against a holder who is not a protected holder any defence based on an underlying transaction prevent the circulation of a cheque. Therefore, they should be deleted.

The term "protected holder" defined in articles 27 and 28 is too complicated to grasp and should be replaced by the concept of the "good faith" holder, which would be much easier and more appropriate for the circulation of a cheque and for international transactions in general.

There must have been a mistake in the provisions of article 27 (3) (b) referring to the signature of the payee or an endorsee instead of an endorser. It is not clear why theft or forged signature of the endorser is the only ground for setting up a defence (paragraph (3) (b)).

**ARTICLE 29***Czechoslovakia*

See the comment of Czechoslovakia in part I, B, *supra* under article 27.

*Norway*

See the comment of Norway in part I, B, *supra* under article 27.

*Article 29 (2)**Denmark*

See the comment of Denmark in part I, B, *supra* under article 27 (2).

**ARTICLE 31***Norway*

See the comment of Norway in part I, B, *supra* under article 29.

**ARTICLE 32***Czechoslovakia*

See the comment of Czechoslovakia in part I, B, *supra* under article 30.

*German Democratic Republic*

See the comment of the German Democratic Republic in part I, B, *supra* under article 30.

*Japan*

See the comment of Japan in part I, B, *supra* under article 30.

*Norway*

See the comment of Norway in part I, B, *supra* under article 30.

*Union of Soviet Socialist Republics*

See the comment of the USSR in part I, B, *supra* under article 30.

*United States of America*

See the comment of the United States in part I, B, *supra* under article 30.

**ARTICLE 33***Denmark*

See the comment of Denmark in part I, B, *supra* under article 31.

*Norway*

See the comment of Norway in part I, B, *supra* under article 31.

*United Kingdom of Great Britain and Northern Ireland*

See the comment of the United Kingdom in part I, B, *supra* under article 31.

## ARTICLE 34

### *Norway*

See the comment of Norway in part I, B, *supra* under article 32 (4).

### *Uruguay*

This provision fails to cover the case of signature of cheques by juridical persons, especially commercial corporations. We suggest that provision be made for this, because, at the international level, this is the manner in which cheques are most frequently drawn.

## ARTICLE 35

### *Denmark*

See the comment of Denmark in part I, B, *supra* under article 33.

### *United States of America*

Although this article states that an order to pay is not an assignment, it does not expressly state the practical consequence that a drawee is not liable on a cheque. The United States suggests that this article be clarified by an amendment which would expressly state that a drawee is not liable on a cheque.

## ARTICLE 36

### *Australia*

Under the BEA, acceptance of a cheque by the drawee banker is in theory possible but in practice rare, as the cheque is normally presented simply for payment. However, under the Geneva Convention (Uniform Law on Cheques—ULC) it is not possible for a cheque to be accepted and a statement of acceptance is disregarded. The Cheques Convention in article 36 follows the ULC by providing that a statement on a cheque indicating certification, confirmation, acceptance, etc. is not an acceptance but nevertheless provides that, where such a statement is written on a cheque, there is an irrebuttable presumption that the statement simply verifies the existence of funds in the hands of the drawee bank. The drawer cannot withdraw those funds nor can the drawee apply them otherwise in payment of the cheque before the expiration of the time limit for the presentation, namely 120 days from the date of the cheque. Given the limited application of this provision to international cheques drawn under the Convention, no difficulty is foreseen with this provision.

### *Denmark*

This provision is unknown in Denmark and obviously clashes with the provision of section 25 of the Danish

Cheques Act according to which only the drawee can certify a cheque.

### *Norway*

1. We suggest that article 36 explicitly reflect that it is dealing with certifications etc. by the drawee. As the article now reads, it suggests that somebody else may certify a cheque too.

2. It is unclear and not discussed in the commentary whether certification etc. of a cheque by the drawee precludes the drawer from countermanding the cheque. The language of article 36 suggests that the answer is no. However, paragraph 5 cf. 2 of the commentary to article 66 indicate a yes. The ambiguity ought to be settled in the final text.

3. According to articles 40 following, a cheque may be guaranteed. As far as we have been able to see, there is nothing in the draft that prevents the drawee from guaranteeing the cheque for the account of the drawer if the drawer asks for it. The drawee will then be liable on the instrument in his capacity as guarantor to the same extent as the drawer unless he has stipulated otherwise, cf. article 41. This mechanism provides for a convenient flexibility. We are not inclined to support inclusion of paragraph (2) in the final text.

### *Spain*

Article 36 provides for the possibility of a cheque containing "special" statements. However, the article over-simplifies the question of "special cheques", attributing identical consequences to hypotheses which are not the same and which are generally recognized as having different effects. Having regard to the various possibilities listed in article 36, which refers even to "any other equivalent expression" and might include, for example, the guaranteeing of the cheque, their diversity should be recognized and they should be regulated accordingly.

### *Article 36 (1)*

### *Yugoslavia*

Article 36 (1) identifies visa and certification on a cheque. In this respect, account should be taken that the legal position of the drawee (bank) and his responsibility as well are not identical in both cases.

### *Article 36 (2)*

### *Canada*

Canada has already referred to what we consider to be the extremely undesirable leniency of the draft Conventions in appearing to sanction local variation on

matters of such fundamental importance to the operation of a cheques Convention as the effect of certification as laid down in this article. If certification of international cheques is to be promoted, there should be no scope for variation of the effect by local domestic law.

#### Czechoslovakia

We recommend that the text of paragraph (2) be adopted.

#### Union of Soviet Socialist Republics

It would be desirable to retain paragraph (2) in this article.

### ARTICLE 37

#### *Article 37 (2)*

#### Spain

The prohibition in article 37, paragraph (2), of exclusion or limitation by the drawer of his liability contrasts with the rule laid down in respect of the bill of exchange. The rule laid down for cheques is the correct one, as is stated in the comments on the draft Convention on International Bills of Exchange.

#### *Article 37 (3) and (4)*

#### Canada

We note that articles 37 (3) and (4), which appear to have been adopted by the UNCITRAL Working Group (A/CN.9/210, paras. 94, 95; *Yearbook 1982*, part two, II, A, 1) have not been reproduced in this draft Convention. Was this deletion intentional?

### ARTICLE 38

#### Yugoslavia

There is no justification for enabling the endorser to exclude or limit his own liability by an express stipulation on the cheque (article 38 (2)). If this can be allowed when a bill is concerned, such a stipulation on the cheque will render it worthless.

### ARTICLE 39

#### Czechoslovakia

See the comment of Czechoslovakia in part I, B, *supra* under article 41.

#### Denmark

See the comment of Denmark in part I, B, *supra* under article 41.

#### Germany, Federal Republic of

See the comment of the Federal Republic of Germany in part I, B, *supra* under article 41.

#### Japan

See the comment of Japan in part I, B, *supra* under article 41.

#### Norway

See the comment of Norway in part I, B, *supra* under article 41.

#### United States of America

See the comment of the United States in part I, B, *supra* under article 41.

#### Uruguay

This provision is particularly stringent. We suggest that the liability of the person who transfers a cheque should be softened in some manner, at least by reversal of the burden of proof, the injured party having to prove culpability.

#### Yugoslavia

A mistake must have been made in article 39 (3) since it is illogical that liability on account of any defect on the cheque is incurred only to a holder who took the cheque without knowledge of such defect.

### ARTICLE 40

#### Japan

See the comment of Japan in part I, B, *supra* under article 42.

#### Norway

1. We refer to our comment No. 3 to article 36.

2. Subparagraph (b) of paragraph (4) does not deal with guarantees. We suggest the provisions of article 40 (4) (b) be transferred to article 14 or 15.

*Yugoslavia*

This article may create difficulties in countries allowing the acceptance of a cheque, because there is not a clear distinction between an endorsement in blank and *aval*.

**ARTICLE 41***Denmark*

The expediency of maintaining rules of law on *aval* is questionable since, in contrast to bills of exchange, *aval* is almost non-existent for cheques.

If rules on *aval* are to continue in existence, the guarantors should in any event be subject to the same rules as those applying to drawer and endorsers. It seems pointless to allow a guarantor to limit his commitment on the cheque (except where partial *aval* is involved).

**ARTICLE 42***United Kingdom of Great Britain and Northern Ireland*

See the comment of the United Kingdom in part I, B, *supra* under article 44.

**CHAPTER FIVE. PRESENTMENT, DISHONOUR  
BY NON-PAYMENT, AND RE COURSE****ARTICLE 43***Australia*

Article 43 of the Cheques Convention provides that a cheque must be presented for payment within 120 days after its stated date. Presentment after that time deprives the holder of the right of recourse against endorsers and their guarantors. Delay in presenting the cheque does not relieve the drawer from liability except to the extent of loss suffered because of the delay. Failure to present the cheque for payment, unless dispensed with, relieves the drawer of the cheque from liability. It is not thought that any difficulty would arise because of the 120 day limit in relation to international cheques, which contrasts with the 12 month period, under s. 80 of the BEA, during which a cheque may be in circulation before becoming stale.

*United Kingdom of Great Britain and Northern Ireland*

This article causes Her Majesty's Government some difficulty in that conflicting positions are adopted by significant banking interests in the UK. On the one hand it is approved subject to clarification of 43 (d) in so far as it appears to be at variance with 43 (c) which could be remedied by reading:

"Notwithstanding article 43 (c), a cheque may be presented for payment to the representative or authorized agent of the drawee at a clearing-house."

On the other hand the counter-argument runs that it should be clear that a bank, to which a cheque is presented, has agreed, under the rules of that clearing-house, that the receipt of the cheque by the clearing-house is presentation. Also, so the argument runs, presentation at a clearing-house should only be made by another member of the clearing-house. The counter-argument would lead to a proposed 43 (d) which would read:

"A cheque may be presented by the holder or his agent through a clearing-house for payment at the place specified where the holder or the agent making the presentation is a member of that clearing-house."

*Article 43 (a)**Norway*

The terms "business day" and "reasonable hour" in paragraph (a) are imprecise. We suggest that the Convention authorize the Contracting States to define these terms more precisely in their national legislation.

*Article 43 (b)**Canada*

Canada agrees with the policy and object of this article but has two technical objections to it. In the first place, we consider that the time limit ought to be 180 days as this would coincide with North American practice and, we believe, the requirements of the Uniform Commercial Code, article 4-404. The practical advantages of having a uniform period for both domestic and international instruments would be salutary and significant. At the same time, we are concerned that there is a tendency for stated maxima to become common minima. Our practice in Canada is very clearly to exercise reasonable diligence to collect a cheque as quickly as is reasonably possible. We understand that this is a commonly held practical objective and we consider that the Convention ought to recognize it by imposing a duty upon holders and their collecting agents to present cheques reasonably promptly. Canada does not advocate any legal sanction for failure to present within the 180 days. However, the draftsmen might wish to consider a provision such as in the Canadian Bills of Exchange Act section 166 which places the risk of the drawee's failure upon the holder where presentment has been unreasonably delayed.

Section 166 of the Canadian Act provides that:

"166. (1) Subject to this Act,

"(a) where a cheque is not presented for payment within a reasonable time of its issue, and the drawer or the person on whose account it is drawn had the

right at the time of such presentment, as between him and the bank, to have the cheque paid, and suffers actual damage through the delay, he is discharged to the extent of such damage, that is to say, to the extent to which the drawer or person is a creditor of such bank to a larger amount than he would have been had such cheque been paid;

"(b) the holder of such cheque, as to which such drawer or person is discharged, shall be a creditor, in lieu of such drawer or person, of such bank to the extent of such discharge, and entitled to recover the amount from it.

"(2) In determining what is a reasonable time, within this section, regard shall be had to the nature of the instrument, the usage of trade and of banks, and the facts of the particular case."

#### *Czechoslovakia*

We feel that the time-limit of 120 days from the date of the cheque for presentation of the cheque for payment is correct. It is, however, not clear whether the drawee may pay also after the lapse of this time limit unless the drawer countermands the order to the drawee to pay the cheque. It would implicitly ensue from the provision of article 45 (second sentence), that the drawee should even be obliged to honour the cheque after the lapse of the said time-limit, unless payment has been countermanded, since the drawer is not released from his responsibility by late presentation of the cheque for payment. It would be useful to clarify this provision. Similarly, we recommend to give a corresponding clarification also to article 66.

#### *Germany, Federal Republic of*

The period of presentation of 120 days seems to be too long. There is a danger of the cheque being used not merely as a means of payment but also as a financing instrument.

#### *Spain*

The very considerable amount of time allowed in article 43 for presentation of the cheque (120 days) contrasts with the period allowed under Spanish law. The time allowed seems excessive, considering the fact that the drawer is not exempted from liability even upon expiry of this period.

Furthermore, if the liability of the drawer continues, that of his guarantor should continue also. This is expressly provided for in article 52 in the case of delay in protesting, but not in article 45 in the case of delay in presentment. Although the liability of the guarantor seems clear, it should be expressly stated, particularly in view of the mainly objective character of the guarantee ("aval") under the Convention.

## ARTICLE 44

#### *Indonesia*

The provision of this article which provides for the excuse of delay in making presentment of a cheque for payment is also set forth in the Indonesian Commercial Code. However, the Indonesian Commercial Code does not stipulate the grounds on which such presentment is dispensed with.

Therefore this article is more advantageous to the holder.

#### *Norway*

We suggest that the expression "reasonable diligence" be worked out in some detail in the proposed commentary to the final text.

#### *Spain*

The causes of cessation of the obligation to present a cheque for payment could include one similar to that contained in article 52, paragraph (2) (d), of the draft Convention on International Bills of Exchange and Promissory Notes. The absence of such a clause in the draft Convention in International Cheques is unjustified.

#### *Article 44 (1)*

#### *Canada*

As with article 52 (1) of the Bills of Exchange Convention this ground for dispensing with presentment should, in the view of Canada, be qualified by requiring only reasonable efforts by the holder or its collecting agent.

#### *Article 44 (2)*

#### *German Democratic Republic*

The provisions in paragraph (2) are contrary to the nature of cheques. Apart from that, they would be of no practical consequence. Therefore, we propose to delete this paragraph.

#### *Union of Soviet Socialist Republics*

The purpose of including paragraph (2) (a) in the draft Convention is understandable in view of the consequences specified in article 46 (1) (b). However, noting the waiver of presentment on the cheque essentially conflicts with the nature of a cheque, which in accordance with the order contained in it is subject to payment by the bank upon presentment of the instrument itself. It can be assumed that international cheques with a note of this kind will not in practice be

drawn (any more than they are at present). In accordance with the Geneva Convention (ULC, article 43) even inclusion in the cheque by the parties of a proviso "without costs", "without protest", etc. does not relieve the holder of the requirement to present the cheque for payment within a set time, and this provision of existing international uniform law appears to be correct and reasonable. It is accordingly suggested that paragraph (2) be deleted.

Remarks similar to those made on the draft Convention on International Bills of Exchange and International Promissory Notes are applicable with regard to waiver of presentment "by implication".

#### *Article 44 (2) (a)*

##### *Czechoslovakia*

We propose to delete this provision.

### **ARTICLE 45**

##### *Denmark*

This provision is wider in scope than the corresponding Danish legislation. First, it would be fair to grant the same status to guarantors *et al.* as that enjoyed by the drawer, cf. the commentary on article 41 above. Second, it will be purposeful to amplify this provision with a compensation clause corresponding to section 57 of the Danish Cheques Act which provides that the holder of a dishonoured cheque shall be allowed a claim against the drawer and any endorsers based on the doctrine of unjustified enrichment.

##### *Norway*

1. The guarantor of the drawer is not included in sentence 2 of article 45. However, he is included in paragraph (2) of article 52. The commentary gives no reason for this important difference between the two articles. We suggest the guarantor of the drawer be included in sentence 2 of article 45. If the guarantor wants the benefit of due presentment for payment being an absolute condition precedent to his liability, he may stipulate for it, cf. article 41.

2. Articles 45 and 52 are analogous and ought to have the same structure. We suggest article 45 be divided into two paragraphs as article 52 is. Article 45 may read, cf. also our comment No. 1:

(1) If a cheque is not duly presented for payment, the drawer, the endorsers and their guarantors are not liable thereon.

(2) Delay in presenting a cheque for payment does not discharge the drawer or his guarantor of liability except to the extent of the loss suffered by the delay.

3. The provisions of articles 45 and 52 on the liability of the drawer are an improvement upon the Geneva Convention (ULC). The drawer will be unable to make an inequitable gain in the event of preclusion of recourse. However, an endorser may do so. The right of recourse being a right on the instrument, it seems unclear whether it will be contrary to the Convention in national law to furnish the holder with a claim off the instrument to such an inequitable gain. We suggest that the Convention state that the contracting States are free to do so, cf. article 25 of the Geneva Convention, annex II. However, the question is considerably less important as regards the draft Convention on Cheques than as regards the draft Convention on Bills of Exchange and Promissory Notes.

##### *Spain*

Delay in presentment of a cheque for payment (article 45) or the withholding of protest (article 52) frees the endorsers from liability but not the drawer. This solution is similar to that adopted in Spanish law where, however, the drawer is given a greater opportunity to protect himself from damage caused by the delay (see article 537 of the Spanish Commercial Code).

### **ARTICLE 46**

##### *Denmark*

See the comment of Denmark in part I, B, *supra* under article 54.

### **ARTICLE 47**

##### *Germany, Federal Republic of*

This provision according to which a post-dated cheque shall not be paid before the date mentioned for payment would make it possible to use the international cheque as a credit voucher. In the Federal Government's opinion the cheque, contrary to bill of exchange, should only have the function of a short-term payment voucher.

##### *Indonesia*

The post-dated cheque referred to in this article is also dealt with in the Indonesian Commercial Code.

However, the Indonesian Commercial Code does not provide the remedy for a refusal by the drawee to pay before the stated date, which according to this article does not constitute a dishonour by non-payment.

##### *Uruguay*

This provision is incompatible with the prohibition in article 11 of specification of a maturity date.

## ARTICLE 48

*Denmark*

See the comment of Denmark in part I, B, *supra* under article 55.

*Uruguay*

See the comment of Uruguay in part I, B, *supra* under article 55.

## ARTICLE 49

*Article 49 (2)**United States of America*

See the comment of the United States in part I, B, *supra* under article 56 (2).

*Article 49 (3)**Norway*

See the comment of Norway in part I, B, *supra* under article 56 (3).

## ARTICLE 50

*Czechoslovakia*

We recommend a modification to the effect that protest for dishonour of the cheque by non-payment may be made within the time-limit for presentation of the cheque for payment.

*Union of Soviet Socialist Republics*

It would be desirable to amend this article by accepting a provision in keeping with the Geneva Convention (ULC, article 41), viz.:

"Protest for dishonour of a cheque by non-payment must be made before the expiry of the time limit for presentation of the cheque. If presentation took place on the last day of the time allowed, protest may be made on the next business day."

## ARTICLE 51

*Article 51 (2) (a)**Czechoslovakia*

See the comment of Czechoslovakia in part I, B, *supra* under article 58 (2) (a).

*Hungary*

See the comment of Hungary in part I, B, *supra* under article 58 (2) (a).

*Union of Soviet Socialist Republics*

See the comment of the USSR in part I, B, *supra* under article 58 (2) (a).

## ARTICLE 52

*Denmark*

This provision is wider in scope than its equivalent in the Danish Cheques Act Art. 57 (claim based on the doctrine of unjustified enrichment) as it does not render the drawer liable. Moreover, endorsers and their guarantors, if any, are discharged, which again does not harmonize with said provision of the Danish Cheques Act.

*Norway*

See the comment of Norway to article 45. A comma is missing after the words "duly protested" in paragraph (1).

## ARTICLE 53

*Germany, Federal Republic of*

The suggested extension of the duties to give notice which is different from the Geneva system seems hardly to be practicable: on the one hand, it may lead to all persons concerned being given notice by all others; on the other hand, the persons party to a cheque often only know their immediate previous holder.

*Norway*

1. Paragraph (2) poses a question of interpretation. Who is the party immediately preceding a guarantor, the party for whom he has guaranteed cf. article 42, or the party immediately preceding that party?

2. With reference to paragraph (2) and the example in the commentary, we mention that according to the language of paragraph (2), the person B in the example must give notice of dishonour to A when he is notified by C.

## ARTICLE 56

*Uruguay*

In order to facilitate implementation of the provision in the various countries which will adopt the Convention, it would be desirable to explain the concept of "reasonable diligence", or to provide some guidelines which would enable judges to interpret it in a more or less uniform manner.

*Article 56 (2) (b)**Czechoslovakia*

We suggest the deletion of the words "or by implication".

*Hungary*

See the comment of Hungary in part I, B, *supra* under article 58 (2) (a).

*Union of Soviet Socialist Republics*

See the comment of the USSR in part I, B, *supra* under article 52.

**ARTICLE 59***Norway*

See the comment of Norway in part I, B, *supra* under article 66 (1) (b) (ii).

*Article 59 (3)**United Kingdom of Great Britain and Northern Ireland*

See the comment of the United Kingdom in part I, B, *supra* under article 66 (2).

**CHAPTER SIX. DISCHARGE****ARTICLE 61***Article 61 (2)**Norway*

See the comment of Norway in part I, B, *supra* under article 68 (3).

*United States of America*

See the comment of the United States in part I, B, *supra* under article 68 (3).

**ARTICLE 62***Denmark*

The provisions do not clearly specify whether the drawee is allowed to refuse partial payment, which it ought to be allowed to do.

*Indonesia*

See the comment of Indonesia in part I, B, *supra* under article 69.

*Norway*

The word "authenticated" appears in paragraphs (4) (b) and (6). We cannot see that the word has any function in the contexts in which it appears. We therefore suggest that it be deleted.

**ARTICLE 63***Indonesia*

See the comment of Indonesia in part I, B, *supra* under article 70.

**ARTICLE 66***Indonesia*

The countermand of a cheque according to this article is effective from the date of the order to stop payment, and the drawee bank must comply with the countermand of the drawer. Such countermand, according to the Indonesian Commercial Code, is without effect until the time limit for presentment. The provision in this article provides legal certainty to the drawee bank.

*Uruguay*

We feel that this provision is undesirable as it weakens confidence in the instrument.

In Uruguayan internal law a cheque is an irrevocable order. Should the draft Convention be adopted with the present provision maintained, Uruguay will have to enter appropriate reservations.

**CHAPTER SEVEN. CROSSED CHEQUES AND CHEQUES PAYABLE IN ACCOUNT****ARTICLES 68, 69, 70, 71 and 72***Australia**Article 68*

There is no provision in article 68 corresponding to s. 86 of the BEA which provides that a bank paying in good faith and without negligence according to the crossing is treated as if it had paid the true owner. In this respect article 68 follows the ULC rather than the BEA. However, it is noted that article 25 (2) specifically leaves matters relating to the liability of a party or drawee who pays, or of an endorsee for collection who collects, a cheque on which there is a forged endorsement, to be regulated by national law.

*United States of America**Articles 68-72*

Crossed cheques and cheques payable in account are unknown in the United States. It is questionable whether persons in the United States would know how to handle these cheques properly. It is possible that bank employees who handle cheques in bulk could be educated to identify these unusual items and to refer them to knowledgeable superiors. However, that would still not protect members of the general public, who also handle cheques regularly but would not be aware of the specialized rules concerning these unusual items. Thus, crossed cheques would confuse an unsuspecting public and might present opportunities for fraud if they were usable in the United States.

Further, even proper use of crossed cheques or cheques payable in account would not provide in the United States the protection expected by the foreign drawer, because the bank-customer relationship is quite different in the United States from what it appears to be in countries where such items are in regular use. In the United States, the bank-customer relationship can be more casual. United States banks do not usually investigate the past history of deposit account customers, and some banks do not even investigate the identity of such customers, so long as they are dealing with collected funds. Thus, the thief who steals a crossed cheque or cheque payable in account would probably be able in the United States to establish an account and realize on it. And, if he steals such a cheque before it reaches the payee, the loss would fall on the foreign drawer who expects to be protected.

For these reasons, the United States suggests that the use of crossed cheques and cheques payable in account in the United States would not protect parties, but might even create new avenues for potential fraud, both on all original parties to the instrument and on the general public. A possible solution might be to allow States ratifying the Convention on International Cheques to omit chapter seven (articles 68-72) by an appropriate reservation.

*Indonesia**Article 71*

The Indonesian Commercial Code does not contain a provision along the lines set forth in this article. Since this article permits the transferee to acquire the rights of a protected holder, we are inclined to adopt this provision.

*Japan**Articles 68-71*

The Japanese Government believes it essential to retain the provision on crossed cheques, which are

similar to those found in the British Bills of Exchange Act and in the Geneva Uniform Law. The non-negotiable crossed cheque which would be established under article 71 is confusing, and the provision should, therefore, be deleted.

*Spain**Articles 68-71*

The draft Convention devotes particular attention to two cases: that of the crossed cheque and that of the cheque payable in account. The Convention provides that the consequences of failure to "cross" a cheque or to indicate that it is payable in account are limited to liability for damages, but there is no reference to the question of legitimation or to the discharging effects of payment. Furthermore, the distinction between the protected and the non-protected holder is again made in article 71, which indicates some consequences of the entry of the words "not negotiable". These seem to be inconsistent with the provision in article 18.

On the whole, the draft Convention's rules concerning special cheques are inadequate. The question should be dealt with more fully or, alternatively, should not be referred to at all in the Convention, which should confine itself to regulating the general prototype of cheque, so that special cheques would be left subject to the applicable national law. We would, however, prefer the first solution.

**CHAPTER EIGHT. LOST CHEQUES****ARTICLE 73***Denmark*

See the comment of Denmark in part I, B, *supra* under article 74.

*Indonesia*

See the comment of Indonesia in part I, B, *supra* under article 74.

*Japan*

See the comment of Japan in part I, B, *supra* under article 74.

*Norway*

See the comment of Norway in part I, B, *supra* under article 74.

*Spain*

Article 73 contains a paragraph (3) which is lacking in the corresponding article of 74 of the draft Convention on International Bills of Exchange and Promissory Notes. Its omission from the latter text is unjustified. The case of non-transferability is regulated in both drafts (see article 18 for the case of cheques and article 16 for the case of bills of exchange and promissory notes).

## ARTICLE 74

*Indonesia*

See the comment of Indonesia in part I, B, *supra* under article 75.

## ARTICLE 75

*Japan*

See the comment of Japan in part I, B, *supra* under article 76.

*Norway*

See the comment of Norway in part I, B, *supra* under article 76.

## ARTICLE 78

*Norway*

See the comment of Norway in part I, B, *supra* under article 79.

*United States of America*

See the comment of the United States in part I, B, *supra* under article 79.

## CHAPTER NINE. LIMITATION (PRESCRIPTION)

## ARTICLE 79

*Denmark*

See the comment of Denmark in part I, B, *supra* under article 80.

*Indonesia*

See the comment of Indonesia in part I, B, *supra* under article 80.

*Japan*

See the comment of Japan in part I, B, *supra* under article 80.

*Norway*

See the comment of Norway in part I, B, *supra* under article 80.

*Uruguay*

We suggest that the provision be worded as follows:

"A right of action arising on a cheque shall cease to exist after four years have elapsed . . ."

The content of the rule will thus correspond to the *nomen juris* of the chapter.

**2. Draft Convention on International Bills of Exchange and International Promissory Notes and Draft Convention on International Cheques: major controversial and other issues: note by the secretariat (A/CN.9/249 and Add.1)<sup>a</sup>**

[A/CN.9/249]

## CONTENTS

	<i>Paragraphs</i>
INTRODUCTION.....	1-4
PART I. GENERAL COMMENTS ON THE DRAFT CONVENTIONS .....	5-11
A. Draft Convention on International Bills of Exchange and International Promissory Notes .....	6-10
B. Draft Convention on International Cheques .....	11

<sup>a</sup>For consideration by the Commission see Report, chapter II, A, 2 (part one, A, above).

	Paragraphs
<b>PART II. MAJOR CONTROVERSIAL ISSUES . . . . .</b>	<b>12-20</b>
A. Forged endorsements (articles 14 (1) (b) and 23) . . . . .	13-14
B. The concept of holder and protected holder . . . . .	15-16
C. Liability of a transferor by mere delivery . . . . .	17-18
D. Crossed cheques and cheques payable in account . . . . .	19-20
<b>PART III. ADDITIONAL ISSUES . . . . .</b>	<b>21-39</b>
A. Draft Convention on International Bills of Exchange and International Promissory Notes . . . . .	22-34
B. Draft Convention on International Cheques . . . . .	35-38

---

## INTRODUCTION

1. The United Nations Commission on International Trade Law, at its sixteenth session (24 May-3 June 1983), decided to devote part of its seventeenth session to a substantive discussion of the draft Convention on International Bills of Exchange and International Promissory Notes and the draft Convention on International Cheques. To this end it requested the secretariat to identify key features and major controversial issues that may be inferred from the comments of Governments and international organizations on the draft Conventions.<sup>1</sup>

2. This note has been prepared in response to the request of the Commission. It analyses the comments of 24 Governments<sup>2</sup> to the extent that these comments reveal major problems and substantial controversies; an analytical compilation of the comments submitted by Governments and the International Monetary Fund is contained in document A/CN.9/248 (reproduced in this *Yearbook*, part two, I, A, 1).

3. The text of the draft Convention on International Bills of Exchange and International Promissory Notes is set forth in document A/CN.9/211 (*Yearbook 1982*, part two, II, A, 3), and the text of the draft Convention on International Cheques in document A/CN.9/212 (*Yearbook 1982*, part two, II, A, 5). The commentary on the draft Convention on International Bills of Exchange and International Promissory Notes is contained in document A/CN.9/213 (*Yearbook 1982*, part two, II, A, 4), and the commentary on the draft Convention on International Cheques in document A/CN.9/214 (*Yearbook 1982*, part two, II, A, 6).

4. This note is in three parts. Part I analyses the major issues raised by Governments in their general comments

on the draft Conventions. Part II deals with the following subject matters in respect of which there appear to be major controversial issues: A. Forged endorsements; B. The concept of holder and protected holder; C. Liability of a transferor by mere delivery; D. Crossed cheques and cheques payable in account. Part III sets forth additional issues raised in the comments by Governments.

### Part I. General comments on the draft Conventions

5. An analytical survey of the general comments of Governments on the draft Conventions obviously cannot reflect the nuances and differences of emphasis which only a reading of the full text of the comments will reveal. Reference is therefore made to document A/CN.9/248 (reproduced in this *Yearbook*, part two, I, A, 1) which reproduces in part I, A, the general comments on the draft Convention on International Bills of Exchange and International Promissory Notes and in part II, A, the general comments on the draft Convention on International Cheques.

#### A. *Draft Convention on International Bills of Exchange and International Promissory Notes*

6. The comments show that a majority of the responding Governments<sup>3</sup> are of the general view that:

(a) The draft Convention represents an acceptable and workable compromise between the civil law and common law systems;

(b) The draft Convention generally simplifies the issue, negotiation and payment of the proposed instruments;

(c) The draft Convention provides certainty in the rules applicable to international commercial transactions and obviates the application of conflict of laws rules;

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its sixteenth session, *Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17* (A/38/17), para. 80 (*Yearbook 1983*, part one, A).

<sup>2</sup>Australia, Austria, Botswana, Canada, China, Cyprus, Czechoslovakia, Denmark, Finland, German Democratic Republic, Germany, Federal Republic of, Hungary, Indonesia, Japan, Mexico, Netherlands, Norway, Spain, Sweden, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland, United States of America, Uruguay and Yugoslavia.

<sup>3</sup>Australia, Canada, China, Czechoslovakia, Finland, German Democratic Republic, Hungary, Indonesia, Japan, Norway, Spain, USSR, United States, Uruguay and Yugoslavia.

(d) The text of the draft Convention is well organized, detailed and of relevance to modern business practices and it solves satisfactorily the problems arising in the context of settling international payment transactions by means of negotiable instruments.

Most of the Governments referred to above are therefore of the view that the draft Convention on International Bills of Exchange and International Promissory Notes constitutes a suitable basis for the adoption of an international convention on the subject.

7. Several Governments, with different emphasis,<sup>4</sup> express doubt about the advantages of adopting a new Convention on International Bills of Exchange and International Promissory Notes. The arguments of these Governments may be summarized as follows:

(a) The establishment of a third system of negotiable instruments law does not add measurably to legal certainty;

(b) Because of the complexity of its provisions, a new convention in the form currently proposed has little or no chance to enter into force;

(c) A convention of the scope proposed by the draft would be effective only if it would be mandatory;

(d) The harmonization of the law of negotiable instruments should be focused on the unification of legal rules concerning domestic negotiable instruments or in the alternative further work should be done in respect of a draft convention resulting in uniform rules for both domestic and international instruments;

(e) The Commission's efforts to bring about unified law should be directed at making the Geneva uniform laws acceptable to the countries of the common law system.

8. *Note by the secretariat:* One may roughly formulate the positions taken by responding Governments as follows:

(a) The efforts of the Commission should be directed towards the adoption of a Convention on International Bills of Exchange and International Promissory Notes for optional use;

(b) The Convention should be of a mandatory character;

(c) It is inadvisable to establish a third system of negotiable instruments law;

(d) The unification of negotiable instruments law should focus on a revision of the Geneva Conventions of 1930 and 1931 with a view of making them acceptable to countries of the common law system. The draft Convention prepared by the UNCITRAL Working Group could serve as a suitable basis for such work.

9. In discussing the above issues the Commission may wish to recall that at its second session (3-31 March 1969) it took its decision in respect of work on negotiable instruments after having considered the following three issues:

<sup>4</sup>Austria, Germany, Federal Republic of; to lesser degree: Netherlands, Sweden, United Kingdom.

(a) Securing a wider acceptance of the Geneva Conventions of 1930 and 1931;

(b) Revising the Geneva Conventions of 1930 and 1931 with a view to making them more acceptable to countries following the Anglo-American legal system;

(c) Creating a new negotiable instrument.

10. After further study and taking into account the replies of Governments and international organizations to a questionnaire, the Commission at its third session (6-30 April 1970) was unanimous in considering that "the only viable approach at the current stage was for it to focus its work on a convention setting forth rules that would be applicable to a special negotiable instrument for use in international transactions. The uniform rules set forth in such a convention would only be applicable to an instrument bearing a heading indicating that it would be subject to the rules of the convention. The use of the instrument would be optional."<sup>5</sup> At its fourth session (29 March-20 April 1971), the Commission gave further consideration to the approach it had approved at its third session and expressed general agreement that "this approach would provide the most feasible solution to the problem and difficulties in this field of international payments".<sup>6</sup>

## B. Draft Convention on International Cheques

11. Those Governments which express doubt about the advantages of adopting a new Convention on International Bills of Exchange and International Promissory Notes have even more serious reservations as regards a new Convention on International Cheques. Most of the Governments which express support for the draft Convention on International Bills of Exchange and International Promissory Notes also, and for the same reasons, express support for the draft Convention on International Cheques. However, some of these Governments<sup>7</sup> take a less positive attitude in respect of the draft Convention on International Cheques. The reasons for these doubts and reservations may be summarized as follows:

(a) Since international bills of exchange and international promissory notes are typically employed by the business community in international transactions and cheques are less frequently used in such transactions, there is not the same need for a convention on international cheques as there is for a convention on international bills of exchange and international promissory notes; future efforts should rather be directed towards the law relating to international payments made by electronic funds transfer;

<sup>5</sup>Report of the United Nations Commission on International Trade Law on the work of its third session (1970), *Official Records of the General Assembly, Twenty-fifth Session, Supplement No. 17 (A/8017)*, para. 112 (*Yearbook 1968-1970*, part two, III, A).

<sup>6</sup>Report of the United Nations Commission on International Trade Law on the work of its fourth session, *Official Records of the General Assembly, Twenty-sixth Session, Supplement No. 17 (A/8017)*, para. 27 (*Yearbook 1971*, part one, II, A).

<sup>7</sup>Norway, United States.

(b) There would be greater difficulty to adapt banking and commercial practices to a convention on international cheques as currently drafted by reason of the absence of specific collection rules such as those contained in article 4 of the Uniform Commercial Code and the presence of rules on crossed cheques and cheques payable in account, both unknown in the United States;

(c) The draft Convention does not do justice to the special function of a cheque as a payment instrument and therefore cannot be considered as a suitable basis for further work in respect of international cheques.

## Part II. Major controversial issues

12. The issues referred to under A, B and C below are presented here in respect of the draft Convention on International Bills of Exchange and International Promissory Notes but concern equally the draft Convention on International Cheques.

### A. Forged endorsements (articles 14 (1) (b) and 23)

13. The comments of Governments show by and large that the proposed scheme in respect of forged endorsements is generally acceptable. However, the following are issues in respect of which there appears to be disagreement:

(a) The transferee from the forger should not be liable if he took the instrument in good faith (Mexico, Spain);

(b) The use of the term "party" in article 23 (1) would prevent a payee (see definition of "party" in article 4 (8)) from recovering compensation for any damage that he may have suffered because of the forgery of his signature (Japan). In this connection Japan suggests that after the words "any party" the words "and any person whose endorsement is forged", be added;

(c) Article 23 should state that the amount which may be recovered as compensation is limited to the amount specified in article 66 or 67 (Japan);

(d) In respect of article 23 (2), the liability of the paper of an instrument or of the endorsee for collection who collects an instrument on which there is a forged endorsement should be specifically regulated (Austria, Hungary, Mexico, USSR). In this connection it is suggested that the payer or the endorsee for collection should be liable for compensation only if he knew of the forgery (Hungary, Mexico, USSR);

(e) An exception should be made to the general rules applicable to forged endorsements in situations where the instrument is issued as part of a fraudulent scheme by an employee of the drawer who causes the instrument to be issued in the name of some person, real or fictitious, with the intention of signing that person's endorsement. In such situations the loss should be placed on the drawer and not on the taker from the forger (United States).

14. *Note by the secretariat:* It would appear that of the five main issues raised in connection with forged endorsements only the first issue materially affects the compromise proposed in the draft Convention. As regards the issue raised under (b) above, it would seem that it was within the intention of the Working Group that any person whose endorsement was forged should be entitled to recover compensation under article 23. Therefore, the amendment proposed by Japan appears to reflect that intention. With regard to the issue raised under (c) above, the Commission may wish to decide whether article 23 (1) should provide for a limit to the amount of compensation recoverable. If so, the Commission might consider that the compensation recoverable under article 23 (1) may not exceed the amount referred to in article 66 or 67.

### B. The concept of holder and protected holder

15. The comments made in respect of articles 4 (7), 25 and 26 of the draft Convention show that several respondents from civil law countries are of the view that the approach of the Geneva uniform laws is to be preferred to that of the draft Convention on the following grounds:

(a) The draft Convention's approach, in operating a distinction between holder and protected holder, lacks clarity and is complex (Austria, Czechoslovakia, Netherlands, Spain);

(b) The requirements which must be met by a holder in order to obtain protected holder status are too strict and go beyond those that should be required for a person to be a holder in good faith (Austria, Czechoslovakia, Federal Republic of Germany, Norway, Spain, Yugoslavia). In particular:

(i) Knowledge of a particular claim or defence should not preclude protection against other claims or defences of which the holder had no knowledge (Austria, Federal Republic of Germany, Norway);

(ii) Under the proposed scheme it would be possible that a person who, in taking the instrument, acts knowingly to the detriment of the debtor nevertheless cuts off a defence because his transferor was a protected holder (cf. shelter rule of article 27), whereas under the Geneva uniform laws he would not be so protected (Austria);

(c) It is difficult to determine, on the basis of the instrument alone, what the rights are of a person in possession of an instrument: is he a holder or a protected holder? (Austria);

(d) The question as to what constitutes a valid claim to the instrument is not regulated but left to the applicable law (Austria).

16. The following suggestions are made:

(a) *In respect of article 4 (7) (definition of protected holder):*

(i) It is unacceptable that a holder cannot be a protected holder if the instrument was in-

complete at the time he became a holder, even if the instrument was subsequently completed by that holder in accordance with the authority given. For example, under the draft Convention such a holder would not be able to cut off a defence unrelated to the element left uncompleted, but completed as authorized (Finland, Norway);

- (ii) The definition of protected holder is not sufficiently comprehensive. In particular the criterion of "regularity" is not clear and requires further study (Japan);
- (iii) In subparagraph (a) the phrase "referred to in article 25" should be deleted. This limitation is not justified since it would permit a person to attain protected holder status even though, when taking the instrument, he knew of breach of contract defences or fraud in the inducement in the transaction underlying the original issue of the instrument (United States);

*(b) In respect of article 25 (rights of a holder):*

The defences that may be set up against a holder should be listed (Austria); a list of specific cross references to articles of the Convention furnishing defences should be added (United States);

*(c) In respect of article 26 (rights of a protected holder):*

- (i) The protected holder should be protected against the defence of *non est factum* (Denmark); the words "or on the fact that such party signed without knowledge that his signature made him a party to the instrument, provided that such absence of knowledge was not due to his negligence" should be deleted (Finland);
- (ii) The defences referred to in article 26 (c) are incomplete; preference is given to leaving the question as to what constitutes a real defence to the applicable law (Netherlands).

### C. Liability of a transferor by mere delivery

17. Several respondents oppose the provision laid down in article 41, which imposes liability, off the instrument, on a transferor by mere delivery, and propose to delete it (Czechoslovakia, Denmark, Federal Republic of Germany, Japan, Netherlands, Norway) or, if the provision is to be retained, to reexamine it in relation to the liability of a transferor by endorsement and delivery (Japan, Netherlands). The view is also expressed that the provision as now drafted would impair the circulation of the instrument (Federal Republic of Germany, Netherlands). In particular, several respondents note that article 41 would impose greater liability on transferors by mere delivery than on transferors by endorsement and delivery (Japan, Netherlands, Norway, United States).

18. The following suggestions are made:

- (a) The liability of the transferor by mere delivery should be left to the applicable national law (Czechoslovakia);

(b) The application of article 41 (1) (a) should be restricted to the forged signature of the drawer (Norway);

(c) The words, in paragraph (1), "by mere delivery" should be deleted so as to make the warranty liability of article 41 applicable to both endorsers and non-endorsers (United States).

### D. Crossed cheques and cheques payable in account (Articles 68-72 of the draft Convention on International Cheques)

19. The United States suggests, for the reasons stated in its comments on articles 68-72, that thought should be given to allowing Contracting States to omit chapter seven (articles 68-72) of the draft Convention by an appropriate reservation.

20. Japan, while in favour of retaining the provisions on crossed cheques, is of the view that the non-negotiable crossed cheque which article 71 establishes is confusing and proposes deletion of that article.

## Part III. Additional issues

21. In addition to the major controversial issues set forth in Parts I and II above, the comments raise many other issues of substance and drafting. Though these issues are of the kind that could be left to a conference of plenipotentiaries, the Commission may wish to discuss some or all of the issues set forth below.

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

#### 22. Article 1 (2) (e): "international elements"

(a) Japan queries whether an instrument should qualify as an international instrument merely because it shows that the place indicated next to the name of the drawee and the place of payment are situated in different States. It is proposed that the places listed in paragraph (2) (e) should be listed in distinct groupings and that the instrument should be considered an international instrument only if at least one of the places in one group and one of the places in another group are situated in different States.

(b) Japan is also of the view that of the places listed in paragraph (2) (e), the place where the instrument is drawn or made and the place of payment are to be regarded as essential factors determining the law applicable to issues not covered by the Convention. For this reason Japan proposes that the place of drawing and the place of payment be made essential requisites for purposes of the application of the Convention.

#### 23. Article 4 (10) and article X: "definition of signature"

(a) Canada opposes a provision along the lines of article X on the ground that permitting contracting

parties to vary the legal effect of signatures other than handwritten signatures would erode the advantages of uniform rules. Canada therefore proposes the deletion of article X. The German Democratic Republic, Hungary and the Union of Soviet Socialist Republics express strong support for the retention of article X and for the inclusion of an article along the lines of article 12 of the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980; *Yearbook 1980*, part three, I, B).

(b) Denmark and the Federal Republic of Germany express doubt about including a provision in the Convention allowing for signatures that are made by mechanical and other means.

(c) Mexico and Spain are of the view that a signature made by the unauthorized use of mechanical means should not be deemed to be a forged signature.

(d) The United States proposes that the definition of forged signature should include both unauthorized signatures and those beyond the scope of an agent's authority.

#### 24. Article 4 (11): "definition of money"

(a) Czechoslovakia, the United States and the International Monetary Fund suggest that the definition of money be improved.

(b) Specifically, the United States proposes that the definition be amended to include both official physical currency and immediately available credit.

(c) The International Monetary Fund proposes a definition of money or currency as follows:

"'Money' or 'currency' includes a monetary unit of account which is established by an intergovernmental institution and which is transferable among the members of this institution or other entities as the institution may prescribe."

#### 25. Article 6 (a): "rate of interest"

(a) Czechoslovakia and the United States propose that where an instrument is to be paid with interest the interest rate should be stated.

(b) The United States proposes that the provision should permit floating rate notes to be negotiable.

#### 26. Article 7 (4): "rate of interest stipulated"

China notes that owing to constant changes in international market rates it is hardly possible to fix the interest rate on a time bill in advance and that sometimes the interest rate is calculated at a floating rate prevailing at the date of payment (see also the observations of the United States under article 6 (a)). China proposes that the following phrase should be added to paragraph (4): "or indicates that interest is to be paid at the international market rate at a definite time and place".

#### 27. Article 10: "bill drawn by drawer on himself"

China observes that a bill drawn by the drawer on himself is by nature a promissory note and that accordingly the holder may treat it as such under the provisions governing international promissory notes.

For this reason China proposes that the article be supplemented by the following wording: "and regarded by the holder as an international promissory note".

#### 28. Article 11: "incomplete instrument"

China proposes that this article be deleted since the provision may give rise to unnecessary disputes.

#### 29. Articles 30, 52, 58, 63: "legal effects of implied act or omission"

The draft Convention recognizes in several provisions the legal effect of an act or omission which is not express but implied. Czechoslovakia, the German Democratic Republic, Hungary and the Union of Soviet Socialist Republics oppose this concept.

#### 30. Article 34 (2): "exclusion of liability by drawer"

Denmark, Norway and Spain are opposed to a provision permitting the drawer to exclude his liability.

#### 31. Article 42: "guarantee"

(a) The Federal Republic of Germany objects to the presumption that if a guarantor has not specified the person for whom he has become guarantor that person is the acceptor or the drawee in the case of a bill and the maker in the case of a note on the ground that the intention of the guarantor is usually expressed by the fact that the guarantor's signature is placed next to that of the person for whom the guarantee is given.

(b) Japan proposes that article 42 should include a provision to the effect that an incomplete instrument may be guaranteed before it has been signed by the drawer or the maker or while otherwise incomplete. Japan notes that the draft Convention makes provision for the acceptance by the drawee of an incomplete instrument.

(c) Spain queries the provision allowing a guarantee to be given for the drawee.

#### 32. Articles 48 and 52: "bankruptcy of drawee"

The German Democratic Republic, Hungary, Spain and the Union of Soviet Socialist Republics are of the view that presentment for acceptance and presentment for payment should be dispensed with in the case where the drawee is bankrupt or insolvent and that an immediate right of recourse should then be available to the holder.

#### 33. Article 58 (2) (d): "dispensation of protest for dishonour"

Spain objects to this provision which dispenses with protest for dishonour by non-acceptance or non-payment if presentment for acceptance or for payment is dispensed with.

#### 34. Article 68 (3): "ius tertii"

(a) Norway suggests that where a third person has asserted a claim to the instrument the provision of article 68 (3) should provide that the law of the place of payment should determine whether payment of the amount of the instrument into court should constitute a discharge.

(b) The United States proposes that article 68 be amended to make an exception to discharge of the payer where a third party claimant both notifies the payer of its claim and provides security deemed adequate by the payer.

### B. Draft Convention on International Cheques

#### 35. Article 4: "postdated cheques"

(a) Uruguay objects to this provision which permits the cheque to bear a date other than the date on which it is drawn, on the ground that to so date a cheque is a criminal offense in Uruguay.

(b) The Federal Republic of Germany, in the context of article 47 which provides that a postdated cheque shall not be paid before its date, objects to the use of postdated cheques on the ground that this would make it possible to use the international cheque as a credit voucher.

*Note by the secretariat:* Under the Geneva Uniform Law on Cheques, article 28, a postdated cheque is payable on demand.

#### 36. Article 12: "cheques drawn by a bank on itself"

The Federal Republic of Germany and Norway are of the view that to allow banks to draw cheques on themselves would amount to the creation of money and that this would not be advisable.

#### 37. Article 24: "transfer after expiration of time for presentment"

Uruguay objects to this provision.

#### 38. Article 66: "stop payment"

Uruguay objects to this provision under which the drawer is entitled to countermand the order to the drawee to pay the cheque.

\* \* \*

39. *Note by the secretariat:* Finally, the secretariat draws the attention of the Commission to article 66 (2) and (3) of the draft Convention on International Bills of Exchange and International Promissory Notes and articles 36 (2) and 59 (3) of the draft Convention on International Cheques which contain square brackets.

[A/CN.9/249/Add.1]

### Addendum

#### Summary of the comments of Romania and Switzerland

(*Note by the secretariat*)

1. This addendum contains an analytical survey of the comments of Romania and Switzerland on the draft Convention on International Bills of Exchange and

International Promissory Notes and the draft Convention on International Cheques. These comments were received after document A/CN.9/249, analysing the comments of 24 Governments and the International Monetary Fund, had been completed. The comments of Romania and Switzerland could also not be included in the analytical compilation of comments by Governments and international organizations (A/CN.9/248).\*

### Part I. General comments on the draft Conventions

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

2. Switzerland is of the opinion that:

(a) The co-existence of two divergent systems of negotiable instruments law (i.e. the Anglo-American system and the Geneva uniform-law system) has not adversely affected international payment transactions by means of these instruments, and that it therefore must be doubted whether the creation of a third system is justified;

(b) Difficulties arising in connection with negotiable instruments do not stem from the applicable law but are due to such problems as the insolvency of the debtor or foreign exchange restrictions.

3. Switzerland also expresses the view that:

(a) Though in international payment transactions the bill of exchange has to a great extent been replaced by the documentary letter of credit and other payment instruments, there are certain commercial transactions that require the use of an instrument such as the bill of exchange which retains its importance as an instrument of credit and of discounting. A modernization of the bill of exchange could well make this type of commercial paper more attractive;

(b) The work carried out by UNCITRAL might serve as the basis for the formulation of a new system that would replace the Geneva Uniform Law. The Convention embodying the new system should unify the law represented by the two major systems. States that become parties to the Convention would undertake to incorporate it in their domestic law;

(c) The proposed draft Convention sets forth rules governing international bills of exchange, whilst what is needed are international rules governing bills of exchange. It is considered inadvisable to establish a new third system in addition to the existing systems. Such an approach would leave current problems unresolved and only create additional problems.

#### B. Draft Convention on International Cheques

4. The comments of Switzerland on the draft Convention on International Cheques take up the gist of the

\*Copies of the comments of Romania and Switzerland in their original language (French) were made available at the seventeenth session of the Commission (see Report, chapter II, A, para. 13; part one, A, above).

comments made in respect of the draft Convention on International Bills of Exchange and International Promissory Notes: the creation of a third system applicable to international cheques is inadvisable and the work of unification should be directed towards a convention, acceptable to both common law and civil law countries, which Contracting States would incorporate in their domestic law.

5. Switzerland is moreover of the view that the cheque, as a widely used payment instrument, requires special collection rules and that a convention on international cheques should set forth rules dealing with the technical aspects of this type of instrument, such as standardization of size of and indications on the cheque, lines of printed numerical symbols (encoding), etc., which would facilitate the electronic processing of cheques.

## Part II. Major controversial issues

6. The issues referred to under A, B and C below are presented here in respect of the draft Convention on International Bills of Exchange and International Promissory Notes but concern equally the draft Convention on International Cheques.

### A. Forged endorsements (articles 14 (1) (b) and 23)

7. Switzerland approves of the principle stated in article 14 (1) (b) in that it facilitates the circulation of the bill of exchange. However, the proposed scheme in respect of forged endorsements presents, in the view of Switzerland, certain disadvantages. In particular, article 23 imposes on the transferee the obligation to verify the authenticity of the signatures on the bill of exchange. Such an obligation has drawbacks on the national level but these would become almost insurmountable on the international level. Article 23 would thus adversely affect two essential properties of the bill of exchange: its ease of circulation and its negotiability. The Swiss comments give the following example: assume a bill is drawn in Hong Kong in favour of a payee domiciled in Switzerland; the payee endorses the bill to an American citizen living in New York. If the signature of the Swiss payee has been forged, the American endorsee would, under article 23, incur liability because he does not know the Swiss payee personally and is not in a position to verify rapidly and correctly the authenticity of the latter's signature.

8. In the opinion of Switzerland the risk of a forged endorsement should be borne by the person who is at fault or has been negligent, i.e. by the person who lost the instrument and by the forger. However, with regard to cheques, Switzerland notes that the solution of the draft Convention may have certain advantages in view of the growing practice of "cheque truncation".

### B. The concept of holder and protected holder

9. Switzerland is of the view that the concept of "protected holder" may give rise to confusion. The

position of a protected holder seems to correspond to that of a holder under the Geneva Uniform Law. In the result, the holder under the draft Convention is, from a legal point of view, in a far less favourable position than the holder under the Geneva system.

10. Switzerland further expresses the view that, by establishing a special category of privileged holders (protected holders), the draft Convention introduces the notion of causality and all kinds of defence may be set up against the non-protected holder. Grave negligence may prevent a holder from being a protected holder. However, under article 17 of the Geneva Uniform Law on bills of exchange and promissory notes, protection is denied only if the holder has knowingly acted to the detriment of the debtor. In the opinion of Switzerland the approach of the draft Convention would impair the circulation of the international bill of exchange. Moreover, that approach is thought to be too complicated. Preference is given to the more simple approach of the Geneva Uniform Law which has proved to be entirely satisfactory.

### C. Liability of the transferor by mere delivery

11. According to the Swiss comments the provision laid down in article 41 is contrary to the Swiss legal order in that it imposes liability on a transferor who has not signed the instrument and who has no knowledge of the irregularities referred to in the article. The provision is not in accordance with the principle of good faith and must, for that reason, be rejected.

## Part III. Additional issues

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

#### 12. Article 4 (10): "signature"

(a) Romania is of the opinion that the draft Conventions should not allow a signature being made by facsimile, because of the inherent danger of forgery.

(b) Switzerland states that this provision could give rise to difficulties under current Swiss law which does not recognize a signature by facsimile.

#### 13. Article 4 (11): "definition of 'money'"

(a) Romania is opposed to the inclusion of monetary units of account in the definition of "money" since this may create difficulties as regards the circulation of negotiable instruments.

(b) Switzerland finds the definition of "money" unacceptable in that it includes a monetary unit of account. It is stated that at present the use of negotiable instruments denominated in a unit of account is unknown.

#### 14. Article 6: "stipulation of interest"

Switzerland would prefer the provision of the Geneva Uniform Law on Bills of Exchange and Promissory

Notes to article 6 of the draft Convention. Under article 5 of the Geneva Uniform Law a stipulation of interest is admissible only in respect of a bill drawn payable at sight or at a fixed period after sight. In respect of bills with a fixed maturity date interest may be calculated in advance and included in the amount of the instrument. It is pointed out that the stipulation of a rate of interest in the bill might give rise to problems particularly when bills are discounted in that the discounting bank applies a discount rate that is independent from the interest rate stipulated.

**15. Article 8 (3) (c) and (d): "instruments payable by instalments"**

Switzerland suggests that subparagraphs (c) and (d) of paragraph (3) of article 8 be deleted.

**16. Article 9: "plurality of drawers or payees"**

Switzerland states that the plurality of drawers or payees is almost never encountered in practice, and it doubts the usefulness of article 9 (1) and (2). It is suggested that, if the provision were retained, the presumption of paragraph (3) be reversed and that an express statement in the bill be required for those cases where payment must be made to two or more payees.

**17. Article 22: "transfer after maturity"**

Switzerland notes that article 22 does not specify the effect of a transfer after protest for non-payment. It is suggested that, in this respect, article 22 should follow article 20 of the Geneva Uniform Law on Bills of Exchange and Promissory Notes according to which such a transfer operates only as an ordinary assignment.

**18. Article 27: "shelter rule"**

Switzerland is opposed to the shelter rule in that it may violate the principle of good faith.

**19. Article 34 (2): "liability of the drawer"**

Switzerland is opposed to a provision permitting the drawer to exclude his liability.

**20. Article 42 (5): "guarantee"**

Switzerland objects to the presumption that if a guarantor has not specified the person for whom he has become guarantor, that person is the acceptor or the drawee in the case of a bill and the maker in the case of a note.

**21. Article 46 (1): "presentment for acceptance"**

Switzerland doubts the appropriateness of the rule that the drawer may stipulate on a bill that it must not be presented for acceptance before the occurrence of a specified event.

**22. Article 48: "dispensation of presentment for acceptance"**

Switzerland suggests that article 48 (a) specify that a necessary or optional presentment for acceptance is dispensed with only if no person or authority entitled under the applicable law to accept the bill can be found.

On the other hand it is submitted that the notion of "reasonable diligence" is too vague and would create a degree of legal insecurity that must be considered inadmissible.

**23. Article 51 (e): "due presentment for payment of an instrument not payable on demand"**

Switzerland suggests that article 51 (e) should follow the rule of article 38 of the Geneva uniform law on bills of exchange and promissory notes according to which a bill not payable on demand may be presented on the date of maturity or on one of the two business days which follow. The Geneva rule is particularly commendable in the context of international payment transactions.

**24. Article 52: "presentment for payment excused"**

In the view of Switzerland the fact that article 52 recognizes that delay in making presentment for payment may be excused for reasons which are personal to the holder might create legal insecurity.

Objection is also made to waiver of presentment for payment by implication.

**25. Article 60: "notice of dishonour"**

Switzerland prefers the approach of the Geneva Uniform Law under which the holder is required to give notice of dishonour merely to his endorser and to the drawer, and every endorser is required to notify his endorser of the notice he has received.

**26. Article 66: "reimbursement of costs"**

Switzerland notes that article 66, as currently drafted, does not make clear whether or not the holder may recover costs he incurred by exercising his right of recourse.

**27. Article 71: "payment in the currency expressed"**

In the opinion of Switzerland the provisions of article 71 are often repetitive and of a too great complexity.

**28. Suggested new article on enforceability**

Romania suggests inclusion in the draft Convention of a new article providing for the enforceability of bills of exchange, as found in certain legal systems (e.g. Italian and Romanian law). Such simplified enforcement procedure would be of advantage to the creditor in that it would ensure speedy recovery of the sum due.

## B. Draft Convention on International Cheques

**29. Article 4: "date of issue"**

Switzerland expresses the view that article 4 is not acceptable if it is to be interpreted as stating the rule that the date of issue on a cheque is of secondary importance. Amongst other things the time within which a cheque must be presented for payment depends on the date of issue (cf. article 43).

**30. Article 6 (3): "definition of 'banker'"**

It is suggested by Switzerland that the commentary to article 6 (3) specify that "any person or institution assimilated to a banker" refers only to such person or institution which is subject to adequate supervision by the State. The reason for this suggestion is that there exist in many countries financial establishments, analogous to banks, that do offer certain banking services but, because they do not refinance themselves from deposits, are not subject to supervision designed to protect the creditors of these establishments. The view is expressed that if such establishments were considered as "bankers" for purposes of the Convention, confidence in the international cheque as a means of payment would be seriously impaired.

**31. Article 8: "definite sum"**

Switzerland notes that this article does not deal with the question whether the sum payable by a cheque may be expressed in more than one currency and, therefore, does not answer the question whether a so-called multiple currency clause meets the requirement of a "definite sum of money". It is further noted that multiple currency clauses are frequently used in practice in connection with the issue of bonds and notes. A multiple currency clause in a cheque could, for instance, read as follows:

"Pay £5,000 in Swiss francs at the rate of exchange of (x) Swiss francs for one pound sterling or in German marks at the rate of (y) German marks for one pound sterling."

It is suggested that the Convention give a clear answer (positive or negative) to this question.

**32. Article 36: "certification, confirmation, acceptance, etc. of a cheque"**

Switzerland is of the view that the provision of article 36 is contrary to the very nature of the cheque which is an instrument of payment and not of credit. The provision would create risks for the drawee banks in light of the rule that, under the draft Convention, the time-limit for presentment is 120 days.

**33. Article 43: "time-limit for presentment"**

Switzerland is of the opinion that the time-limit of 120 days within which a cheque must be presented for payment is too long and would transform the cheque into an instrument of credit. It is suggested that the time-limit of 70 days laid down in the Geneva Uniform Law on Cheques (article 29) in cases where the place of issue and the place of payment are situated in different continents should be the maximum period of time allowed for presentment.

## B. Electronic funds transfers

### Draft legal guide on electronic funds transfers: report of the Secretary-General (A/CN.9/250 and Add.1 to 4)<sup>a</sup>

#### CONTENTS

[A/CN.9/250]	<i>Paragraphs</i>
I. Report of the Secretary-General .....	1-7
[A/CN.9/250/Add.1]	<i>Page</i>
II. Preface .....	1-8
III. Terminology used in this guide .....	1-7
Introduction .....	1-7
Glossary .....	120

<sup>a</sup>For consideration by the Commission see Report, chapter II, B (part one, A, above).

[A/CN.9/250/Add.2]	<i>Paragraphs</i>
<b>IV. Chapter on electronic funds transfer system in general</b>	
A. Enhanced role of the system .....	1-5
B. Two types of funds transfers .....	6-16
1. Credit transfer .....	8-13
2. Debit transfer.....	14-16
C. Routing of funds transfer instruction.....	17-28
1. One-bank transfer .....	18
2. Two-bank transfer.....	19-25
3. Three-bank transfer.....	26-28
D. Settlement .....	29-39
1. In general .....	29-31
2. Settlement through a third bank .....	32
3. Settlement through a clearing-house.....	33-39
E. Some particular features of electronic funds transfers.....	40-52
1. Replacement of one or more paper-based steps .....	40-41
2. Telecommunications .....	42-44
3. Batch transmission .....	45-48
4. Customer-activated electronic funds transfers.....	49-52

*Figures*

	<i>Page</i>
I. One bank holding accounts of transferor and transferee.....	124
II. Two banks in direct relation each holding account of the other .....	125
III. Correspondent bank holding accounts of two other banks.....	126
IV. Correspondent bank holding <i>loro</i> accounts of two other banks.....	126

[A/CN.9/250/Add.3]	<i>Paragraphs</i>
<b>V. Chapter on agreements to transfer funds and funds transfers instructions</b>	
A. General agreement between bank and customer to transfer funds .....	1-11
1. Contract for cash payment.....	2-4
2. Agreement for transfer to or from an account .....	5-11
B. Authority to transfer funds and to debit transferor's account .....	12-25
1. Debit and credit transfer instruction issued by transferor and presented to transferor bank .....	12
2. Debit transfer instruction truncated at transferee bank .....	13-18
3. Paper-based debit transfer instructions not issued by the transferor ..	19-20
4. Electronic debit transfer instructions not issued by the transferor ..	21-23
5. Authority of one bank to debit account of another bank .....	24-25
C. Funds transfer instruction .....	26-54
1. Authentication .....	26-39
(a) Form of authentication .....	30-35
(b) What must be authenticated .....	36-39
2. Data elements .....	40-46
3. Format .....	47-54
D. Time within which bank must act on the instruction .....	55-81
1. General considerations .....	55-56
2. Customer's concern about speed and consistency of performance .....	57-66
(a) Impact on relations between customers .....	58-59
(b) Interest earning potential of customer bank balances .....	60-65
(c) Irrevocability of funds transfer instruction .....	66
3. Bank's concern about speed and consistency of performance.....	67-73
(a) Interest earning potential of bank assets .....	68-71
(b) Security of reimbursement to transferee bank .....	72-73

	<i>Paragraphs</i>
4. Responsibility of destination bank to act promptly .....	74-78
(a) Credit transfer .....	74-76
(b) Debit transfer .....	77-78
5. Effect of branch banking .....	79-81

## [A/CN.9/250/Add.4]

## VI. Chapter on fraud, errors, improper handling transfer instruction and related liability

Introductory note .....	1-3
A. Fraud .....	4-28
1. Opportunity for fraud .....	4-23
(a) Dishonest employees of bank customer .....	5-12
(b) Fraudulent use of customer-activated terminals .....	13-21
(c) Customer-supplied machine-readable instructions .....	22
(d) Fraud by bank employees .....	23
(e) Fraud by tapping telecommunications transmissions .....	24
2. When may a fraudulent instruction justify a debit to an account .....	25-30
B. Errors .....	31-46
1. General sources of errors using computers .....	31-36
2. Current sources of errors peculiar to the electronic funds transfer system .....	37-41
(a) Non-standardization of messages .....	37
(b) Re-creation of messages .....	38-39
(c) Non-standardized procedures .....	40-41
(d) Computer failure and software errors .....	42
3. Conceivable methods to prevent errors from occurring .....	43-46
C. Need for customers to verify status of accounts .....	47-55
1. Statement of account activity .....	47-50
2. Customer's examination of the statement .....	51-54
3. Duty of a bank to correct entries .....	55
D. Responsibility of an originating bank to its customer for errors or fraud made in an inter-bank transfer; a network liability approach .....	56-60
E. Permissibility of disclaimer of liability .....	61-77
1. Technical failure of computer hardware or software .....	64-67
2. Data-communications service .....	68-73
3. Should an originating bank be exonerated from a delay or non-delivery of a funds transfer instruction after dispatch .....	74-77
F. Malfunctioning in an electronic clearing-house or in a switch owned by or operated for a group of banks; loss sharing by participating banks .....	78-81
G. Improper handling of transfer instructions .....	82-88
1. Wrongful dishonour of instructions by a transferor bank and damages to the transferor .....	82
2. Inaction on debit instructions by the transferor bank within the required time-limits .....	83-88
(a) General rules for negotiable instruments .....	83-85
(b) Delay in honouring debit transfer instruction .....	86
(c) Delay in dishonouring debit transfer instruction .....	87-88
H. Recoverable losses .....	89-100
1. Loss of principal .....	90-91
2. Loss of interest .....	92-95
3. Exchange loss .....	96-97
4. Indirect damages .....	98-100

[A/CN.9/250]

### I. Report of the Secretary-General

1. The subject of international payments was one of the three placed on the priority list of topics at the first session of the Commission in 1968.<sup>1</sup> At its fifth session in 1972 the significant changes in international banking practices brought about by developments in electronic funds transfer methods and procedures were first brought to its attention and the hope was expressed that the Commission's work in the field of international payments would take account of those developments.<sup>2</sup> In 1975 in connection with its assessment of the desirability of preparing uniform rules applicable to international cheques, the Working Group on International Negotiable Instruments requested the secretariat "to obtain information regarding the impact, in the near future, of the increased use of telegraphic transfers and of the development of telecommunication systems between banks on the use of cheques for settling international payments".<sup>3</sup> In 1978 the subject of electronic funds transfers was added to UNCITRAL's programme of work.<sup>4</sup>

2. By 1978 the subject of electronic funds transfers was already being considered to a minor degree by the UNCITRAL Study Group on International Payments. In connection with its advice to the secretariat of the Commission on practical banking experience on matters arising in the preparation of the draft Convention on International Bills of Exchange and International Promissory Notes and the draft Convention on International Cheques, the Study Group had commented on the questions raised in 1972 and 1975 about the impact of electronic techniques on the future course of development in respect of the international funds transfer system. As a result, in 1979 UNCITRAL requested that the preparatory work of the secretariat on electronic funds transfers be carried on in the framework of the Study Group.<sup>5</sup>

3. In order to obtain more information on the electronic funds transfer networks in operation and in the planning stages and on the legal regime governing those networks, in 1980 a questionnaire was sent to central banks throughout the world. Only a small

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its first session, *Official Records of the General Assembly, Twenty-third Session, Supplement No. 16* (A/7216), para. 48 (2) (*Yearbook 1968-1970*, part two, I, A).

<sup>2</sup>Report of the United Nations Commission on International Trade Law on the work of its fifth session, *Official Records of the General Assembly, Twenty-seventh Session, Supplement No. 17* (A/8717), para. 57 (*Yearbook 1972*, part one, II, A).

<sup>3</sup>"Report of the Working Group on International Negotiable Instruments on the work of its third session" (A/CN.9/99) para. 136 (*Yearbook 1975*, part two, II, I).

<sup>4</sup>Report 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).

<sup>5</sup>Report 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).

number of central banks replied to the questionnaire in detail. Several others sent more general information about their funds transfer systems, including the use of electronic funds transfers, and many, including central banks from developing countries, indicated that they would be interested in whatever information they could be given.

4. As a source of information on the legal regimes governing electronic funds transfers, the questionnaire was only a limited success. It made clear, however, that only a few of the central banks which replied in detail—principally central banks in western Europe and North America—were certain as to what rules governed many of the important issues. In many cases the responses to the questionnaire assumed that some or most of the rules governing paper-based transfers applied, although a number of the responses also indicated an awareness that those rules did not always give appropriate results.

5. In the light of the responses to the questionnaire and an awareness of the rapid growth in the use of electronic means of transferring funds both domestically and internationally, the UNCITRAL Study Group on International Payments recommended to the fifteenth session of the Commission in 1982 that, as a first step, the Commission should prepare a guide on the legal problems arising out of electronic funds transfers.<sup>6</sup> The guide, it was suggested, should be oriented towards providing guidance for legislators or lawyers preparing the rules governing particular systems.

6. The Commission accepted this recommendation and requested the Secretariat to begin the preparation of a legal guide on electronic funds transfers, in co-operation with the Study Group.<sup>7</sup> Some draft chapters which are annexed to this report in addenda are the product of that co-operation and are hereby submitted to the Commission for general observations.

7. At the eighteenth session of the Commission, the secretariat will submit a draft chapter on finality of honour and a check-list of legal issues to be considered by legislators or lawyers in preparing the rules governing electronic funds transfers.

[A/CN.9/250/Add.1]

### II. Preface

1. This legal guide has been prepared to aid legislators and lawyers considering the rules for particular networks. Since the guide is intended to be of practical value in a number of countries, there has been a conscious effort not to rely upon or to discuss legal

<sup>6</sup>"Electronic funds transfers: report of the Secretary-General" (A/CN.9/221) para. 85 (*Yearbook 1982*, part two, II, C).

<sup>7</sup>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), para. 73 (*Yearbook 1982*, part one, A).

theories or to consider problems which arise only in a small number of countries. On the contrary, there has been a deliberate effort to find the common elements in the law and the banking practice of funds transfers so as to ease the process of adapting the law governing paper-based transfers to the requirements of electronic funds transfer techniques. Although the greatest use of electronic funds transfer techniques is to be found at present in the economically developed countries, this guide may be of most value in the developing countries where the need is being felt to modernize their funds transfer systems for both domestic and international purposes.

2. Computers first entered the back rooms of banks as a means of handling more efficiently the increasing volume of paper-based funds transfers. The introduction of magnetic ink character recognition (MICR), and later optical character recognition (OCR), on both debit and credit transfer instructions permitted the automated processing of standardized paper documents. This development increased the efficiency with which clearing-houses and individual banks were able to cope with the increased number of funds transfers, and often caused a wholesale reorganization of the clerical operations of the banks. The creation of computer centres by banks led some of them to centralize the record keeping of customer accounts at the computer centre rather than to continue the previous decentralized record keeping of accounts by each branch.

3. Once many banks were equipped with computers to handle paper-based funds transfer instructions, it was possible to devise means to exchange funds transfer instructions in electronic form, either by the physical exchange of computer memory devices or by telecommunications. In some countries it has been possible to take this step with no fundamental change in the established institutional structure. In other countries new institutions have been created to operate interbank telecommunications facilities, message switches and electronic clearing-houses. Computer memory devices can be submitted by banks to automated clearing-houses for sorting the funds transfer instructions contained on those devices and redispaching to the receiving banks.

4. Funds transfer instructions have long been sent by telegram and telex. The international teletransmission of computer-to-computer funds transfer instruction is now available through connection to the Society for Worldwide Interbank Financial Telecommunications (S.W.I.F.T.) as well as through the internal telecommunications systems of banks with multi-national branches. Several of the consumer-oriented debit-card and credit-card networks are developing international telecommunications systems for purposes of authorization of transactions, transmission of funds transfer data and the linking of automated cash dispensers and automated teller machines. International point-of-sale systems are expected to follow soon. In a related development Eurocheque is moving towards truncation in the country of deposit with electronic presentment to the transferor (drawee) bank in its country.

5. Several international organizations have undertaken projects to explore the significance of these developments. The Bank for International Settlements (BIS) published in 1980 a monograph entitled *Payment Systems in Eleven Developed Countries*, which looks into the payment systems in operation in those countries and the possible changes these systems may undergo with the increased use of automated data processing techniques. A new edition is to be published in 1984 with statistical data to the end of 1983. The Organisation for Economic Co-operation and Development (OECD) published in 1983 a monograph by J. R. S. Revell entitled *Banking and Electronic Funds Transfers*. The monograph describes the nature of electronic funds transfer systems which have been introduced into OECD member States and the impact that those systems have on banking and on monetary policy, although legal factors are not considered in depth. BIS has also published a monograph entitled *Security and Reliability in Electronic Systems for Payments*, 2nd ed. (September 1982).

6. In a broader context of automated data processing, several other organizations are active in the field. For example, the Working Party on Facilitation of International Trade Procedures, a subsidiary organ of the Economic Commission for Europe which works closely with UNCTAD's Special Programme on Trade Facilitation (UNCTAD/FALPRO), is responsible for facilitating international trade and transport by promoting rationalization of trade procedures and the effective use for this purpose of electronic and other forms of automated data processing and the teletransmission of trade data. Among the recent activities of the Working Party has been the identification of legal issues arising out of the use of these new procedures.

7. The Council of Europe adopted in 1981 the Convention for the Protection of Individuals with Regard to Automatic Processing of Personal Data. The Convention will come into force three months after five member States of the Council of Europe have expressed their consent to be bound. The OECD in 1980 also adopted "Guidelines governing the protection of privacy and transborder flows of personal data". The Council of Europe adopted in 1981 a recommendation to its member States concerning the conditions under which computer records would be admissible as evidence in a court or arbitral tribunal.

8. Work is progressing in other international organizations such as the Customs Co-operation Council, International Maritime Organization and the International Civil Aviation Organization on legal aspects of automatic data processing arising out of the special concerns of those organizations. Although of no direct relevance to electronic funds transfers, the solutions adopted in one context are apt to be of significance in other contexts. The United Nations Commission on International Trade Law, as the core legal body in the field of international trade law, serves as the central forum for co-ordination of these various efforts.

### III. Terminology used in this guide

#### *Introduction*

1. With the exception of negotiable instruments, where the three parties on the face of a bill of exchange or a cheque are consistently referred to as the drawer, drawee and payee, there is no generally accepted terminology in use to describe the parties or the activities involved in a funds transfer. In each country terms have developed which have reflected the realities of the funds transfer system in use in that country. It has also been true within many countries that bankers and lawyers have used different terms to describe the same party or the same activity, or that the same term had different meanings depending on the circumstances.

2. The problems arising out of inconsistent terminology in funds transfers have become serious only in recent years. The rapid switch to electronic means of data transmission between banks, coupled with the use of computers for processing funds transfer messages, has called for the standardization of the content of the messages and their formats. This in turn has required standardization of the terms used to describe the data elements in each type of funds transfer message.

3. To remedy this situation the Banking Committee of the International Organization for Standardization (ISO, TC 68) is developing international standards for various aspects of automated banking operations and has prepared a Draft International Standard (DIS 7982) in English and French for data elements and terms used in describing, processing and formatting messages relating to credit transfers transmitted over computer-to-computer telecommunications networks. The terminology in DIS 7982 has been followed closely in the preparation of DIS 7746 on telex formats for inter-bank funds transfer messages. The development of these international standards and general adherence to them by banks making international funds transfers should have the effect of reducing the number of errors and loss suffered. However, the terminology used in other international standards which have been adopted or are in preparation by the ISO Banking Committee and by the other ISO committees whose work is relevant to electronic funds transfers have defined some terms inconsistently with the definitions in DIS 7982. Therefore, the Banking Committee is compiling a list of all such terms defined by ISO committees in published documents. The compilation, which will also contain terms defined by other organizations interested in electronic funds transfers, is expected to serve as the basis for a consistent definition of terms used in international electronic funds transfers.

4. The terminology in DIS 7982 has generally been established from the viewpoint of the bank which receives a funds transfer message, "since it is incumbent upon the receiver of a funds transfer message to interpret and understand the full intent and meaning of funds transfer messages received through a variety of services or systems". This reflects the purpose of DIS 7982, which is to aid in formatting individual funds transfer messages.

5. However, the decision to identify and define terms and data elements used in individual credit transfer instructions sent by computer-to-computer telecommunications in order eventually to establish an international standard for the format of such instructions and to establish mapping conventions to help translate funds transfer instructions from one network to another makes it inevitable that the terminology chosen for that purpose will be oriented towards the message passing between any given pair of banks. Such a terminology emphasizes the instruction for a funds transfer as the central element at the expense of the entire funds transfer. Therefore given the purpose of the terminology, it is unlikely to be appropriate for other kinds of funds transfers for which it was not intended, such as batch mode credit transfer by means of exchange of computer memory devices or debit transfers of all types.

6. The terminology as used in this guide starts from that in DIS 7982. However, in spite of the general desirability of international agreement on terminology for use in all contexts to describe the parties and the activities involved in an electronic funds transfer, the terminology used in this legal guide sometimes deviates substantially from that found in DIS 7982, since the primary orientation of this legal guide is to describe parties and actions in relation to the funds transfer rather than to the funds transfer instruction.

7. In this orientation the principal parties are the "transferor" of the funds, his bank the "transferor bank", the "transferee" of the funds, and his bank the "transferee bank". If there are any banks between the transferor bank and the transferee bank, they are "intermediary banks". The transfer may be either a "debit transfer" or a "credit transfer", and the "funds transfer instruction" may be further described as either a "debit transfer instruction" or a "credit transfer instruction". The principal terms used in this guide are defined in the Glossary which follows.

#### *Glossary*

**Authentication:** The identification of a message in a physical, electronic or other manner which permits the receiver to determine that the message comes from the source indicated. For the purposes of this guide it is immaterial whether authentication may also permit the receiver to determine that the message has not been deliberately or inadvertently altered. The authentication of a message does not necessarily indicate that the message as received was authorized or that the person sending the message had authority to do so. (Compare the definition of "authentication" given by the subcommittee on test-keys of the ISO Banking Committee: "The process of determining that a message comes from a source authorized to originate messages of that type" (ISO document 68/2 N 80 or 68 N 118). Compare also the definition of "authenticator result" in DIS 7982, "A code in a message between the sender and the receiver used to validate the source and the full text of the message".)

*Automated clearing-house:* See electronic clearing-house.

*Bank:* A financial institution which as an ordinary part of its business engages in funds transfers for itself or other parties, whether or not it is recognized as a bank under the relevant law.

*Clearing-house:* An institution which effects the exchange of funds transfer instructions between participating banks and performs the accounting to enable settlement. (See also electronic clearing-house.)

*Closed-user network (for funds transfers):* A paper-based or electronic clearing-house, a communications service or a switch which is restricted to the banks or their customers who agree to adhere to particular technical standards and banking procedures.

*Communications service:* A service that moves messages, including funds transfer instructions, among subscribers but which does not perform the accounting to enable settlement. (Similar to definition of "communication service" in DIS 7982.)

*Computer memory device:* An external support on which data in computer-readable form can be stored.

*Credit transfer:* A funds transfer where the account of the originating bank or its customer is to be debited and the account of the destination bank or its customer is to be credited.

*Debit transfer:* A funds transfer where the account of the originating bank or its customer is to be credited and the account of the destination bank or its customer is to be debited. (Compare to definition of "debit transfer" in DIS 7982.)

*Destination bank:* The bank to which the chain of funds transfer instructions is ultimately addressed. In a credit transfer the transferee bank is the destination bank. In a debit transfer the transferor bank is the destination bank.

*Destination party:* The customer of the destination bank.

*Electronic clearing-house:* A clearing-house for funds transfer instructions in electronic form. An electronic clearing-house may be either on-line or off-line. An electronic clearing-house operating in batch mode is also referred to as an automated clearing-house.

*Entry date:* Date on which entries are made in records of an account. (Identical to DIS 7982.)

*Funds transfer:* Movement of funds between the transferor and the transferee. (Almost identical to first sentence of DIS 7982. Compare definitions of "funds transfer transaction" and of "payment" in DIS 7982.)

*Funds transfer instruction:* A message or that part of a message that contains the instruction and required details for a funds transfer. A funds transfer instruction may be further indicated to be a debit transfer instruction or a credit transfer instruction. (First sentence almost identical to definition of instruction in DIS 7982. Second sentence is new. Compare definition of "payment order" in DIS 7982. This term is not used both because it seems to duplicate "instruction" and in order to avoid use of the word "payment" in regard to the inter-bank funds transfer.)

*Interest date:* Date as of which funds credited to an account begin to earn interest or funds debited to an account cease to earn interest.

*Intermediary bank(s):* Bank(s) between the originating bank and the destination bank through which a funds transfer passes. (Compare to definition in DIS 7982.)

*Originating bank:* The bank which transmits the first of a chain of funds transfer instructions to another bank. In a credit transfer the transferor bank is the originating bank. In a debit transfer the transferee bank is the originating bank.

*Originating party:* The customer of the originating bank.

*Pay date:* Date on which the funds are to be freely available to the transferee for withdrawal in cash. (Almost identical to DIS 7982.)

*Personal identification number (PIN):* The secret code used to authenticate funds transfer instructions initiated through a customer-activated terminal. (Based on definition in ISO 4909 "Bank cards—Magnetic stripe data content for track 3".)

*Receiving bank:* The bank to which a message, including a funds transfer instruction, is delivered. (Almost identical to DIS 7982.)

*Sending bank:* The bank which sends a message, including a funds transfer instruction, to a receiving bank. (Based upon DIS 7982. Has been modified so that a bank sending a funds transfer instruction by transmission of a computer memory device or by sending a paper-based funds transfer instruction is also a sending bank.)

*Settlement:* A transfer of funds from a bank with a debit position to a bank with a credit position or an agreed accounting entry between them to cover one or more prior funds transfer transactions. (Based on DIS 7982.)

*Standing authorization to debit:* Authorization given by transferor to the transferor bank, the transferee bank or the transferee authorizing the transferor bank to honour debit transfer instructions presented in accordance with the terms of the authorization.

*Standing instruction to credit:* Funds transfer instruction given by transferor to transferor bank to transfer a specified sum to the account of a specified transferee at regular intervals.

*Switch:* A mechanism which receives, sorts and directs messages, including funds transfer instructions.

*Transferee:* The customer of the transferee bank. (Compare to definition of "beneficiary" in DIS 7982.)

*Transferee bank:* The bank which credits the transferee's account as a result of a funds transfer. (Compare to definition of "beneficiary bank" in DIS 7982.)

*Transferor:* The customer of the transferor bank. (Compare to definition of "originator" in DIS 7982.)

*Transferor bank:* The bank which debits the transferor's account as a result of a funds transfer. (Compare to definition of "originator's bank" in DIS 7982.)

[A/CN.9/250/Add.2]

#### IV. Chapter on electronic funds transfer systems in general

##### A. Enhanced role of the system

1. The funds transfer system as a whole refers to the total set of institutions and banking practices which permit and facilitate inter-bank funds transfers. Until recently this system was essentially paper-based. As it developed over time, it became increasingly standardized for both domestic and international funds transfers as a result of the efforts of banking associations, clearing-houses, and other bodies representing the banking industry and the State. Nevertheless, while the funds transfer system as a whole provided the structure within which individual banks executed funds transfers, until recently in most countries the system did not restrict significantly the judgment of banks as to the methods by which funds transfers were made.

2. This situation began to change when the essential data on paper-based funds transfer instructions was encoded on the instructions in machine-readable form, i.e. magnetic ink character recognition (MICR) or optical character recognition (OCR). The technical requirements of these procedures called for a further standardization of the size of the funds transfer instructions, the location of the data fields, their length and the characters to be used.

3. Associated with the need for increased standardization has been the development of closed-user networks for funds transfers. Closed-user networks have existed for a long time in the form of clearing-houses for paper-based funds transfer instructions to which some, but not all, banks had access as direct participants. However, beginning in the 1960s a new type of closed-user network for paper-based funds transfers appeared in the form of bank credit cards and of Eurocheque. In both cases essentially all banks within the countries where the network existed were permitted to become members. However, if they became members, they had to conform to its technical standards and banking practices. While these requirements were not excessively stringent, the individual banks relinquished a degree of autonomy in order to participate. The system itself had become a more active participant in effectuating the funds transfers and in establishing the technical and banking standards to which the individual banks had to adhere.

4. The development of efficient computer-to-computer transmission of funds transfer instructions, whether by physical transmission of computer memory devices or by telecommunications, has further enhanced the active role of the system. New closed-user networks for electronic funds transfers have been created. The

technical requirements of these networks have led to more stringent requirements as to formatting of messages and to the operating and emergency procedures to be used. The vulnerability of electronic funds transfer systems to fraud has led to mandatory security procedures. By the present time the quality and security of inter-bank funds transfers have become a function of the quality of design and of operation of these closed-user networks as well as of the quality of operation of the banks involved. Furthermore, banking standards and practices first developed within the closed-user networks are being adapted by national and international standards bodies concerned with banking to the broader needs of the funds transfer system as a whole.

5. The design of the system determines whether funds transfers can be made promptly, accurately and securely. The legal rules should include provisions determining who bears the responsibility when the failure of that design leads to loss for individual banks or their customers. On a number of occasions throughout this legal guide, attention is drawn to the need to reconsider the currently existing rules in the light of the fact that many of the important technical and banking decisions having been previously the sole province of the individual banks have become matters of concern for the system as a whole.

##### B. Two types of funds transfers

6. An electronic funds transfer as the term is used in this guide is a funds transfer in which one or more of the steps in the process that were previously done by paper-based techniques are now done by electronic techniques. The replacement of the physical transportation of a paper-based debit or credit transfer instruction between the banks involved in the funds transfer by the sending of an electronic message between them and the processing of debit or credit transfer instructions by a computer are the most obvious and most important of them. By combining the various electronic techniques it has also been possible to create new electronic systems which are not simply modifications of earlier paper-based systems.

7. It would be possible to consider the banking and legal problems which arise in funds transfers conducted in a pure electronic environment without reference to funds transfers using paper-based techniques. It would not, however, be useful to do so. Many funds transfers contain elements of both electronic and paper-based funds transfer techniques. Moreover, the basic patterns for funds transfers are the same whatever may be the means of transmission of the instruction between the banks or the manner in which the accounts of the banks are kept. This chapter will describe the basic procedures for executing funds transfers in general with special reference to electronic funds transfers.

###### 1. Credit transfer

8. A credit transfer is often described as one in which the funds are pushed from the transferor to the

transferee. Where both the transferor and the transferee maintain bank accounts, the transferor instructs his bank to debit his account and to credit or to cause to be credited the account of the transferee at the same or at a different bank. Where the transferor does not have an account to be debited, he may pay the transferor bank in cash the sum to be transferred. Where the transferee does not have an account to be credited, the transferor bank may undertake to pay the sum to the transferee in cash as is often done by the postal service. The instruction may pass between the transferor and the transferor bank in writing, by telex, by telephone, by submission of a magnetic tape containing a series of accounts to be credited or by any other means agreed on by the parties. Upon receipt of the instruction from the transferor, the transferor bank would normally authenticate the instruction and check the balance in the transferor's account before acting upon the instruction to transfer funds to the transferee's account.

9. A credit transfer instruction directing credit of an account at the same bank as that of the transferor may be completed by a book transfer whereby the account of the transferor is debited and the account of the transferee is credited. When a credit transfer instruction directs that an account be credited at another bank (the transferee bank), the transferor bank debits the transferor's account, passes the instruction to credit the transferee's account through an appropriate channel to the transferee bank, and reimburses the transferee bank for the amount of the transfer. Reimbursement of the transferee bank by the transferor bank is referred to as settlement.

10. In some cases the credit transfer instruction from the transferor is in a form which can be passed directly to the transferee bank unaltered. This is most common in domestic paper-based systems where the original form completed by the transferor can be sent to the transferee bank. It can also occur if the transferor (i.e. the customer) prepares magnetic tapes or other computer memory devices where all of the instructions on the device call for crediting accounts at the same transferee bank. In other cases a new credit transfer instruction directed to the transferee bank (or to an intermediary bank) must be prepared based upon the instruction received from the transferor. In either case the receiving bank (i.e. the transferee bank or intermediary bank) can verify only that the instruction came from the transferor bank. It can neither verify the authenticity of the transferor's original instruction nor ascertain whether the transferor bank has been or will be reimbursed by the transferor.

11. Although a credit transfer is generally described in this guide as a complete movement of funds between the transferor and the transferee, a credit transfer need not involve any customers of the banks, or there may be a transferor but no transferee or a transferee but no transferor. For example, S.W.I.F.T. and ISO in DIS 7746, the draft international standard setting forth uniform telex formats, distinguish three types of credit transfer instructions, only one of which is directly applicable to a transfer for a customer. DIS 7746

describes these three types of credit transfer instruction as follows (the terminology used in this guide is inserted in the description in square brackets):

	<i>Number and name</i>	<i>Description</i>
100	Customer transfer	A payment order [credit transfer instruction] in which either the originator [transferor] and/or the beneficiary [transferee] is a non-bank.
200	Bank transfer for own account	A payment order [credit transfer instruction] in which the sender [transferor bank] and the beneficiary [transferee bank] are the same bank without reference to any other transaction.
202	General bank transfer	A payment order [credit transfer instruction] where the originator [transferor bank] and the beneficiary [transferee bank] are banks but not the same bank. Such a transfer is always in relation to some other transaction.

12. The credit transfer is particularly well suited to the use of electronic means of communication. In the normal case neither the transferor nor the transferee has any reason to object to such use and, since negotiable instruments are not used in credit transfers, the legal problems which must be overcome to collect negotiable instruments electronically do not arise. Credit transfers in electronic form have been widely used for over a hundred years in the form of telegraphic transfers. Telex payment instructions and computer-to-computer links are but modern versions of this venerable device. Even in countries in which the majority of domestic inter-bank transfers are made by debit transfer using cheques, electronic credit transfers are often used for business payments. In some of these countries the electronic funds transfer facilities have been substantially improved in recent years and the majority of large-value business payments are made in this way.

13. A recent development has been the payment of such obligations as salaries, pensions and monthly social security benefits to the transferee's bank account, a service available only by virtue of the increasing number of individuals who maintain accounts in banks. This type of credit transfer is particularly suited to computer processing. Large volume transferors who possess equipment compatible with that used by the banks may be encouraged to prepare themselves the magnetic tapes or other computer memory devices with the necessary funds transfer data for use by their bank.

## 2. Debit transfer

14. A debit transfer is often described as one in which the funds are pulled from the transferor to the transferee. In a debit transfer the transferee instructs his

bank to collect a specific sum of money from the transferor. The transferee's instruction may be accompanied by a debit transfer instruction signed by the transferor, such as a cheque or a promissory note payable at the transferor bank, which directs the transferor bank to transfer the sum to the account of the transferee and to debit the account of the transferor. The transferee may also be able to receive the sum in cash by presenting the debit transfer instruction over the counter to the transferor bank for immediate honour. Alternatively, the transferee may attach to his instruction a bill of exchange which he has drawn himself calling on the transferor or his bank to pay the sum indicated. The drawing of a bill of exchange by the transferee would normally have been previously authorized by the transferor, for example, in a sales contract or by a letter of credit which the transferor had opened for the benefit of the transferee.

15. In order to avoid problems arising out of the collection of bills of exchange, problems arising not only out of the legal régime of negotiable instruments but also out of stamp taxes and other considerations, an increasing share of debit transfers in international trade involve a claim made by the seller-transferee without the use of a bill of exchange. Such claims are suitable for transmission by electronic means so long as they do not have to be accompanied by commercial documents in a paper-based form. The most difficult problem for the international use of electronic debit transfers has been to devise means of carrying out commercial letter of credit transactions and bank financing without resort to a paper-based bill of lading.

16. In addition to debit transfers arising out of specific transactions, debit transfers may be instituted in favour of a transferee to whom large numbers of parties are indebted on a regular basis. Debit transfers based on standing authorizations to debit are particularly susceptible to electronic processing and large customers with their own computer facilities may themselves prepare the magnetic tapes or other computer memory devices with debit transfer instructions on them.

### C. Routing of funds transfer instruction

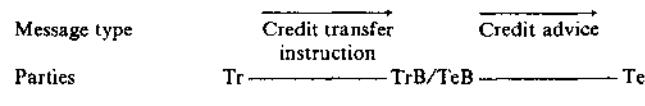
17. There are several standard patterns for routing funds transfer instructions between the banks concerned. These patterns are the same whether a single funds transfer instruction is sent as a discrete item or whether a number of items are sent as a batch. The routing patterns are also basically the same for debit transfers and for credit transfers, although the nature of the instruction differs. These standard routing patterns can be described as one-bank, two-bank and three-bank transfers. In some countries legal rules governing such matters as finality of honour depend on the number of banks involved in the funds transfer. The routing of debit and credit transfers in certain standard situations, the type of message sent between the parties and the bookkeeping entries by the different banks are shown in figures I to IV.

### 1. One-bank transfer

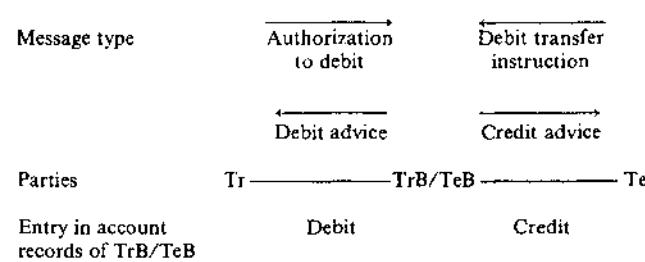
18. When the transferor and the transferee have their accounts at the same bank, both debit transfers and credit transfers are executed by debiting the account of the transferor and crediting the account of the transferee. The distinction between the two types of transfer is that the transferor gives the bank a credit transfer instruction while the transferee gives the bank a debit transfer instruction. If the accounts are kept at more than one record keeping centre of the same bank (which might be a branch or a regional data processing centre of the bank), the instruction must be transmitted between those centres in a manner similar to the transmission of an instruction between separate banks. In a one-bank funds transfer the bank serves both as transferor bank and as transferee bank, and has separate obligations in these two roles.

*Figure I. One bank holding accounts of transferor and transferee*

#### A. Credit transfer



#### B. Debit transfer



Key to symbols used in figures I to IV

Tr: transferor  
TrB: transferor bank  
IB: intermediary bank  
TeB: transferee bank  
Te: transferee

### 2. Two-bank transfer

19. Many funds transfer instructions calling for the transfer of funds between accounts in two different banks are transmitted directly between the two banks concerned. This most often occurs when the two banks are geographically close to one another, when they have a high volume of instructions to transmit to one another, when one bank acts as a clearing agent for the other, when the amount to be transferred is very large or when the transfer must be executed promptly. Before any two banks begin direct transmission of funds transfer instructions, they reach prior agreement to do

so, exchange signature lists, test keys or other means of authenticating funds transfer instructions and make arrangements for settlement of the funds transfers.

20. Direct transmission of funds transfer instructions from one bank to another may be accomplished by the physical transmission of paper-based funds transfer instructions or of computer memory devices such as magnetic tape. Direct transmission is also considered to have taken place when the funds transfer instruction passes between the two banks with no intermediaries other than a communications service or a clearing-house.

21. A communication service by which funds transfer instructions are transmitted may be available for public use, as is the postal service or a telex service, or it may be restricted to the transmission of messages between the members of a group of banks, as is S.W.I.F.T. In either case the communications service carries the instructions and sorts or "switches" them to the correct addressee. In some electronic on-line clearing-houses, the funds transfer instructions are carried on the public facilities of the telecommunications carrier from the banks to a "switch" owned by or operated for the banks participating in that particular network.

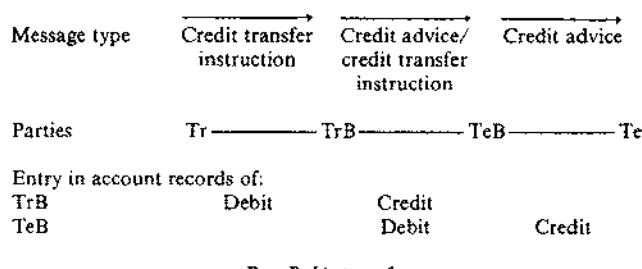
22. Whether the transmission facilities and the switch are public or are owned by or operated for the banks, and without regard at this point to the party who bears the loss in case of late or non-delivered instructions or of fraud or error in the content of an instruction, the communications service does not affect or take part in the banking relationship. The banking relationship exists only between the sending and the receiving bank.

23. To the extent that an electronic clearing-house, like a communications service, switches funds transfer instructions to the correct addressee and, in some cases, carries the instruction from transferor bank to transferee bank, it is as transparent to the transmission of the instruction as is a communications service. In addition, even when a clearing-house establishes net balances for the participating banks, it does not affect the relationship between sending and receiving banks.

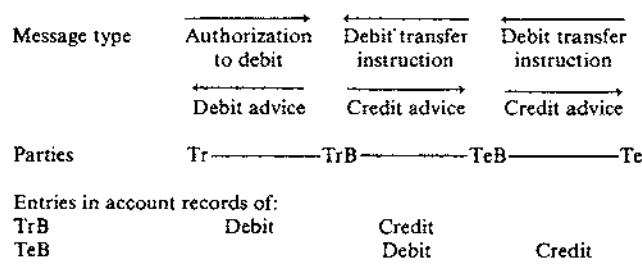
24. Figure II-A, therefore, represents a credit transfer where the transferor bank has sent the funds transfer instruction to the transferee bank either by physical transmission or by a communications system, but not through a clearing-house, and where the two banks can settle by debits and credits in the accounts they hold with each other. The message from the transferor bank to the transferee bank serves both as an instruction to the transferee bank to credit the account of the transferee and as an advice that the account that the transferor bank services for the transferee bank has been credited. This message also serves as the authorization for the transferee bank to debit the account of the transferor bank.

*Figure II. Two banks in direct relation each holding account of the other*

A. Credit transfer



B. Debit transfer



25. Figure II-B represents a debit transfer made under the same conditions as the credit transfer in figure II-A. The arrows indicate that the debit transfer instruction is given by the transferee to the transferee bank and by the transferee bank to the transferor bank. The authorization to debit given by the transferor to the transferor bank may be incorporated in a cheque drawn by the transferor in a standing authorization to debit or it may be requested by the bank after presentation of the debit transfer instruction.

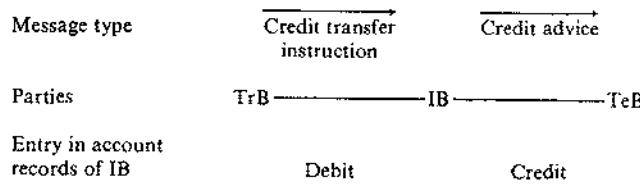
3. Three-bank transfer

26. If the two banks are not in a direct relationship, and are not both participants in the same clearing-house, the funds transfer instruction may have to pass through one or more intermediary banks which are the correspondent bank of both. The effect of using a correspondent bank on the relations of the parties to a funds transfer is not always well understood.

27. When a credit transfer is not a customer transfer, i.e. when a message type 200 or 202 as described in paragraph 11, above, is appropriate, the banks are in exactly the same banking and legal situation as are two non-bank customers of the same bank. In both cases the funds transfer is carried out by debiting the account of the transferor (bank) and crediting the account of the transferee (bank). In the context of funds transfers, banks offering a correspondent bank service include not only commercial banks, but also any central bank which holds accounts of other banks and which accepts instructions to transfer balances from the account of one bank to that of another for general banking purposes.

**Figure III. Correspondent bank holding accounts of two other banks**

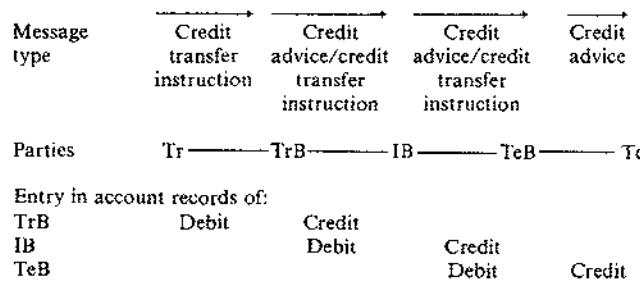
Credit transfer—message type 202



28. When a credit funds transfer is made at the request of a customer of the transferor bank for the benefit of a customer of the transferee bank, the funds transfer involves five parties. There are three separate credit transfer instructions and two separate inter-bank funds transfer transactions, in addition to the funds transfer from the transferor to the transferee. Although for some purposes the entire funds transfer may be treated as a single banking and legal activity, for other banking and legal purposes it may be necessary to treat separately each pair of relations, and especially each inter-bank funds transfer transaction. The messages between transferor bank and intermediary bank and between intermediary bank and transferee bank serve the functions described in paragraph 24.

**Figure IV. Correspondent bank holding *loro* accounts of two other banks**

Credit transfer on instructions of transferor for benefit of transferee



#### D. Settlement

##### 1. In general

29. A transferee bank which credits the account of the transferee increases the obligation it owes to the transferee or decreases the obligation owed by the transferee to the bank. It must either reduce a corresponding obligation or receive value equal to the amount of the credit. When the transferor and the transferee both hold their accounts with the same bank, the bank receives value for the credit to the transferee's account by debiting the transferor's account. When the transfer is between banks, the transferee bank must receive value from the transferor bank in settlement.

30. Settlement may be made between the banks either item by item or by batches of items. The choice depends

in part on the nature of the funds transfer, the size of the individual transfer and the funds transfer mechanism used. A documentary draft would normally be treated as a special item throughout the entire period of its collection and settlement for that specific funds transfer instruction could be expected. In many countries it is typical to settle for batches of cheques, but cheques for a large sum may be transmitted to the transferor (drawee) bank, or to one of its correspondents, outside the normal collection process and settled individually. In general, electronic funds transfers made by exchange of computer memory devices are settled on the basis of all the instructions contained on the memory device, but large-value electronic funds transfer instructions sent by telecommunications are often settled individually. However, large-value transfers which pass through certain electronic clearing-houses such as the Clearing House Interbank Payment System (CHIPS) in New York or the Clearing House Automated Payment System (CHAPS) in London are settled on a net (or net-net) basis for the day's activities, as described further in paragraph 37.

31. For all practical purposes settlement will usually be effected by appropriate bookkeeping entries in accounts of one or the other of the two banks or in appropriate accounts of a third bank. This basic concept of inter-bank settlement is simple, but there are many possible variations of this basic concept. The sending bank or the receiving bank may keep a deposit account with the other bank or both may do so. In such a case, settlement for any instruction or group of instructions may be made by an appropriate debit or credit to the account. A frequently encountered variation is that neither bank keeps a deposit account with the other, but both banks keep an account in the name of the other bank. As individual instructions or batches of instructions are passed between the banks, each bank enters appropriate debits and credits. Settlement for the individual instructions or batches of instructions in question is completed by the entry of the debits and credits. The banks keep the net debit or credit balances within agreed limits by periodically transferring the necessary funds. In yet another variation the banks might agree that the net balance at the end of the day's activities should always be zero. In that case settlement would not be complete until the bank with a debit balance transferred sufficient funds to cover the debit balance. International funds transfers involving the use of two currencies are settled by debiting and crediting *lоро* and *nostro* accounts which the banks keep with one another. In the case of Eurocheques, each day every national Eurocheque centre debits the *nostro* account of each of the other national Eurocheque centres for the total amount of Eurocheques drawn on banks in that country plus the standard commission, with an interest date of two days later.

##### 2. Settlement through a third bank

32. In many cases settlement for individual instructions or batches of instructions is made by a transfer of the necessary amount in the accounts of a third bank. The

third bank may be a correspondent bank of both the sending bank and receiving bank or it may be the central bank of that country. When settlement is to take place by entries on the books of a third bank, the transferor bank must notify the third bank to debit its account and to credit the account of the transferee bank. This is accomplished either by a message by telecommunications from the transferor bank to the third bank (e.g. a message type 202 as noted in paragraph 11, above) or by a paper-based transfer instruction. In case of settlement by use of a debit transfer instruction the transferee bank must present the instruction for honour to the third bank for settlement to be completed.

### 3. Settlement through a clearing-house

33. A clearing-house serves not only as a message switch, as indicated in paragraph 21, above, but also as a means to aid in settlement between the banks. Periodically the total amount of transfers submitted to and received from each of the participating banks is totalled and settlement is made by those banks with a net debit position in favour of those banks with a net credit position. The clearing-house, therefore, aids the settlement function by permitting settlement to be made on the net position of each bank rather than on the basis of its gross value of transactions.

34. There are several possible variations on settlement in a clearing-house having to do with the frequency the transactions are netted, the period of time after netting within which settlement of the net balance is made, whether netting and settlement is by pairs of banks or for the clearing as a whole, and the means of settlement for the net balances.

35. First, there are two possible approaches to the time at which a clearing-house can net the funds transfer instructions which have been submitted. A clearing-house for funds transfer instructions submitted in batches, whether paper-based or on computer memory devices, may net the value of the instructions submitted before any bank is permitted to withdraw the instructions addressed to it. If there are several clearings per day, there would be as many nettings. Alternatively, the value of the funds transfer instructions may be netted once a day or after any other longer or shorter period of time. Periodic netting can be used in any form of clearing-house. A paper-based or electronic off-line clearing house with multiple clearings per day may establish net balances at each clearing but also establish net balances for the entire day preparatory to settlement for the day. Periodic netting is, however, the only practicable form for an electronic on-line clearing-house such as CHIPS or CHAPS. The significance of periodic netting is that some or all the instructions are released to the receiving bank for further processing prior to the netting and settlement for those items. In theory, it is irrelevant when netting takes place. However, the longer the delay, the more danger there is that a bank in a net debit position will fail to settle and that the transferee banks will already have made the amount of the transfers available to their customers.

One way to reduce this risk is to net and settle as frequently as possible, to the point where each individual transaction could be settled individually. While this would eliminate the credit risk, it would also change the electronic clearing-house into a communications service.

36. Closely associated with the time when netting occurs is the time when settlement takes place. Some clearing-houses in which netting before the withdrawal of instructions from the clearing-house is insisted upon involve banking systems in which the failure of a bank to settle is a significant risk. In those clearing-houses prompt settlement would also be expected. Conversely, where the concern over a bank failing to settle is not as great, both periodic netting and a more relaxed attitude to the time of settlement could be expected. However, since the time of settlement has an effect on the amount of money available to the individual banks for investment and, in some countries, on their reserve position, a long delay in settlement would still be of significance.

37. Normally, it does not make much difference whether netting is by pairs of banks or for the clearing-house as a whole. In some clearing-houses the net position of each pair of banks is first established and then the net-net position of each bank as against all other banks in the clearing-house is calculated. If netting is by pairs of banks, settlement can also be by pairs of banks. One effect of settlement by pairs of banks could be that each bank would need to have immediately available enough cash or credit to cover all its net debit positions. A more substantial consequence of netting by pairs of banks is that if a bank fails to settle, the loss will be suffered by the individual banks with which the failing bank has a net debit position. On the other hand, if the position of each bank is determined by its net-net balance, the loss arising out of the failure of a bank to settle must be spread among the banks participating in the clearing-house by some formula which should have been previously established or absorbed by some other group or body, such as the central bank.

38. A bank's debit position must be covered in cash or its functional equivalent. Most clearing-houses probably settle on the basis of appropriate entries in the accounts of the participating banks on the books of the central bank. Position may also be covered by appropriate entries on the books of one or more large banks.

39. In a number of countries the inter-bank settlement is of interest to the non-bank transferor and transferee as well as to the banks themselves. Where the transferee bank runs a significant risk that the transferor bank will fail to settle, or in the case of a clearing-house that any one of the participating banks may fail to settle, the transferee bank may delay crediting the transferee's account or otherwise making the funds available until it is satisfied it is not at risk. Furthermore, if settlement is delayed for any appreciable period of time, the loss of interest which ensues may be sufficient to cause the transferee bank to delay crediting the transferee's account for an equivalent period of time.

### E. Some particular features of electronic funds transfers

#### 1. Replacement of one or more paper-based steps

40. The most elementary, but perhaps most widespread, use of electronic funds transfer techniques is to replace one or more steps in a funds transfer process that remains basically paper-based. A paper-based funds transfer system is characterized by the fact that the funds transfer instruction is prepared and submitted to the banking system in a paper-based form and often passes from bank to bank through the system in that form. There may be no reason, however, why a bank which receives an instruction in a paper-based form cannot transmit the information contained in it to the receiving bank in electronic form. This is most easily accomplished in domestic credit transfer systems. The transferor normally neither knows nor cares how the credit transfer instruction is passed between the banks so long as the transfer is accomplished promptly and accurately. Banks may therefore be able to convert paper-based instructions to magnetic tape or other computer memory devices and to exchange them directly between themselves or through automated clearing-houses or to send credit transfer instructions by telecommunications if that proves more efficient.

41. Essentially the same technical process can occur in respect of paper-based debit transfer instructions, such as cheques and bills of exchange. The instructions can be retained at the transferee (depositary) bank and the essential data can be transmitted to the transferor (drawee) bank by exchange of computer memory device or by telecommunications, i.e. the paper-based cheque can be truncated at the transferee bank allowing for its electronic presentment to the transferor bank. However, the law relevant to negotiable instruments would continue to apply to debit transfer instructions issued in the form of cheques, bills of exchange or promissory notes with some potential consequences if the law is not modified to accommodate electronic processing.<sup>8</sup>

#### 2. Telecommunications

42. Even though large-value telegraphic and telex transfers by banks became routine long ago, until recently the largest proportion of large-value transfers continued to be made by paper-based funds transfer instructions sent by mail. No need was seen in most countries to codify the banking law and practice of telegraphic or telex funds transfers since they remained an exceptional form of funds transfer. The consumer oriented electronic funds transfer service offered by many postal services has been largely ignored in discussions of electronic funds transfers. However, detailed regulations have long been in existence governing domestic and international telegraphic money orders (when the transferee has no account with the postal giro system or bank) and international giro transfers (when the transferee has such an account). Among the interesting features of the

regulations are a prescribed format for the telegraphic funds transfer instruction and a requirement that the text be in French, unless otherwise agreed between the two postal services.

43. These two electronic funds transfer systems have historically serviced different markets and have had as little to do with one another as have their paper-based counterparts. However, they have shared one characteristic. Although the postal giro had a procedure for sending lists of accounts to be credited, both systems could fairly be characterized as available for the sending of individual funds transfer instructions. They were not designed for the batch movement of funds transfer instructions.

44. The decreasing cost of telecommunications and the increasing cost of ground and air transportation has made it less expensive for banks to transmit large numbers of funds transfer instructions of large and small value in a batch-mode by telecommunications, particularly when lower tariffs are offered during the night and other periods of under-utilization of the telecommunications system. S.W.I.F.T. in particular has signed agreements for the batch transfer of details of certain credit card transactions. Furthermore, in many cases it currently costs the customer no more to send an individual funds transfer instruction by telecommunications than to use a paper-based instruction. It used to be possible to classify a "wire transfer of funds" as a transfer containing elements of urgency to it, whether the transfer was for large-value through the banking system or for low-value through the postal system, and rules of law developed in some cases reflecting the urgency of acting promptly in response to the message. However, as the use of telecommunications for the transmission of funds transfer instructions has become more routine, it has lost its special character. The use of telecommunications can now be described only as another means by which the funds transfer instruction passes from sending bank to receiving bank.

#### 3. Batch transmission

45. Most paper-based as well as electronic inter-bank funds transfer instructions are of neither a value nor an urgency to justify the cost of transmitting them individually between banks. Therefore, the instructions are accumulated and exchanged in batches. Batch transmission of electronic funds transfer instructions is usually accomplished by the physical exchange of computer memory devices. The computer memory devices containing the funds transfer instructions are usually prepared by the banks themselves. The major types of transactions recorded are paper-based funds transfer instructions submitted to the bank, transactions by customers of other banks recorded in off-line automated cash dispensers or automated teller machines, standing authorizations to debit and standing instructions to credit.

46. Customers of the banks which have the necessary facilities and which send a large number of debit or

<sup>8</sup>See the fuller discussion in chapter "Agreements to transfer funds and funds transfer instructions", A/CN.9/250/Add.3 (reproduced in this Yearbook, part two, I, B).

credit transfer instructions may prepare the computer memory devices themselves. In most systems bank customers submit the memory devices to their bank. In some systems customers are allowed to submit memory devices directly to the automated clearing-house. In either case the bank is responsible to the clearing-house for the value of the funds transfer instructions contained on the memory devices submitted by its customers and for their technical quality.

47. As with batch transmission of paper-based funds transfer instructions, computer memory devices can be exchanged directly between the participating banks. If there are too many banks for this to be feasible, the instructions can be exchanged through an automated clearing-house. An automated clearing-house furnishes almost identical services to those furnished by a clearing-house for paper-based instructions. If the banks submit funds transfer instructions already sorted by receiving banks and each batch is on a separate memory device, the banks can simply exchange the memory devices. More often the banks submit memory devices on which the individual instructions are not sorted by receiving banks or, although sorted, instructions addressed to more than one bank are on the same device. In either case the automated clearing-house would sort the instructions using its own computers and prepare new memory devices containing the instructions addressed to each receiving bank.

48. Although batch transmission is usually accomplished by the physical exchange of computer memory devices, it has already been noted in paragraph 44 above, that as the cost of teletransmitting data has been reduced, batch data is being increasingly sent by telecommunications.

#### *4. Customer-activated electronic funds transfers*

49. The electronic aspect of most electronic funds transfers is activated by an employee of a bank who receives an instruction from a responsible official of the bank in the case of a transfer initiated by the bank, from the customer or from another bank. However, an increasing number of electronic funds transfers are initiated on a customer-activated terminal. Customer-activated terminals include cash dispensers, automated teller machines, point-of-sale terminals, home banking and on-line computer terminals located in the business establishment of commercial customers. The category of customer-activated electronic funds transfers might also be considered to include the preparation by the customer of computer memory devices containing debit or credit transfer instructions.

50. A large number of funds transfers which are initiated on customer-activated terminals pass through the entire funds transfer process with no human intervention on the part of the banks concerned. The computers of the banks verify that the technical norms required to make the transfer have been met, that the proper authentication for the transfer has been given and that the account of the transferor has a sufficient balance to support the debit to the account. In some

cases, especially those involving large sums, an official of the sending bank may need to authorize the funds transfer before the instruction is acted upon, even though it has been initiated from a customer-activated terminal.

51. Electronic funds transfers which can be initiated by use of a plastic card with a magnetic stripe on the back containing information for identification of the card holder and his account, including either the PIN or the information by which the bank's computer can derive the PIN by use of the proper algorithm, constitute a special sub-set of customer-activated electronic funds transfers. The concerns over the use of magnetic stripe cards as access devices arise in large part because of the technical problems in achieving an adequate level of security against fraud. These concerns have been highlighted by the fact that the vast majority of magnetic stripe cards are used for the initiation of consumer funds transfers, giving rise to concerns for consumer protection.

52. With the advent of microcircuit technology on a silicon chip, it has been possible to create a plastic card containing a microprocessing device. This offers additional possibilities for storing and processing information relevant to the card holder, introducing among other features a higher level of security. Microcircuit cards are being considered for use in banking applications, especially in the field of customer-activated electronic funds transfers. The expectation is that they will find their widest application in point-of-sale systems, where the concerns with security are the most serious.

[A/CN.9/250/Add.3]

### V. Chapter on agreements to transfer funds and funds transfer instructions

#### A. General agreement between bank and customer to transfer funds

1. Funds transfers are executed by banks under the terms of agreements between the banks and their customers. The contracts governing cash in-payment or out-payment transfers are rudimentary while those governing transfers to and from accounts are more complex.

##### 1. Contract for cash payment

2. A cash in-payment transfer occurs when a person pays to the transferor bank in cash the sum to be transferred plus service charge and the bank undertakes to transfer that sum to the transferee in cash or to the credit of his account. The contractual obligation of the transferor bank is limited to the specific transaction in question.

3. A paper-based debit transfer cash in-payment service is offered by banks and some other financial organizations which provide the transferor either with a

demand payment instruction, which might be a cheque, drawn by the bank on itself or on another bank or with some other form of debit transfer instruction which the transferor can mail or otherwise transmit to the transferee. The obligations of the transferor bank are based upon the law of cheques or, when the debit transfer instruction is not in the form of a cheque, on the law governing the paper-based instruction in question.

4. A cash out-payment transfer occurs when the bank, postal service or private telecommunications company undertakes to pay the transferee in cash. This service is often associated with a consumer-oriented cash in-payment service. The obligation of the transferee bank, including the receiving office of the postal service or telecommunication company, may be either to seek out the transferee at an address given by the transferor, or to hold the funds awaiting the transferee to present himself. Although the transferee bank holds the funds for the benefit of the transferee, there is no contractual relationship between the two and it is not clear in many legal systems what right, if any, the transferee has in the funds until the time they are handed over to him.

## 2. *Agreement for transfer to or from an account*

5. At the time an account is opened, the bank and its customer will enter into a contract governing the services the bank will perform. The contract will often be in writing, although in some countries it is normal for there to be no written contract between the bank and its customers. As regards funds transfers, the contract will distinguish between those services the bank will provide as a transferor bank and the services it will provide as a transferee bank. In those countries in which there is typically no written contract, the implied terms of the contract are found in banking practice. In many countries the basic terms of the contract are found in the general conditions of the bank, which may be uniform throughout the country. The contract governing an important commercial account may be individually negotiated and, while its terms could not call for changes in funds transfer procedures that would be disruptive to the operations of the bank, it may contain significant special provisions, particularly in regard to the types of transfers that can be made, the authorization and authentication necessary, and the time at which the customer's account will be debited or credited.

6. The arrangement between the bank and its customer may provide that on his credit transfer instruction or on his authorization to honour the debit transfer instruction of a transferee, the bank will transfer funds to the accounts of the indicated transferees. The arrangement will also provide that the bank is authorized to take steps to reimburse itself for the sums transferred. The first, and usually the only necessary, step to reimburse itself is to debit the account of the transferor.

7. The contract will normally specify the types of funds transfers which the bank is authorized to make

against that account as well as the authentication required before the bank is authorized to act upon a funds transfer instruction. The contract may specifically or by implication permit all forms of funds transfers generally available through that bank. Certain forms of funds transfers may be permitted only by special agreement. In particular, a bank should be sure it has proper authority, including a resolution of the corporate board of directors, before it installs at the place of business of a customer a terminal by which funds transfer instructions can be sent directly to the bank.

8. Until recently in many countries any customer could deliver any form of debit transfer instruction to the bank and the bank would transmit it through the clearing or collection arrangements available to it for presentation to the transferor bank. There would probably have been standard provisions as to the time when the customer's account would be credited with the proceeds and the amount of discount, if any, from the face amount of the debit transfer instructions received, although special arrangements with particular customers would also have been common.

9. That situation no longer exists except for cheques. Only those bank customers who have signed special contracts with the bank are permitted to submit such debit transfer instructions as bank credit card vouchers, and the amount of discount charged by the bank can vary considerably between different transferees. In some countries only certain categories of transferees may be permitted by law to submit debit transfer instructions under a standing authorization to debit and, even where there are no such legal restrictions, banks will allow only customers of established integrity and financial standing to do so.

10. An account to which entries are made reflecting funds transfers may be of a type that normally carries a credit balance or of a type that normally carries a debit balance. It is not important for the funds transfer process whether or not the transferor receives interest when the account is in credit or is charged interest when it is in debit. Nor is it important for the funds transfer process whether the account is of a type which is normally used to make or receive funds transfers. However, many countries restrict the types of accounts which can be debited for the amount of funds transfer instructions. Moreover, in some countries there are legal restrictions on the extent to which an account of a type expected to carry a credit balance may be allowed to carry a debit balance. In any case, all banks will eventually place a limit on the extent to which they will allow a customer to be in debit to them. When that limit is reached, the bank will no longer honour funds transfer instructions issued by the customer until the customer has taken remedial action.

11. In countries where the normal method of funds transfer has been by credit transfer, the opening of an account automatically gives the bank the right to receive credit transfers to that account. There are few restrictions on the type of account which can be credited with a funds transfer. However, in some

countries where the normal method of funds transfer has been by debit transfer, particularly by the collection of cheques, it has been suggested that no person other than the owner of an account should be allowed to deposit funds to the account. If a bank has doubts as to its authority to receive a credit transfer to an account, specific authorization from its customer might be necessary before it credits to the customer's account sums received by credit transfer.

#### **B. Authority to transfer funds and to debit transferor's account**

##### **1. Debit and credit transfer instruction issued by transferor and presented to transferor bank**

12. A funds transfer instruction issued by the transferor and transmitted or presented to the transferor bank serves as an authorization to the transferor bank both to transfer the funds to the account of the transferee at the same or a different bank and to debit the transferor's account. In all paper-based and electronic credit transfers, the credit transfer instruction is delivered by the transferor to the transferor bank. In some paper-based debit transfers, especially those involving the traditional collection of a cheque, the debit transfer instruction issued by the transferor is presented for honour to the transferor bank. In both cases, so long as no question is raised as to the authenticity of the debit or credit transfer instruction, the transferor bank has clear authority to act based upon the funds transfer instruction in its possession.

##### **2. Debit transfer instruction truncated at transferee bank**

13. Rather than physically moving the paper-based debit transfer instructions such as cheques from the transferee (depositary) bank to the transferor bank in order to present them for honour, in many cases it would be less expensive for the transferee bank to keep the debit transfer instructions and to forward to the transferor bank by electronic means the necessary funds transfer data for presentment, i.e. to truncate the instructions. Furthermore, it would usually be possible to present the cheque electronically to the transferor bank in less time than to present the cheque itself. This would allow the transferee bank and the transferee to receive value sooner and would shorten the period of uncertainty whether a cheque would be dishonoured. Truncation of the instruction and its electronic processing is used with a number of newer forms of debit transfer instructions signed by the transferor, such as credit card receipts and some cheque-like or bill of exchange-like instruments not subject to the law of bills of exchange or of cheques. It is also followed in respect of cheques in a few countries such as Belgium, Denmark and Sweden, but in the majority of countries the law relative to cheques is thought to preclude the truncation of cheques and their electronic processing.

14. The right of the transferor bank (drawee bank) to require physical possession of the cheque before

honouring it is designed to provide it with an opportunity to examine the signature or other authentication on the cheque, to examine the cheque for its accord with the formal requirements of law, to assure itself that the cheque has not been altered and to assure itself that the cheque cannot be presented a second time. In a few countries, but not in most, the transferor bank is also expected to verify that the cheque has not been presented prior to the date on the cheque, and conversely, that the cheque is not so old as to have lost its validity. These verifications are intended to ensure that the transferor bank is properly authorized by the transferor before it transfers the funds and debits the transferor's account. Since the policies in favour of the physical presentation of the cheque are in large measure for the protection of the transferor (drawer), they cannot be waived on his behalf by the transferor bank. They can, it would seem, be waived by the transferor himself, and some experiments with truncation of cheques have been based on customer agreement.

15. In addition, in some countries a dishonoured cheque must be protested by notation on the cheque itself in order for the depositor to charge a prior endorser, a rule which requires the physical availability of the dishonoured cheque. Although banks no longer return cancelled cheques to the transferor in several of the countries in which this practice previously prevailed, in at least one country (the United States of America) the law governing the collection of cheques provides that the time-limits within which a transferor can raise certain defences against the debits to his account commence on his receipt of the statement of account activity and of the cancelled cheques which authorized the debits. Banks in that country are reluctant to engage in cheque truncation which might extend inordinately the period during which the debit to the account may be questioned. Furthermore, as a result of extensive advertising by banks that cancelled cheques returned to the transferors were particularly good evidence of payment of the underlying obligation, many bank customers no longer keep other receipts and some companies no longer furnish receipts when payment is by cheque.

16. The experience with credit card receipts and the cheque-like debit transfer instructions not subject to the presentment requirement as well as the experience with cheque truncation and electronic processing in Belgium, Denmark and Sweden has shown that it is an acceptable banking procedure for the transferor bank to debit the transferor's account on the basis of a statement by the transferee bank that it has in its possession an authorization from the transferor. If the transferor claims that he did not give any such authorization, the transferee bank must of course be prepared to produce the original cheque, credit card receipt or other debit transfer instruction. If the transferee bank cannot produce the original, or a legally acceptable copy, or if it is shown that the transferor bank would not have been authorized to debit the transferor's account if the original had been presented to the transferor bank, the transferor bank must be required to re-credit the transferor's account in such a way as to eliminate any

consequences in respect of interest, fees or the like arising out of the mishandling. The applicable rules must in turn provide for the transferor bank to be reimbursed by the transferee bank for the amount in question and for the transferee bank to be reimbursed by the transferee. If the law regarding cheques was modified in this manner, the truncation of cheques and their electronic processing would be greatly facilitated.

17. As a partial step towards cheque truncation, in several countries the essential data on the cheques is captured and forwarded by telecommunications to the transferor bank for debit to the transferor's account. Although the debits are provisional until the cheques are received by the transferor bank for verification, the transferor's available balance is immediately reduced and the banks in the collection chain are assured that, if there are insufficient funds, notice will be received promptly. On the other hand, provisional debit may not terminate any right the transferor may have to revoke the bank's authority to debit his account. This procedure is used in some countries for all cheques while in others for only those over a certain value.

18. Cheques, cheque-like instruments and bank credit card vouchers are the principal forms of debit transfer instruction which authorize the transferor bank to make the funds transfer to the transferee and to debit the transferor's account. In the forms of debit transfer described in the following paragraphs the authorization is separate from the instruction.

### *3. Paper-based debit transfer instructions not issued by the transferor*

19. An example of the separation of the debit transfer instruction from the authorization is the bill of exchange drawn by a seller (transferee) on the buyer (transferor) payable at the buyer's bank (transferor bank). Before the transferor bank honours the bill of exchange, it must receive an authorization from the transferor to do so. The authorization may be in the form of an acceptance of the bill; it may have been given by the transferor in anticipation of the presentment of the bill; it may have been given in a general authorization to pay bills of exchange drawn by a particular transferee or it may have been requested by the transferor bank after presentment to it of the bill. In all of these cases, the transferor bank's authority to honour it arises out of the transferor's separate authorization to the transferor bank.

20. A specific authorization to honour the bill may not be necessary where the context in which it was issued gives sufficient assurance that the debit to the account would be authorized. Under the General Conditions of Delivery for trade between the member States of the Council for Mutual Economic Assistance, payment is made by the buyer's bank (transferor bank) without prior authorization from the buyer (transferor) upon receipt of the seller's claim for payment, accompanied by the necessary documents. The buyer has the right for fourteen days from the receipt by his

bank of the seller's invoice to demand return of all or part of the amount paid if the payment was not in conformity with the contract. Authorization to honour the bill is assumed in the absence of a claim by the transferor to the contrary.

### *4. Electronic debit transfer instructions not issued by the transferor*

21. The development of electronic funds transfer capability has given new life to transfers made pursuant to a standing authorization to debit. Such transfers are particularly useful for the collection of large numbers of periodic payments, which may be of a constant amount, such as for rent, in which case a standing instruction to credit would serve the same purpose, or they may be of a fluctuating amount, such as for telephone service. The debit transfer instructions can be prepared on a computer memory device by the transferee or by the transferee bank and presented by the transferee bank to the various transferor banks either directly or through an automated clearing-house. Some automated clearing-houses permit transferees to submit the computer memory devices directly to them.

22. Since electronic debit transfer instructions by their very nature cannot be issued by the transferor, the authorization given by the transferor to debit his account is separate from the debit transfer instruction prepared by the transferee or the transferee bank. A standing authorization to debit, which would usually be in written form signed by the transferor, may be given to the transferor bank. In this case the bank would notify the transferee that it had received authorization from the transferor to honour claims made against it for the indicated purposes. If the authorization is given by the transferor to the transferee, the transferee could keep it or give it to the transferee bank. In either of the latter cases the transferor bank, not having the authorization, would honour the claim on the strength of a representation by the transferee, or by the transferee bank, that a proper authorization existed.

23. The public attitude towards standing authorizations to debit varies widely from country to country. Its efficiency as a means of collecting relatively small amounts from large numbers of transferors has led to its wide-spread use in some countries. In other countries there is a concern that transferees may become arrogant towards their customers if they can too easily reach into their customer's bank accounts to secure payment. These concerns have led to restrictions in some countries on the extent of the authorization to debit which a transferor can give. Furthermore, when the amount to be debited varies from one period to the next, it is felt that the transferor should be warned of the amount of the forthcoming debit. One technique has been to require that the transferor be given a notice that a debit of a specified amount would be made to his account on a given date in the future. It might also give him the opportunity to withdraw the authorization to debit his account, though that would not eliminate his obligation to pay the sum due.

*5. Authority of one bank to debit account of another bank*

24. It is common practice for banks to debit the account of another bank on their books for the amount of the debit transfer instructions which have been sent to the receiving bank for honour. One example is that under the Eurocheque Package Deal Agreement the clearing centres in each of the participating countries send once a day to the clearing centres of each of the other participating countries the Eurocheques drawn on banks in the receiving country which were cashed in the sending country. The sending clearing centre is authorized under the Package Deal Agreement to debit the account of the receiving clearing centre for the total amount of the cheques plus the standard commission charged on all Eurocheques cashed abroad. The debit is made with an interest date of two working days after the date of dispatch.

25. This practice of authorizing the sending bank to debit the account of the receiving bank greatly facilitates the clearing of routine debit transfer instructions directly between banks, or as in the case of Eurocheques, between national clearing centres. The sending bank automatically has value on its books for the amount of the instructions sent for honour as of the interest date agreed upon by the banks. If any of the instructions are not honoured upon presentment, the debit can be reversed to the extent of the dishonoured instructions.

*C. Funds transfer instruction*

*1. Authentication*

26. The authentication of a document or message gives it a legal form which renders it worthy of belief. A formal authentication consists of the execution of the document before a notary or other public official authorized to execute such functions, and especially in the civil law countries, it gives the document a special weight in any subsequent legal proceedings. Informal authentication consists of marking the document or message in such a way as to indicate its source. Funds transfer instructions are informally authenticated.

27. The term authentication as used here should be distinguished from the use of the same term in computer-to-computer telecommunications, and especially as it is defined in ISO DIS 7982. In that context, because of the availability of certain techniques using computers, the authentication of the message can validate the full text of the message as well as its source. This is, of course, a desirable attribute of those techniques. However, since those techniques are available only by use of computers, they are available neither for those electronic funds transfers which do not rely on the use of computers nor for paper-based funds transfers.

28. The relative rarity of electronic funds transfers prior to the use of computers may have led to a lack of statutory or regulatory provisions which require electronic funds transfer instructions to be authenticated

before the banks concerned are permitted to act upon them. However, it is probable that all agreements between banks and their customers require that funds transfer instructions issued by the customer must be authenticated before the bank is authorized to execute them. The agreement would also include the form of the authentication.

29. Many closed-user networks for electronic funds transfers establish required means of authenticating a funds transfer instruction passing through them. Consumer oriented networks, such as networks of automated teller machines, automated cash dispensers and point-of-sale terminals, specify the authentication required of the customer. Inter-bank funds transfer networks specify the authentication required from the sending banks.

*(a) Form of authentication*

30. An authentication of a paper-based funds transfer instruction is usually accomplished by the signature of an authorized person. Signature is usually understood to mean the manual writing of a specific individual's name or initials. The signature so written is considered to be personal to the individual. Its existence on the funds transfer instruction gives a strong indication of that person's intent to issue the instruction. Moreover, the possibility of comparing it with a specimen of a signature known to be genuine provides a means of verifying that the signature on the instruction is also genuine.

31. The demands of modern commerce have led many legal systems to permit the signature to be made by stamp, symbol, facsimile, perforation or by other mechanical or electrical means.<sup>9</sup> This is in line with developments in other fields of trade law. For example, all of the principal multilateral conventions governing the international carriage of goods which require a signature on the transport document permit that signature to be made in some way other than by hand.<sup>10</sup>

32. Authentication of a funds transfer instruction made electronically must be made by a means which is appropriate to the means of communication used. Telex and computer-to-computer telecommunications often employ call-back procedures and test keys to verify the source of the message. Certain encryption techniques authenticate the source of a message, as well as its content. Withdrawals from an automated cash dispenser, transfers from an account through an automated teller machine or a point-of-sale electronic funds transfer by use of a plastic card are authenticated, under the most widely used current technology, by the entry into the terminal of a personal identification

<sup>9</sup>See the definition of "signature" in the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/211), article 4 (10) and the draft Convention on International Cheques (A/CN.9/212), article 6 (8), both of which have been elaborated by UNCITRAL (reproduced in *Yearbook 1982*, part two, II, A, subdivisions 3 and 5 respectively).

<sup>10</sup>"Co-ordination of work: international transport documents: report of the Secretary-General" (A/CN.9/225) para. 47 (*Yearbook 1982*, part two, VI, C).

number (PIN) which agrees with the PIN assigned to that card holder. Dynamic signature analysis by computer is in experimental use as a replacement for the PIN. A funds transfer instruction given over the telephone may be authenticated by use of codes and the transferor bank may call back to the transferor to verify the source of the request.

33. Although an authentication in any form serves the basic functions of identifying the source of the instruction and indicating that the instruction was intended to be issued, there is a fundamental difference between a handwritten signature and authentication by electronic means. Even though a handwritten signature can be forged so well that the forgery is difficult to detect, nevertheless the signature can properly be made only by a specific individual. A signature shares this quality with only a few other forms of authentication, such as a fingerprint. Therefore, if a signature has been forged it is by its very nature an invalid authentication, even though other considerations may lead a legal system to hold that in certain cases the person whose signature was forged should bear the consequences rather than a person who relied on the forged signature in good faith and without negligence.

34. Mechanical forms of signature on paper documents and various techniques for authentication of an electronic funds transfer instruction can be authenticated in a proper form by an unauthorized person or by a person exceeding his authority. If such a person had access to the legitimate stamp, perforating device, test key, encryption key or plastic card and PIN, the instructions which he caused to be issued would be identical to those issued under proper authorization.

35. This difference between the various means of authenticating a funds transfer instruction has certain legal consequences when the bank honours a funds transfer instruction which has an unauthorized authentication. These legal consequences are discussed in connection with the allocation of loss arising out of fraud.<sup>11</sup> However, this difference should not be understood to mean that a handwritten signature requiring visual comparison is a more secure form of authentication than is an electronic authentication. On the contrary, a person's signature can easily be forged well enough to be accepted by a bank, even if an expert could later determine with a high degree of certainty that the signature was forged. Moreover, visual comparison of signatures is so time-consuming and costly that in many countries it is not done for funds transfer instructions of a small amount, even though the applicable legal rules may assume or require the visual comparison of all signatures. On the other hand an electronic form of authentication can be verified at an acceptable cost for even the smallest of transactions. Moreover, a well designed authentication system and rigorous adherence to the procedures necessary to keep the system secure can reduce to a minimum the likelihood that funds transfer instructions containing unauthorized authentications will be honoured.

<sup>11</sup>See discussion in chapter "Fraud, errors, improper handling of transfer instruction and related liability", A/CN.9/250/Add.4.

#### (b) *What must be authenticated*

36. As indicated in paragraph 12 above, in all paper-based and electronic credit transfers and some paper-based debit transfers, especially those involving the traditional collection of a cheque, the funds transfer instruction issued by the transferor is transmitted or presented to the transferor bank. Since this funds transfer instruction serves as the authorization to make the funds transfer and to debit the transferor's account, it is the only message which must be authenticated for this purpose. Where the paper-based debit transfer instruction is truncated, the transferor bank debits the transferor's account on the basis of a funds transfer instruction issued by the presenting bank. Therefore, in this case both this latter instruction and the original debit transfer instruction must be authenticated.

37. Where a debit transfer instruction was not issued by the transferor as in cases of a bill of exchange drawn by a transferee (seller) on a transferor (buyer) payable at the transferor bank, a bill of exchange drawn by the transferee on the transferor bank pursuant for example to a letter of credit, or a debit transfer instruction submitted pursuant to a standing authorization to debit, the debit transfer instruction does not constitute an authorization by the transferor either to transfer the funds to the transferee or to debit his account. Therefore, both the debit transfer instruction issued by the transferee or the transferee bank and the authorization given by the transferor to the transferor bank, transferee bank or transferee must be authenticated.

38. When a paper-based or electronic funds transfer is between two banks and does not involve a customer either as transferor or as transferee, it is obvious that the funds transfer instruction passing between the two banks must be authenticated. If an electronic funds transfer must pass through intermediary banks, a new funds transfer instruction must be created for each funds transfer transaction and each instruction must be separately authenticated. Similarly, if an electronic funds transfer is initiated by a non-bank customer, both the instruction from the customer and the instruction passing between each pair of banks must be authenticated.

39. Where funds transfer instructions are transmitted in batches, there is usually a single authentication for the entire batch. In the case of the teletransmission of a batch, the authentication is found in the message header. In the case of electronic funds transfer instructions transmitted by the physical exchange of computer memory devices, the authentication may be in the header, on a separate piece of paper, or on both.

#### 2. *Data elements*

##### (a) *In general*

40. Negotiable instruments drawn on or payable at or by a bank are more than funds transfer instructions. They are also instruments which embody certain rights in the instrument and which may free certain holders of

the instrument from some defences which might have been available to the drawer against the payee. As a result there are strict requirements as to the data elements which must appear on a negotiable instrument and those which must not appear on a negotiable instrument. An instrument which does not conform to these requirements fails to be a negotiable instrument. However, an instrument which fails to meet the requirements of a negotiable instrument might still serve as a valid funds transfer instruction.

41. There are no general statutory requirements as to the necessary data elements in a non-negotiable funds transfer instruction. However, many electronic clearing-houses and communications services specify the data elements required for different types of funds transfer instructions transmitted through them. ISO DIS 7982 establishes a list of the data elements which can be used in a computer-to-computer telecommunication of a funds transfer instruction and gives examples of how they are to be represented in various types of instructions, but it does not attempt to specify which data elements may be necessary in a given type of funds transfer. The data elements for funds transfer instructions to be used in telex messages and in debit and credit card message exchange among financial institutions are also being standardized by the Banking Committee of ISO. When consumer protection legislation specifies certain information which must appear on a periodic statement of account activity, the funds transfer instruction to the transferor bank must also contain that information so that the transferor bank can include it in the statement.

42. When paper-based debit or credit transfer instructions are truncated before they reach the destination bank, the electronic instruction prepared by the truncating bank may not contain all of the data elements which were on the paper-based instruction. Words of negotiability on a cheque are not forwarded. The account to be debited or credited may be indicated only by account number, if it is available, and not by name. The amount may be indicated only by figures, even if the paper-based instruction contained both words and figures and even if the applicable law provides that the words control. The date of the paper-based instruction may not be included.

43. It is the responsibility of the sending bank to be sure it has sent all of the data elements that would be necessary for the receiving bank to act on the instruction. Failure to do so renders the instruction incomplete. The receiving bank, however, may not recognize that the instruction is incomplete, in which case the instruction may be executed incorrectly. On the other hand the receiving bank may be able to deduce some of the data elements from the context of the funds transfer instruction. A domestic funds transfer can be assumed to be in the local currency unless otherwise specified. Some of the required data elements can be derived from those data elements given. The number of an account to be debited or credited and the relevant branch of the bank can usually be determined if the name of the account is given correctly. In other cases

the receiving bank may be able to repair the incomplete instruction on the basis of prior transactions or other information in the possession of the receiving bank. However, since attempted repair of the instruction by the receiving bank may lead to an incorrect instruction, the receiving bank may become liable for the error rather than the sending bank. Therefore, when the receiving bank is in doubt, it should ask for clarification.

(b) *Identification of account by name or number*

44. Bank accounts are usually opened in the name of a particular person or entity. A single customer may have several different accounts for different purposes. These accounts are often identified by similar, even if not identical, names. Likewise, different customers may have similar, or even identical, names. Moreover, customers may not be consistent or entirely accurate in the name they use in connection with their account or accounts. Banks usually attempt to overcome this problem by assigning a unique number to each account, permitting them to distinguish between accounts with similar names or different accounts of the same customer. If each bank has also been assigned a unique number, the entire process of sorting and routing funds transfer instructions between banks and within banks can be accomplished automatically through machine-readable magnetic ink character recognition (MICR) or optical character recognition (OCR) techniques in the case of paper-based funds transfer instructions or by a computer in the case of electronic funds transfers. In a fully automated banking environment the account of the transferor would be debited and the account of the transferee would be credited entirely on the basis of the machine-readable account numbers, thereby decreasing the cost of the bookkeeping operations as well as decreasing the likelihood of entering the debits or credits to an incorrect account.

45. In spite of the advantages of making funds transfers on the basis of the number of the account rather than the name of the account holder, there are several problems. A bank may allocate the same account number to two different customers, though it could be expected that this error would soon be corrected. The customer may give his own or the other party's account number incorrectly or, if the bank must transcribe the number to the code line of a paper-based funds transfers instruction or to a new electronic instruction, it may do so incorrectly. For paper-based funds transfers this problem can be reduced by the use of funds transfer instruction forms containing pre-printed machine-readable account numbers. The account number of both the transferor and transferee can be pre-printed when the funds transfers are regularly made between them. However, usually only the transferor's or the transferee's account number can be pre-printed on funds transfer instruction forms and the other account number must be entered on the form at the time of the transfer. The account numbers to be debited and credited in funds transfers processed by computer can be verified as being in existence, thereby reducing the possibility of error, but all cases of fraud cannot be eliminated through these verifications.

46. Although the use of machine-readable paper-based funds transfer instructions and of electronic funds transfer techniques have led banks to rely largely on the account number for these transfers, it is not clear at present to what extent in the various legal systems a bank is legally justified in relying only upon the account number as disclosed in the funds transfer instruction to post debits and credits, and especially to post them automatically from the code line of a paper-based funds transfer instruction or from an electronic funds transfer instruction. Where the transfer is identified only by account number, as it is for example in a transaction activated by the use of a magnetic stripe plastic card and a PIN, in an automated teller machine, automated cash dispenser or point-of-sale terminal, the bank can identify the account to be debited only by reference to that number and it is believed that this practice is legally justified. However, if the funds transfer instruction carries both the name and the number of the account to be debited or credited and the two are not in agreement, the legal rules in force may provide that the name of the account controls. The legal system may go even further and hold that the bank must investigate because of the obvious existence of either error or fraud. However, to the extent it can be reconciled with laws of general application in force in a jurisdiction, the development of a fast, reliable and inexpensive electronic funds transfer system would clearly be furthered by enabling banks to rely entirely upon the account number in the funds transfer instruction.

### 3. Format

47. Although there have been no general legal rules requiring that funds transfer instructions be in a particular format, certain world-wide conventions developed over time as to the general formats to be used for the traditional paper-based instructions. This has been particularly true of cheques and bills of exchange, where the formats used are clearly recognizable in all countries. This similarity in format has greatly aided the international clearing and collection of these traditional forms of debit transfer instructions.

48. In order to process paper-based funds transfer instructions by automated data processing it is necessary that the data elements be located in a specific place and be machine-readable. This has called for the standardization of the size and the format of funds transfer instructions and this standardization has often been accomplished within the relevant clearing and collection systems. Therefore, in a country where there are several different clearing or collection systems for paper-based funds transfer instructions, such as one system amongst the commercial banks and a second operated by the postal system, and the funds transfer instructions are not cleared freely between the two systems, each of the clearing systems may have standardized the size and formats of the funds transfer instructions, but in an incompatible manner. Where there is only one clearing system or where funds transfer instructions are cleared freely between the different clearing systems, nationwide standardization of the size and format will usually be found.

49. Similarly, where paper-based funds transfer instructions are intended to be cleared or collected internationally, or where forms prepared in one country are to be useable in other countries, international agreement has sometimes been reached on the size and formats to be used. Therefore, the size and format of Eurocheques has been standardized, thereby also standardizing the cheques as used domestically in those Eurocheque countries (with the current exception of France and the United Kingdom) and the forms to be used for the various types of international funds transfers through the postal system have also been standardized.

50. In the past electronic funds transfer instructions sent by telegraph or telex were not standardized. The move to standardize message formats of electronic funds transfer instructions undoubtedly began when banks began to exchange, either directly or through an automated clearing-house, computer memory devices containing funds transfer instructions. In order for the computers of the receiving bank to process the instructions, the programs for the computers of the banks, as well as those of the automated clearing-houses, must be compatible and the data elements must be entered according to a standard format.

51. The concerns are essentially the same for funds transfers made by computer-to-computer telecommunications. Although there is nothing in the nature of a computer-to-computer telecommunication network which precludes the use of free-form messages, since the receiving computer can show the message on a screen or produce a paper print-out which can then be used as the equivalent of a telex message, the use of free-form messages eliminates many of the advantages to be derived from a computer-to-computer network. Therefore, standard formats have been created for the different types of funds transfer instructions permitted in each network. A bank which programs its computers to interface with the standard format used for domestic and international funds transfers can enter transactions into its accounts directly from the instructions received, as well as from those sent, with at most a minimum of additional data to be entered relevant only to that bank.

52. Once a standard format for a funds transfer instruction has been adopted by a particular closed-user network for funds transfers, the use of that format should be obligatory. A bank within the network which fails to use a required format should be responsible for loss to the receiving bank caused by the failure. However, where banks can use the network also for messages necessarily sent in free-form, the evidence suggests that the computer operators use the required formats for messages of a type they send often but prefer to use free-form messages in place of message types they use less often. Since failure to follow a required format may cause extra work and delay to the receiving bank, even though no quantifiable loss may be created, consideration could be given to the levy of a standard charge on the sending bank for each deviation from the required format.

53. The standard formats developed for the various closed-user networks have been neither identical nor compatible in all respects. If the formats are compatible, even though not identical, software is available to convert funds transfer instructions from one format to the other. If the formats for the closed-user networks for computer-to-computer funds transfers in which a bank participates are not compatible with one another, a bank which receives a funds transfer instruction from one closed-user network and passes it on through a different network may have to re-enter the data for the out-going instruction with the consequent delays, extra expense, and, most important of all, the increased likelihood of errors. The incompatibility of the formats precludes the clearing of funds transfer instructions between banks, or limits the access of some banks to some aspects of a market for funds transfers.

54. Incompatibility of format is most serious when the message format of one network does not contain data elements which are required in another network. This latter problem has arisen in its most acute form in respect of the use of magnetic stripe plastic cards in point-of-sale networks. Merchants in most countries in which point-of-sale networks have been created or actively discussed tend to insist that they can accommodate only one point-of-sale terminal at each cash register. If point-of-sale terminals which can accept only one of several competing magnetic stripe cards are installed in large numbers of stores, an adverse effect can be expected on the competitive position of those banks which belong to the rival systems. As a result, in several countries official pressure has been exerted leading to the adoption of a compatible format for such cards. This problem has often been referred to as a problem in shared facilities.

#### D. Time within which bank must act on the instruction

##### 1. General considerations

55. The agreement between the customer and the bank not only governs the extent of the bank's obligation to complete the funds transfer or cause the funds transfer to be completed, but also governs the period of time within which the funds transfer must be completed or within which the various banks and other entities in the funds transfer process must act. That period of time may be explicit or it may be implicit. The length of the period will vary depending on the funds transfer technique chosen. Few countries have statutory provisions prescribing the period within which the banks must act. However, some agreements between banks and their customers and a larger percentage of inter-bank agreements, including the regulations governing clearing-houses and closed-user networks, contain rules governing such period of time. Although in some countries the inter-bank agreements have no formal effect on the rights of the bank customers, they govern the rights of banks between themselves and, by providing the structure for the funds transfer system, they determine the period of time within which a customer can reasonably expect his funds transfers to be completed.

56. The law and practice governing the period of time within which banks must act in a funds transfer varies widely in different countries. Undoubtedly this reflects differences in such factors as the size of the country, the nature of the banking system, whether funds transfers are primarily made by debit transfer or credit transfer, the transportation system and clearing arrangements available for paper-based funds transfers and the extent to which various forms of electronic funds transfers are available. The development of international closed-user networks for paper-based funds transfers (e.g. Euro-cheque), consumer electronic funds transfers (various debit and credit card systems) and commercial funds transfers (e.g. S.W.I.F.T. and, in a different sense, CHIPS) has tended to unify the time-limits applicable to transfers through those networks. However, even in these networks national differences are significant and, since an international funds transfer may also pass through domestic channels in the originating or destination country, the total period of time necessary for an international funds transfer is often still difficult to determine. It is likely, however, that the development of these networks is having an effect on the domestic practice in the countries which are active participants.

##### 2. Customer's concern about speed and consistency of performance

57. The concerns of bank customers about the speed and consistency of performance of the funds transfer system fall into two broad categories. On one hand, the funds transfer system must function in such a manner that bank customers can fulfill their business and personal obligations to make funds available to the credit of the transferee at the time and place required. On the other hand customers and banks alike share the desire to maximize the interest earning potential of their account balances.

##### (a) Impact on relations between customers

58. A transferee may be primarily interested in knowing that the transfer process has begun and can be expected to be completed in due course. On that assurance he may be willing to ship additional goods or provide additional services. A debit transfer system by which he receives a cheque from the transferor or in which he can initiate a bill of exchange or electronic debit transfer instruction may satisfy this concern. When the transferee has doubts whether the funds transfer will be completed in an acceptable period of time or when the transferee needs the money prior to proceeding further, he may require completion of the funds transfer with irrevocable credit to his account before he will act further.

59. If the funds must be available to the credit of the transferee by a certain date, the transferor using an ordinary cheque must furnish the cheque to the transferee in sufficient time for the cheque to be presented, honoured and credited to the transferee's account. If the transfer is by credit transfer, the transferor must make it in sufficient time and by a

method that will assure the availability of the credit in time. In either case the transferor needs at least a reliable estimate of the time necessary for the funds transfer. In some cases he may need a firm commitment of the bank that the funds transfer will be completed by the point of time stipulated. If the transferor suffers a loss as a result of the failure to complete the funds transfer within the period of time explicitly or implicitly provided in the transferor's agreement with his bank, the transferor bank, or the other bank or entity responsible for the delay, may be liable for that loss.

(b) *Interest earning potential of customer bank balances*

60. Many bank customers want to maximize the interest earning potential of their bank balances by delaying debits as long as possible and securing credits as early as possible, while at the same time keeping only the minimum balance necessary in accounts which earn no interest or only a low rate of interest. Although customers have little control over the timing of debits and credits to their accounts once the funds transfer instruction has been issued, they can influence the timing by their choice of funds transfer techniques.

61. A transferor may be able to delay debits to his account for a significant period of time if he can effectively discharge an obligation by issuing a debit transfer instruction, such as a cheque, whether or not issuing the instruction legally discharges the obligation. In many countries cheques are debited to the account only as of the date they are presented. In these countries the transferor has the continued use of the funds until the point of time the cheque is honoured, which may be days or weeks later. By careful management of the account balance, the transferor can ensure that there are sufficient funds in the account to honour the cheques as they are presented. Such a practice is often formally prohibited by a rule that there must be at all times a balance sufficient to cover all cheques issued, but official action is rare so long as cheques are in fact honoured.

62. The interest gained by the transferor from a delayed debit to his account is usually lost to the transferee, since it can be expected that the transferee will not be credited at least until the cheque has been honoured or, if he is credited more promptly, that the credit will not usually earn interest or be freely transferable until the cheque has been honoured.

63. In some countries the debit to the transferor's account and the credit to the transferee's account are entered as of the date the funds transfer instruction was issued as shown by the date on the instruction. In those countries the amount of time it takes to complete a funds transfer is of less importance to the customers and to the banks. Although funds cannot be available to the transferee as a practical matter until the credit is entered, that may be of little consequence if the transferee is permitted to carry a debit balance larger than his immediate cash flow needs. Carrying a debit balance does not generate net interest charges to the extent that credits entered subsequently are credited as

of the date the instruction was issued. Entering the debits and credits as of the date the instruction was issued may cause difficulties for inter-bank clearance. However, this practice has been in existence for a long time in some countries and the problems would seem to be minimized when computers are used in the clearance. This system of dating the entries reduces the incentive to a bank to delay entering customer credits beyond that necessary for a normal flow of work.

64. In a credit transfer the transferor's account is debited at the time the transferor bank begins to process the credit transfer instruction while the transferee's account is credited only after the transferee bank receives the instruction. Unless the debits and credits are made as of the date of issuance of the credit transfer instruction, all inter-bank credit transfers necessarily envisage a gap between the point of time at which the transferor's account is debited and the transferee's is credited. As with debit transfers no generalizations can be made as to the extent of the gap, which could run from fractions of a second in an on-line computer-to-computer network to days or even weeks for other transfers.

65. Since electronic funds transfer techniques almost always permit the banks to complete the funds transfer faster than do paper-based techniques, the transferee's account can be, and usually is, credited and the transferor's debited sooner than when a cheque is involved. This has been a major deterrent to the introduction of electronic funds transfer techniques in some cheque oriented countries, since in most cases it is the transferor who decides the means by which the funds transfer is made. This concern has been met in some point-of-sale networks by delaying the debit to the transferor's account for some specific period of time. There would be no such deterrent to the substitution of electronic funds transfer techniques in place of paper-based credit transfer techniques when the transferor's account is debited at the same time.

(c) *Irrevocability of funds transfer instruction*

66. It is in the interest of transferees, and of transferee banks, that funds transfer instructions be irrevocable as early in the funds transfer process as possible. On the other hand on occasion transferors wish to revoke funds transfer instructions they have issued, usually because of problems associated with the underlying transaction or because of the intervening insolvency of the transferee. Although specific rules vary in different legal systems, a matter which is discussed at more length in the chapter on finality of honour, the transferor's right to rescind the funds transfer instruction terminates no later than when the funds transfer is completed. Since electronic funds transfers tend to be completed sooner than are paper-based funds transfers and the operating rules of many on-line and off-line electronic clearing-houses further restrict the right to revoke a funds transfer instruction once it has been submitted to the clearing-house, transferors tend to lose their right to revoke funds transfer instructions at an earlier time when the funds transfer is made electronically than when made by paper-based techniques.

**3. Bank's concern about speed and consistency of performance**

67. Banks are at least as interested as their customers that the funds transfer system operate in a consistent and predictable manner. Banks transfer large sums of money for their own account and they too must be able to count on being able to deliver funds when they have promised to do so and to receive funds which were promised to them. If the funds transfer service does not operate well, in many countries the banks risk losing both deposits and funds transfer fees to other financial entities which can furnish competitive, if not identical, services. This leads banks to work for the reliability of the system, including both improvements in the hardware, software and procedures and a strengthening of the rules requiring prompt action by the receiving bank of a funds transfer instruction. However, in addition to the pressures exerted on the banks to increase the speed with which the funds transfer system operates, there are countervailing pressures on the banks to retain some of the delay that was inherent in the paper-based system. The two main pressures of this type being the impact which the speeding up of the funds transfer process has on the interest earning potential of the bank and on the security of the transferee bank that it will be reimbursed by the transferor bank.

**(a) Interest earning potential of bank assets**

68. A banking system as a whole increases its net earnings when there is an increase in the amount of interest earning assets not subject to a corresponding obligation to pay interest to a customer. Interest obligations of a banking system to its customers are decreased during the period after the account of the transferor has been debited and before that of the transferee has been credited. In effect, during this period of time the deposit liability for funds transfers in transit is not recognized as due or available to any specific bank customer. Since the introduction of electronic funds transfer techniques in credit transfers tends to reduce the period of time before which transferee banks receive the credit transfer instructions, prompt crediting of the transferee's account as of the day of receipt of the instruction tends to increase the obligations of the banks to their customers reflected in customer bank balances as compared to the situation using paper-based credit transfer techniques.

69. In many parts of continental Europe it is common practice in an inter-bank transfer to credit the transferee's account with an interest date two banking days subsequent to the entry date. The time stretches to four calendar days over an ordinary weekend. This period of two banking days is intended to allow the transferee bank to receive settlement from the transferor bank prior to the date on which the transferee would begin to earn interest. Under the usual rule for a credit transfer the credits once entered are firm and the transferee has usually an unqualified availability of the funds. They can be withdrawn or transferred to another account immediately. However, the funds do not draw interest until the indicated interest date. Moreover, if they are

withdrawn before that date, the customer is charged for the relevant period. This practice assures the banks a minimum period of two days during which neither bank is paying interest on the amount transferred in addition to any period of time necessary to make the transfer.

70. Interest earning assets are also created if the transferee bank receives a credit to its account before the transferor bank is debited. In effect, in this case both banks recognize the same asset. This occurs in debit transfers in the United States of America where the Federal Reserve uses an availability schedule to determine when it will give credit to transferee banks for cheques they have submitted to the Federal Reserve for collection. This availability schedule on average calls for crediting the transferee banks somewhat sooner than the Federal Reserve is able to present the cheques to transferor banks and to receive value from them. The Federal Reserve, however, has acted to reduce this unique form of bank asset by, *inter alia*, encouraging the development of electronic credit transfers and by the faster presentation of cheques, including a proposal for the electronic presentation of large cheques.

71. Where the interest earning potential which existed in the previous paper-based funds transfer system has been decreased by the introduction of electronic funds transfer techniques, or by the action of the public authorities, it has been expected that explicit charges for funds transfers would result. While the advantages or disadvantages of explicit charging for funds transfer services go beyond the scope of this legal guide, a funds transfer service adequate to the needs of many bank customers calls for rules which do not reward delay in processing any aspect of the transfer in order to create interest income for themselves.

**(b) Security of reimbursement to transferee bank**

72. In some countries banking rules permitting delay in entering a legally final credit to the transferee's account is associated with the transferee bank's concern that it may not receive reimbursement from the transferor bank. When a bank becomes legally committed to its customer for the credit before it has a final legal right to the corresponding debit in a form acceptable to it, the bank runs a credit risk that the debit may not become final or that the person or bank indebted to it on the debit may become insolvent. In a debit transfer there may be an additional risk for the transferee bank that the debit transfer instruction will be dishonoured.

73. The risk for the transferee bank has been reduced in most countries in respect of paper-based debit transfers by a legal rule permitting the transferee bank to reverse the credit to the transferee's account in case of dishonour. A similar rule seems to prevail in electronic funds transfer systems permitting debit transfers. The risk that the transferor bank may fail to settle for either a debit or a credit transfer is also reduced in some countries by a similar legal rule that the credit to the transferee's account can be reversed if the transferee bank does not receive value. The most notable example

is that of the United States where the risk of bank failure underlies many of the rules governing funds transfers. However, where the legal rules do not permit reversal of a credit to a transferee's account, or give a priority in insolvency, the risk can be placed on the transferee rather than on the transferee bank by delaying the entry of the credit to the transferee's account until after settlement is final.

#### *4. Responsibility of destination bank to act promptly*

##### *(a) Credit transfer*

74. In a credit transfer the transferee bank is the bank which finally executes the instruction of the transferor to credit the account of the transferee, although in many legal systems the transferee bank's legal obligation to do so promptly arises out of the inter-bank agreement between it and the transferor bank or intermediate bank which sent it the instruction.

75. *Pay date:* The transferor's instruction to the transferor bank may include a pay date on which the transferee's account is to be credited. Although the pay date may constitute a contractual commitment on the part of the transferor bank that the transferee's account will be credited by that date, it is less clear what significance the pay date has for the transferee bank. ISO DIS 7982 defines the pay date as the "date on which the funds are to be available to the beneficiary [transferee] for withdrawal in cash". This would appear to make the pay date as that date appears in the instruction received by the transferee bank as legally binding on it unless the transferee bank were to reject the instruction because it could not credit the transferee's account by that date or because it refused to do so unless it had already received settlement. Failure by the transferee bank to credit the transferee's account by the appropriate time, which would seem to be the pay date if one is specified, would therefore ordinarily constitute breach of an inter-bank agreement and the transferee bank may be liable for the consequent losses, if any, caused by the delay.

76. The transferee bank also has an agreement with the transferee to credit his account within some appropriate period of time for all credit transfers received. When crediting is delayed beyond the appropriate time, there would be a loss of interest in many cases, even if the loss would be so minor for each transaction that it would not be worth the transferee's time to complain. The transferee might also fail to complain because he may not be in a position to know when the credit transfer instruction was received. However, if a bank was consistently slow in crediting the transferee's account, the total loss to the bank's customers and gain to the bank could be substantial. It is for this reason that some countries and some credit transfer networks prescribe the maximum period of time after receipt of a credit transfer instruction for the transferee bank to credit the transferee's account.

##### *(b) Debit transfer*

77. In a debit transfer the transferor bank acts on the instruction or authorization of the transferor to debit his account and to transfer or cause to be transferred the sum in question to the account of the transferee. If the transferor bank wrongfully fails to honour the instruction, it may be liable to its customer for damages. The transferor bank by debiting the transferor's account also acts as the bank which finally executes the instruction given by the transferee to the transferee bank to collect the sum in question from the transferor's account in the transferor bank. As a practical matter, few transferees would be in a position to insist that the transferor bank honour the instruction promptly. On the other hand the transferee bank may be able to exert pressure in this direction. Furthermore, in some countries the public authorities also press transferor banks to settle promptly.

78. The principal concern of the legal system, however, has not been the amount of time before the debit transfer instruction is honoured but the amount of time available to the transferor bank to dishonour a debit transfer instruction. A transferor bank to which an instruction is presented that would, if honoured, create an unacceptably high debit balance in the transferor's account might decide to retain the item for a period of time to allow the transferor an opportunity to deposit additional funds to the account. If the additional funds are not deposited, the debit transfer instruction will eventually be dishonoured. However, when the transferor's financial position has worsened during this period of time before dishonour, the transferee and the transferee bank may suffer more losses because they were not notified of the transferor's financial difficulties by an immediate dishonour of the debit transfer instruction. It is common to find in clearing-house rules and similar inter-bank agreements a strictly limited period of time measured from the presentation of the instruction after which it can no longer be returned through the clearing-house. However, it is usually somewhat less clear for how long the dishonoured instruction can be returned outside the clearing-house although there is general agreement that such a time-limit exists.

#### *5. Effect of branch banking*

79. In respect of paper-based funds transfers, separate branches of banks have often been treated as separate banks for the purpose of determining the applicable time-limit for the transmission of a funds transfer instruction from one bank to the next or for the honour or dishonour of the instruction by the transferor bank. This rule is based on the premise that many of the crucial actions to be taken by the transferor bank and transferee bank can take place only when the funds transfer instruction has arrived at the office of the bank where the customer records of account and specimen signatures are kept and the account is managed.

80. When the customer records of account are kept off-line at a centralized data processing centre but the

specimen signatures for paper-based funds transfer instructions are maintained at the branch, it is less clear whether the time-limit for the bank to act should be measured from the time of receipt of the paper-based instruction at the data processing centre or from its receipt at the branch where the verification of the authentication can take place. Many clearing-house rules measure the time for return of a dishonoured debit transfer instruction or of an unprocessable credit transfer instruction from the point of time when the receiving bank withdraws it from the clearing-house. This does not take into account any need for the receiving bank to process the instruction at both the data processing centre and the branch. Nevertheless, if many banks participating in the clearing-house found the periods of time to be too short, it could be expected that the clearing-house rules would be amended to allow additional time for return of such instructions.

81. Since the PIN, password or other customer authorizations for off-line as well as on-line electronic funds transfers are contained in the computer along with the records of account, the funds transfer instructions would need to be delivered only to the data processing centre, and not to the branch. Furthermore, if the branches and offices of the bank are on-line, the customer records of account and authorizations for electronic funds transfers could be accessed from terminals at any of those points. However, in case of paper-based funds transfers, it might be necessary for the transferor bank to send the instructions to the appropriate branch for verification of signature even though the debit or credit entries to the customer's account could be made from an on-line terminal at another convenient point. On the other hand, if banks truncate the paper-based funds transfer instructions, there is no necessity to allow them time to send those instructions to the branch for verification of signature.

based funds transfers, there remain a surprising number of unanswered questions in many legal systems. Moreover, the changes in procedures necessitated by the use of electronic techniques raise questions as to whether the rules on liability for paper-based transfers should be applied to electronic funds transfers.

2. The problems are complicated by the rapidly changing role of the telecommunications carriers and the pressures on the law governing liability which have ensued. Whereas previously telecommunications were a service external to the bank offered by a common carrier monopoly, today the office equipment in many banks is linked in local area networks, branches are linked by dedicated lines and banks are transmitting an increasing share of their funds transfer messages to other banks by telecommunications. Telecommunications are no longer external to the bank; they have become a vital internal operating medium, as they have in many other fields of economic activity. Because of the blurring of the lines between computers and telecommunications, the former monopoly of telecommunications service has been broken in some countries and is under pressure in others. As a result of these developments, questions are being raised as to whether the former (and largely still existing) exemption from liability accorded to the telecommunications carriers is still a valid policy.

3. This chapter considers first some of the factors which contribute to the occurrence of errors or fraud in electronic funds transfers and the actions that can be taken to minimize their occurrence. Secondly, it considers the allocation of the loss among the various parties to the funds transfer. Then, the focus is on the extent to which and the party from whom the bank customer as transferor or transferee can recover losses suffered as a result of an improper handling of transfer instructions.

[A/CN.9/250/Add.4]

## VI. Chapter on fraud, errors, improper handling of transfer instruction and related liability

### *Introductory note*

1. The volume of electronic funds transfers and the sums involved suggest that the potential losses could exceed the losses experienced with paper-based funds transfers. At the same time customers of banks have been concerned that the move from paper-based funds transfers to electronic funds transfers would result in their bearing a larger share of any losses arising out of errors or fraud. The result has been an unusually unsettled state of the law as the participants have attempted to establish appropriate grounds for assigning loss in the multitude of new and rapidly changing factual situations. The problems would be difficult enough if only the banking law governing the responsibility of various parties to a funds transfer were involved. In spite of the many years during which such problems have been considered in regard to paper-

### A. Fraud

#### 1. Opportunity for fraud

4. Fraud in an electronic funds transfer involves an unauthorized instruction, alteration of the account to which an entry is to be made or alteration of the amount of the entry. To avoid losses from fraud, adequate steps must be taken by the party in a position to do so to prevent unauthorized instructions from appearing as though they were authorized.

#### (a) Dishonest employees of bank customer

5. Many losses due to fraud in electronic funds transfers are caused by the application of techniques well-known in connection with paper-based funds transfers. Three common examples involve dishonest employees of the bank customer.

6. A clerk charged with preparing the payroll or preparing the vouchers authorizing payment to a supplier may falsify the payroll or the vouchers so that

payment is made to a person not entitled to receive it. If payment is made by means of a cheque, the dishonest employee gains possession of the cheque and, after endorsing it in the name of the fictitious person, deposits it in an account he has previously opened in that name. If payment is made by means of paper-based or electronic credit transfer, the funds are credited to the account of the fictitious person in due course. The fraud is completed by the subsequent withdrawal of the funds from the account by the dishonest employee.

7. If the dishonest employee has the authority to authorize the funds transfer on behalf of his employer, rather than the responsibility of preparing the substantiating documentation, he signs the cheques or paper-based credit transfer instruction or authorizes transmission of the data in electronic form to the bank. The fraud is completed in the same manner by withdrawal of the funds by the dishonest employee.

8. In both cases, the funds transfer instruction appears to the bank to be genuine and authorized, although it is fraudulent in fact. These cases have caused considerable difficulties in some countries when the funds transfer instruction was in the form of a cheque, since the completion of the fraud requires the endorsement of the cheque by the dishonest employee in the fictitious payee's name. Nevertheless, the endorsements of the dishonest employee (or of his accomplice) have usually been held to authorize the bank to honour the cheque.

9. The allocation of the loss to the bank customer causes fewer doubts when the fraudulent payment is by paper-based or electronic credit transfer, since the fraud does not require any equivalent of a forged endorsement.

10. A third type of fraud by a dishonest employee who has no authority for issuing funds transfer instructions on behalf of the employer is possible when a computer terminal located at a bank customer's place of business can be used to make funds transfers. If the dishonest employee is able to gain access to the terminal and learns how to enter a funds transfer instruction, including the necessary password or other security measures, the instruction will be followed by the bank. For many countries this is a new form of fraud which could not be committed in a paper-based funds transfer. However, in some countries which permit the use of mechanical forms of signature on cheques or paper-based credit transfer instructions, a similar problem arises when a dishonest employee (or third person) gains access to the mechanical signing apparatus and causes cheques or credit transfer instructions to be issued payable to himself or to a fictitious person.

11. In those countries which do not prohibit mechanical signatures, it seems to be the general rule, often reached by agreement between banks and their customers, that a bank which honours in good faith a cheque or credit transfer instruction signed fraudulently by a genuine signature apparatus can debit its customer's account. Although different legal theories might be used to support such a result, the underlying

reasons are that the bank cannot distinguish a genuine usage of the signature apparatus from an improper usage, the bank customer has a responsibility to guard carefully an apparatus which can so easily be used fraudulently, and the bank customer is negligent in allowing the signature mechanism to be used fraudulently.

12. The reasons for allowing the bank to debit the customer's account in the case of a fraudulent use of the signature apparatus would also apply to the right of a bank to debit its customer's account for the amount of fraudulent funds transfer instructions made by use of a computer terminal located at the customer's place of business. However, it should be noted that the responsibility for security over the terminal at the place of business of a bank customer is shared by the bank customer and by the bank necessitating an allocation between them of that responsibility and of a failure to exercise it adequately.

#### *(b) Fraudulent use of customer-activated terminals*

13. Terminals located at the place of business of a bank customer as well as automated teller machines, cash dispensers, point-of-sale terminals and home banking terminals share the characteristic of being customer-activated. One of the purposes of a customer-activated terminal is to eliminate the need for human intervention on the part of the bank. This has the effect of reducing the likelihood of error by the bank in processing funds transfer instructions. However, the use of customer-activated terminals also has the effect of increasing the possibilities for fraud.

14. All computer terminals which can authorize a funds transfer work in essentially the same way. Before an individual can use the terminal, he must first establish his authorization to do so. A bank employee may log-in one time to establish his authority to use the terminal for the day. A customer-activated terminal would normally require separate authorization for each transaction, unless it was in constant use by the customer. A given terminal or customer may also have a limit placed on the types of transactions which can be authorized, the accounts which can be debited or credited and the monetary amount, which may be calculated per transaction, per day or in any other relevant way.

15. The log-in or authorization procedure to be followed before a customer-activated terminal can be used is established by the bank. In deciding on the procedure to be followed, the bank (or the electronic funds transfer network of which the bank is a member) must balance considerations of safety, cost and customer acceptance. Usually, the more secure the authorization procedure, the more expensive it is for the bank to install and maintain and the more difficult it is for customers to use. For marketing reasons it may be desirable for the customer-activated terminal to be user-friendly, but a user-friendly terminal also tends to be intruder-friendly. This is a delicate balance for the bank

to make, and it is a balance which changes as technological developments occur.

16. Restrictions on the types of transactions which can be authorized or accounts which can be debited or credited can be an effective way to reduce the likelihood of fraudulent transactions. Restrictions on the monetary amount have only a limited effect on eliminating the incidence of fraud, but they can be an important means of limiting the financial consequences of fraud. This may, however, be meaningful only in regard to consumer oriented networks since the upward limit in commercially oriented networks may need to be so high that sufficient room for serious fraud is allowed.

17. Current models of cash dispensers, automated teller machines and point-of-sale terminals require the convergence of two items to authorize the transaction, i.e. a plastic card with magnetic stripe containing certain information and the entry by the bank customer of a personal identification number (PIN). New and more secure forms of plastic cards are in experimental use. In some proposed home banking systems it would not be feasible to use a plastic card for authorization purposes; therefore, the authorization procedure depends on a PIN or password alone. A terminal located at a business establishment can have more complicated and presumably more secure procedures, but in essence they usually revolve around the use of passwords and the possible use of a plastic card.

18. There are currently two different approaches used by banks for protecting the security of the PIN. One approach concentrates on eliminating the possibility that an employee of the bank or funds transfer system can know the PIN. The PIN is generated by a computer using an algorithm and certain basic data relevant to the customer. The resulting four or six digit number is inserted by the computer into a sealed envelope and mailed or otherwise delivered to the customer. If properly followed, this method can give a secure PIN for each customer. However, since the number is abstract and may be difficult to remember, many bank customers feel the need to carry the number with them whenever they intend to use their plastic card, thereby seriously compromising the security of the PIN.

19. The other approach attempts to make it easier for the bank customer to remember the PIN by allowing the customer to choose his own number. A customer often chooses a number based on his own or his spouse's birthday, his street address, telephone number or other number already well known to him. While this has the advantage of making it less likely the bank customer will carry the number with him in written form, it has the disadvantage of reducing to a minimum the combination of numbers likely to be chosen by any given person and making it thereby easier to determine what that person's PIN might be. Moreover, the PIN is known to at least several of the bank's employees and, since the PIN is no longer generated by computer, it must be entered into the customer's file and be available to anyone having access to that file.

20. Password security for terminals located in businesses or in homes raises the same kind of problem. The password should be neither so obvious that it could easily be guessed nor so obscure that the user will keep it in written form, unless the writing is to be kept under strict security controls. A terminal from which a wide range of funds transfers can be made for significant amounts of money should be subject to additional safeguards. Log-in might require the concurrence of two different persons with different passwords. Passwords can be changed at relatively short intervals, although that introduces difficulties of their distribution from the bank to the customer, or vice versa. The bank can cancel a password automatically if it is not used for a particular period of time, since this may mean that the person to whom the password is assigned is absent.

21. Protection against fraud in the use of customer-activated terminals is, therefore, a joint endeavour of the bank and the customer. The bank must install and maintain as good a security system as is practicable considering the cost involved and the interference with use which may result. One measure of the quality of the security system is the extent to which the customers of the bank, who are often non-professionals in the use of computers and in funds transfers, follow the security instructions given them by the bank.

(c) *Customer-supplied machine-readable instructions*

22. A somewhat similar situation exists when the customer supplies the bank or an automated clearing-house with funds transfer instructions in batch on computer memory device or in machine-readable paper-based form. Although it is the responsibility of the customer to prepare the instructions properly including the use of internal controls to guard against both fraud and error in their preparation, the bank or clearing-house should be responsible for verifying that item counts and value agree with the sums indicated, that they are within the parameters authorized by the customer for such batches, and that the batch otherwise appears to be free from alteration subsequent to its preparation. These controls can easily be exercised by the bank or clearing-house at the time it verifies the devices prior to processing.

(d) *Fraud by bank employees*

23. Employees of banks and other entities in the funds transfer system also have access to terminals with which they can enter fraudulent transactions. Fraud by such parties can be particularly difficult to discover unless the bank has a well designed system. The possibility of a dishonest employee programming the computer to credit his account and to erase all records of the transaction has been well publicized. This should not be possible, however, since the bank's computers can be programmed to leave a complete audit trail of all activity, including instruction to delete transactions. For this to be done effectively, the audit trail should be programmed by different persons from those who prepare the applications programs and should be subject to independent audit.

(e) *Fraud by tapping telecommunications transmissions*

24. It is relatively easy to tap any telecommunications system over which electronic funds transfer instructions might be sent. The cost for complete physical security of the transmission system is such that it is not feasible for commercial purposes. Therefore, the design of any electronic funds transfer system should assume the possibility of interception and reading of messages, alteration of genuine messages and the introduction of false messages. The first line of protection against such fraud is encryption. If the encryption standard used is powerful enough, there is no danger of interception, alteration or the introduction of false messages. However, an encryption standard which is highly secure today may be rendered insecure within a few years by the development of more powerful computers and new techniques for factoring the large numbers on which encryption is based. Moreover, the proposals in some countries that a government agency have all encryption keys used for transborder data flows would create a potential weak link in the system of security over which the parties would have no control. The creation of rigorous logs of all in-coming and out-going funds transfer instructions and the assignment of in-put and out-put sequential numbers provide a means of verifying the time of receipt or dispatch of the message and the other party to the message. These procedures increase the likelihood that a fraudulent instruction will be recognized and they are an essential means of subsequently discovering and tracing suspected fraudulent instructions.

2. *When may a fraudulent instruction justify a debit to an account*

25. Although a bank is normally authorized to debit a customer's account only for the amount of an authorized instruction, it may also debit the customer's account for the amount of certain unauthorized instructions, particularly when the fraud was made possible through the lack of adequate controls on the part of the customer. There is, for example, little doubt that the customer's account can be debited for the amount of fraudulent transfers initiated by those employees authorized to act for the customer, unless there was something about the transaction which was so unusual that it ought to have raised the suspicions of the bank.

26. However, it is less clear whether the bank or the customer should bear the loss for fraud committed by means of a customer-activated terminal. Since the bank designs the basic security and authorization procedures and the customer carries them out, one approach is to assign the loss on the basis of comparative negligence in each case. This approach may be feasible for those cases where it is evident that the fraud was made possible through a clearly inadequate security and authorization procedure or that the customer had been unusually negligent in following those procedures. It is not, however, an efficient means of distributing the loss, particularly in cases of fraud in consumer oriented systems, where the individual loss is often not large enough to support a full judicial inquiry.

27. As a result, there is a tendency to search for formulas of general validity for the vast majority of the cases. Bank-customer contracts, which are normally standard form contracts prepared by the bank, typically authorize the bank to debit the customer's account for any transfer made by use of the particular type of customer-activated terminal when the proper PIN or password and plastic card, if any, was used. In the case of systems in which transfers are authorized in part by use of a plastic card, customer liability normally ceases once the customer has notified the bank of the loss or theft of the card and the bank has had the possibility of entering the information in the bad-card file. This may be immediate in the case of an on-line system or the next banking day in the case of an off-line system.

28. An alternative approach, which has been most evident in respect of some consumer-oriented systems, has been to allow the bank to debit the customer's account for the fraudulent transfer, up to a limit of a relatively small amount. The customer bears a risk of loss large enough to encourage him to report the existence of any loss or theft of the plastic card or the compromise of the password, PIN or security procedure, while the bank bears the risk of major loss, thereby encouraging it to strive for a more secure authorization procedure. This approach may be supplemented by a rule that the bank may debit the customer's account for the full amount of fraudulent transfers which are the result of certain actions of the customer. These may include loaning a magnetic stripe card to a third person and telling him the PIN, or writing the PIN on the card or otherwise carrying the two together so that the loss or theft of one results in the loss or theft of both.

29. A third means of assigning the loss in a large number of cases is to place on the bank or on the customer the burden of proving how the fraud took place since in many cases the party who carries the burden of proof will lose. It is particularly difficult to prove that a fraud committed by a third party who has not been apprehended was caused by such actions of the customer as leaving a password in a desk drawer or writing the PIN on the plastic card. It would normally be even more difficult for a customer to show that a bank had designed an inadequate security system or had failed to follow its own authorization and security procedures.

30. Insurance can also be used to shift fraud loss from both bank and customer. However, large or repeated losses are soon reflected in higher premiums.

## B. Errors

1. *General sources of errors using computers*

31. At the time computers were first widely used in some countries for commercial purposes, the experience with the large number of errors encountered was discouraging for the firms that owned the computers and upsetting to their customers. Not only were there

large numbers of errors, but it seemed difficult for the firms to correct many of them. However, the early bad error experience of many firms in the use of computers lay in part in the quality control of the hardware itself and in the inexperience in designing software. These are no longer the source of constant frustration they once were; the hardware is highly reliable and software, while still a problem, is of a much better quality than before. The errors which occur as a result of hardware or software failure are a minute proportion of the total number of transactions.

32. The early bad error experience also lay in the inadequate procedures adopted by many firms in relation to their newly acquired computer systems. In order to gain the volume of transactions necessary to support a main-frame installation, a central data processing center was often established which was organizationally and physically separated from the operating departments which received, generated and used the data. The data-processing center was often in a separate building, and in the case of organizations with branches in different cities, it was by necessity in a different city from many of those branches. The personnel in the operating departments too often did not understand the needs of the data-processing department for presentation and data in a consistent format; the data-processing department became the province of specialists who too often did not understand the operations and needs of the firm; procedures for eliminating and resolving errors did not always command the same level of support as did the installation of the new equipment; and it was often difficult for customers, suppliers and employees alike to locate the person with authority to rectify problems which had arisen.

33. Although these problems are far from eliminated, it can be said with some confidence that errors arising out of the separation of the data-processing department from the operating sectors of the firm and arising out of inadequate internal procedures in general are no longer the source of concern they once were. Operating personnel are more familiar with the procedures required to function with computers and data-processing personnel have learned better how to shape the technological needs and possibilities of computers to the requirements of the commercial or administrative activities within which they operate.

34. Equally important, especially in the banking context, has been the decentralization of data input to the computer facilities. It is now common in many parts of the world for terminals to be located throughout the operating departments. Tellers dealing with banking customers over the counter can enter deposits and withdrawals directly into the computer, as can operating personnel who receive funds transfer instructions and other banking instructions through the mail, over the telephone or by other means.

35. The decentralization of data input in the bank has reduced the likelihood of error in several ways. By entering the data in the operating departments re-

sponsible for the transactions, the personnel entering the data are responsible for the entire transaction. They may feel a greater sense of responsibility for the accuracy of the data; they get a response from the computer immediately and know if the transaction was accepted; they are more apt to understand the context in which the data was created, thereby permitting them to recognize ambiguities and to resolve those ambiguities promptly and correctly; and the data need be entered only once in the bank's records, rather than two or more times as sometimes occurred with centralized data processing or with paper-based systems.

36. The introduction of customer-activated terminals with the capacity of ordering routine funds transfers further reduces the likelihood of bank error since the funds transfer instruction would normally be processed automatically without intervention of the bank's personnel. Errors are less likely to occur in a fully automatic electronic funds transfer system than in a semi-automatic system or in a paper-based system. However, the errors that do occur may be more serious because of the extremely large number of transactions processed by computer. Furthermore, there is a constant fear of massive failure out of all proportion to prior experience.

## 2. Current sources of errors peculiar to electronic funds transfers

### (a) Non-standardization of messages

37. Because there is as yet no universally recognized standard format for electronic funds transfer instructions, the possibility of error in composition of the message by the sender and comprehension by the receiver is increased. Moreover, if the message fields in two computer-to-computer funds transfer networks are not fully compatible allowing for automatic conversion from one message format to the other by interface software, a funds transfer instruction received from one network will have to be fully or partially re-keyed to be sent through the second network.

### (b) Re-creation of messages

38. Re-keying a transfer message creates the possibility of error. This possibility of error is to some degree unavoidable in all electronic funds transfers. In contrast to paper-based funds transfers where the original paper form filled in by the customer can usually be forwarded through the banking system precluding the possibility that the payment instruction will be altered except by fraud, an electronic funds transfer message is re-created at each processing point. Payment instructions given to a bank in paper form are transformed into electronic messages which may again be reproduced on paper at receipt. Telex transfers through a correspondent bank require the correspondent bank to pass on a new message with a somewhat different data content. Messages sent over packet-switching networks are broken into segments of a uniform length which are sent by separate circuits and reassembled at the destination. Transfer instructions submitted on magnetic

tapes to an automated clearing-house are sorted and recorded on new magnetic tapes before being sent to the receiving bank.

39. Each of these processes introduces the possibility of an inadvertent change in the content of the payment instruction through human error, an incorrect computer program or a breakdown or defect in the equipment. However, these errors can be detected before they pass through the system if the necessary controls are designed into the system as well as into the operations of each bank and if those controls are rigorously applied.

#### (c) *Non-standardized procedures*

40. International funds transfers, whether electronic or paper, are more difficult for banks to handle without error than are domestic transfers because of the lack of international agreement on appropriate procedures. Each transfer message must, therefore, be read carefully to be sure as to the procedure being used by the sending bank. That message may be unclear, especially when it is composed in unstructured cable language.

41. This confusion may be compounded when the local banking practices in the receiving country are different from those in the sending country. In particular, expectations as to the time within which funds will be made available to the transferee bank and to the transferee may turn out to be incorrect because of a local practice that a correspondent bank may withhold settlement for several days, or that remittance will be made to remote locations by mail or by cheque, even though the international funds transfer instruction requested the highest priority be given to the transfer.

#### (d) *Computer failure and software errors*

42. One source of errors in electronic funds transfers which does not exist in paper-based transfers is the electronic equipment itself. This includes the computer hardware of the banks, telecommunications carriers and clearing-houses or other switches and the software to make them operate. Although errors from these sources are comparatively few compared to those experienced only a few years ago, they are particularly serious. An error which arises out of a mistake in keying a funds transfer instruction into the system affects only that one message. However, a defect in the computer hardware or software may treat an entire series of instructions incorrectly. Moreover, the very nature of the problem in the hardware or software may cause the error to bypass the validity checks which are built into most computer programs. Most importantly from a legal point of view, errors arising out of defects in the computer hardware or software itself raise difficult questions as to the responsibility for the losses which result.

### 3. *Conceivable methods to prevent errors from occurring*

43. Fortunately, most of the actions necessary to reduce the number of errors occurring in electronic

funds transfers can be taken by each bank individually. However, some actions can be taken only by the banking community as a whole. In particular, standardized message formats and banking procedures should be established for both domestic and international funds transfers. In some respects agreement at the international level may be the more important as well as the more difficult. Large amounts are transferred through international wholesale networks, and international consumer electronic funds transfer networks are increasing in importance. Moreover, agreement at the international level should lay a firm basis for agreement at the domestic level.

44. The international banking community is currently engaged in several projects within the Banking Committee (TC 68) of the International Standards Organization (ISO) which should lead to generally accepted formats for the most commonly used message types in international funds transfers. ISO Draft International Standard (DIS) 7982, Part 1, contains vocabulary and data elements used in describing, processing and formatting funds transfer instructions. ISO/DIS 7746 provides standard telex formats for inter-bank funds transfer instructions. These standard formats, based upon S.W.I.F.T. message formats, are intended (1) to eliminate misinterpretation by the receiving bank of the sending bank's instruction and (2) to provide a basis from which can be developed systems for the automatic handling of telex funds transfer instructions. Other work of ISO TC 68 on such matters as test keys, technical characteristics of magnetic stripe cards and interchange message specifications for debit and credit cards will also contribute to more efficient, error-free and fraud-free electronic funds transfers.

45. The eventual adoption by ISO of standard formats for telex funds transfer instructions which are in harmony with the S.W.I.F.T. message formats and agreement on vocabulary to be used in funds transfer instructions and their adoption and use throughout the world for both domestic and international funds transfers would reduce the likelihood of errors arising out of the needs to re-key funds transfer instructions. A standard telex format with numeric field tags as well as field descriptors will permit the receiving bank to key the instruction into its computer system for entry into the records of the bank and for re-transmission, if necessary, with no necessity for interpretation of the instruction. This will be of particular value when the sending and receiving banks are from different language areas.

46. It can also be hoped and expected that the international banking community through appropriate institutions will over time be able to agree upon the procedures to be followed by a receiving bank, especially when it is not the transferee bank. It must be recognized, however, that when the receiving bank must re-transmit the funds transfer instruction through the domestic funds transfer system, agreement on the actions it should take would require a large degree of harmonization of the technical means by which funds transfers are processed domestically in different coun-

tries as well as the attendant banking laws and procedures. As an interim step, a clearer delineation of the actions which are taken by receiving banks in different countries in standard situations and the time required for these various actions might lay the basis for future harmonization efforts.

### C. Need for customers to verify status of accounts

#### 1. Statement of account activity

47. In spite of the most rigorous efforts on the part of all concerned, a certain number of improper entries will be made to the accounts. Once these entries have passed the various controls instituted by the bank to eliminate errors and fraud, they can in most cases be discovered and rectified only by the complaint of the customer. In order for the customer to discover any errors in his account, he must have a means of reconciling the records of the bank with his own record of transactions in that account.

48. There have been two traditional means of furnishing the customer with a statement of account activity. In some countries, perhaps in particular those countries in which credit transfers have been the normal means of inter-bank funds transfer for commercial and consumer purposes alike, a notice is sent by the bank whenever a debit or credit entry is made to the account. The notice can, and often does, indicate the opening balance, the debit and credit entries made that day and the closing balance. A quarterly or yearly statement may also be sent to reflect interest debited or credited to the account and to state officially the bank's record of the account balance. In other countries, a statement of account activity is sent periodically to the account owner. Statements on ordinary accounts may be monthly, quarterly or yearly, while statements on active commercial accounts may be weekly or even daily. Although a daily statement on an active account may appear to be the same as a daily notice to the customer of an active account of debits or credits to the account, it implements a different policy.

49. Where the account is inactive, the customer may receive no statement for a long period of time. In a country in which notices are sent to the customer each time there is a debit or credit to the account, this would indicate that no action had occurred during that period. In a country in which statements of account activity are normally sent on a periodic basis, the bank and the customer may agree that no statement is required because of the infrequency of expected transactions or because the customer wishes to keep the account secret. However, this is a dangerous practice since it leaves open the possibility that fraudulent or mistaken entries to the account may not be discovered for long periods of time.

50. The advent of customer-activated terminals changes somewhat the need for statements of account activity, whether the statement is furnished periodically or as a notice of debit or credit to the account. If the customer

can access the bank's record of his account, and especially if the customer has the facility of producing a hard copy of that record, there may be no need for the bank to go to the expense of mailing statements to the customer. At the present time some commercial customers of many large banks can access their accounts in this manner, and this facility is being actively promoted by banks serving multinational corporations as part of a cash management programme. It is also available in some home banking experiments, but automated teller machines which permit balance inquiry may not permit inquiry as to account activity.

#### 2. Customer's examination of the statement

51. There are several arguments for holding that a customer should examine the statement sent by the bank to find fraudulent entries, errors or other discrepancies. The statement, especially a periodic statement, may be seen as an offer to settle the account between the bank and its customer on the basis of the statement, a form of settlement which is known in various legal systems under different doctrinal names. The recipient of the statement must reply within a specific period of time or, in some countries, it is accepted as the correct statement of the account at that point of time, while in others the burden of proof of showing whether it is correct or not shifts from the bank to the customer.

52. The policy supporting this result is directly applicable to a transaction account in a bank. It is useful for the parties to agree periodically on the status of their mutual relations so that at the end of an extended period of time it is not necessary to retrace each entry to the account long after the details have been forgotten and the records may no longer exist. Furthermore, an incorrect entry to one account, whether caused by error or fraud, is often mirrored by an incorrect entry to another account. Delay in notifying the bank of an incorrect entry may reduce the possibility that the bank can correct the transaction or otherwise reduce the loss.

53. In some countries the customer is said to have no duty to examine the statement of account activity and may raise an objection to an incorrect entry at any time until the period under the statute of limitations or prescription has passed. This rule is more protective of the customer and it may be particularly justified in the case of individuals who are either new to the banking system, and therefore are unaware of the need to reconcile their statements or are not able to do so, or in the case of individuals who travel a great deal or live in a distant place and may have more difficulty in receiving the statement promptly. However, even in these jurisdictions it may be contributory negligence if a customer does not examine the statement and object to incorrect entries.

54. It should be recognized, nevertheless, that whatever the rule may be, an improper entry to an account which has passed through the controls of the bank will often be discovered only if the customer reconciles the

statement of account activity received from the bank and notifies the bank of the improper entry. This is particularly relevant when cheques are truncated at the bank of deposit and the essential funds transfer data are electronically processed because this practice reduces the likelihood that the transferor bank (drawee bank) will detect a forged signature of the transferor (drawer). The practical difference in the rules lies primarily in the fact that the customer has a shorter period of time within which to notify the bank of the improper entry when the customer is said to have a duty to examine the account than when the customer is said not to have such a duty.

### *3. Duty of a bank to correct entries*

55. It is evident that a bank must correct improper entries in the account promptly after being notified of them by the customer, unless there is a legitimate question whether the entry is improper. Detailed rules governing error correction by banks in respect of consumer electronic funds transfers have been adopted by some countries and proposed in others.<sup>12</sup> The need or desirability of such rules depends on the experience in each country.

### **D. Responsibility of an originating bank to its customer for errors or fraud made in an interbank transfer; a network liability approach**

56. As used in this discussion, the originating bank is the bank which receives the funds transfer instruction from its customer and transmits it through appropriate channels to the destination bank. In a debit transfer the originating bank is the transferee bank (or depository bank) while in a credit transfer the originating bank is the transferor bank. The originating party is the party who submits the funds transfer instruction to the originating bank. In respect of the issue discussed in this section, there seems to be no particular difference in the law governing paper-based transfers between the transferee bank as the originating bank in a debit transfer and the transferor bank as the originating bank in a credit transfer.

57. The fundamental problem is that associated with any field of economic activity in which a customer contracts with one firm to achieve a result which requires the participation of one or more other firms. The first firm may be held responsible only for its own performance, including the choice of appropriate collaborators, or it may be held responsible to the customer for the performance of all parties necessary to achieve the result contracted for i.e. a transaction-liability approach. The closest analogy to the funds-transfer situation is that of the carriage of goods by common carrier where the carriage of the goods from origin to

destination may require the participation of freight forwarders and terminal operators as well as several carriers of the same or of different types.

58. *In favour of transaction liability:* Although the originating party designates the general type of funds transfer and the destination bank, with few exceptions, neither the means of communication between the banks nor the intermediary banks are designated. The choice of a proper channel is left to the discretion of the bank. In a highly automated bank this choice may be exercised by a computer according to programmed criteria. Where alternative means of communication or intermediary banks are available, the bank must use reasonable care in the selection of appropriate means.

59. If the funds transfer is not made correctly, it is often difficult to determine where, how and why the error occurred. Each bank, clearing-house, switch and telecommunications carrier has an interest in claiming that the problem did not occur with it. The customer, being outside the system and having no continuing relationships except with his own bank, may find it unusually difficult to investigate and determine who appears to be at fault. If it appears that the party at fault can be sued only in a distant part of the country or in a foreign country, the originating party faces additional difficulties and expense to pursue his claim. However, if the originating bank has accepted or is deemed by the applicable law to have accepted responsibility for the successful completion of the funds transfer, subject to the loss not having occurred for specified exonerating reasons, it would be in a better position to seek reimbursement from the bank or other entity at fault. Under this approach, the originating bank would suffer the loss rather than the originating party if it could not be determined how the loss causing event occurred. The increase in cost to the banking system as a whole, not taking into account any increase or decrease in litigation expenses, would be the amount customers had previously been unable to recover because of an inability to prove where or how the error had occurred.

60. In the context of debit and credit cards issued by a bank, these same considerations have led to the opposite result, i.e. to acceptance of the destination bank (often referred to as the card issuing bank in this context) as the sole bank responsible to the customer for any improper debits to his account arising out of the use of the card. If an error or fraud has occurred in connection with the use of the card or the forwarding of the funds transfer instruction for which the customer cannot be charged, the banks in the card network distribute the loss between themselves according to the terms of the network agreement.

### *E. Permissibility of disclaimer of liability*

61. Disclaimer provisions are found in contracts between the originating bank and its customer and between the banks, clearing-houses, operators of switches, telecommunications carriers and other parties

<sup>12</sup>The right of a bank to correct entries to a customer's account when the error was in favour of the customer is considered in chapter "Finality of honour". This chapter will be submitted to the Commission at its eighteenth session and will be reproduced in Yearbook 1985.

who may participate in the funds transfer. A disclaimer provision may provide that the disclaiming party is not to be held liable for loss caused by third persons, for loss caused by some or all of the disclaiming party's own acts or failures or for certain types of losses, and especially for indirect damages.

62. The extent to which disclaimer provisions in contracts governing electronic funds transfers will be enforced depends in part on the general attitude of the legal system towards such clauses and in part on the extent to which the law governing funds transfers is regarded as mandatory or non-mandatory. It could be expected that disclaimer provisions directly affecting rights and obligations in respect of a negotiable instrument would not be enforced, whereas provisions affecting its collection or affecting electronic funds transfers, neither of which are covered by comprehensive statutes in most countries, might more likely be enforced. Where a statute has been enacted to protect consumer rights in electronic funds transfers, as in the United States of America, those rights can be modified to only a limited extent by contractual provisions.

63. The contractual disclaimers in contracts between the banks, between the banks and other entities in the funds transfer process, and between banks and their suppliers of computers and software have no formal effect on the relations between a bank and its customers. The customer as originating party may be able to present his claim to the entity whose actions or non-actions caused the loss without regard to disclaimer provisions in contracts to which he was not a party.

#### *1. Technical failure of computer hardware or software*

64. Many bank-customer contracts provide expressly or by implication that the bank is exonerated from liability for failure to carry out a funds transfer instruction in the proper manner if it can show technical failure of computer hardware or software.<sup>13</sup> However, exoneration on these grounds should be carefully limited.

65. Although computers have become considerably more reliable than in the past, computer downtime is a regular occurrence. Banks which use computers for funds transfer and other purposes should have, and normally do have, sufficient redundancy of equipment available either on their own premises or at another firm (e.g. supplier of computer equipment, computer-service bureau, another bank or other firm with compatible equipment) to operate during the period their own computers are out of service, although perhaps with some impairment of service. Therefore, computer downtime of an expectable level which should be compensated by redundant capacity should not be

readily accepted as a justification for failure to carry out a funds transfer instruction within the otherwise applicable time-limits. On the other hand, some delay may have to be tolerated. Furthermore, computer failure beyond an expectable level, especially if associated with a general disaster or loss of electricity in the area where the bank is located or if associated with a major disaster to the bank, such as a fire, may justify exoneration of the bank.

66. Banks which do not have available sufficient redundant computer capacity should retain the capacity to receive and dispatch funds transfer instructions by other appropriate means.

67. There would be no particular legal difficulties in denying exoneration if a failure to carry out a funds transfer instruction was caused by defective software designed by personnel of the bank. The defective software would seem to be merely the means by which the bank failed in its obligations. The answer would be the same even if the source of the problem was defective or inappropriate software purchased from an outside supplier. In general, neither a bank nor any other business should as a matter of course be exempt from liability because equipment or software it uses in its business is inadequate for the task at hand.

#### *2. Data-communications service*

68. Most inter-bank and many intra-bank electronic funds transfers must use the services of a data-communication service. Traditionally the telecommunications carriers have often been free of most liability for harm as a result of the delay or non-delivery of a message or for any change in the content of the message.

69. The argument in support of exemption from liability that the telecommunications carrier could not foresee the consequences of a late or non-delivered message or of a change in its content because it did not know the content has not always been satisfactory in respect of telegraphic or telex service where the customer handed a message to the carrier to be transmitted. In many cases the personnel of the carrier fully understand the significance of the message being sent. In any case, when the damages were unforeseeable, at most the types or amount of damages might have been limited, but this did not justify complete exemption from liability.

70. Computer-to-computer telecommunications over a common carrier would seem on their face to be a prime example of a case in which the carrier has no idea of the content of the message, especially when the message is encrypted. Once the integrated services digital networks (ISDN) are installed, the carrier may not even know whether it is carrying data, written messages, voice or pictures; all will be transmitted as a string of digits. However, at the same time, the carriers are no longer limiting themselves to the provision of a basic telecommunications service. As the line between computer services and telecommunications has blurred,

<sup>13</sup>The related problems as to whether a bank should be exonerated for failure occurring while the instruction was transiting the telecommunications carrier which is itself immune from liability or while transiting a clearing-house or switch owned by or operated on behalf of a group of banks are treated in paragraphs 68 to 73 and 78 to 81.

the carriers are offering sophisticated enhanced services while the purveyors of computers and office equipment are linking their equipment together into networks. In many cases a bank or other user can receive the same or equivalent service from either a value-added network (VAN) or from the telecommunications carrier. Among the services available in many countries which no longer are the exclusive province of the carrier is the ability to switch messages. Therefore, even if the carrier's exemption from liability remains a good public policy in respect of the basic external telecommunication service, the exemption from liability for that basic service should be restricted to those services not available from other sources which do not have the same exemption.

71. In many countries telecommunications services have been provided by the State, often through the same ministry as the postal service. As a result, the telecommunications service has benefited from the general exemption of the State from liability. Where necessary, the general exemption has been buttressed by a specific regulation protecting the telecommunications service. In countries where the telecommunications service has been provided by private companies, the regulatory structure within which these companies have operated has permitted the limitation of liability in the tariffs filed by them.

72. However, the former monopoly position of the telecommunication carriers may no longer be self-evident and the question has been raised whether the exemption from liability should continue to be sustained. The deregulation of domestic carriers in the United States has already removed the former legal basis for exemption from liability in that country. It is not as yet clear whether the courts will still sustain clauses inserted in contracts by the carriers purporting to limit liability for their own negligence.

73. Questions of liability are a secondary issue within the broader debate over the future shape of public data-communications services. However, as major private users, such as banks, establish private networks in which they control the facilities and take the risk that messages will be late, non-delivered or altered in transmission, the public telecommunications carriers will be under increasing pressure to take an equivalent risk.

3. *Should an originating bank be exonerated from a delay or non-delivery of a funds transfer instruction after dispatch*

74. Since it has not been possible to hold the telecommunications carrier responsible for losses arising out of its failure to deliver a message properly, parties using telecommunications have acted to allocate between themselves the resulting losses. In the context of funds transfers by telegraph or telex, it has been normal for banks to provide in their contracts with their customers that the bank was not responsible for such losses. As a result the customers of the banks have borne the entire risk that the funds transfer message would not be

received or that it would be received in an altered condition. The reasonableness of such a contract provision was based upon the inability of the bank to exercise any control over the message once it was handed over to the carrier for dispatch.

75. The reasonableness of the contractual provision is less obvious when the message is sent by the bank on its own telex machine directly to the telex machine at the receiving bank. The carrier furnishes only the circuit and the switch to connect the two machines. The bank sends the message, it can request an answer-back to verify that the proper connection has been made, and it can send a test-key to establish the identity of the sender and verify that key portions of the message have not been altered by error. When there is any doubt whether the message has been received correctly or the message is particularly important, at the cost of a second transmission the sending bank can request the receiving bank to repeat the message in full.

76. All of the possibilities available to verify the receipt and the correct content of a funds transfer instruction sent by telex are also available to the sending bank in a computer-to-computer message. Additional safeguards are available in closed-user networks such as S.W.I.F.T. where all transactions entering the system are validated to ensure that they originate from an authorized terminal, that they meet mandatory format and message-text standards and that they are addressed to a valid S.W.I.F.T. recipient. The messages sent by each bank are assigned an out-put sequential number and the messages received by each bank are assigned an in-put sequential number reducing to a minimum the possibility that a message will be lost. Store-and-forward capability reduces the likelihood that a message cannot be delivered and undeliverable message reports assure the sending bank that any messages which could not be delivered were accounted for. Alternate routings are provided in case one of the switching centres is out of commission and member banks are instructed on how to access the S.W.I.F.T. network over the public switched network in case of failure of the regional processor.

77. Not all of the safety measures taken in a closed-user network such as S.W.I.F.T. are available to a bank operating over a public switched network. Nevertheless, procedures can be followed which reduce to a minimum the possibility that a failure in the communication net will go undetected and uncorrected by the sending bank. The availability of these techniques to avoid errors arising during transmission of the electronic funds transfer instruction raise serious questions as to whether banks should be free to avoid liability for such errors, even if they cannot seek reimbursement from the carrier.

F. *Malfunctioning in an electronic clearing-house or in a switch owned by or operated for a group of banks; loss-sharing by participating banks*

78. A clearing-house is an integral part of the funds transfer system. It may be operated by the central bank,

another large bank or the banking association. Alternatively, the clearing-house may be organized by a group of banks. In some countries on-line electronic funds transfer networks have been established in which the message switch without a net settlement function is operated for the participating banks by a company which is neither a bank, clearing-house nor a telecommunications carrier. The company may be a computer service bureau, value added network or the like.

79. In many cases the clearing-house or switch provides in its regulations or by contract with the participating banks that it has no liability or only limited liability for errors or fraud which occur at the clearing-house. If the clearing-house is operated by the central bank, the liability of the clearing-house or central bank may be limited or excluded by statute, by regulation or by general doctrines of law applicable to agencies or instrumentalities of the State. However, since the clearing-house is acting for the banks, exemption from liability may not pose the same level of concern as it does in respect of telecommunications carriers.

80. Nevertheless, it is significant that a clearing-house is an integral part of the funds transfer system. It cannot be argued that the banking system as a whole should not be held responsible to its customers for the failures of a clearing-house, as it could in the case of a telecommunications carrier. It seems evident that the originating party should in principle have an effective means of pursuing any claim arising out of such a failure.

81. At the same time, the collective nature of a clearing-house or switch for banking transactions may call for a sharing of the resulting losses among the participating banks. There are a number of ways in which a sharing of losses can be arranged, including insurance, constituting a compensation fund and levy upon all of the other participating banks. The losses which may be attributed to a clearing-house or a switch, and therefore subject to sharing, might include losses suffered by a bank as a result of following the procedures outlined for transfers through the clearing-house or switch. In particular, it may be appropriate to share losses which are attributable to a weakness in the security system, including the procedures and the algorithm for enciphering the funds transfer instructions.

#### G. Improper handling of transfer instructions

##### 1. Wrongful dishonour of instructions by a transferor bank and damages to the transferor

82. The transferor bank is responsible to the transferor for damages suffered as a result of the bank's wrongful dishonour of a proper funds transfer instruction. A bank which dishonours a credit transfer instruction should inform the transferor promptly of that fact and the reasons for so doing. The transferor's claim for any damages resulting from improper dishonour would be evaluated and settled as would any

other claim arising out of delay in effecting a funds transfer. Wrongful dishonour of a debit transfer instruction may have more serious consequences. When the transferee of a debit transfer instruction is notified that the instruction has been dishonoured, whether or not a reason is given for the dishonour, doubts as to the solvency and the integrity of the transferor naturally arise. If the dishonour was wrongful, the transferor bank (e.g. drawee of a cheque or bill of exchange) should also be responsible for the damages which were caused to the transferor in that connection.

##### 2. Inaction on debit instructions by the transferor bank within the required time-limits

###### (a) General rules for negotiable instruments

83. If the transferor bank does not act within the required time to honour or dishonour a debit transfer instruction or to give notice of its dishonour, the transferee has a claim against the transferor bank.

84. Except in France and other countries which follow the doctrine that a negotiable instrument transfers to the holder ownership of the fund (*provision*), i.e. the right in the account up to the amount of the instrument, the standard doctrine in respect of cheques and bills of exchange is that the instrument is not such an assignment and that the transferee (payee or other holder) has no right on the instrument against the transferor bank (drawee) until the instrument has been honoured. However, once the instrument has been presented to the transferor bank for honour, the bank may have a duty to the transferee or to the transferee bank to act within certain time-limits either to honour or to dishonour the instrument. If the instrument is dishonoured, the transferor bank owes a duty to the transferee to give a prompt notice of the dishonour. The party to whom the notice of the dishonour may or must be given varies in different countries and in some countries the notice must be given by formal protest.

85. These rules from the law governing paper-based negotiable instruments and their collection should be generally applicable to debit transfers in electronic form. However, since these rules usually appear in statutes governing negotiable instruments or in the law or agreements governing their collection, it may be necessary to extend them to electronic debit transfers.

###### (b) Delay in honouring debit transfer instruction

86. If the transferor bank honours the debit transfer instruction, but does so later than it should have under the applicable rules, the consequences of its delay depend on the means by which settlement was made. If the transferor bank provisionally settled for the instruction when it was presented, for example, by net settlement through a clearing-house, the delay in honouring would have no practical consequences. If settlement for the instruction was delayed until the instruction was honoured, the presenting bank would be denied use of its funds for the period of time of the delay. The transferee in turn may not have been given

credit for the transfer until the transferee bank received credit. The delay may, therefore, lay the basis for a claim of damages such as for loss of interest or, in an international transfer, for exchange losses.

(c) *Delay in dishonouring debit transfer instruction*

87. The delay in dishonouring a debit transfer instruction by the transferor bank sometimes arises because the transferor is on the edge of insolvency. In some cases, when there are not sufficient funds in the transferor's account to honour the instruction, the transferor bank may wish to give the transferor time to replenish the account so as to be able to cover the outstanding instruction. In other cases the bank may, whenever possible, wish time to decide whether to set off against the transferor's account other obligations due it from the transferor before it honours the funds transfer instruction. In either case, the instruction may subsequently be dishonoured.

88. In such a case, the debit transfer instruction may be deemed to be honoured or the transferee may be allowed to recover for the delay. However, the transferee may find it difficult to prove the amount of its loss in these circumstances. It would be possible to overcome this problem by placing on the transferor bank, which was in delay, the burden of proof of showing that the transferee had suffered no loss from the delay. Another way to achieve the same result would be to permit the transferee to recover the face amount of the instruction from the transferor bank and to assign to the bank the transferee's rights in the insolvency proceedings of the transferor.<sup>14</sup>

## H. Recoverable losses

89. An improperly executed transfer can lead to a loss of part or all of the principal amount transferred, as well as to consequential losses. In the context of a funds transfer, consequential losses can arise out of loss of interest, changes in exchange rates and indirect losses arising out of lost business opportunities and the like.

### I. Loss of principal

90. When an electronic funds transfer is credited to the wrong account, credited to the correct account for an excessive amount or processed twice, the transferor or the transferor bank risks losing the principal amount of the incorrect transfer. In most cases, the error can be rectified by a debit to the account of the incorrect transferee with a corresponding credit to the account of either the transferor (in which case the transfer has been reversed) or to the correct transferee (in which case the transfer has been made correctly).<sup>15</sup>

<sup>14</sup>The periods of time within which the transferor bank should honour a debit transfer instruction or should give a notice of the dishonour are discussed in chapter "Agreements to transfer funds and funds transfer instructions", A/CN.9/250/Add.3, paras. 77 and 78 (reproduced in this Yearbook, part two, I, B).

<sup>15</sup>The right of the bank to debit the incorrect transferee's account without his prior consent is discussed in chapter "Finality of honour". This chapter will be submitted to the Commission at its eighteenth session and will be reproduced in Yearbook 1985.

91. If the incorrect transferee withdraws and uses the funds, whether or not he knew of the error, and subsequently is unable to restore the amount used, the loss of principal must be allocated between the transferor and the bank or banks at which the error occurred. Similarly, if a transfer has been made fraudulently, the resulting loss of principal must be allocated between the transferor, whose account has been debited, and the bank or banks where the fraud may have occurred. In cases of loss of principal there is seldom any argument over the amount of loss which is to be allocated. The argument goes, rather, to determine which party should bear the burden of the loss, a subject covered by the general rules on liability discussed above.

### 2. Loss of interest

92. The one form of consequential damages which has generally been admitted in the law has been interest when payment of a sum due was late. Interest claims for late funds transfers by commercial customers of banks are now a frequent occurrence. In part this is because interest rates are high and the amount of interest which can be earned in even one day is measurable and may be worth claiming. In part it is because of the funds transfer possibilities made available to corporate treasurers by the new electronic funds transfer techniques. When commercial payments are made by slow paper-based credit transfer methods, a transferor cannot withhold his funds transfer instructions to the last moment before payment is due. It is understood that the time between the debit to the transferor's account and the credit to the transferee's account might be sizeable and somewhat unpredictable. However, now that some banks advertise their ability to transfer funds instantaneously, many commercial customers attempt to retain their cash until the last possible moment before issuing funds transfer instructions. Cash-management techniques have made public and corporate treasurers throughout the world conscious of the interest-earning potential of their cash balances.

93. Sometimes it is the transferee rather than the transferor who should have the right to claim interest. In the typical electronic credit transfer the transferor's account is debited before or at the time the funds transfer is sent. If the transfer is delayed, it is the transferee who is denied the use of the funds, not the transferor. Nevertheless, the transferee is currently understood to have no right against any bank, except perhaps his own, to claim interest because of delay in completing the funds transfer.<sup>16</sup> If indeed the payment is late under the underlying agreement, the transferee's claim for interest because of late payment would be against the transferor. The transferor in turn may have a right of reimbursement from his bank or from the bank at fault. The problem, however, is how to determine the exact period of time within which a funds transfer should take place. There are few agreed rules on the matter.

<sup>16</sup>By analogy to the law governing the carriage of goods, where the consignee of the goods has a right to claim for the damage even though the contracting parties are the shipper and the carrier, consideration might be given to providing the transferee a convenient means of claiming lost interest in appropriate cases.

94. With regard to adjusting interest charges between banks, there are several sets of rules governing the allocation of interest when the delay in transfer of the funds was due to the fault of one party or the other. Many of the rules governing the reimbursement of lost interest allow recovery only if the claim is for more than a specified amount. An interesting feature of the most prominent set of rules in use in the United States for compensation between banks when the claim is the result of an inter-bank funds transfer error is that the bank which receives money by mistake from another bank is required to pay to the bank which sent the money by mistake interest at the prevailing rate, less a service charge to the receiving bank. The rationale which lies behind this provision is that a bank which receives money will have the benefit of its use.

95. The existing rules, however, are limited in their application to the bilateral relation between any two banks or, in the case of some interbank telecommunications systems or clearing-houses, such as S.W.I.F.T. or CHIPS, to some losses caused by that system. They specifically do not apply to losses caused by or to third parties.

### 3. Exchange loss

96. With exchange rates fluctuating daily, customer claims for reimbursement of exchange losses arising out of late payments have become a more frequent occurrence. By the nature of the loss, claims for losses occasioned by an adverse movement of the exchange rates during the period of a late transfer will normally be made only by transferors of large sums. However, in the case of a devaluation by a significant percentage, customer claims arising out of international consumer transactions or consumer transfers should also be expected. The difficulties of establishing the appropriate period of time within which the transfer should have been made apply as much to losses occasioned by adverse movements of exchange rates as to loss of interest.

97. However, a claim for loss arising out of an adverse movement of the exchange rate will not normally be presented as such. Instead, it will be asserted that the date for conversion from one currency to the other should be the date on which the conversion would have been made if the transfer had taken place properly. Giving the customer the choice between the exchange rate on the date the conversion should have taken place and the exchange rate on the date it did take place is the policy expressed in articles 71 and 72 of the draft Convention on International Bills of Exchange and International Promissory Notes, prepared by a Working Group of the United Nations Commission on International Trade Law, which provide that in case of dishonour of an instrument by non-payment, "the amount to be paid in local currency is to be calculated, at the option of the holder, according to the rate of exchange ruling on the day of presentment or on the date of the actual payment". This option is given to the holder "in order to protect him against any loss he may suffer because of speculation by the party liable"

(A/CN.9/213, article 71, commentary, para. 8; *Yearbook 1982*, part two, II, A, 4).

### 4. Indirect damages

98. The least frequent, but potentially the most serious losses are the indirect damages suffered when a contract is lost, a penalty is incurred or a ship is withdrawn from a charter-party because a required payment was improperly handled. When these events occur, the damages can easily amount to many times the size of the transfer. In most electronic funds credit transfers the party who usually suffers the harm is the transferor who did not fulfill a contractual obligation to pay on a certain date or who missed a business opportunity which required having funds available at a particular place at a particular time. On occasion the harm may be suffered by the transferee who does not have the funds available when needed and who cannot find alternative funds.

99. In some systems the bank is held not to be liable for the indirect damages which it could not foresee at the time it received the funds transfer instruction from the transferor unless the bank deliberately delayed the funds transfer or was grossly negligent. This rule is a direct application of general principles of contract law. However, the limitation on indirect damages to those which are foreseeable is not completely satisfactory in the context of electronic funds transfers. It is particularly difficult for a transferor to give the required information to the proper parties in a legal system which does not recognize network liability. Even if the transferor bank may have had the requisite information to foresee the eventual indirect damages, it would often be the case that the information was not passed on to the intermediary bank or transferee bank at which the negligent actions occur. Neither the S.W.I.F.T. format for a customer transfer nor the ISO draft international standard telex format for a customer transfer (DIS 7746) provides a field for informing the intermediary bank of the possible consequences of a failure to credit the transferee's account by the pay date, although this information could always be added to the instruction by the sending bank. In one recent frequently discussed case, the intermediary bank was negligent in allowing its telex machine to run out of paper without cutting off the machine. It may be of interest that the same negligence which caused the funds transfer instruction to fail precluded the possibility that the intermediary bank could receive the information which might have made it possible for it to foresee the eventual damages.

100. It is often pointed out that, if banks were to be routinely held liable for indirect damages, the fee charged for funds transfers would need to increase several fold. However, transferors making particularly important transfers might be willing to pay a premium for guaranteed performance by the bank. Therefore, consideration should be given to a new "guaranteed performance" message category in addition to the existing categories. Failure to perform as guaranteed would subject the bank to indirect damages suffered as a result.

## II. INTERNATIONAL COMMERCIAL ARBITRATION

### A. Sixth session of the Working Group on International Contract Practices (Vienna, 29 August-9 September 1983)

#### 1. Report of the Working Group on the work of its sixth session (A/CN.9/245)<sup>a</sup>

#### CONTENTS

	<i>Paragraphs</i>
INTRODUCTION .....	1-11
DELIBERATIONS AND DECISIONS .....	12-220
I. Consideration of revised draft articles A to G of a model law on international commercial arbitration (A/CN.9/WG.II/WP.44) .....	17-56
II. Consideration of revised draft articles XIII to XXIV (A/CN.9/WG.II/WP.40) .....	57-123
III. Consideration of revised draft articles XXV to XXX (A/CN.9/WG.II/WP.46) .....	124-158
IV. Consideration of redrafted articles I to XII (A/CN.9/WG.II/WP.45) .....	159-220

#### INTRODUCTION

1. At its fourteenth session (1981) 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.<sup>1</sup>
2. The Working Group commenced its work at its third session (February 1982) 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.<sup>2</sup>
3. At its fourth session (October 1982) the Working Group completed its discussion on questions prepared by the secretariat on possible features of a draft model law and 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.<sup>3</sup>

4. At its fifth session (February 1983) the Working Group considered further features and draft articles of a model law and revised draft articles I to XXVI of a model law on international commercial arbitration. At that session the Working Group also considered draft articles 37 to 41 on recognition and enforcement of awards and on recourse against awards.<sup>4</sup>

5. According to a decision by the Commission to expand the membership of the Working Group to all States members of the Commission,<sup>5</sup> the Working Group consists of the following 36 States:

<sup>a</sup>"Report of the Working Group on International Contract Practices on the work of its fourth session" (A/CN.9/232; *Yearbook 1983*, part two, III, A).

<sup>1</sup>"Report 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).

<sup>2</sup>"Report 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).

<sup>3</sup>"Report of the United Nations Commission on International Trade Law on the work of its sixteenth session (1983), *Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17* (A/38/17), para. 143 (*Yearbook 1983*, part one, A).

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.

6. The Working Group held its sixth session at Vienna from 29 August to 9 September 1983. All the members were represented except Algeria, Central African Republic, Cuba, Egypt, Iraq, Peru, Senegal, Sierra Leone, Singapore, Trinidad and Tobago, Uganda and Yugoslavia.

7. The session was attended by observers from the following States: Argentina, Belgium, Bolivia, Ecuador, Finland, Ghana, Greece, Holy See, Lebanon, Morocco, Norway, Romania, Switzerland and Thailand.

8. The session was attended by observers from the following unit of the United Nations Secretariat: United Nations Industrial Development Organization. The session was also attended by observers from the following intergovernmental organizations: Asian-African Legal Consultative Committee, Commission of the European Communities 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.

9. The Working Group elected the following officers:

Chairman: I. Szasz (Hungary)  
Rapporteur: M. Mwagiru (Kenya)

10. 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; *Yearbook 1981*, part two, III);

(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; *Yearbook 1982*, part two, III, B);

(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; *Yearbook 1983*, part two, III, A);

(d) 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; *Yearbook 1983*, part two, III, D);

(e) Provisional agenda for the session (A/CN.9/WG.II/WP.43);

(f) Tentative draft articles A to G on adaptation and supplementation of contracts, commencement of

arbitral proceedings, minimum contents of statements of claim and defence, language in arbitral proceedings, court assistance in taking evidence, termination of arbitral proceedings, and period for enforcement of arbitral award (A/CN.9/WG.II/WP.44; reproduced in this *Yearbook*, part two, II, A, 2 (a));

(g) Revised draft articles XIII to XXIV on competence of arbitral tribunal, place and conduct of arbitration proceedings, rules applicable to substance of dispute, making of award and other decisions, and duration of mandate of arbitral tribunal (A/CN.9/WG.II/WP.40; *Yearbook 1983*, part two, III, D, I);

(h) Revised draft articles XXV to XXX on recognition and enforcement of arbitral award, and recourse against award (A/CN.9/WG.II/WP.46; reproduced in this *Yearbook*, part two, II, A, 2 (c));

(i) Redrafted articles I to XII on scope of application, general provisions, arbitration agreement and the courts, and composition of arbitral tribunal (A/CN.9/WG.II/WP.45; reproduced in this *Yearbook*, part two, II, A, 2 (b)).

11. The Working Group adopted the following agenda:

(a) Election of officers

(b) Adoption of the agenda

(c) Consideration of revised draft articles of a model law on international commercial arbitration

(d) Other business

(e) Adoption of the report

## DELIBERATIONS AND DECISIONS

12. The Working Group considered the following draft provisions of a model law prepared by the secretariat: tentative draft articles A to G, as contained in document A/CN.9/WG.II/WP.44; revised draft articles XIII to XXIV, as contained in document A/CN.9/WG.II/WP.40; revised draft articles XXV to XXX, as contained in document A/CN.9/WG.II/WP.46; and redrafted articles I to XII, as contained in document A/CN.9/WG.II/WP.45. The Working Group requested the secretariat to redraft these articles in the light of its discussion and decisions at the present session.

13. The Working Group decided to hold its seventh session from 6 to 17 February 1984 in New York, as authorized by the Commission at its sixteenth session.<sup>6</sup>

14. The Working Group was agreed that it was desirable to establish corresponding language versions of the text of the model law before it was sent to Governments and international organizations for comments. The Working Group therefore requested the secretariat to make the necessary arrangements for convening a Drafting Group in connection with the next session of the Working Group.

<sup>6</sup>*Ibid.*, para. 141.

15. The Working Group was agreed that it would be highly desirable to have summary records of its deliberations in view of the fact that the Working Group was now composed of all members of the Commission and the main legislative work would be undertaken in the Working Group.

16. As regards representation at the Working Group, a concern was expressed that many developing countries found it difficult, for financial reasons, to send delegates to the important meetings of the Group and that measures should be considered for achieving wider participation of delegates from such countries.

**I. Consideration of revised draft articles A to G of a model law on international commercial arbitration  
(A/CN.9/WG.II/WP.44)**

17. The Working Group considered revised draft articles A to G on adaptation and supplementation of contracts, commencement of arbitral proceedings, minimum contents of statements of claim and defence, language in arbitral proceedings, court assistance in taking evidence, termination of arbitral proceedings and period for enforcement of arbitral award, as set forth in document A/CN.9/WG.II/WP.44. These revised draft articles had been prepared by the secretariat on the basis of the discussion and decisions of the Working Group at its fifth session.<sup>7</sup>

**A. Adaptation and supplementation of contracts**

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

*"Article A*

*"Alternative A*

"(1) The arbitral tribunal has the power to adapt or supplement the contract upon request of a party provided that the parties have [expressly] authorized the arbitral tribunal [in writing] to do so; the arbitral tribunal shall decide on the adaptation or supplementation of the contract in accordance with any indication agreed upon by the parties as to [the specific conditions under which the contract should be adapted or supplemented] [the changed circumstances to which the contract or certain provisions of the contract should be adapted or any indication as to the issues which should be regulated in the contract].

"(2) The arbitral tribunal authorized to decide on the adaptation or supplementation of the contract shall apply [the provisions of this Law] [the provisions of articles . . . of this Law].

"(3) [The decision of the arbitral tribunal adapting or supplementing the contract] [The arbitral award in

which the arbitral tribunal adapts or supplements the contract] shall be binding on the parties and [the parties shall give effect to it] [shall be carried out by the parties] as an integral part of the contract."

*"Alternative B*

"(1) The person or persons appointed as arbitrators have the power to adapt or supplement the contract upon request of a party provided that the parties [expressly] authorized him or them [in writing] to do so; the person or persons shall decide on the adaptation or supplementation of the contract in accordance with any indication agreed upon by the parties as to [the specific conditions under which the contract should be adapted or supplemented] [the changed circumstances to which the contract or certain provisions of the contract should be adapted or any indication as to the issues which should be regulated in the contract].

"(2) The person or persons authorized to decide on the adaptation or supplementation of the contract shall apply [the provisions of this Law by analogy] [the provisions of articles . . . of this Law by analogy].

"(3) The decision adapting or supplementing the contract shall be binding on the parties and [the parties shall give effect to it] [shall be carried out by the parties] as an integral part of the contract."

19. The Working Group recognized the usefulness of procedures to which parties, in particular parties to long-term contracts, might resort in order to have their contracts adapted or supplemented and also recognized that procedural safeguards contained in such procedures would enhance legal certainty in international trade. For this reason some support was expressed for a provision in the model law granting the power to the arbitral tribunal to adapt and supplement contracts. Since some legal systems already granted such power to arbitral tribunals, unification of rules on this power was considered desirable. It was also felt that, once rules on the power of arbitral tribunals to adapt and supplement contracts had been internationally agreed in a model law, such rules would be more acceptable to States which had no provisions on or did not allow adaptation and supplementation of contracts in the framework of arbitration.

20. However, after extensive discussion, the view prevailed that adaptation and supplementation of contracts should not be dealt with in the model law. It was pointed out that there was no need for regulating this question in the model law since many legal systems already provided, outside the domain of arbitration, mechanisms for third party assistance in adapting and supplementing contracts. Also, there were great difficulties in unifying arbitral procedures on adaptation and supplementation of contracts.

21. It was further noted that in adaptation and supplementation of contracts it was difficult to separate questions pertaining to procedural law and questions pertaining to substantive law and that, therefore, the

<sup>7</sup>"Report of the Working Group on International Contract Practices on the work of its fifth session" (A/CN.9/233) paras. 15-45 (Yearbook 1983, part two, III, D).

model law, as a system of procedural rules, should not contain rules which may touch upon substantive rights of the parties. This difficulty in separating procedural and substantive questions would cause problems in interpretation of such rules. However, while recognizing this difficulty, it was noted by others that it should and could be made clear in the model law that only procedural aspects were regulated without regulating substantive conditions for adapting or supplementing a contract.

22. In regard of the practical effects of a rule on adaptation and supplementation of contracts it was also observed that in international trade suppliers of equipment and large industrial works were often economically stronger than buyers and that procedures for adaptation and supplementation of contracts might be used to the advantage of suppliers.

23. There was general agreement that the discussion in the Working Group was useful because it revealed the complexity of problems relating to adaptation and supplementation of contracts and possible solutions to these problems. This might prompt national legislators to adopt rules on adaptation and supplementation of contracts or improve existing rules taking into account the needs of modern international trade. Once national rules in this field and practice on the basis of such rules would be more developed, a harmonization might be achieved more easily.

#### **B. Commencement of arbitral proceedings**

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

##### *"Article B"*

"Unless otherwise agreed by the parties, the arbitral proceedings shall be deemed to commence on the date at which a request that a dispute be referred to arbitration is received by the respondent provided that such a request [sufficiently] identifies the claim."

25. The Working Group was of the view that article B defining the moment of the commencement of arbitral proceedings was useful.

26. There was wide support for the deletion of the word "sufficiently" placed between square brackets because it might cause unnecessary disputes in its interpretation.

27. It was observed that a request for arbitration in order to commence arbitral proceedings necessarily had to identify the claim and, since vague requests for arbitration could not commence arbitral proceedings, the requirement that a request for arbitration had to identify the claim should not be cast in the form of a proviso.

28. The prevailing view in the Working Group was that a general rule, modelled on article 2 (1) of the UNCITRAL Arbitration Rules, on the date when a

notice or other communication is deemed to have been received was useful and should be included in the model law.

#### *C. Minimum contents of statements of claim and defence*

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

##### *"Article C"*

"(1) The claimant shall state the facts supporting his claim, the points at issue and the relief or remedy sought. The respondent shall state his defence in respect of these particulars. [The parties may annex to their statements all documents they deem relevant or may add a reference to the documents or other evidence they will submit.]

"[(2) Unless otherwise agreed by the parties, the statements of the claimant and the respondent [, made in accordance with the preceding paragraph,] shall be communicated to the other party and to each of the arbitrators within a period of time to be determined by the arbitral tribunal.]

"[(3) During the course of the arbitral proceedings either party may amend or supplement his claim or defence unless the arbitral tribunal considers it inappropriate to allow such amendment having regard to the delay in making it or prejudice to the other party or any other circumstances.]"

##### *Paragraph (1)*

30. There was wide support in the Working Group for the policy of this paragraph including the provision in square brackets. However, it was noted that it might be too onerous for the claimant to state all points at issue already at this stage of the proceedings since he might become aware of all such points only after he had been fully informed about the defences the other party intended to raise.

##### *Paragraph (2)*

31. There was wide support in the Working Group for the policy of this paragraph. It was noted that the wording of this paragraph would have to be aligned with the wording of article XVII (3) in document A/CN.9/WG.II/WP.40 (*Yearbook 1983*, part two, III, D, 1). It was also noted that the words between square brackets were not necessary and could be omitted.

32. A suggestion was made that it should be made clear in this paragraph whose duty it was to communicate the statements to the other party.

##### *Paragraph (3)*

33. There was general support in the Working Group for this paragraph. It was noted, however, that the question whether this provision was mandatory or not would be discussed in the context of article I *ter* (as contained in document A/CN.9/WG.II/WP.45) when the question of mandatory and non-mandatory charac-

ter of individual provisions of the model law would be considered generally.

#### D. *Language in arbitral proceedings*

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

##### *"Article D"*

"(1) The parties are free to agree on the language or languages to be used in the arbitral proceedings. Failing such agreement, the arbitral tribunal shall determine the language or languages to be used in the proceedings. This agreement or determination, unless otherwise specified therein, shall apply to any written statement by a party, any oral hearing, and any award, decision or other communication by the arbitral tribunal.

"(2) The arbitral tribunal may order that any documentary evidence shall be accompanied by a translation into the language or languages agreed upon by the parties or determined by the arbitral tribunal."

35. There was general support in the Working Group for the policy of this article.

36. A view was expressed that the wording was unnecessarily detailed in listing and distinguishing cases to which the agreement on or the determination of the language or languages of the proceedings applied and cases in which the arbitral tribunal may order a translation and that maximum flexibility should be left to the parties and the arbitral tribunal in agreeing on or determining this issue. However, the view prevailed that the present wording should be retained because, in view of the great practical importance of the language used in arbitral proceedings, it was useful to draw the attention of the parties to different instances in which the agreed or determined language could affect their position in the proceedings.

#### E. *Court assistance in taking evidence*

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

##### *"Article E"*

"(1) The arbitral tribunal or a party [with the approval of the arbitral tribunal] may request from [a court] [the Court specified in article V] assistance in taking evidence. The court shall execute such a request by either taking the evidence itself or by ordering a party or a third person to give evidence to the arbitral tribunal.

"(2) Where an arbitration takes place outside this State, the arbitral tribunal or a party [with the approval of the arbitral tribunal] may submit such a request through a court of the State where the arbitration takes place. Such a request shall be treated by the court referred to in paragraph (1) as a request by that foreign court."

#### *Paragraph (1)*

38. There were divergent views in the Working Group on the question whether it was useful to have a provision on court assistance in the State where the arbitration took place. Under one view opposing the inclusion of a provision on court assistance in the model law, such a provision would encourage dilatory tactics by making requests for assistance to courts and, also, it would be contrary to the private nature of arbitration to involve courts in taking evidence. However, the prevailing view was that such a provision would be useful because it would enable the parties to obtain relevant evidence when a person would not comply with a request to give such evidence. A suggestion was made to indicate in that paragraph that court assistance included the possibility of a request by a court to a foreign competent body to gather evidence in that foreign State.

39. The proponents of the prevailing view suggested that it was necessary to prevent the possibility of abuse of court assistance. Under one view this could be achieved by adopting the words in the first square brackets according to which the arbitral tribunal had to approve the request for court assistance because an arbitral tribunal would not have an interest in deliberately abusing court assistance. Under another view abuse could only be prevented by more detailed rules specifying the grounds on which a court could refuse to give assistance; such detailed rules could either be made applicable by reference to domestic rules on court assistance or by including appropriate rules in the model law.

40. Some representatives suggested that only parties may request court assistance and the arbitral tribunal should not have a right to refuse to approve a request for court assistance nor should it be engaged in gathering evidence to be used in arbitral proceedings because this would be contrary to the adversary principle according to which the parties have to produce evidence in support of their case.

41. The Working Group requested the secretariat to prepare alternative wordings in the light of the discussion.

#### *Paragraph (2)*

42. Divergent views were expressed in the Working Group on the question whether the model law should have a provision on international court assistance in taking evidence. Under one view it was desirable to include in the model law a unilateral obligation of domestic courts to give assistance to foreign arbitral tribunals because this would facilitate the functioning of international commercial arbitration. However, the view prevailed that it was not feasible for a model law on arbitration to regulate such a complex matter.

43. In support of the prevailing view it was noted that international court assistance in taking evidence was an issue which fell within the domain of international co-operation between States and that such international

co-operation could only be achieved in a satisfactory way by international instruments such as conventions or bilateral treaties. An acceptable system of international court assistance could not be established unilaterally through a model law since the principle of reciprocity and bilaterally or multilaterally accepted procedural rules were essential conditions for the functioning of such a system.

44. It was further noted that, even if a unilateral system of international court assistance could be established, it would be necessary to include in the model law more detailed procedural rules and that this would not be in balance with other parts of the model law where procedure was not provided in such detail. It was also observed that conditions for giving court assistance to an arbitral tribunal in a foreign State might have to touch upon issues which were in the domain of the respective foreign procedural law and that such interference with foreign procedural rules was to be avoided.

45. However, the view favouring the inclusion of a provision on international court assistance in the model law suggested that it was feasible for the model law to have a provision in the context of domestic law on the status of requests made from abroad without interfering with procedural rules of foreign States.

46. The Working Group decided to reconsider the matter at its next session and requested the secretariat to redraft this provision in the light of the discussion.

#### F. Termination of arbitral proceedings

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

##### *"Article F"*

"(1) The arbitral proceedings are terminated:

"(a) by the [making] [delivery] of the final award which constitutes or completes the disposition of all claims submitted to arbitration; or

"(b) by an agreement of the parties that the arbitral proceedings are to be terminated; or

"(c) by an order of the arbitral tribunal in accordance with paragraph (2) of this article.

"(2) After having given suitable notice to the parties, the arbitral tribunal shall issue an order for the termination of the arbitral proceedings when the claimant withdraws his claim or if for any other reason the continuation of the proceedings becomes unnecessary or inappropriate.

"(3) The mandate of the arbitral tribunal is terminated with the termination of the arbitral proceedings, subject to the provisions of article XXIV."

##### *General considerations*

48. Some support was expressed for the deletion of this article because it was not necessary to regulate in

such detail the ending of the mandate of the arbitral tribunal. However, the view prevailed that the article should be retained since there may be other cases where the moment of termination of arbitral proceedings may be important, like, for example, the continuation of the running of a limitation period or the possibility to institute legal proceedings before another forum on the same dispute.

##### *Paragraph (1)*

49. The Working Group adopted subparagraph (a) with the word "making" instead of the word "delivery".

50. Regarding subparagraph (b) it was suggested that the wording should define more clearly the moment of the termination of the arbitral proceedings. It was also suggested that subparagraph (b) should make clear whether an agreement of the parties to terminate arbitral proceedings covered only specific agreements to that effect or also cases where the parties had agreed in advance on a deadline for making the award.

51. Regarding subparagraph (c) it was suggested that, while the arbitral tribunal should be under an obligation to issue an order for the termination of the proceedings, in the absence of such an order the interested party should have a possibility to establish that the proceedings had terminated.

##### *Paragraph (2)*

52. The Working Group was of the view that the withdrawal of a claim should not *ipso facto* terminate arbitral proceedings since the defendant might have a legitimate interest in a final settlement of the dispute.

##### *Paragraph (3)*

53. There was general support for paragraph (3) of this article. It was noted that this paragraph should include a reference to article XXX (3) as suggested in footnote 16 of document A/CN.9/WG.II/WP.44.

#### G. Period for enforcement of arbitral awards

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

##### *"Article G"*

"Enforcement of an arbitral award shall be refused if the request is made after ten years have elapsed from the date at which the award was [made] [received by the party requesting the enforcement] [received by the party against whom enforcement is sought]. [However, if the award contains an obligation which is to be performed later than two years after the date at which the award was made, the period for enforcement commences to run on the date at which the obligation is to be performed.]"

55. Some support was expressed for the policy of this article because a time period for enforcement of arbitral awards would contribute to certainty in international trade.

56. However, the view prevailed that the model law should not contain a provision on this point. In support of this view it was noted that many legal systems already had rules on the period for enforcement of arbitral awards, either by assimilating for this purpose arbitral awards to court judgments or by special legislation. Harmonization of these rules would be difficult to achieve since they were based on differing national policies closely linked to procedural law aspects of States.

## II. Consideration of revised draft articles XIII to XXIV (A/CN.9/WG.II/WP.40)<sup>b</sup>

57. The Working Group proceeded to a consideration of revised draft articles XIII to XXIV of a model law on international commercial arbitration, as set forth in document A/CN.9/WG.II/WP.40. These 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.<sup>c</sup>

### *Article XIII*

58. The text of article XIII as considered by the Working Group was as follows:

#### *"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]."

<sup>b</sup>Yearbook 1983, part two, III, D, 1.

<sup>c</sup>"Report of the Working Group on International Contract Practices on the work of its fourth session" (A/CN.9/232; Yearbook 1983, part two, III, A).

#### *Paragraph (1)*

59. The Working Group adopted this paragraph.

#### *Paragraph (2)*

60. The Working Group adopted this paragraph, subject to the following modifications. In the first sentence, the wording between the first square brackets was preferred to the alternative wording between the second square brackets. In the penultimate sentence, the words "taken up" were considered as too vague; accordingly, the secretariat was requested to propose a clearer wording.

61. In this connection, a question was raised as to the legal consequences of the failure of a party to invoke lack of jurisdiction in accordance with paragraph (2). If the legal consequence was that such party was precluded from later invoking lack of jurisdiction, it was doubted whether such solution was compatible with paragraph (1) (a) of article XXVII or XXVIII and article XXX (1) under which lack of a valid arbitration agreement could be relied on, although it was recognized that such reliance might be limited by operation of the waiver rule embodied in draft article I *quater*. It was felt that this question could appropriately be dealt with in an overall review of the various provisions of the model law relating to jurisdiction and validity of arbitration agreement.

#### *Paragraph (3)*

62. The Working Group accepted the policy underlying this paragraph, except for the last sentence which was placed between square brackets.

63. As regards this last sentence, there was some support for allowing a party to contest before a court the ruling of an arbitral tribunal that it has no jurisdiction. It was suggested that the aim of such recourse need not be to have the same arbitrators continue the proceedings but could be limited to a decision on the existence of a valid arbitration agreement.

64. The prevailing view, however, was that the last sentence of paragraph (3) should not be retained. It was stated that the ruling of an arbitral tribunal that it lacked jurisdiction was final and binding as regards these arbitral proceedings but did not finally settle the question whether the substantive claim was to be decided by a court or by an arbitral tribunal. It was also suggested that the substantive claim would consequently be submitted to a court which would then be able to rule on this question. Yet another view was that any formal ruling by the arbitral tribunal was in the form of an award against which a party might bring an action for setting aside, although it was noted by others that the present wording of draft article XXX did not make it sufficiently clear whether such an award would be covered.

65. One delegation proposed to add to article XIII a paragraph along the lines of previous draft paragraph (3) of article 28 (set forth in document A/CN.9/WG.II/WP.38; Yearbook 1983, part two, III, B, 2).

*Suggested new paragraph (4)*

66. The Working Group considered in this context the revised version of paragraph (3) of article IV which the secretariat had suggested as new paragraph (4) of article XIII (see A/CN.9/WG.II/WP.45, footnote 17):

"(4) Where, after arbitral proceedings have commenced, a party invokes before a court lack of jurisdiction of the arbitral tribunal, whether impliedly by bringing a substantive claim or expressly by requesting a decision on the jurisdiction of the arbitral tribunal directly from the court without first raising this plea before the arbitral tribunal, the arbitral tribunal may continue the proceedings while the issue is pending with the court."

67. The Working Group agreed with the two policies underlying this provision. One policy was that the arbitral tribunal should be empowered to continue the proceedings while the question of its jurisdiction was pending with a court, although it was understood that this provision should not preclude a court from ordering a stay or suspension of the arbitral proceedings. The other policy was that a party had the right, in addition to the plea regulated in paragraphs (2) and (3) of article XIII, to request a ruling on the competence of the arbitral tribunal directly from a court.

68. It was felt, however, that the wording of paragraph (4) was not sufficiently clear, in particular, as regards its relationship to article IV. It was suggested, therefore, to deal separately with the case where lack of jurisdiction was invoked impliedly by bringing a substantive claim before the court, which was dealt with in article IV, and, on the other side, with the case where the question of competence was expressly (and solely) brought before the court. It was suggested that this important right of the party—and the concurrent power of the court—deserved a more direct expression and treatment than at present accorded in draft paragraph (4). Finally, it was noted that this provision would have to be examined in an over-all review of the provisions relating to jurisdiction and validity of arbitration agreement.

69. The Working Group requested the secretariat to revise this provision in the light of the above discussion.

*Article XIV*

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

*"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."

71. The Working Group adopted the policy underlying article XIV according to which the arbitral tribunal had an implied power to order certain interim measures of protection. While there was some support for the scope of possible measures as laid down in article XIV, the prevailing view was that this scope was too limited and too much geared to only one type of transaction, i.e. sale of goods. It was decided, therefore, to adopt a more general formula (e.g. "interim measures of protection"), with a possible restriction to those measures which the parties themselves could have achieved by agreement, thus excluding any measures affecting the rights of third parties.

72. Divergent views were expressed on the question of enforceability as dealt with in the last sentence of article XIV. Under one view, executory assistance by courts was desirable and should be available not only to the arbitral tribunal but also to a party, in particular the one favoured by the interim measure. Under another view, which the Working Group adopted after deliberation, the last sentence should be deleted since it dealt in an incomplete manner with a question of national procedural law and court competence and was unlikely to be accepted by many States. It was noted that the model law, in its article IV (2), envisaged enforcement of interim measures ordered by a court and that the power of the arbitral tribunal under article XIV was of practical value even without executory assistance by courts. It was understood that the deletion of the last sentence should not be read as a preclusion of such executory assistance in those cases where a State was prepared to render such assistance under its procedural law.

*Article XV*

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

*"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,] 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."

*Paragraph (1)*

74. The Working Group adopted paragraph (1) in the following modified form:

"Subject to the provisions of this Law, the parties are free to agree on the procedure to be followed by the arbitral tribunal in conducting the proceedings."

*Paragraph (2)*

75. The Working Group adopted paragraph (2) subject to the deletion of the words placed between square brackets. The Working Group reaffirmed its view that the power conferred upon the arbitral tribunal by this paragraph includes the power to adopt its own rules of evidence. While some considered it desirable to express this understanding in the last sentence, the prevailing view was that the present wording of this sentence already covered this point in sufficient clarity.

*Article XVI*

76. The text of article XVI as considered by the Working Group was as follows:

*"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,] 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.”

*Paragraph (1)*

77. The Working Group adopted paragraph (1) subject to the deletion of the words placed between square brackets.

*Paragraph (2)*

78. The Working Group adopted the policy underlying paragraph (2) which allowed the arbitral tribunal, subject to contrary agreement by the parties, to meet for certain purposes at places other than the place of arbitration. It was felt that the need for meeting at another place may not only arise with regard to the types of meeting listed under (a), (b) and (c) but also, for example, for hearings of experts or normal hearings with the parties. It was suggested, therefore, to adopt a more general formula which would also cover such other meetings.

79. On the other hand, a concern was expressed that such wide powers of the arbitral tribunal might be in conflict with the expectations of the parties when

agreeing on the place of arbitration, taking into account considerations of convenience and costs.

*Article XVII*

80. The text of article XVII as considered by the Working Group was as follows:

*"Article XVII"*

"(1) [Failing agreement by the parties,] 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].

"(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,] 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.]"

*Paragraph (1)*

81. The Working Group adopted paragraph (1) subject to the following modifications. While some support was expressed for deleting the introductory phrase "Failing agreement by the parties", the prevailing view was to retain such a proviso, however in a different wording: "Subject to any contrary agreement by the parties". As regards subparagraph (a), the Working Group decided not to retain the wording placed between square brackets. As regards subparagraph (b), the Working Group also decided to delete the words placed between square brackets, although there was some support for retaining them.

*Paragraph (2)*

82. The Working Group adopted this paragraph with the word "sufficient" placed between the first square brackets and, accordingly, without the alternative wording placed between the second square brackets since a fixed time-period was considered as inappropriate in view of the great variety of cases.

*Paragraph (3)*

83. The Working Group adopted this paragraph with the word "communicated" placed between the first square brackets in lieu of the alternative wording "made available". The same preference was expressed with regard to the second sentence where, accordingly, the words "made available" are to be replaced by the word "communicated". It was noted that the paragraph laid down the important principle that each party should receive all relevant documents or information without, however, regulating the mechanics of how precisely and by whom the documents would have to be communicated to the party.

*Paragraph (4)*

84. The Working Group adopted this paragraph with the proviso placed between square brackets. It was suggested, however, that any contrary agreement had to be concluded before the appointment of the arbitrators so that any arbitrator when accepting his mandate would know about the restriction on his power to appoint experts.

*Paragraph (5)*

85. The Working Group adopted the first sentence of this paragraph. It decided to delete the second sentence placed between square brackets since it dealt in an unsatisfactory manner with a detail question not appropriate for inclusion in a law. A suggestion was made that in this article consideration be given, under appropriate circumstances, to safeguarding trade secrets.

*Article XVIII*

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

*"Article XVIII"**"Alternative A:*

"[Unless otherwise agreed by the parties], 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] the arbitration proceedings shall continue;

"(c) a party, duly notified in accordance with article XVII (2), fails to appear at a hearing, the arbitral tribunal may proceed with the arbitration;

"(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."

*"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."

87. The Working Group considered whether alternative A of article XVIII or the shorter version presented as alternative B was more appropriate for inclusion in the model law. There was some support for alternative A since it provided more detailed rules on the important subject of default proceedings. The prevailing view, however, was to include a more general provision along the lines of alternative B, with one or two points added from alternative A.

88. A point to be included is the claimant's failure to communicate his statement of claim (or to state his case) as covered by subparagraph (a) of alternative A.

89. Another point which was noted as missing in alternative B was the possible assessment by the arbitral tribunal of the respondent's failure to communicate his statement of defence. Divergent views were expressed as to whether and, if so, in which way this point should be regulated in the model law. Under one view, such failure by the respondent may be treated as a denial of the claim. Under another view, it was sufficient and necessary to provide that such failure shall not be treated as an admission of the claimant's allegations. Under yet another view, the arbitral tribunal should be given full discretion by not providing any rule on the legal assessment of such failure. The Working Group was agreed that this question should be decided at its next session in the light of draft provisions prepared by the secretariat.

90. The Working Group was also agreed that the provision should not contain any fixed time-period. In view of the great variety of cases, it was more appropriate to use a more flexible formula such as "a reasonable time" or "sufficient time" or merely to refer to the "time stipulated by the parties or fixed by the arbitral tribunal". This would also include the possibility, which was generally supported, that any time-period could be extended by the arbitral tribunal in appropriate cases.

91. Finally, the Working Group adopted the view that the provision should not be mandatory.

92. The Working Group requested the secretariat to prepare a revised draft provision on the basis of the above discussion, taking into account also the drafting suggestions which were made during the deliberations.

#### *Article XIX*

93. The text of article XIX as considered by the Working Group was as follows:

##### *"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."

#### *Paragraph (1)*

94. There was some support for the wording placed between the second square brackets which was understood as referring to the law of one given State. The prevailing view, however, was to adopt the wording between the first square brackets, to which the words "as applicable to the substance of the dispute" should be added. The reference to "the rules of law" (instead of "the law") was deemed preferable since it provided the parties with a wider range of options and would, for example, allow them to designate as applicable to their case rules of more than one legal system, including rules of law which had been elaborated on the international level. While some representatives would have preferred an even wider interpretation or an even broader formula, to include, for example, general legal principles or case law developed in arbitration awards, the Working Group, after deliberation, was agreed that this was too far-reaching to be acceptable to many States, at least for the time being.

95. The Working Group noted that the word "pertinent" placed between square brackets was designed to refine the rule of interpretation, contained in the second sentence, with regard to the case where a national legal system had two bodies of law dealing with the same subject-matter (e.g. law on domestic sale of goods and

law on international sale of goods). While some support was expressed for retaining the word "pertinent" or similar wording, the prevailing view was that it should be deleted since it was self-evident or incomplete.

#### *Paragraph (2)*

96. There was considerable support for aligning this paragraph with the solution adopted in paragraph (1) and not to require the arbitral tribunal to apply conflict of laws rules. A provision according to which the arbitral tribunal "shall apply the rules of law it considers appropriate" was deemed desirable not only because it would be in harmony with paragraph (1) but also because it would avoid the difficulties of applying rules of private international law and because it would better accord with present practices in international commercial arbitration.

97. However, the prevailing view was to retain paragraph (2) in its present form. It was felt that a more cautious approach in paragraph (2) was advisable in view of the fact that paragraph (1) already presented a rather progressive step. While recognizing the disparity between the two paragraphs, it was deemed to be acceptable in view of the fact that paragraph (1) was addressed to the parties who could take advantage of the wider scope while paragraph (2) was addressed to the arbitral tribunal and applied only in the case where the parties had not made their choice.

#### *Paragraph (3)*

98. There was some support for retaining paragraph (3), though possibly with some modifications. For example, it was suggested to align the reference to trade usages with the provision of article 9 of the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980). It was also suggested that the reference to the terms of the contract (to be redrafted as "terms of any agreement") should be incorporated into paragraph (1) since this formed the basis or starting-point of the decision of the dispute.

99. The prevailing view, however, was not to retain this provision in view of the many questions and concerns it raised. For example, the reference to the terms of the contract could be misleading where such terms were in conflict with mandatory provisions of law or did not express the true intent of the parties. Also, this reference did not belong in an article dealing with the law applicable to the substance of the dispute and was not needed in a law on arbitration, though appropriate in arbitration rules. As regards the reference to trade usages, the concerns related to the fact that their legal effect and qualification was not uniform in all legal systems. Also, where they derived from a national law they were covered already by paragraph (1) or (2).

#### *Paragraph (4)*

100. The Working Group adopted this paragraph, although it was recognized that this type of arbitration was not known in all legal systems.

*Article XX*

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

*"Article XX"*

"(1) When there are three [or another uneven number of] 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.] 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."

*Paragraph (1)*

102. The Working Group adopted the majority-principle embodied in this paragraph. It was agreed that the wording of this provision could be simplified along the following lines: "In arbitration proceedings with more than one arbitrator, any award or other decision of the arbitral tribunal shall be made, unless otherwise agreed by the parties, by a majority of all its members".

103. In view of the importance of the decisions covered by paragraph (1), the Working Group did not adopt a suggestion according to which paragraph (1) should adopt the approach of paragraph (2) and give the presiding arbitrator the decisive vote if there was no majority for a decision envisaged in that paragraph.

*Paragraph (2)*

104. The Working Group adopted the principle that questions of procedure, for the sake of expediency and efficiency, may be left to a presiding arbitrator, provided that the arbitral tribunal or the parties had authorized him to do so. It was agreed that, once this authorization had been given, an individual decision on procedure should not be subject to revision by the arbitral tribunal.

*Article XXI*

105. The text of article XXI as considered by the Working Group was as follows:

*"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."

*Paragraph (1)*

106. The Working Group adopted this paragraph, subject to improvement of its wording along the following lines: "If, during arbitration proceedings, the parties settle the dispute, the arbitral tribunal shall terminate the proceedings and, if requested by the parties and not objected to by the arbitral tribunal, record the settlement in the form of an arbitral award on agreed terms".

*Paragraph (2)*

107. The Working Group adopted this paragraph. It was noted that the last sentence might later have to be modified in order to qualify this statement as regards reasons for recourse against such an award or its enforcement.

*Article XXII*

108. The text of article XXII as considered by the Working Group was as follows:

*"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.

"(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."

*Paragraph (1)*

109. The Working Group adopted this paragraph, subject to improvement of its second sentence along the following lines: "In arbitration proceedings with more than one arbitrator, the signatures of the majority of all members of the arbitral tribunal shall suffice, provided that the reason for any missing signature is stated".

*Paragraph (2)*

110. The Working Group adopted this provision.

**Paragraph (3)**

111. The Working Group noted that the date and the place at which an arbitral award was made was of great importance, in particular, with regard to its recognition and enforcement and any possible recourse against such award.

112. As regards the date, the Working Group decided to require in paragraph (3) that "the award shall state its date".

113. As regards the place, the Working Group adopted the principle that the award shall be made at the place of arbitration as determined pursuant to article XVI (1). However, divergent views were expressed as to how one could best link this principle with the requirement of establishing clearly the place at which the award was made.

114. Under one view, the above principle should be embodied in the model law as a rule binding on the arbitral tribunal, followed by a provision according to which the award shall state the place at which it is made. The prevailing view, however, was to adopt the approach taken in paragraph (3), i.e. to require that the award state the place of arbitration as determined pursuant to article XVI (1), followed by a provision according to which the award shall be deemed to have been made at that place. It was noted that the making of the award was a legal act which in practice was not necessarily one factual act but, for example, done in deliberations at various places, by telephone conversation or correspondence.

115. While there was some support for retaining the word "irrebuttably", the prevailing view was in favour of its deletion. It was understood, however, that such deletion should not be construed as making the presumption rebuttable.

**Paragraph (4)**

116. The Working Group adopted this paragraph.

*Article XXIII*

117. The text of article XXIII as considered by the Working Group was as follows:

*"Article XXIII"**"Alternative A:"*

"The [making] [delivery] of the final award, which constitutes or completes the disposition of all claims submitted to arbitration, terminates the mandate of the arbitral tribunal, subject to the provisions of article XXIV."

*"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."

118. There was some support for alternative B since it addressed in a more direct manner the question which the article was intended to answer, i.e. to make clear that the making of, for example, interim, interlocutory or partial awards did not terminate the mandate of the arbitral tribunal. The prevailing view, however, was in favour of the approach taken in alternative A. Yet, it was deemed desirable to express in some provision of the model law in positive terms that an arbitral tribunal had the power to render awards or decisions of the kind listed by way of example in alternative B.

119. It was noted that the rule in alternative A did not add anything to what was provided in (the more recently drafted) article F, paragraphs (1) (a) and (3). There was, thus, no need for maintaining article XXIII, unless it was used for incorporating the above idea concerning interim and similar awards or article F itself was later reconsidered and changed.

*Article XXIV*

120. The text of article XXIV as considered by the Working Group was as follows:

*"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."

**Paragraph (1)**

121. The Working Group adopted this paragraph including the wording between the two square brackets, subject to possible revision of the time-periods fixed therein. It was felt that the different time-periods for

the various actions envisaged in this and the following paragraph should be harmonized. It was also noted that these time-periods should be taken into account when considering the length of the time-period during which an action may be brought under article XXX for setting aside or remission.

*Paragraph (2)*

122. The Working Group adopted this paragraph. It was noted with approval that this paragraph provided for the making of an additional award only if no further hearings or evidence were required.

*Paragraph (3)*

123. The Working Group adopted this paragraph.

**III. Consideration of revised draft articles XXV to XXX  
(A/CN.9/WG.II/WP.46)**

124. The Working Group proceeded to a consideration of revised draft articles XXV to XXX of a model law on international commercial arbitration, as set forth in document A/CN.9/WG.II/WP.46. These revised draft articles had been prepared by the secretariat on the basis of the discussion and decisions of the Working Group at its fifth session.<sup>9</sup>

*General discussion*

125. The Working Group was agreed that it was desirable to discuss general matters of policy before embarking upon a detailed consideration of the revised draft articles on recognition and enforcement of arbitral awards and on recourse against such awards. The main questions of policy, which were inter-related, were (a) whether the model law should contain provisions on recognition and enforcement of awards made in the territory of the State of the model law and of awards made outside that State, (b) if so, whether and to what extent separate treatment of these two categories was necessary and justified, and (c) how closely any provisions on recognition and enforcement should follow the corresponding articles of the 1958 New York Convention.

126. Divergent views were expressed on whether provisions on recognition and enforcement should be retained in the model law. Under one view, there was no need for such retention. In support of this view, different reasons were advanced in respect of foreign awards and of "domestic" awards.

127. It was pointed out that provisions concerning foreign awards were not necessary in view of the existence of the 1958 New York Convention, which

many States adhered to. It was also noted that a substantial number of these States had made use of the reciprocity reservation, the effect of which should not be adversely affected by any provision of the model law. Furthermore, States which were not members to that Convention were unlikely to adopt the very similar provisions of the model law (i.e. articles XXVI and XXVIII). Finally, these provisions were thought to give rise to uncertainty and possible conflicts with that Convention.

128. As regards recognition and enforcement of "domestic" awards, it was stated that this matter was satisfactorily dealt with in the individual national laws which often treated such awards like court decisions rendered in the State. It was also pointed out that the existing national laws often set less onerous conditions than envisaged in the model law and, for example, did not provide for a special procedure for obtaining recognition or enforcement of "domestic" awards. Finally, it was unacceptable to retain the system of double control set forth in articles XXVII and XXX.

129. The prevailing view, however, was to include in the model law provisions on recognition and enforcement of awards made within and outside the territory of the State of the model law. One reason advanced in support of this view was that a model law on international commercial arbitration would be incomplete if it did not regulate this important matter. Another consideration, for which there was considerable and apparently growing support, was that one should strive for uniform treatment of all awards in international commercial arbitration irrespective of their place of origin. Yet, the main reason supporting the prevailing view was the conviction that the above concerns expressed in opposition to any provisions on recognition and enforcement did not necessitate or warrant deletion of those articles.

130. As regards foreign awards, it was thought that provisions in the model law which were not in conflict with the 1958 New York Convention were useful by establishing, for those States prepared to adopt them, a supplementary network, though on a unilateral basis, of recognition and enforcement of awards not falling under a multilateral or bilateral treaty. In order to avoid any conflict, it was suggested that the model law should not adversely affect the reciprocity reservation adopted by a substantial number of States members to the 1958 New York Convention and that the provisions of the model law should be closely modelled on the corresponding articles of that Convention.

131. As regards awards made in the territory of the State of the model law, provisions on recognition and enforcement were deemed desirable for the sake of unification and certainty, since the present treatment, even if equated to that of court decisions, did not lead to uniform results in all legal systems. It was also pointed out that the "domestic" awards covered by the model law were of a special nature in that they related

<sup>9</sup>"Report of the Working Group on International Contract Practices on the work of its fifth session" (A/CN.9/233) paras. 121-195 (Yearbook 1983, part two, III, D).

to international commercial arbitration as defined in article I.

132. The proponents of this view recognized that articles XXV and XXVII envisaged more onerous conditions than presently existing in a number of legal systems and suggested, therefore, that these provisions should be seen as setting maximum standards which would allow States to require less than provided therein. Furthermore, it was proposed to reconsider the contents of these articles (and of those concerning foreign awards) with regard to the issue of recognition standing alone, i.e. where it is not merely relevant as a pre-condition of enforcement. Finally, it was recognized that the double control under articles XXVII and XXX was undesirable and should be avoided by an appropriate technique (e.g. by referring a party against whom enforcement is sought within the time-period set in article XXX to the procedure of setting aside for invoking any objections against the award).

133. The Working Group, after deliberation, was agreed not to take a final decision on these policy matters. Recognizing that these matters were of great importance and ultimately related to a question of acceptability by any given State, it was deemed desirable to retain provisions on recognition and enforcement of "domestic" and of foreign awards, closely modelled on the 1958 New York Convention, but taking into account the need for reconsidering the issue of recognition and of the relationship between articles XXVII and XXX. It was suggested that a final decision might not be appropriate before all Governments had been given the opportunity to comment on the draft model law.

#### *Articles XXV and XXVI*

134. The Working Group considered articles XXV and XXVI together. The text of these articles 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.\*

"An application shall be made in writing to the competent court, 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 [duly certified] translation of these documents into such language [, certified by an official or sworn translator or by a diplomatic or consular agent]."

\*The procedure set forth in this article is intended to set maximum standards. It would, thus, not be contrary to the harmonization to be achieved by the model law if a State retained an even less onerous procedure.

#### *"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:

"An application shall be made in writing to the 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."

135. The Working Group, after deliberation, was agreed that these draft articles could be consolidated in one article, since there was no convincing reason for laying down different rules for the two categories of awards. It was agreed, however, that the conditions in the consolidated article were maximum standards and that it should be made clear that a State may set less onerous conditions or not even envisage any special procedure. It was further agreed that, subject to reconsideration at the next session, the model law should itself not retain any procedure on recognition standing alone and, for example, merely state that an award should be recognized, subject to possible objections as set forth in articles XXVII and XXVIII. The next phrase would, then, start with the words: "To obtain enforcement . . .".

136. As regards the contents of a consolidated article which would apply to "domestic" and foreign awards, it was not yet decided whether it was sufficient to refer merely to "an arbitral award" or whether it was preferable to add the words "made within or outside the territory of this State". The Working Group was agreed that the judicial authority to which an application for enforcement was to be made should be referred to in the article as the "competent court" and not "the Court of article V" since the function envisaged here was one of enforcement for which States had well established systems of competence. Finally, the Working Group was agreed that the consolidated article should require a "duly certified" translation and not retain the detailed and somewhat problematic wording "certified by an official or sworn translator or by a diplomatic or consular agent".

#### *Article XXVII*

137. The text of article XXVII as considered by the Working Group was as follows:

#### *"Article XXVII"*

"(1) Recognition and enforcement of an arbitral award made in the territory of this State shall 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 some incapacity] [lacked the capacity to conclude such an agreement], or the said agreement is not valid; 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 arbitral proceedings or was otherwise unable to present his case; or

"(c) the award 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 [, unless in conflict with any mandatory provision of this Law,] or, failing such agreement, was not in accordance with the provisions of this Law [, whether mandatory or not]; or

"(e) the award has not yet become binding on the parties or has been set aside by a court of this State.

"(2) Recognition and enforcement of an award [may] [shall] also be refused if the court finds that the recognition or enforcement would be contrary to the public policy of this State."

\* \* \*

(In view of the suggestion reported in A/CN.9/233, para. 139 (Yearbook 1983, part two, III, D), the Working Group may wish to consider the following short version of draft article XXVII:

"Recognition and enforcement of an arbitral award made in the territory of this State may be refused if:

"(a) the arbitral tribunal was not competent to make that award; or

"(b) the subject-matter of the award was not [arbitrable] [capable of settlement by arbitration]; or

"(c) the award is not binding; or

"(d) recognition and enforcement would be contrary to public policy.")

138. The Working Group recalled the conclusions of its general discussion on the policies relevant to the articles on recognition and enforcement (see above, paras. 125-133). It noted, in particular, the need for special consideration of the case where recognition alone was at stake and not as a pre-condition or interim step to enforcement. It also noted the need for avoiding the double control envisaged under articles XXVII and XXX and decided to consider this question in the context of article XXX.

139. Subject to these special considerations, the Working Group, after deliberation, adopted the prevailing view which was to consolidate articles XXVII and XXVIII on the basis of article XXVIII. This would allow harmony with article V of the 1958 New York Convention and, thus, avoid any undesirable disparity. It was felt that there were no cogent reasons for providing different rules for domestic awards and for foreign awards.

140. Nevertheless, in view of the tentative nature of the basic policy decision, observations were made on the wording of article XXVII in case it were retained as a separate regime for domestic awards in international commercial arbitration. There was agreement that the short version of article XXVII (set forth in A/CN.9/WG.II/WP.46 after the text of the draft article) was too short to deal with sufficient clarity with the important grounds for refusal.

141. As regards draft article XXVII proper, according to the prevailing view, the words "shall be refused" in the opening phrases of paragraphs (1) and (2) should be replaced by the words "may be refused"; as regards paragraph (1), the wording between the second square brackets in subparagraph (a) was preferable to the wording between the first square brackets; the wording between the second square brackets in subparagraph (c) was preferable to the wording between the first square brackets; the wording between the two square brackets in subparagraph (d) should be deleted; paragraph (2) should specifically mention the ground of non-arbitrability, like the corresponding provision in article XXVIII.

#### *Article XXVIII*

142. The text of article XXVIII as considered by the Working Group was as follows:

#### *"Article XXVIII"*

"(1) Recognition and enforcement of an arbitral award made outside the territory of this State [may] [shall] be refused, at the request of the party against whom it is invoked, only if that party furnishes [to the competent authority where the recognition and enforcement is sought] proof that:

"(a) the parties to the arbitration agreement referred to in article II were, under the [applicable law] [law applicable to them], 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 the country where the award was made; 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 arbitral proceedings or was otherwise unable to present his case; or

"(c) the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to

arbitration, provided that, if the 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; or

"(e) the award has not yet become binding on the parties or has been set aside or suspended by a [court] [competent authority] of the country in which, or under the [procedural] law of which, that award was made.

"(2) Recognition and enforcement of an arbitral award may also be refused if the [competent authority] [Court] 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 public policy of this State.

"(3) If an application for the setting aside or suspension of an award has been made to a [court] [competent authority] referred to in paragraph (1)(e), the [authority before which the award is sought to be relied upon] [Court] 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."

143. The Working Group recalled the conclusions of its general discussion on the policies relevant to the provisions on recognition and enforcement, in particular, its tentative decision to use article XXVIII as the basis of a consolidated article covering domestic and foreign awards and to model it closely on article V of the 1958 New York Convention. The Working Group reaffirmed its view that the model law should not cast any doubt on the legal effect of a reciprocity reservation made with regard to a multilateral treaty such as the 1958 New York Convention. On the other hand, the Working Group did not adopt a suggestion to include in article XXVIII a provision which would, on a unilateral basis, allow a similar restriction as regards awards not covered by a multilateral or bilateral agreement.

144. The Working Group was agreed to use in the opening phrase of paragraph (1) the words "may be refused" instead of the words "shall be refused". As regards subparagraph (a), there was some support for the wording adopted in article XXVII (1) (a); there was also some support for the wording between the first square brackets in paragraph (1) (a) of article XXVIII. The prevailing view, however, was to retain the wording between the second square brackets since this was the wording used in the 1958 New York Convention.

145. As regards subparagraph (e), the word "procedural" was not retained. Also, the term "court" was preferred to the term "competent authority" in view of the fact that the model law, in general, did not use the term "competent authority" and that the term "court", as defined in draft article I bis (d), included any judicial authority even if not called "court" in a given legal system. The same preference for the term "court" (or "Court") prevailed with regard to paragraphs (2) and (3) of article XXVIII.

#### *Article XXIX*

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

#### *"Article XXIX"*

"No recourse against an arbitral award made under this Law may be made to a court except as provided in article XXX."

147. The Working Group noted that article XXIX was closely linked with article XXX in that it expressed the exclusive nature of the recourse available under article XXX. It was, therefore, suggested to incorporate the provision of article XXIX into article XXX.

148. The Working Group noted that both articles applied to arbitral awards "made under this Law" and that this scope of application was different from the one used in articles XXV and XXVII where the territorial approach had been adopted ("awards made in the territory of this State"). It was thought that this disparity could lead to conflicts and undesirable results.

149. The Working Group was agreed to reconsider the matter at its next session in the light of a general study by the secretariat on the scope of application of the various provisions of the model law, including the question of the choice of a procedural law of a country other than the place of arbitration and some suggestions as to possible rules on conflict of laws.

#### *Article XXX*

150. The text of article XXX as considered by the Working Group was as follows:

#### *"Article XXX"*

"(1) An award made under this Law may be set aside, whether in whole or in part, only on grounds on which recognition and enforcement may be refused under article XXVII (1) (a), (b), (c), (d) or (2) [or on which an arbitrator may be challenged under article IX (2)].

"(2) An [application] [action] for setting aside may not be [made] [brought] after four months have elapsed from the date on which the party [making that application] [bringing that action] had received the award [in accordance with article XXII (4)].

[However, where the arbitration agreement provides for appeal to another arbitral tribunal, this period commences on the date of the receipt of the decision of that arbitral tribunal.]

"(3) The Court, when asked to set aside an award, may also order, where appropriate [and if so requested by a party], that the arbitral proceedings be continued. Depending upon the [reason for setting aside] [procedural defect found by the Court], this order may specify the matters to be considered by the arbitral tribunal and may contain other instructions concerning the composition of the arbitral tribunal or the conduct of the proceedings."

#### *Paragraph (1)*

151. A suggestion was made to widen the supervisory power of the court under article XXX by adding to the list of grounds "manifest injustice". However, this suggestion was not adopted since it was considered as too vague and too broad and since most cases of such injustice would fall under the grounds listed in paragraphs (1) (b) and (2) of article XXVII referred to in article XXX.

152. The Working Group adopted the grounds as listed in paragraph (1) of article XXX which corresponded to the reasons for refusal of recognition and enforcement under the 1958 New York Convention. It was noted that the ground placed between square brackets was not needed if the Working Group would adopt the second alternative in article X (3).

#### *Paragraph (2)*

153. The Working Group was agreed that the time-period within which an application for setting aside may be made should be three months. The Working Group was also agreed that the wording between square brackets at the end of the first sentence was not needed and that the second sentence could be deleted, too.

#### *Paragraph (3)*

154. Divergent views were expressed as to whether paragraph (3) should be retained. Under one view, the draft provision was useful in that it provided some guidance on procedural questions which were relevant in the case of remission. Under another view, the provision should be deleted since remission was not known in all legal systems and, in particular, the idea of orders or instructions to an arbitral tribunal was not acceptable. Under yet another view, the option of remission should be retained, without the giving of orders or instructions as envisaged in the second sentence; it was stated in support that this device would allow to cure a procedural defect without having to vacate the award.

155. The Working Group, after deliberation, adopted this latter view and requested the secretariat to revise the provision accordingly.

#### *Relationship between articles XXVII and XXX*

156. The Working Group recalled the concern expressed in the context of article XXVII that this article, even if consolidated with article XXVIII, would for domestic awards establish a procedure which would duplicate the examination of the very reasons set forth in article XXX for the setting aside of awards made under the law of this State. While some support was expressed for maintaining this double procedure in view of the different purposes of article XXVII and article XXX, the prevailing view was that it should be avoided, not only for the sake of economy and efficiency but also in order to prevent conflicting decisions.

157. In this respect, a suggestion was made to delete the provisions of article XXVII, with the result that the only control of domestic awards (if made under this Law) was exercised upon an application for setting aside if made within the time-period provided therefore in article XXX. However, this suggestion was not adopted since it was not justified to deprive a party from raising objections if "domestic" enforcement was sought after expiration of this time-limit while the same objections could still be raised against enforcement in any other State.

158. The Working Group was, thus, agreed that the double procedure should be avoided during the time-period for setting aside and requested the secretariat to prepare a draft provision to that effect. One possible technique was to refer a party against whom enforcement was sought within three months after receipt of the award to the procedure of setting aside. It was further suggested that the decision in that procedure would be binding on the enforcement judge or court and that a provision along the lines of paragraph (3) of article XXVIII might be appropriate also in this "domestic" context.

#### **IV. Consideration of redrafted articles I to XII (A/CN.9/WG.II/WP.45)**

159. The Working Group proceeded to a consideration of redrafted articles I to XII of a model law on international commercial arbitration, as set forth in document A/CN.9/WG.II/WP.45. These redrafted articles had been prepared by the secretariat on the basis of the discussion and decisions of the Working Group at its fifth session.<sup>10</sup>

#### *Article I*

160. The text of article I as considered by the Working Group was as follows:

<sup>10</sup>Ibid., paras. 47-120.

*"Article I"*

"(1) This Law applies to international commercial\* arbitration [, subject to any multilateral or bilateral agreement entered into by this State].

"(2) An arbitration is international if the parties to an arbitration agreement have [, at the time of the conclusion of that agreement,] their places of business 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.

"[(3) An arbitration shall also be regarded as international for the purpose of paragraph (1) where the parties to an arbitration agreement have stipulated that this Law shall apply in lieu of a national law on domestic arbitration, provided that [their relationship involves international trade interests. A relationship is deemed to involve international trade interests if] not all of the following places are situated in the same State: the place where the offer for the contract containing the arbitration clause or for the separate arbitration agreement was made; the place where the corresponding acceptance was made; the place of performance of any contractual obligation or of the location of the subject-matter; the place where each party is registered or incorporated or where its central management and control is exercised; the place of arbitration if determined in the arbitration agreement.]"

*Paragraph (1)*

161. The Working Group adopted this paragraph, including the words placed between square brackets, although there was some support for expressing the proviso in a separate provision.

162. As regards the footnote to the term "commercial", there was some support for incorporating the illustrative list set forth therein into the body of the text of paragraph (1) since the legal effect of a footnote to a law was not clear. There was also some support for not retaining any such illustrative list at all. The prevailing view, however, was to retain the footnote since it provided some useful guidance for the interpretation of the term "commercial".

163. As regards the text of the footnote, there was some support for retaining the words "or economic" and for deleting the phrase "irrespective of whether the parties are 'commercial persons' (merchants) under any

given national law". The prevailing view, however, was to retain this latter phrase and to delete the words "or economic".

*Paragraphs (2) and (3)*

164. The Working Group was agreed that the definition of "international" was of utmost importance for the practical effects of a model law on international commercial arbitration and crucial for its acceptability. It was recognized that to find a satisfactory solution was one of the most difficult tasks in the preparation of the model law.

165. Divergent views were expressed as to which would be the most appropriate test of internationality for the model law. Under one view, it was sufficient to use the standard set forth in paragraph (2) which was the test adopted in the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980; *Yearbook 1980*, part three, I, B). It was stated in support that this test provided a workable and precise formula which would allow easy determination of whether in a given case the (model) law on international arbitration or the national law on domestic arbitration would apply.

166. Under another view, the standard of paragraph (2) was too narrow and should be supplemented by further criteria which would avoid the vagueness of a general formula but cover the variety of cases for which the model law should establish a special régime. Objective criteria to be used for that purpose were the ones listed in paragraph (3), to which could be added, as suggested by one representative, the substantial ownership of a party. In support of this view to add objective criteria for the purpose of establishing the international character of an arbitration, it was stated that the opting-in mechanism provided under paragraph (3) was not appropriate for the many cases where the parties assumed that, because of some foreign element, their relationship was an international one and, thus, did not see any reason for a special act (of opting-in) on their part.

167. Under yet another view, it was impossible to cover all deserving cases by individual criteria. It was, therefore, necessary to adopt a general formula such as "involving international commercial interests", despite its possible shortcomings in view of the possibility that divergent interpretations would be given to it by the different courts of different States.

168. The Working Group, after deliberation, decided not to adopt the latter approach of a general formula but to widen the standard used in paragraph (2) by adding other objective criteria, in particular, the place of performance of contractual obligations and the location of the subject-matter of the transaction, as well as the place of arbitration if determined in the arbitration agreement. The Working Group requested the secretariat to prepare a draft provision embodying this compromise solution which should meet with the approval of the greatest number of States.

\*The term "commercial" should be given a wide interpretation so as to cover matters arising from all relationships of a commercial [or economic] nature, irrespective of whether the parties are "commercial persons" (merchants) under any given national law. Relationships of a commercial nature include, but are not limited to, the following transactions: any trade transaction for the supply or exchange of goods; distribution agreement; commercial representation or agency; factoring; leasing; construction of works; consulting; engineering; licensing; investment; financing; banking; insurance; exploitation agreement or concession; joint venture and other forms of industrial or business co-operation; carriage of goods or passengers by air, sea, rail or road.

*New article I bis*

169. The text of new article I *bis* as considered by the Working Group was as follows:

*"New article I bis"*

"For the purposes of this Law:

"(a) where a provision of this Law grants the parties freedom to determine a certain issue, such freedom includes the right of the parties to authorize a third person or institution to make that determination;

"(b) where a provision of this Law refers to the fact that the parties have agreed or that they may agree or in any other way refers to an agreement of the parties, such agreement includes any arbitration rules referred to in that agreement;

"(c) 'arbitral tribunal' [refers to] [means] a sole arbitrator or a [panel] [plurality] of arbitrators [, as the case may be];

"(d) 'court' means a body or organ of the judicial system of a country;

"[(e) if a party does not have a place of business, reference is to be made to his habitual residence.]"

170. The Working Group adopted subparagraphs (a) and (b) of new article I *bis*.

171. As regards subparagraph (c), there was some support for deleting this provision since it stated the obvious. The prevailing view, however, was to retain this provision since it underlined the difference between arbitral tribunal and court, as defined in subparagraph (d). Accordingly, subparagraph (c) was adopted as follows: (c) "arbitral tribunal" means a sole arbitrator or a panel of arbitrators.

172. As regards subparagraph (d), there was some support for deleting this provision since it was regarded as self-evident or as undesirable interference with national systems. There was also some support for defining the term "court" as "judicial body established by the law of a country, not including an arbitral tribunal". However, the wording of subparagraph (d) as drafted by the secretariat received the widest support.

173. The Working Group adopted subparagraph (e) and decided to incorporate it into article I (2), unless it was found to be relevant to another provision of the model law, too.

*New article I ter*

174. The text of new article I *ter* as considered by the Working Group was as follows:

*"[New article I ter]*

"The parties may not derogate from the following provisions of this Law: articles . . . (to be listed here: all mandatory provisions).]"

175. The Working Group adopted this new article and decided to consider at its next session which provisions

of the model law should be listed as mandatory in this article.

*New Article I quater*

176. The text of new article I *quater* as considered by the Working Group was as follows:

*"New article I quater"*

"A party who knows that any provision of, or requirement under, this Law has not been complied with and yet proceeds with the arbitration without stating his objection to such non-compliance promptly or, if a time-limit is provided therefor in this Law, within such period of time shall be deemed to have waived his right to object."

177. There was some support for deleting this draft article since such a provision was not appropriate for a law, though suitable for arbitration rules, and because it made a drastic legal consequence dependent on the knowledge of a party. The prevailing view, however, was to retain a waiver rule but in a less rigid form in order to exclude its operation in cases of fundamental violations of procedural provisions.

178. Two suggestions were made for "softening" the provision. One proposal was to replace the word "promptly" by less strict wording such as "without delay". Another suggestion was to limit the waiver rule to non-compliance with non-mandatory provisions. The Working Group adopted this suggestion subject to possible refinement at the next session when deciding in the context of article I *ter* which provisions of the model law should be mandatory.

*Article II*

179. The text of article II as considered by the Working Group was as follows:

*"Article II"*

"(1) 'Arbitration agreement' is an agreement by the parties to submit to arbitration, whether or not administered by a permanent arbitral institution, all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not. An arbitration agreement may be in the form of an arbitration clause in a contract or in the form of a separate agreement.

"(2) The arbitration agreement shall be in writing [whether] [. An agreement is in writing if it is] contained in a document signed by the parties or in an exchange of letters, telex, telegrammes or other means of tele-communication which would [preserve a record of the agreement] [produce a record on paper automatically or at the option of the recipient]. 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."

*Paragraph (1)*

180. The Working Group adopted paragraph (1).

*Paragraph (2)*

181. The Working Group adopted paragraph (2) subject to the following modifications. The word "whether" was deleted and the wording between the following square brackets retained. As regards the alternatives qualifying other means of telecommunication, the Working Group adopted the wording "which provide a record of the agreement". While some concern was expressed about giving the provision contained in the last sentence too wide a scope, the Working Group adopted this rule with the following wording: "The reference in a contract to a document 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 term of the contract".

182. One representative expressed the concern that paragraph (2), if understood as a mandatory provision, was too strict in requiring written form for the arbitration agreement and any later modification of that agreement, for example in the not uncommon case where the parties during arbitration proceedings agreed orally to submit a further issue, not included in the original agreement, to the arbitral tribunal for decision.

*Article III*

183. 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.]"

184. The Working Group decided to postpone its final decision on this article to a later stage when it was clear which instances of court intervention or assistance would be dealt with in the model law.

*Article IV*

185. 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, [decline jurisdiction and] refer the parties to arbitration unless it finds that the agreement is null and void, inoperative or incapable of being performed. [A plea that the court has no jurisdiction because of] [Such a request based on] the existence of an arbitration agreement may be made by a party not later than when submitting his first statement on the substance of the dispute.

"(2) It shall not be deemed incompatible with the arbitration agreement that a party, before or during arbitral proceedings, requests from a court interim measures of protection [in respect of the subject-matter of the dispute or in respect of evidence] and that a court [orders or takes] [grants] such measures."

*Paragraph (1)*

186. The Working Group adopted paragraph (1) subject to the following modifications. While there was some support for retaining the words "decline jurisdiction and", the prevailing view was to delete these words for the sake of conformity with the 1958 New York Convention (article II (3)). As regards the introductory phrase to the second sentence, the Working Group adopted the words "Such a request based on".

187. In this connection, a suggestion was made to include in article IV or another appropriate article (e.g. article II) a reference to the arbitrability of the subject-matter, as found in article II (1) of the 1958 New York Convention ("concerning a subject matter capable of settlement by arbitration") and recognized by the model law only in the chapter on enforcement (article XXVIII (2) (a)). However, this suggestion was not adopted since article IV was not regarded as an appropriate place for dealing with this issue and because an arbitration agreement concerning a non-arbitrable subject-matter would, at least in some jurisdictions, be regarded as null and void.

*Paragraph (2)*

188. The Working Group was agreed that the interim measures of protection envisaged under this provision would include measures of conservation of the subject-matter of the dispute and measures in respect of evidence as well as pre-award attachments. Nevertheless, it was not deemed necessary to specifically list the various possible measures; instead, a general formula such as the one adopted in the European Convention on International Commercial Arbitration (Geneva 1961; article VI (4)) was considered as more appropriate.

189. As regards the thrust of this provision, there was some support for merely addressing it to the parties and, thus, omit the reference to the action of the court itself. The prevailing view, however, was that the question of compatibility with the arbitration agreement was relevant not only with regard to the attitude of the parties but also to the granting of such measures by the courts.

*Article V*

190. The text of article V as considered by the Working Group was as follows:

*"[Article V]*

"The Court [with jurisdiction] [entrusted] to perform the functions referred to in articles VIII (2), (3), X (3), XI (2), XIII (3), XIV, XXVI and XXX shall be the... (blanks to be filled by each State when enacting the model law)."

191. There was wide support for retaining this article, with the words placed between the first square brackets. It was agreed that the reference to the individual articles entrusting the court with certain functions would have to be revised and finalized at a later stage. It was also noted that consideration may be given to the question which Court of article V, i.e. the court of which State, should render assistance in a given case, for example assist in the appointment of an arbitrator where the place of arbitration had not yet been determined. It was agreed that this and similar questions of scope of application and international competence should be considered at the next session, on the basis of a study by the secretariat.

#### *Article VI*

192. The text of article VI as considered by the Working Group was as follows:

##### *"Article VI"*

"No person shall be by reason of his nationality precluded from acting as an arbitrator, unless otherwise agreed by the parties."

193. Some support was expressed for the deletion of this article because it would be difficult to implement this provision in States where nationals of certain States were precluded from serving as arbitrators. However, after noting that the model law, not being a convention, would not exclude the possibility for a State to reflect its particular policies in national legislation, the Working Group agreed to adopt this article, subject to the addition of the words "or citizenship" after the word "nationality".

#### *Article VII*

194. The text of article VII as adopted by the Working Group was as follows:

##### *"Article VII"*

"(1) The parties are free to determine the number of arbitrators.

"(2) Failing such determination, the number of arbitrators shall be three."

195. The Working Group adopted this article.

#### *Article VIII*

196. The text of article VIII as considered by the Working Group was as follows:

##### *"Article VIII"*

"(1) The parties are free to agree on a procedure of appointing the arbitrator or arbitrators.

"(2) Failing such agreement,

"(a) in an arbitration with three arbitrators, each party shall appoint one arbitrator, and the two arbitrators thus appointed shall appoint the third arbitrator; if a party fails to appoint the arbitrator within 30 days after having been requested to do so [by the other party], or if the two arbitrators fail to agree on the third arbitrator within 30 days from their appointment, the appointment shall be made [, upon request of a party,] by the Court specified in article V;

"(b) if, in an arbitration with a sole arbitrator, the parties [are unable to agree] [do not within 40 days after the request for arbitration agree] on the arbitrator, he shall be appointed by the Court specified in article V.

"(3) Where, under an appointment procedure agreed upon by the parties,

"(a) a party fails to act as required under such procedure; or

"(b) the parties, or two arbitrators, are unable to reach an agreement expected from them under such procedure; or

"(c) an appointing authority fails to perform any function entrusted to it under such procedure, any party may request the Court specified in article V to take the necessary measure instead, unless the agreement on the appointment procedure [, in particular by reference to arbitration rules,] provides [another procedure for meeting such contingency] [other means for securing the appointment].

"((3 bis) Any decision entrusted by paragraphs (2) and (3) to the Court specified in article V shall be final.]

"(4) This Court, in appointing an arbitrator, shall have due regard [to any qualifications required of the arbitrator by agreement of the parties and] to such considerations as are likely to secure the appointment of an independent and impartial arbitrator and, in the case of a sole or third arbitrator, shall take into account as well the advisability of appointing [an arbitrator of a nationality other than the nationalities of the parties] [the national of a State where neither of the parties has his relevant place of business as referred to in article I (2)]."

##### *Paragraph (1)*

197. The Working Group adopted this paragraph.

##### *Paragraph (2)*

198. There was some support for replacing the fixed time-periods by more flexible wording such as "within reasonable time". The prevailing view, however, was to retain the fixed time-periods for the sake of certainty. The Working Group adopted subparagraph (a) including the words placed between the two sets of square brackets. The Working Group was agreed that the words placed between the last square brackets should also be inserted in subparagraph (b). While some

support was expressed for the wording in the second brackets of subparagraph (b), though with a time-period of 30 days for the sake of harmony with subparagraph (a), the prevailing view was to adopt the wording between the first square brackets ("are unable to agree").

#### *Paragraph (3)*

199. The Working Group adopted this paragraph subject to the deletion of the text placed between the first two sets of square brackets.

#### *Paragraph (3 bis)*

200. The Working Group adopted this paragraph.

#### *Paragraph (4)*

201. The Working Group adopted this paragraph subject to the deletion of the wording between the last square brackets and to adjustment in accordance with its decision on article VI (see above, para. 193). A suggestion was made to replace the words "shall take into account" by the words "may take into account".

### *Article IX*

202. The text of article IX as considered by the Working Group was as follows:

#### *"Article IX"*

"(1) When a person is approached in connexion with his possible appointment as an arbitrator, he shall disclose any circumstances likely to give rise to justifiable doubts as to his impartiality or independence. An arbitrator [, from the time of his appointment and thereafter,] 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."

#### *Paragraph (1)*

203. The Working Group adopted this paragraph including the words placed between square brackets. It was also agreed to insert in both sentences of this paragraph the words "without delay".

#### *Paragraph (2)*

204. The Working Group adopted this paragraph.

### *Article X*

205. 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.

"(2) Failing such agreement, a party may challenge an arbitrator before the arbitral tribunal within 15 days after knowing any circumstance referred to in article IX (2). The mandate of the arbitrator terminates when he withdraws from his office or the other party agrees to the challenge; [in neither case does this imply] [neither reaction implies] acceptance of the validity of the grounds for the challenge.

"(3) If a challenge is not successful within 30 days under the procedure of paragraph (2) or is not successful under any procedure agreed upon by the parties, the challenging party may [pursue his objections before a court only in an action for setting aside the arbitral award] [request, within 15 days, from the Court specified in article V a decision on the challenge which shall be final; while such a request is pending, the arbitral tribunal, including the challenged arbitrator, may continue the arbitral proceedings]."

#### *Paragraph (1)*

206. The Working Group adopted this paragraph.

#### *Paragraph (2)*

207. It was noted that under this provision "a party may challenge an arbitrator before the arbitral tribunal" but that the power of the arbitral tribunal to decide on such challenge was not clearly expressed in this provision. The Working Group was agreed that, unless the challenged arbitrator withdrew from his office or the other party agreed to the challenge, the arbitral tribunal should decide on the challenge and that this step in the challenge procedure should be clearly stated in paragraph (2), without laying down the procedural details. It was understood that this step had no practical relevance in the case of a sole arbitrator challenged by a party.

208. As to how the paragraph should be redrafted, various suggestions were made and accepted by the Working Group. One proposal was to transfer to article IX the whole text which followed the first sentence of paragraph (2), including the words between the first square brackets. Paragraph (2) of article X would then merely deal with the decision of the arbitral tribunal on the challenge which would become necessary where neither the challenged arbitrator withdrew from his office nor the other party agreed to the challenge. It was further suggested to require in paragraph (2) that a party who challenged an arbitrator should state the reasons for the challenge.

#### *Paragraph (3)*

209. It was noted that the introductory wording of paragraph (3) had to be revised in the light of the decision on paragraph (2). Divergent views were expressed concerning the alternative solutions placed

between square brackets. Under one view, resort to a court should not be allowed during the arbitration proceedings but only by way of an application for setting aside the award, as provided in the first square brackets. The main reason advanced in support of this view was that dilatory tactics should be prevented, although it was recognized by some proponents of that view that the revised version of the alternative solution (between the second square brackets) contained some elements to alleviate such fears.

210. Under another view, it was unacceptable to continue the arbitral proceedings without first settling the matter by a final decision on the challenge. For that reason, the second alternative should be adopted but without its last part which allowed the arbitral tribunal to continue the arbitral proceedings while the question of challenge was pending with the court.

211. Under yet another view, the second alternative should be adopted including its last part which, as was pointed out in support of this view, did not oblige the arbitral tribunal to continue the proceedings but merely entitled it to do so. It was stated that this discretion left to the arbitral tribunal would enable it to limit the adverse effects of an unjustified challenge for dilatory purposes.

212. The Working Group, while recognizing the divergency of views and the validity of the different reasons advanced in support thereof, was agreed that the issue had to be settled and adopted, after deliberation, the latter view (reported in para. 211) as a compromise solution.

#### *Article XI*

213. The text of article XI as considered by the Working Group was as follows:

##### *"Article XI"*

"(1) In the event that an arbitrator fails to act or in the event of the *de jure* or *de facto* impossibility of his performing his functions, his mandate terminates if he withdraws from his office or if the parties agree on the termination; in neither case does this imply acceptance of the validity of any ground referred to in the first sentence.

"(2) If [the mandate of the arbitrator does not terminate in accordance with paragraph (1) and if] a controversy remains concerning any of the events envisaged in paragraph (1), any party [or arbitrator] may request from the Court specified in article V a decision on the termination of the mandate [which shall be final]."

##### *Paragraph (1)*

214. Some support was expressed for aligning this paragraph with the provision of article X (2) and to provide that the arbitral tribunal should decide on the

failure or impossibility to act, where neither the respective arbitrator withdrew from his office nor the parties agreed on the termination of the mandate. The prevailing view, however, was that such alignment was not warranted in view of the different events or grounds covered by article XI.

215. It was noted that the last phrase of paragraph (1), as presently drafted, was not easily reconcilable with the first sentence, where the very events were stated as objective and existing, while the last phrase precluded any inference as to their validity. While recognizing the policy underlying this last phrase, the Working Group decided to delete that phrase in paragraph (1) and to express the idea in the context of article IX, in line with its decision concerning paragraph (2) of article X (see above, para. 208). As regards the remaining text of paragraph (1), the Working Group requested the secretariat to prepare a revised draft, possibly combined with the provision of paragraph (2).

##### *Paragraph (2)*

216. The Working Group adopted paragraph (2), subject to the deletion of the text placed between the first two sets of square brackets, although there was some support for retaining the words between the second square brackets ("or arbitrator") and for deleting the words between the last square brackets ("which shall be final").

#### *Article XII*

217. The text of article XII as considered by the Working Group was as follows:

##### *"Article XII"*

"Where the mandate of an arbitrator terminates under article X or XI, or in the event of his death or resignation, 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."

218. The Working Group adopted the policy underlying this article. It was observed that the introductory wording did not specify in a systematical manner the cases where the need for appointing a substitute arbitrator arose.

219. In connection with this article, a concern was expressed that, in the case of a party-appointed arbitrator, the mechanism of resignation and replacement, in particular by using it repeatedly, could be abused for the purposes of obstructing the proceedings. Without denying the validity of this concern with regard to some cases, the Working Group decided not to deal, at least not at this stage, with this problem for which no easy solution could be found.

### *Reference to conciliation*

220. A suggestion was made to consider including in the part of the model law setting forth general provisions (articles I *bis* to I *quater*) a new provision as

follows: "Conciliation can be used as an additional method of settling disputes where parties so wish". The Working Group decided to consider this suggestion at its next session when discussing the above general provisions.

## 2. Working papers submitted to the Working Group at its sixth session

### (a) *Model law on international commercial arbitration: revised draft articles A to G on adaptation and supplementation of contracts, commencement of arbitral proceedings, minimum contents of statements of claim and defence, language in arbitral proceedings, court assistance in taking evidence, termination of arbitral proceedings and period for enforcement of arbitral award: note by the secretariat (A/CN.9/WG.II/WP.44)*

#### INTRODUCTORY NOTE

1. This working paper contains revised draft articles A to G 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 fifth session (New York, 22 February-4 March 1983).<sup>1</sup>

2. It may be noted that headings of draft provisions are merely for reference purposes, not intended to be later included in the model law.

3. In view of the tentative nature of the revised draft articles A to G, proposals as to the possible place where they may be included in the model law will be made at a later stage.

6. In the discussion at the Working Group it appeared that there was a widely shared view that there was a practical need for the parties to have a possibility of agreeing to entrust a third person with the task of adapting or supplementing their contract. The main issue on which divergent views were expressed in the Working Group was whether such third party assistance would be within the domain of arbitration. Under one view, such assistance could be rendered by an arbitral tribunal, although it was recognized that there were certain differences between the cases where the arbitral tribunal adapted or supplemented a contract and cases where it decided legal disputes. Under another view, it was inappropriate and, in fact, not necessary to qualify such assistance as arbitration.

### 2. *Object of a provision in the model law on adaptation of contracts*

7. After the conclusion of a contract circumstances may change and affect the original balance in the obligations to be performed by the parties. For such cases the parties may wish to have available a procedure under which a third party could decide on whether the change of circumstances warrants a modification of the contract and, if so, would modify the contract to adapt it to the changed circumstances.

8. The provision on adaptation of contracts in the model law would deal with cases in which the adaptation of a contract is an independent objective of the proceedings, i.e. where the goal is to rewrite one or more terms of the contract which would then have to be carried out by the parties.

9. The provision on adaptation of contracts would, thus, not deal with cases in which a party to a legal dispute over a contract may raise a defence in that dispute or may claim a remedy or relief from the other party on the grounds of changed circumstances which have allegedly caused him undue hardship. If in such legal dispute a court or arbitral tribunal reaches the decision that because of fundamentally changed circumstances the claim or defence is justified, the final

<sup>1</sup>"Report of the Working Group on International Contract Practices on the work of its fifth session" (A/CN.9/233) paras. 15-45 (*Yearbook 1983*, part two, III, C).

<sup>2</sup>Ibid., paras. 15-20; and A/CN.9/WG.II/WP.41, paras. 2-11 (*Yearbook 1983*, part two, III, D, 2).

<sup>3</sup>See A/CN.9/233, para. 20.

decision on the dispute would be preceded, as a matter of logic, by an adaptation of the relevant contract provision to the changed circumstances. Such adaptation of the contract would form an interim step in the process of making the final decision. For this type of adaptation no special authorization by the parties is needed and no provision need be included in the model law.

10. Furthermore, the provision on adaptation of contracts in the model law would only regulate procedural aspects of adaptation of contracts; it would not regulate substantive conditions, as may be contained in a contract clause or in a substantive law provision, for the right of a party to request an adaptation of a contract.

### *3. Object of a provision in the model law on supplementation of contracts*

11. The parties may at the time of the conclusion of the contract consider it necessary to postpone the agreement on some issues. Also, after the conclusion of the contract a provision on an issue which has not been dealt with in the contract may be found to be needed. In such cases the parties may wish to authorize a third person to supplement the contract by formulating additional contract provisions on that issue.

12. As in the case of adaptation of contracts, the provision on supplementation of contracts in the model law would deal with cases where the supplementation of a contract is an independent objective of the proceedings, i.e. where the goal is to add one or more contract terms to the original contract.

13. The provision on supplementation of contracts would, thus, not deal with deciding legal disputes arising from breach of contract where the arbitral tribunal may have to deal with situations which are not expressly covered by the contract. If the resolution of a legal dispute on a claim for a remedy or relief based on breach of contract depends on a question which is not expressly covered by a contract provision, a court or arbitral tribunal may fill such gap by interpreting the contract. As regards the power to fill such gaps in the course of deciding legal disputes, no special authorization by the parties is needed and no provision need be included in the model law.

### *4. Reasons against the inclusion of a rule on adaptation and supplementation of contracts in the model law*

14. The main reason against allowing arbitral tribunals to assist parties by adapting or supplementing contracts stems from the position of many legal systems according to which the courts are not allowed to adapt or supplement contracts. Under this reasoning the

competence of an arbitral tribunal could not be wider than the competence of a court since the competence of arbitral tribunals is substituted, by an agreement of the parties, for the competence of the courts.

15. A related reasoning is that a decision adapting or supplementing a contract is made on the basis of an assessment of economic factors and not in direct application of substantive legal rules or trade usages. As a court may lack special expertise to make such economic assessment, an arbitral tribunal should not engage in such decision-making either.

16. A further reason is that there is no need for such a provision in a model law on arbitration because legal systems often provide procedures for adaptation and supplementation of contracts outside the framework of arbitration.

### *5. Reasons in favour of the inclusion of a rule on adaptation and supplementation of contracts in the model law*

17. In support of the view that adaptation and supplementation should fall within the domain of arbitration it may be said that the competence of arbitral tribunals need not be regarded as parallel to the competence of courts. The mere fact that arbitration is to the exclusion of court competence does not necessarily mean that the competence of the arbitral tribunal cannot be wider than the (excluded) competence of the court.

18. A further reason for defining more broadly the domain of arbitration is that parties, especially those engaged in long-term contracts, have a legitimate interest in a mechanism for adapting and supplementing their contracts. Parties may have an interest to entrust such task to arbitrators who have their confidence and are familiar with their business relationship.

19. Furthermore, rules governing the conduct of arbitral proceedings would also be appropriate for third-party assistance in adapting or supplementing contracts. By subjecting the process of adaptation and supplementation to the same procedural safeguards which arbitrators have to observe in deciding legal disputes, the model law would further enhance legal certainty in international trade.

20. Lastly, a procedure for adaptation and supplementation of contracts would enable the third party to intervene immediately after a controversy arises concerning the need for adaptation or supplementation of a contract. Such instant decision is particularly desirable in ongoing relationships and certainly preferable to having a party adjust his conduct to changed circumstances or decide on his conduct in the absence of a clear contract provision, and determining only later, in arbitral proceedings or litigation, whether such conduct was justified and what claims result therefrom.

**6. Possible contents of a provision on adaptation and supplementation of contracts**

21. A provision in the model law on adaptation and supplementation of contracts would possibly have to deal with the following issues:

- (a) The capacity in which a third person decides on the adaptation or supplementation of contracts;
- (b) The authorization to decide on the adaptation or supplementation of contracts;
- (c) Procedural rules which are to govern the adaptation and supplementation of contracts; and
- (d) The legal status and effect of decisions adapting or supplementing contracts.

**(a) The capacity in which a third person decides on the adaptation or supplementation of contracts**

22. In deciding the question whether an arbitral tribunal, in its capacity as an arbitral tribunal, may be authorized to adapt or supplement a contract, account may be taken of the trend towards a broader concept of arbitration and of the goal of the model law to meet the needs of parties in international trade in decades to come. However, because of possible difficulties for some legal systems to give arbitral tribunals a broader competence than courts, two approaches may be considered.

23. The first approach is a rule under which an arbitral tribunal, acting as an arbitral tribunal, would not be precluded from adapting or supplementing a contract if the parties have authorized it to do so. This approach has been adopted in alternative A of the draft provision.<sup>4</sup>

24. The second approach is a rule which would enable the parties to authorize the persons appointed as arbitrators to adapt or supplement a contract, making it clear, however, that such proceedings are special and are not necessarily to be qualified as arbitration. It is submitted that a provision along these lines would not preclude future developments of law and practice in this field. This second approach has been adopted in alternative B of the draft provision.<sup>4</sup>

**(b) The authorization to decide on the adaptation or supplementation of contracts**

25. The provision in the model law should also deal with the form and contents of the authorization given by the parties to a third person to adapt or supplement their contract. The Working Group may wish to consider whether such authorization should be in writing (like the arbitration agreement under article II (2) in A/CN.9/WG.II/WP.45; reproduced in this Yearbook, part two, A, 2, b) and whether the authorization should be made expressly or whether an implied authorization would suffice. Since the power of the arbitral tribunal to adapt or supplement a contract is based on the authorization, the parties are free to limit the mandate

of the arbitral tribunal by giving certain instructions or indicating certain conditions which the third person would have to observe in making a decision.

**(c) Procedural rules which are to govern the adaptation and supplementation of contracts**

26. Regarding the procedures to be followed in deciding on the adaptation and supplementation of contracts and the rules governing the decision on adaptation and supplementation, the Working Group may consider whether all or only certain provisions of the model law would be applicable. A related question would be whether the applicable provisions of the model law are to be applied directly or by analogy.

27. It is submitted that the answers to these questions to a large extent depend on which of the alternative draft provisions the Working Group adopts.

**(d) The legal status and effect of decisions adapting or supplementing contracts**

28. The objective of third-party assistance in adapting or supplementing a contract is to lay down new contract provisions to be implemented by the parties in the future. It would accord with that objective if the decision adapting or supplementing a contract had the same legal status and effect as the contract which it adapts or supplements. The newly determined contract provisions should, thus, become an integral part of the contract.

29. With regard to a decision on adaptation or supplementation establishing new contract terms to be observed by the parties, disputes may arise about the interpretation or the fulfilment of these terms. Since the terms form an integral part of the adapted or supplemented contract, such disputes would be treated like any other dispute relating to a contract, i.e. a claim would be submitted to a court or to an arbitral tribunal which would then render an enforceable decision.

30. The contract terms established by a decision on adaptation or supplementation, like any other contract, should not be contrary to mandatory rules of the applicable law. Thus, this decision could be challenged before a court or an arbitral tribunal for violation of a mandatory law provision. In addition to that, in view of the specific process in which the obligation has come into existence, there are also other grounds on which a decision adapting or supplementing a contract may later be challenged before a court or an arbitral tribunal: e.g. there has been no valid authorization to adapt or supplement the contract; the third party has exceeded the mandate or disregarded instructions given in the authorization; or the right of the party to be heard has been violated.

31. It may be noted that the above considerations as to the status and effect of a decision adapting or supplementing a contract would also apply if that decision would be qualified in the model law as an

<sup>4</sup>See para. 32, below.

arbitral award (see wording between the second square brackets of alternative A of article A (3) in the next paragraph).

*7. Draft provision on adaptation and supplementation of contracts*

32. The following draft provisions may form a basis for discussion:

*Article A*

*Alternative A*

(1) The arbitral tribunal has the power to adapt or supplement the contract upon request of a party provided that the parties have [expressly] authorized the arbitral tribunal [in writing] to do so; the arbitral tribunal shall decide on the adaptation or supplementation of the contract in accordance with any indication agreed upon by the parties as to [the specific conditions under which the contract should be adapted or supplemented] [the changed circumstances to which the contract or certain provisions of the contract should be adapted or any indication as to the issues which should be regulated in the contract].

(2) The arbitral tribunal authorized to decide on the adaptation or supplementation of the contract shall apply [the provisions of this Law] [the provisions of articles . . . of this Law].

(3) [The decision of the arbitral tribunal adapting or supplementing the contract] [The arbitral award in which the arbitral tribunal adapts or supplements the contract] shall be binding on the parties and [the parties shall give effect to it] [shall be carried out by the parties] as an integral part of the contract.

*Alternative B*

(1) The person or persons appointed as arbitrators have the power to adapt or supplement the contract upon request of a party provided that the parties [expressly] authorized him or them [in writing] to do so; the person or persons shall decide on the adaptation or supplementation of the contract in accordance with any indication agreed upon by the parties as to [the specific conditions under which the contract should be adapted or supplemented] [the changed circumstances to which the contract or certain provisions of the contract should be adapted or any indication as to the issues which should be regulated in the contract].

(2) The person or persons authorized to decide on the adaptation or supplementation of the contract shall apply [the provisions of this Law by analogy] [the provisions of articles . . . of this Law by analogy].

(3) The decision adapting or supplementing the contract shall be binding on the parties and [the parties shall give effect to it] [shall be carried out by the parties] as an integral part of the contract.

*B. Commencement of arbitral proceedings<sup>5</sup>*

*Article B*

Unless otherwise agreed by the parties, the arbitral proceedings shall be deemed to commence on the date at which a request that a dispute be referred to arbitration is received<sup>6</sup> by the respondent provided that such a request [sufficiently] identifies the claim.

*C. Minimum contents of statements of claim and defence<sup>7</sup>*

*Article C*

(1) The claimant shall state the facts supporting his claim, the points at issue and the relief or remedy sought. The respondent shall state his defence in respect of these particulars. [The parties may annex to their statements all documents they deem relevant or may add a reference to the documents or other evidence they will submit.]<sup>8</sup>

(2) Unless otherwise agreed by the parties, the statements of the claimant and the respondent [, made in accordance with the preceding paragraph,] shall be communicated to the other party and to each of the arbitrators within a period of time to be determined by the arbitral tribunal.]<sup>9</sup>

(3) During the course of the arbitral proceedings either party may amend or supplement his claim or defence unless the arbitral tribunal considers it inappropriate to allow such amendment having regard to the delay in making it or prejudice to the other party or any other circumstances.]<sup>10</sup>

<sup>5</sup>See A/CN.9/233, paras. 21-23 (Yearbook 1983, part two, III, C) and A/CN.9/WG.II/WP.41, paras. 12-18 (*idem*, D, 2).

<sup>6</sup>It may be desirable to include in the model law a general rule on the date when any notice or other communication is deemed to have been received. Such a rule, modelled on article 2 (1) of the UNCITRAL Arbitration Rules, might read as follows: "For the purposes of this Law, any written communication is deemed to have been received if it is physically delivered to the addressee or if it is delivered at his place of business, habitual residence or mailing address, or, if none of these can be found after making reasonable inquiry, then at the addressee's last-known place of business or residence. Communication shall be deemed to have been received on the day it is so delivered."

<sup>7</sup>See A/CN.9/233, paras. 24-26 (Yearbook 1983, part two, III, C) and A/CN.9/WG.II/WP.41, paras. 19-21 (*idem*, D, 2).

<sup>8</sup>The provision in square brackets is modelled on article 18 (2) and article 19 (2) of the UNCITRAL Arbitration Rules.

<sup>9</sup>Draft paragraph (2) is modelled on article 18 (1) and article 19 (1) of the UNCITRAL Arbitration Rules. It may be noted that the decision whether paragraph (2) of this draft article is necessary largely depends on the decision of the Working Group on the two alternatives in draft article XVII (3) (A/CN.9/WG.II/WP.40; Yearbook 1983, part two, IV, D, 1); if the first alternative in draft article XVII (3) is adopted, i.e. that all documents or information supplied to the arbitral tribunal by one party shall be communicated to the other party, there may be little need for the provision of paragraph (2) of this draft article.

<sup>10</sup>Draft paragraph (3) is modelled on article 20 of the UNCITRAL Arbitration Rules (Yearbook 1976, part one, II, A, para 57; or UNCITRAL Arbitration Rules, United Nations publication, Sales No. E.77.V.6).

**D. Language in arbitral proceedings<sup>11</sup>**

*Article D<sup>12</sup>*

(1) The parties are free to agree on the language or languages to be used in the arbitral proceedings. Failing such agreement, the arbitral tribunal shall determine the language or languages to be used in the proceedings. This agreement or determination, unless otherwise specified therein, shall apply to any written statement by a party, any oral hearing, and any award, decision or other communication by the arbitral tribunal.

(2) The arbitral tribunal may order that any documentary evidence shall be accompanied by a translation into the language or languages agreed upon by the parties or determined by the arbitral tribunal.

**E. Court assistance in taking evidence<sup>13</sup>**

*Article E*

(1) The arbitral tribunal or a party [with the approval of the arbitral tribunal] may request from [a court] [the Court specified in article V] assistance in taking evidence. The court shall execute such a request by either taking the evidence itself or by ordering a party or a third person to give evidence to the arbitral tribunal.

(2) Where an arbitration takes place outside this State, the arbitral tribunal or a party [with the approval of the arbitral tribunal] may submit such a request through a court of the State where the arbitration takes place. Such a request shall be treated by the court referred to in paragraph (1) as a request by that foreign court.

**F. Termination of arbitral proceedings<sup>14</sup>**

*Article F*

(1) The arbitral proceedings are terminated:

<sup>11</sup>See A/CN.9/233, paras. 27-30 (*Yearbook 1983*, part two, III, C) and A/CN.9/WG.II/WP.41, paras. 22-26 (*idem*, D, 2).

<sup>12</sup>This provision is modelled on article 17 of the UNCITRAL Arbitration Rules.

<sup>13</sup>See A/CN.9/233, paras. 31-37 (*Yearbook 1983*, part two, III, C) and A/CN.9/WG.II/WP.41, paras. 27-37 (*idem*, D, 2).

<sup>14</sup>See A/CN.9/233, paras. 38-41 (*Yearbook 1983*, part two, III, C) and A/CN.9/WG.II/WP.41, paras. 38-41 (*idem*, D, 2).

(a) by the [making] [delivery] of the final award which constitutes or completes the disposition of all claims submitted to arbitration; or

(b) by an agreement of the parties that the arbitral proceedings are to be terminated;<sup>15</sup> or

(c) by an order of the arbitral tribunal in accordance with paragraph (2) of this article.

(2) After having given suitable notice to the parties, the arbitral tribunal shall issue an order for the termination of the arbitral proceedings when the claimant withdraws his claim or if for any other reason the continuation of the proceedings becomes unnecessary or inappropriate.

(3) The mandate of the arbitral tribunal is terminated with the termination of the arbitral proceedings, subject to the provisions of article XXIV.<sup>16</sup>

**G. Period for enforcement of arbitral award<sup>17</sup>**

*Article G*

Enforcement of an arbitral award shall be refused if the request is made after ten years have elapsed from the date at which the award was [made] [received by the party requesting the enforcement] [received by the party against whom enforcement is sought]. [However, if the award contains an obligation which is to be performed later than two years after the date at which the award was made, the period for enforcement commences to run on the date at which the obligation is to be performed.]

<sup>15</sup>This subparagraph also covers the case where the parties agree on the settlement of the dispute without requesting the recording of the settlement in the form of an arbitral award; such a case implies the agreement of the parties that the arbitral proceedings are to be terminated. If the parties, after having settled the dispute, request that the settlement be recorded in the form of an award, the arbitral proceedings are terminated by the making of the award on agreed terms.

<sup>16</sup>Another possible extension of the mandate of the arbitral tribunal to be listed in this article could be the case of remission by a court as envisaged under article XXX (3) in A/CN.9/WG.II/WP.46 (reproduced in this *Yearbook*, part two, II, A, 2, c).

<sup>17</sup>See A/CN.9/233, paras. 42-45 (*Yearbook 1983*, part two, III, C) and A/CN.9/WG.II/WP.41, paras. 42-45 (*idem*, D, 2).

**(b) Model law on international commercial arbitration: redrafted articles I to XII on scope of application, general provisions, arbitration agreement and the courts, and composition of arbitral tribunal: note by the secretariat (A/CN.9/WG.II/WP.45)**

**INTRODUCTORY NOTE**

on International Contract Practices at its fifth session (New York, 22 February-4 March 1983).<sup>1</sup>

<sup>1</sup>"Report of the Working Group on International Contract Practices on the work of its fifth session" (A/CN.9/233), paras. 47-120 (*Yearbook 1983*, part two, III, C). The revised draft articles were set forth in A/CN.9/WG.II/WP.40 (*Yearbook 1983*, part two, III, D, 1), together with a comparative table of numbers of previous draft articles.

2. In addition to this second revision of draft articles I to XII, three new draft articles (*I bis*, *I ter* and *I quater*) are submitted for consideration by the Working Group. They contain some rules of interpretation or definitions and other provisions of general relevance, based on decisions or suggestions made by the Working Group.

3. It may be noted that not only the heading of these three new articles ("General provisions") but also all other chapter headings are tentatively suggested by the secretariat for reference purposes. The Working Group may wish to decide at a later stage whether and, if so, which headings should be used.

### REDRAFTED ARTICLES I TO XII OF A MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION

#### A. Scope of application

##### *Article I<sup>2</sup>*

(1) This Law applies to international commercial\* arbitration [, subject to any multilateral or bilateral agreement entered into by this State].<sup>3</sup>

(2) An arbitration is international if the parties to an arbitration agreement have [, at the time of the conclusion of that agreement,]<sup>4</sup> their places of business 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.<sup>5</sup>

[(3) An arbitration shall also be regarded as international for the purpose of paragraph (1) where the

\*(The following explanations could be given in a footnote to the term "commercial", as envisaged by the Working Group at its fifth session; see A/CN.9/233, para. 56; *Yearbook 1983*, part two, III, C.)

The term "commercial" should be given a wide interpretation so as to cover matters arising from all relationships of a commercial [or economic] nature, irrespective of whether the parties are "commercial persons" (merchants) under any given national law. Relationships of a commercial nature include, but are not limited to, the following transactions: any trade transaction for the supply or exchange of goods; distribution agreement; commercial representation or agency; factoring; leasing; construction of works; consulting; engineering; licensing; investment; financing; banking; insurance; exploitation agreement or concession; joint venture and other forms of industrial or business co-operation; carriage of goods or passengers by air, sea, rail or road.

<sup>2</sup>See relevant discussion and conclusions by the Working Group in A/CN.9/233, paras. 48-60 (*Yearbook 1983*, part two, III, C).

<sup>3</sup>The Working Group may wish to consider whether this proviso, which was felt to be a principle of general application (A/CN.9/233, para. 128; *Yearbook 1983*, part two, III, C), should be expressed in this paragraph or in a separate article (following article I).

<sup>4</sup>The Working Group may wish to consider whether the words placed between square brackets are necessary in order to clarify the decisive point of time.

<sup>5</sup>While 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 (see A/CN.9/233, para. 59; *Yearbook 1983*, part two, III, C), it is submitted that such additions might introduce an undesirable degree of uncertainty and that the first criterion (i.e. implementation of the arbitration agreement) tends to relate to a third ("neutral") place which seems less appropriate for determining the link to the place of business of one of the parties.

parties to an arbitration agreement have stipulated that this Law shall apply in lieu of a national law on domestic arbitration, provided that [their relationship involves international trade interests. A relationship is deemed to involve international trade interests if] not all of the following places are situated in the same State: the place where the offer for the contract containing the arbitration clause or for the separate arbitration agreement was made; the place where the corresponding acceptance was made; the place of performance of any contractual obligation or of the location of the subject-matter; the place where each party is registered or incorporated or where its central management and control is exercised; the place of arbitration if determined in the arbitration agreement.]<sup>6</sup>

#### B. General provisions

##### *New article I bis*

For the purposes of this Law:

(a) where a provision of this Law grants the parties freedom to determine a certain issue, such freedom includes the right of the parties to authorize a third person or institution to make that determination;<sup>7</sup>

(b) where a provision of this Law refers to the fact that the parties have agreed or that they may agree or in any other way refers to an agreement of the parties, such agreement includes any arbitration rules referred to in that agreement;<sup>8</sup>

(c) "arbitral tribunal" [refers to] [means] a sole arbitrator or a [panel] [plurality] of arbitrators [, as the case may be];<sup>9</sup>

(d) "court" means a body or organ of the judicial system of a country;<sup>9</sup>

[(e) if a party does not have a place of business, reference is to be made to his habitual residence.]<sup>10</sup>

<sup>6</sup>This draft provision would form a separate provision in addition to paragraph (2), if accepted by the Working Group as an "opting-in" provision. Another possibility suggested at the previous session (A/CN.9/233, para. 60; *Yearbook 1983*, part two, III, C) would be to replace the test laid down in paragraph (2) by a wider formula along the lines of the proviso set forth in draft paragraph (3).

<sup>7</sup>The draft provisions under lit. (a) and (b) are designed to implement the decision of the Working Group reported in A/CN.9/233, paras. 101-102 (*Yearbook 1983*, part two, III, C).

<sup>8</sup>This draft provision might be deemed useful not only in view of the clarification expressed therein but also as an aid in emphasizing the distinction between arbitral tribunal and "court" as defined in the following provision.

<sup>9</sup>This draft provision attempts to define, for two different reasons, the term "court" as used in the model law. One reason is to clarify that "court" includes any competent "judicial authority" even if not called court in the respective country. The other reason is to emphasize the distinction between arbitral tribunal and court which seems particularly desirable in languages other than English since, for example, in French and Spanish the term *tribunal* could otherwise be misunderstood as an abbreviated reference to *tribunal arbitral*.

<sup>10</sup>This draft provision, which is modelled on article 10 (b) of the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980; *Yearbook 1980*, part three, 1, B), might, if adopted, be incorporated in article I (2) unless the place of business is referred to in other provisions as well (e.g. draft article on receipt of communications).

*[New article I ter]*

The parties may not derogate from the following provisions of this Law: articles . . . (to be listed here: all mandatory provisions).]<sup>11</sup>

*New article I quater<sup>12</sup>*

A party who knows that any provision of, or requirement under, this Law has not been complied with and yet proceeds with the arbitration without stating his objection to such non-compliance promptly or, if a time-limit is provided therefor in this Law, within such period of time shall be deemed to have waived his right to object.

**C. Arbitration agreement and the courts***Article II<sup>13</sup>*

(1) "Arbitration agreement" is an agreement by the parties to submit to arbitration, whether or not administered by a permanent arbitral institution, all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not. An arbitration agreement may be in the form of an arbitration clause in a contract or in the form of a separate agreement.

(2) The arbitration agreement shall be in writing [whether] [. An agreement is in writing if it is] contained in a document signed by the parties or in an exchange of letters, telex, telegrammes or other means of telecommunication which would [preserve a record of the agreement] [produce a record on paper automatically or at the option of the recipient]. 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.

*[Article III]*

In matters governed by this Law, no court shall intervene except where so provided in this Law.]<sup>14</sup>

<sup>11</sup>The Working Group may wish to consider at a later stage the appropriateness of a general provision on which rules of the law are of a mandatory character (cf. A/CN.9/232, paras. 77, 181; *Yearbook 1983*, part two, III, A).

<sup>12</sup>This draft provision, which is modelled on article 30 of the UNCITRAL Arbitration Rules, is designed to implement a suggestion made in various contexts (e.g. A/CN.9/233, paras. 66, 188; *Yearbook 1983*, part two, III, C).

<sup>13</sup>See A/CN.9/233, paras. 62-68 (*Yearbook 1983*, part two, III, C).

<sup>14</sup>The Working Group, at its fifth session, postponed the decision on this tentative draft article to a later stage but accepted its underlying policy as an intention to clarify, in the course of the preparation of the draft model law, instances of court intervention (A/CN.9/233, para. 73; *Yearbook 1983*, part two, III, C).

*Article IV<sup>15</sup>*

(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, [decline jurisdiction and] refer the parties to arbitration unless it finds that the agreement is null and void, inoperative or incapable of being performed. [A plea that the court has no jurisdiction because of] [Such a request based on] the existence of an arbitration agreement may be made by a party not later than when submitting his first statement on the substance of the dispute.<sup>16, 17</sup>

(2) It shall not be deemed incompatible with the arbitration agreement that a party, before or during arbitral proceedings, requests from a court interim measures of protection [in respect of the subject-matter of the dispute or in respect of evidence] and that a court [orders or takes] [grants] such measures.

*Article V<sup>18</sup>*

The Court [with jurisdiction] [entrusted] to perform the functions referred to in articles VIII (2), (3), X (3), XI (2), XIII (3), XIV, XXVI and XXX shall be the . . . (blanks to be filled by each State when enacting the model law).<sup>19</sup>

<sup>15</sup>See A/CN.9/233, paras. 75-81 (*Yearbook 1983*, part two, III, C).

<sup>16</sup>This draft provision combines the provisions previously set forth in paragraphs (1) and (2). Two modifications are suggested in an attempt (a) to emphasize the issue dealt with in this provision, i.e. the competence—or lack of competence—of a court before which a substantive claim is brought; (b) to clarify the relationship between the "request", mentioned in the first sentence, and the "plea", previously referred to in paragraph (2).

<sup>17</sup>It is suggested that the provision previously contained in paragraph (3) of article IV be transferred, with some modifications, to article XIII as new paragraph (4):

"(4) Where, after arbitral proceedings have commenced, a party invokes before a court lack of jurisdiction of the arbitral tribunal, whether impliedly by bringing a substantive claim or expressly by requesting a decision on the jurisdiction of the arbitral tribunal directly from the court without first raising this plea before the arbitral tribunal, the arbitral tribunal may continue the proceedings while the issue is pending with the court."

In this context, the Working Group may wish to consider the relationship between the two ways of pleading lack of jurisdiction of the arbitral tribunal as envisaged in article XIII (2), (3), i.e. plea raised before arbitral tribunal, with later control by court, and in above paragraph (4), i.e. direct resort to court without first requesting a ruling by the arbitral tribunal on its jurisdiction. The main question would be whether these two procedures are provided cumulatively or alternatively. In the latter case, a party who has chosen one of the procedures would be precluded from using the other one.

<sup>18</sup>See A/CN.9/233, paras. 83-86 (*Yearbook 1983*, part two, III, C). It may be recalled here that, according to a decision by the Group, the procedural issues previously dealt with in (now deleted) paragraph (2), i.e. right to request the court to act and finality of the court's decision, should be considered in the context of the individual provisions entrusting certain functions to the court.

<sup>19</sup>The "Court" to be designated by each State may be a court or part of a court (e.g. special chamber), whether already existing (e.g. commercial court) or established for that purpose; certain functions of a more administrative nature and where speed is required (e.g. appointment, challenge) may be assigned to a specific person (e.g. president of court or chamber).

**D. Composition of arbitral tribunal**

*Article VI<sup>20</sup>*

No person shall be by reason of his nationality precluded from acting as an arbitrator, unless otherwise agreed by the parties.<sup>21</sup>

*Article VII<sup>22</sup>*

(1) The parties are free to determine the number of arbitrators.

(2) Failing such determination, the number of arbitrators shall be three.

*Article VIII<sup>23</sup>*

(1) The parties are free to agree on a procedure of appointing the arbitrator or arbitrators.

(2) Failing such agreement,

(a) in an arbitration with three arbitrators, each party shall appoint one arbitrator, and the two arbitrators thus appointed shall appoint the third arbitrator; if a party fails to appoint the arbitrator within 30 days after having been requested to do so [by the other party], or if the two arbitrators fail to agree on the third arbitrator within 30 days from their appointment, the appointment shall be made [, upon request of a party,] by the Court specified in article V;

(b) if, in an arbitration with a sole arbitrator, the parties [are unable to agree] [do not within 40 days after the request for arbitration agree] on the arbitrator, he shall be appointed by the Court specified in article V.

(3) Where, under an appointment procedure agreed upon by the parties,

(a) a party fails to act as required under such procedure; or

(b) the parties, or two arbitrators, are unable to reach an agreement expected from them under such procedure; or

(c) an appointing authority fails to perform any function entrusted to it under such procedure,

any party may request the Court specified in article V to take the necessary measure instead, unless the agreement on the appointment procedure [, in particular by reference to arbitration rules,] provides [another procedure for meeting such contingency] [other means for securing the appointment].

[(3 bis) Any decision entrusted by paragraphs (2) and (3) to the Court specified in article V shall be final.]

<sup>20</sup>See A/CN.9/233, paras. 88-91 (*Yearbook 1983*, part two, III, C).

<sup>21</sup>This provision might later be combined with the provisions of article VII or VIII.

<sup>22</sup>See A/CN.9/233, para. 93 (*Yearbook 1983*, part two, III, C).

<sup>23</sup>*Ibid.* paras. 95-100.

(4) This Court, in appointing an arbitrator, shall have due regard [to any qualifications required of the arbitrator by agreement of the parties and] to such considerations as are likely to secure the appointment of an independent and impartial arbitrator and, in the case of a sole or third arbitrator, shall take into account as well the advisability of appointing [an arbitrator of a nationality other than the nationalities of the parties] [the national of a State where neither of the parties has his relevant place of business as referred to in article I (2)].

*Article IX<sup>24</sup>*

(1) When a person is approached in connection with his possible appointment as an arbitrator, he shall disclose any circumstances likely to give rise to justifiable doubts as to his impartiality or independence. An arbitrator [, from the time of his appointment and thereafter,] 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<sup>25</sup>*

(1) The parties are free to agree on the procedure for challenging an arbitrator, subject to the provisions of paragraph (3) of this article.

(2) Failing such agreement, a party may challenge an arbitrator before the arbitral tribunal within 15 days after knowing any circumstance referred to in article IX (2). The mandate of the arbitrator terminates when he withdraws from his office or the other party agrees to the challenge; [in neither case does this imply] [neither reaction implies] acceptance of the validity of the grounds for the challenge.

(3) If a challenge is not successful within 30 days under the procedure of paragraph (2) or is not successful under any procedure agreed upon by the parties, the challenging party may [pursue his objections before a court only in an action for setting aside the arbitral award] [request, within 15 days, from the Court specified in article V a decision on the challenge which shall be final; while such a request is pending, the arbitral tribunal, including the challenged arbitrator, may continue the arbitral proceedings].<sup>26</sup>

<sup>24</sup>*Ibid.*, paras. 104-106.

<sup>25</sup>*Ibid.*, paras. 108-111.

<sup>26</sup>In the latter alternative, some elements have been added (i.e. time-limit for request; finality of decision; discretion to continue arbitral proceedings) in an attempt to alleviate the fear of dilatory tactics. An additional device could be to accelerate the decision by assigning it to a person rather than a court (cf. footnote 19).

*Article XI<sup>27</sup>*

(1) In the event that an arbitrator fails to act or in the event of the *de jure* or *de facto* impossibility of his performing his functions, his mandate terminates if he withdraws from his office or if the parties agree on the termination; in neither case does this imply acceptance of the validity of any ground referred to in the first sentence.

(2) If [the mandate of the arbitrator does not terminate in accordance with paragraph (1) and if] a controversy remains concerning any of the events

<sup>27</sup>See A/CN.9/233, paras. 113-117 (*Yearbook 1983*, part two, III, C).

envisioned in paragraph (1), any party [or arbitrator] may request from the Court specified in article V a decision on the termination of the mandate [which shall be final].

*Article XII<sup>28</sup>*

Where the mandate of an arbitrator terminates under article X or XI, or in the event of his death or resignation, 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.

<sup>28</sup>Ibid., paras. 119-120.

(c) *Model law on international commercial arbitration: revised draft articles XXV to XXX on recognition and enforcement of arbitral award and recourse against award: note by the secretariat (A/CN.9/WG.II/WP.46)*

### INTRODUCTORY NOTE

1. This working paper contains revised draft articles XXV to XXX 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 fifth session (New York, 22 February-4 March 1983).<sup>1</sup> These revised draft articles (on recognition and enforcement of arbitral award and on recourse against award) are based on previous draft articles XXV, XXVI and 37 to 41.<sup>2</sup>

2. It may be noted that the revised draft articles are presented in the same order as the previous ones, although two suggestions for rearranging the articles were made at the last session: (a) to place the articles on recourse against award before the articles on recognition and enforcement; (b) to combine the provisions on setting aside with the articles on recognition and enforcement of domestic awards. It may be recalled that the Working Group was agreed that these suggestions could be considered at a later stage.<sup>3</sup>

3. In fact, it seems premature to rearrange these draft articles before final decisions are made on their retention and exact contents. This is particularly true with regard to the draft provisions on recognition and enforcement, since conflicting views were expressed on policy questions such as the extent to which draft article XXVII (previously 37) and especially article XXVIII (previously 38) should be aligned with article V of the 1958 New York Convention and whether one should

strive for a uniform system for all awards irrespective of their place of origin.<sup>4</sup>

### REVISED DRAFT ARTICLES ON RECOGNITION AND ENFORCEMENT OF ARBITRAL AWARD AND ON RE COURSE AGAINST AWARD

#### J. Recognition and enforcement of arbitral award

##### *Article XXV<sup>5</sup>*

An arbitral award made in the territory of this State shall be recognized as binding and enforced in accordance with the following procedure.\*

An application shall be made in writing to the competent court, 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 [duly certified] translation of these documents into such language [, certified by an official or sworn translator or by a diplomatic or consular agent].

\*The following text might be given in a footnote to this article in the model law in order to express the common understanding in the Working Group that the objective of article XXV was to set forth maximum procedures (see A/CN.9/233, para. 123):

"The procedure set forth in this article is intended to set maximum standards. It would, thus, not be contrary to the harmonization to be achieved by the model law if a State retained an even less onerous procedure."

<sup>1</sup>Ibid., paras. 137-139, 159-161.

<sup>2</sup>Ibid., paras. 122-126.

<sup>3</sup>Report of the Working Group on the work of its fifth session" (A/CN.9/233) paras. 121-195 (*Yearbook 1983*, part two, III, C).

<sup>4</sup>The previous draft articles were set forth in A/CN.9/WG.II/WP.40 and 42 (*Yearbook 1983*, part two, III, D, 1 and 3).

<sup>5</sup>See A/CN.9/233, para. 182 (*Yearbook 1983*, part two, III, C).

### *Article XXVI<sup>6</sup>*

An arbitral award made outside the territory of this State shall be recognized as binding and enforced in accordance with the following procedure:

An application shall be made in writing to the 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.

### *Article XXVII<sup>7</sup>*

(1) Recognition and enforcement of an arbitral award made in the territory of this State shall 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 some incapacity] [lacked the capacity to conclude such an agreement], or the said agreement is not valid; 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 arbitral proceedings or was otherwise unable to present his case; or

(c) the award 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 [, unless in conflict with any mandatory provision of this Law,] or, failing such agreement, was not in accordance with the provisions of this Law [, whether mandatory or not]; or

(e) the award has not yet become binding on the parties or has been set aside by a court of this State.

(2) Recognition and enforcement of an award [may] [shall] also be refused if the court finds that the recognition or enforcement would be contrary to the public policy of this State.

\* \* \*

<sup>6</sup>Ibid., paras. 128-131. It should be noted that the proviso contained in the previous version of this article ("subject to any multilateral or bilateral agreement...") is now contained in a provision of general application (i.e. article I (1) in A/CN.9/WG.II/W.P.45; reproduced in this Yearbook, part two, II, A, 2, b).

<sup>7</sup>See discussion and conclusions by the Working Group on the relevant previous draft article 37 in A/CN.9/233, paras. 134-156 (Yearbook 1983, part two, III, C).

(In view of the suggestion reported in A/CN.9/233, para. 139 (Yearbook 1983, part two, III, C), the Working Group may wish to consider the following short version of draft article XXVII:

Recognition and enforcement of an arbitral award made in the territory of this State may be refused if:

(a) the arbitral tribunal was not competent to make that award; or

(b) the subject-matter of the award was not [arbitrable] [capable of settlement by arbitration]; or

(c) the award is not binding; or

(d) recognition and enforcement would be contrary to public policy.)

### *Article XXVIII<sup>8</sup>*

(1) Recognition and enforcement of an arbitral award made outside the territory of this State [may] [shall] be refused, at the request of the party against whom it is invoked, only if that party furnishes [to the competent authority where the recognition and enforcement is sought]<sup>9</sup> proof that:

(a) the parties to the arbitration agreement referred to in article II were, under the [applicable law] [law applicable to them], 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 the country where the award was made; 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 arbitral proceedings or was otherwise unable to present his case; or

(c) the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the 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; or

(e) the award has not yet become binding on the parties, or has been set aside or suspended by a [court] [competent authority] of the country in which, or under the [procedural] law of which, that award was made.

<sup>8</sup>See discussion and conclusions by the Working Group on the relevant previous draft article 38 in A/CN.9/233, paras. 158-175 (Yearbook 1983, part two, III, C).

<sup>9</sup>The wording between square brackets, which is taken from the 1958 New York Convention, might be regarded as superfluous, or it could be replaced by the words "to the Court" (in line with the decision on article XXVI according to which "the Court specified in article V" is the competent one).

(2) Recognition and enforcement of an arbitral award may also be refused if the [competent authority] [Court]<sup>10</sup> 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 public policy of this State.

(3) If an application for the setting aside or suspension of an award has been made to a [court] [competent authority] referred to in paragraph (1) (e), the [authority before which the award is sought to be relied upon] [Court] 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.<sup>11</sup>

#### K. Recourse against arbitral award

##### Article XXIX<sup>12</sup>

No recourse against an arbitral award made under this Law may be made to a court except as provided in article XXX.

##### Article XXX<sup>13</sup>

(1) An award made under this Law may be set aside, whether in whole or in part, only on grounds on which

<sup>10</sup>The term "Court" seems to be more appropriate than the words "competent authority" in view of the decision on the competent body under article XXVI (cf. footnote 9).

<sup>11</sup>This draft provision, which is based on previous draft article 39, has been incorporated into article XXVIII in view of the decision of the Working Group to limit the scope of this rule to recognition and enforcement of only foreign awards (A/CN.9/233, para. 177; *Yearbook 1983*, part two, III, C).

<sup>12</sup>See discussion and conclusions of the Working Group on the relevant previous draft article 40 in A/CN.9/233, paras. 179-180 (*Yearbook 1983*, part two, III, C).

<sup>13</sup>See discussion and conclusions of the Working Group on the relevant previous draft article 41 in A/CN.9/233, paras. 182-195 (*Yearbook 1983*, part two, III, C).

recognition and enforcement may be refused under article XXVII (1) (a), (b), (c), (d) or (2) [or on which an arbitrator may be challenged under article IX (2)].<sup>14</sup>

(2) An [application] [action] for setting aside may not be [made] [brought] after four months have elapsed from the date on which the party [making that application] [bringing that action] had received the award [in accordance with article XXII (4)]. [However, where the arbitration agreement provides for appeal to another arbitral tribunal, this period commences on the date of the receipt of the decision of that arbitral tribunal.]<sup>15</sup>

(3) The Court, when asked to set aside an award, may also order,<sup>16</sup> where appropriate<sup>17</sup> [and if so requested by a party], that the arbitral proceedings be continued. Depending upon the [reason for setting aside] [procedural defect found by the Court], this order may specify the matters to be considered by the arbitral tribunal and may contain other instructions concerning the composition of the arbitral tribunal or the conduct of the proceedings.

<sup>14</sup>The words between square brackets would not be necessary if the Working Group were to decide in favour of the second alternative set forth in article X (3) in A/CN.9/WG.II/WP.45 (reproduced in this *Yearbook*, part two, II, A, 2, b).

<sup>15</sup>The sentence between square brackets is submitted for consideration in the light of the suggestion reported in A/CN.9/233, para. 184 (*Yearbook 1983*, part two, III, C). If a provision concerning appeal to another arbitral tribunal were to be included in the model law, the Working Group may wish to consider also the case where a party does not bring such appeal (within any agreed period of time) but directly requests the court to set aside the award (of first instance).

<sup>16</sup>This opening phrase would leave it open whether remission to the arbitral tribunal is an alternative or a supplementary remedy to setting aside. The Working Group may wish to consider whether the provision should leave open this question to which varying answers are given in different national laws.

<sup>17</sup>This almost self-evident proviso is submitted in this short form since no other, more detailed formula could be found which would cover the great variety of cases where remission would either be appropriate or inappropriate.

## B. Seventh session of the Working Group on International Contract Practices (New York, 6-17 February 1984)

### 1. Report of the Working Group on the work of its seventh session (A/CN.9/246—6 March 1984)<sup>a</sup>

#### CONTENTS

	<i>Paragraphs</i>
INTRODUCTION .....	1-12
DELIBERATIONS AND DECISIONS .....	13-202

<sup>a</sup>For consideration by the Commission see Report, chapter III (part one, A, above).

	Paragraphs
A. CONSIDERATION OF COMPOSITE DRAFT TEXT OF A MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION .....	16-190
CHAPTER II. ARBITRATION AGREEMENT .....	17-26
CHAPTER III. COMPOSITION OF ARBITRAL TRIBUNAL .....	27-48
CHAPTER IV. JURISDICTION OF ARBITRAL TRIBUNAL .....	49-59
CHAPTER V. CONDUCT OF ARBITRAL PROCEEDINGS .....	60-101
CHAPTER VI. MAKING OF AWARD AND TERMINATION OF PROCEEDINGS .....	102-125
CHAPTER VII. RECOURSE AGAINST AWARD .....	126-139
CHAPTER VIII. RECOGNITION AND ENFORCEMENT OF AWARDS	140-155
CHAPTER I. GENERAL PROVISIONS .....	156-190
B. OTHER ISSUES .....	191-201
1. Headings .....	191
2. "Award" .....	192-194
3. Reference to conciliation .....	195
4. Counter-claim .....	196
5. Reference in article 34 to article 36 .....	197
6. Conflict of laws issues .....	198-201
C. OTHER BUSINESS .....	202

*Annex*

DRAFT TEXT OF A MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION AS ADOPTED BY THE WORKING GROUP<sup>b</sup>

## 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.<sup>1</sup>

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.<sup>2</sup>

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 and 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.<sup>3</sup>

<sup>b</sup>Reproduced in this Yearbook, part two, II, B, 2.

<sup>1</sup>"Report 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).

<sup>2</sup>"Report 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).

<sup>3</sup>"Report of the Working Group on International Contract Practices on the work of its fourth session" (A/CN.9/232, Yearbook 1983, part two, III, A).

4. At its fifth session, the Working Group considered further features and draft articles of a model law and revised draft articles I to XXVI of a model law on international commercial arbitration. At that session, the Working Group also considered draft articles 37 to 41 on recognition and enforcement of awards and on recourse against awards.<sup>4</sup>

5. At its sixth session, the Working Group considered tentative draft articles A to G, revised draft articles XIII to XXIV and XXV to XXX and redrafted articles I to XII of a model law on international commercial arbitration.<sup>5</sup>

6. According to a decision by the Commission to expand the membership of the Working Group to all States members of the Commission,<sup>6</sup> the Working Group consists of the following 36 States: Algeria, Australia, Austria, Brazil, Central African Republic, China, Cuba, Cyprus, Czechoslovakia, Egypt, France, German Democratic Republic, Germany, Federal

<sup>4</sup>"Report of the Working Group on International Contract Practices on the work of its fifth session" (A/CN.9/233; Yearbook 1983, part two, III, C).

<sup>5</sup>"Report of the Working Group on International Contract Practices on the work of its sixth session" (A/CN.9/245; reproduced in this Yearbook, part two, II, A, 1).

<sup>6</sup>"Report of the United Nations Commission on International Trade Law on the work of the sixteenth session, *Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17* (A/38/17), para. 143 (Yearbook 1983, part one, A).

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.

7. The Working Group held its seventh session in New York from 6 to 17 February 1984. All the members were represented except the Central African Republic and Peru.

8. The session was attended by observers from the following States: Argentina, Barbados, Canada, Chile, Congo, Ecuador, El Salvador, Finland, Ghana, Greece, Guinea, Holy See, Honduras, Norway, Panama, Republic of Korea, Romania, Suriname, Switzerland, Thailand, Tunisia, Turkey and Venezuela.

9. The session was attended by observers from the following intergovernmental organizations: Asian-African Legal Consultative Committee, Commission of the European Communities and Hague Conference on Private International Law, and from the following international non-governmental organizations: Inter-American Commercial Arbitration Commission, International Bar Association, International Chamber of Commerce, International Council for Commercial Arbitration and International Law Association.

10. The Working Group elected the following officers:

*Chairman:* Ivan Szasz (Hungary)

*Rapporteur:* James C. Droushiotis (Cyprus)

11. 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; *Yearbook 1981*, part two, III);

(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; *Yearbook 1982*, part two, III, B);

(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; *Yearbook 1983*, part two, III, A);

(d) 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; *Yearbook 1983*, part two, III, D);

(e) Report of the Working Group on International Contract Practices on the work of its sixth session (Vienna, 29 August-9 September 1983) (A/CN.9/245; reproduced in this *Yearbook*, part two, II, A, 1);

(f) Provisional agenda for the session (A/CN.9/WG.II/WP.47);

(g) Composite draft text of a model law on international commercial arbitration (A/CN.9/WG.II/WP.48; reproduced in this *Yearbook*, part two, II, B, 3, a);

(h) Territorial scope of application of the model law and related issues (A/CN.9/WG.II/WP.49; reproduced in this *Yearbook*, part two, II, B, 3, b);

(i) Some notes on the composite draft text of a model law (A/CN.9/WG.II/WP.50; reproduced in this *Yearbook*, part two, II, B, 3, c).

12. The Working Group adopted the following agenda:

(a) Election of officers

(b) Adoption of the agenda

(c) Consideration of composite draft text of a model law on international commercial arbitration

(d) Other business

(e) Adoption of the report

#### DELIBERATIONS AND DECISIONS

13. The Working Group considered the composite draft text of a model law on international commercial arbitration (A/CN.9/WG.II/WP.48; reproduced in this *Yearbook*, part two, II, B, 3, d), as revised by the Drafting Group (A/CN.9/WG.2/7/CRP.1). In connection with pertinent articles of the draft text, the Working Group also considered issues of territorial scope of application of the model law and related issues raised in document A/CN.9/WG.II/WP.49 (reproduced in this *Yearbook*, part two, II, B, 3, b) and some comments and suggestions by the secretariat on the composite draft text which were contained in document A/CN.9/WG.II/WP.50 (reproduced in this *Yearbook*, part two, II, B, 3, c).

14. The Working Group adopted the draft text of the model law on international commercial arbitration as contained in the annex to the present report. It was noted that, for lack of time, the Working Group was unable to review the articles as to their correlation and consistency.

15. The Working Group noted that the secretariat had convened a drafting group in order to establish corresponding language versions of the text of the model law before it was sent to governments and international organizations for comments. The Working Group expressed its appreciation to the Drafting Group which met before and during the session of the Working Group.

#### A. Consideration of composite draft text of a model law on international commercial arbitration

16. The Working Group decided to postpone its consideration of chapter I, "General provisions", to a later stage of the session and to commence its deliberations with a consideration of chapter II, "Arbitration agreement".

## CHAPTER II. ARBITRATION AGREEMENT

### *Article 7*

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

*"Article 7. Definition and form of arbitration agreement*

"(1) 'Arbitration agreement' is an agreement by the parties to submit to arbitration, whether or not administered by a permanent arbitral institution, all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not. An arbitration agreement may be in the form of an arbitration clause in a contract or in the form of a separate agreement.

"(2) The arbitration agreement shall be in writing. An agreement is in writing if it is contained in a document signed by the parties or in an exchange of letters, telex, telegrams or other means of telecommunication which provide a record of the agreement. The reference in a contract to a document 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 part of the contract."

18. The Working Group adopted that article.

19. The Working Group was agreed that the last part of the last sentence of paragraph (2) should not be understood as requiring an explicit reference to the arbitration clause contained in a document referred to.

### *Article 8*

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

*"Article 8. Arbitration agreement and substantive claim before court*

"(1) A court, before which an action is brought in a matter which is the subject of an arbitration agreement, shall, if a party so requests not later than when submitting his first statement on the substance of the dispute, refer the parties to arbitration unless it finds that the agreement is null and void, inoperative or incapable of being performed.

"(2) Where, in such case, arbitral proceedings have already commenced, the arbitral tribunal may continue the proceedings while the issue [of its jurisdiction] is pending with the court [unless the court orders a stay of the arbitral proceedings]."

21. The Working Group adopted that article, including, in paragraph (2), the words "of its jurisdiction" but deleting the words "unless the court orders a stay of the arbitral proceedings", although there was some support for their retention.

22. The Working Group considered the question raised in the note prepared by the secretariat (A/CN.9/WG.II/WP.50, para. 15; reproduced in this Yearbook, part two, II, B, 3, c) whether the model law should deal with the effect of a party's failure to invoke the arbitration agreement in accordance with paragraph (1) of that article. The Working Group was agreed that article 8 (1) certainly prevented a party from invoking the arbitration agreement later than the point of time indicated in paragraph (1), and that the court was not empowered without a request of a party, i.e. *ex officio*, to refer the parties to arbitration. While there was wide support for the view that the failure of the party should have a wider effect precluding that party from relying on the arbitration agreement also in other contexts or proceedings, the Working Group decided not to incorporate a provision on such general effect because it would be impossible to devise a simple rule which would satisfactorily deal with all the aspects of this complex issue.

23. The Working Group did not accept a suggestion to add at the end of paragraph (1) the words "or that the dispute concerns a matter that is not capable of settlement by arbitration". While recognizing the importance of the requirement of arbitrability, the prevailing view was that there was no need for an express provision as the one suggested. It was noted that an arbitration agreement concerning a non-arbitrable subject-matter would normally be regarded as null and void. It was also pointed out by some representatives that the issue of non-arbitrability was adequately addressed in articles 34 and 36.

### *Article 9*

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

*"Article 9. Arbitration agreement and interim measures by court*

"It is not incompatible with the arbitration agreement for a party to request, before or during arbitral proceedings, from a court an [interim measure of protection] [interim measure or a measure of conservation] and for a court to grant such measure."

25. The Working Group adopted that article, including the words "interim measure of protection" and deleting the words "interim measure or a measure of conservation". While there was some support for the latter wording which was taken from the 1961 Geneva Convention, the prevailing view was in favour of the term "interim measure of protection" which was taken from the UNCITRAL Arbitration Rules.

26. The Working Group was agreed that the range of measures covered by article 9 was a wide one and included, in particular, pre-award attachments. It was noted that that provision, as regards the range of measures covered, including their enforcement, was considerably wider than article 18 which empowered the arbitral tribunal to order certain interim measures of protection but did not deal with the enforcement of such orders.

### CHAPTER III. COMPOSITION OF ARBITRAL TRIBUNAL

#### *Article 10*

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

*"Article 10. Number of arbitrators"*

"(1) The parties are free to determine the number of arbitrators.

"(2) Failing such determination, the number of arbitrators shall be three."

28. The Working Group adopted that article.

#### *Article 11*

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

*"Article 11. Appointment of arbitrators"*

"(1) No person shall be precluded by reason of his nationality from acting as an arbitrator, unless otherwise agreed by the parties.

"(2) The parties are free to agree on a procedure of appointing the arbitrator or arbitrators, subject to the provisions of paragraphs (4) and (5) of this article.

"(3) Failing such agreement.

"(a) in an arbitration with three arbitrators, each party shall appoint one arbitrator, and the two arbitrators thus appointed shall appoint the third arbitrator; if a party fails to appoint the arbitrator within thirty days after having been requested to do so by the other party, or if the two arbitrators fail to agree on the third arbitrator within thirty days of their appointment, the appointment shall be made, upon request of a party, by the Court specified in article 6;

"(b) in an arbitration with a sole arbitrator, if the parties are unable to agree on the arbitrator, he shall be appointed, upon request of a party, by the Court specified in article 6.

"(4) Where, under an appointment procedure agreed upon by the parties,

"(a) a party fails to act as required under such procedure; or

"(b) the parties, or two arbitrators, are unable to reach an agreement expected of them under such procedure; or

"(c) an appointing authority fails to perform any function entrusted to it under such procedure,

any party may request the Court specified in article 6 to take the necessary measure, unless the agreement on the appointment procedure provides other means for securing the appointment.

"(5) A decision on a matter entrusted by paragraph (3) or (4) to the Court specified in article 6 shall be final. The Court, in appointing an arbitrator, shall have due regard to any qualifications required of the arbitrator by the agreement of the parties and to such considerations as are likely to secure the appointment of an independent and impartial arbitrator and, in the case of a sole or third arbitrator, shall take into account as well the advisability of appointing an arbitrator of a nationality other than those of the parties."

30. The Working Group adopted that article.

31. The Working Group noted that the words "or citizenship" following the word "nationality" in paragraphs (1) and (5) had been deleted by the Drafting Group. While there was some support for retaining the words "or citizenship", the prevailing view was to delete them since in many legal systems only the term "nationality" was used. However, the Working Group was agreed that, in view of the purpose of this provision to achieve non-discrimination, the term "nationality" should be given a wide interpretation so as to embrace citizenship, where such term was used.

32. As regards the function entrusted to the court by paragraph (4) of that article, the Working Group was agreed that the words "to take the necessary measure" meant that the court had to take the necessary measure itself (that is, to make the appointment) and not, for example, order an appointing authority, which had failed to do so, to perform the function entrusted to that authority by the parties.

#### *Article 12*

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

*"Article 12. Grounds for challenge"*

"(1) When a person is approached in connection with his possible appointment as an arbitrator, he shall [without delay] disclose any circumstances likely to give rise to justifiable doubts as to his impartiality or independence. An arbitrator, from the time of his appointment and throughout the arbitral proceedings, shall without delay disclose any such circumstances to the parties unless they have already been informed of them by him.

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

"(3) The fact that, in cases under article 13 (2) or 14, an arbitrator withdraws from his office or a party agrees to the termination of the mandate of an arbitrator does not imply acceptance of the validity of any ground referred to in [that provision] [paragraph (2) of this article or in article 14]."

34. The Working Group adopted that article, subject to the deletion of the words "without delay" in the first sentence of paragraph (1) and subject to the addition, in the second sentence of paragraph (2), after the words "the arbitrator appointed by him" of the words "or in whose appointment he has participated". That addition was felt to be necessary since the policy considerations which applied to the case of the party-appointed arbitrator were of equal force in the case where the parties jointly appointed an arbitrator.

35. As regards paragraph (3), the Working Group noted that the Drafting Group had recommended to place that provision after article 14 as a new article 14 *bis*. The Working Group requested the Drafting Group to implement that idea and also to select the more appropriate wording of the two variants presented between square brackets at the end of that paragraph.

#### *Article 13*

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

##### *"Article 13. Challenge procedure*

*"(1) The parties are free to agree on a procedure for challenging an arbitrator, subject to the provisions of paragraph (3) of this article.*

*"(2) Failing such agreement, a party who intends to challenge an arbitrator shall, within fifteen days after becoming aware of any circumstances referred to in article 12 (2), send a written statement of the reasons for the challenge to the arbitral tribunal. Unless the challenged arbitrator withdraws from his office or the other party agrees to the challenge, the arbitral tribunal shall decide on the challenge.*

*"(3) If a challenge under any procedure agreed upon by the parties or under the procedure of paragraph (2) is not successful, the challenging party may request, within fifteen days [after having received the decision rejecting the challenge], the Court specified in article 6 to decide on the challenge, which decision shall be final; while such a request is pending, the arbitral tribunal, including the challenged arbitrator, may continue the arbitral proceedings."*

37. The Working Group adopted that article, subject to the replacement, in paragraph (2), of the words "after becoming aware of any circumstances referred to in article 12 (2)" by the words "of the constitution of the arbitral tribunal or after becoming aware of any circumstance referred to in article 12 (2), whichever is later".

38. The Working Group was agreed that the decision entrusted to the arbitral tribunal by paragraph (2) of that article was not to be considered as a decision on a question of procedure in the terms of article 29 and that the decision was entrusted to all members of the tribunal, including the challenged arbitrator. In an arbitration with more than one arbitrator, that decision

may be made by a majority of all its members in accordance with article 29 (first sentence).

39. The Working Group did not accept a suggestion to include in article 13 an explicit statement to the effect that a successful challenge led to the termination of the mandate of the challenged arbitrator. The Working Group felt that that legal effect of a successful challenge was sufficiently clear by implication.

#### *Article 14*

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

##### *"Article 14. Failure or impossibility to act*

*"If an arbitrator [fails to act or becomes *de jure* or *de facto* unable to perform his functions] [becomes *de jure* or *de facto* unable to perform his functions or for other reasons fails to act], his mandate terminates if he withdraws from his office or if the parties agree on the termination. Otherwise, if a controversy remains concerning any of these grounds, any party may request the Court specified in article 6 to decide on the termination of the mandate, which decision shall be final."*

41. The Working Group adopted that article, including the words "*becomes de jure or de facto unable to perform his functions or for other reasons fails to act*" and deleting the words "*fails to act or becomes de jure or de facto unable to perform his functions*".

42. It was noted that that article envisaged the termination of the mandate only for certain reasons specified in that provision and that neither article 14 nor article 15 indicated clearly in what other cases the mandate of an arbitrator would terminate. In particular, there was no provision on the termination of the mandate of an arbitrator by agreement of the parties and it was, therefore, not clear whether the parties by consent could remove an arbitrator only for certain reasons or whether their freedom in that respect was unlimited. Another important question in need of clarification was whether an arbitrator was free to resign only for certain reasons or whether he was free to resign without showing sufficient cause.

43. In discussing those questions it was understood that, as had been decided at earlier sessions, the model law would not deal with the legal responsibility of an arbitrator or other issues pertaining to the party-arbitrator relationship.

44. As regards the question of removal of an arbitrator by consent, there was wide support for the view that, because of the consensual nature of arbitration, the parties had unrestricted freedom to agree on the termination of the mandate of an arbitrator. As regards the question of resignation of an arbitrator, there was some support for the view that a person who had accepted to act as an arbitrator should not be allowed to resign for capricious reasons. The prevailing view,

however, was that it was impractical to require just cause for the resignation, since an unwilling arbitrator could not, in fact, be forced to perform his functions.

45. While recognizing the complex nature of those questions the Working Group, after deliberation, decided that the model law should take a stand on those issues and express the views prevailing in the Group. It was thought that the appropriate place for doing so was article 15. That provision already envisaged resignation "for any other reason", so that only the case of removal by consent had to be added there.

#### *Article 15*

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

##### *"Article 15. Appointment of substitute arbitrator*

[Where the mandate of an arbitrator terminates under article 13 or 14 or because of his resigning for any other reason,] 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."

47. The Working Group adopted that article, subject to the insertion after the words "resigning for any other reason" of the words "or because of the revocation of his mandate by agreement of the parties or in any other case of termination of his mandate".

48. The words "or because of the revocation of his mandate by agreement of the parties" were added in pursuance of the decision of the Working Group taken during its deliberations on article 14 (see para. 45, above). The words "or in any other case of termination of his mandate" were added in order to cover all possible cases in which the need for the appointment of a substitute arbitrator could arise. While there was some support for a detailed list of instances (e.g., death, illness, incapacity), the general formula was preferred for the sake of simplicity and since the detailed list was liable to being incomplete.

## CHAPTER IV. JURISDICTION OF ARBITRAL TRIBUNAL

#### *Article 16*

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

##### *"Article 16. Competence to rule on own jurisdiction*

"(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. A party is not precluded from raising such a plea by the fact that he has appointed, or participated in the appointment of, an arbitrator. A plea that the arbitral tribunal has exceeded the scope of its authority shall be raised promptly after the arbitral tribunal has indicated its intention to [deal with] [decide on] the matter alleged to be beyond the scope of its authority. The arbitral tribunal may in either case, admit a later plea if it considers the delay justified.

"(3) The arbitral tribunal may rule on a plea referred to in paragraph (2) either as a preliminary question or in an award on the merits. [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.]"

50. The Working Group adopted that article, subject to the revision of the third sentence in paragraph (2) as follows: "A plea that the arbitral tribunal is exceeding the scope of its authority shall be raised promptly after the arbitral tribunal has indicated its intention to decide on the matter alleged to be beyond the scope of its authority".

51. It was observed, with reference to the question raised in the note prepared by the secretariat (A/CN.9/WG.II/WP.50, para. 16; reproduced in this Yearbook, part two, II, B, 3, c), that a party who failed to raise the plea as required under article 16 (2) should be precluded from raising such objections not only during the later stages of the arbitral proceedings but also in other contexts, in particular, in setting aside proceedings or enforcement proceedings, subject to certain limits such as public policy, including arbitrability.

52. As regards paragraph (3) of that article, the Working Group decided to retain that paragraph in the light of its decision to delete article 17 (see paras. 54-56, below).

#### *Article 17*

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

##### *"Article 17. Concurrent court control*

"(1) [Notwithstanding the provisions of article 16,] a party may [at any time] request the Court specified in article 6 to decide whether a valid arbitration agreement exists and [, if arbitral proceedings have commenced,] whether the arbitral tribunal has jurisdiction [with regard to the dispute referred to it].

"(2) While such issue is pending with the Court, the arbitral tribunal may continue the proceedings [unless the Court orders a stay of the arbitral proceedings]."

54. The Working Group decided to delete that article.

55. It was noted that the concurrent court control provided for in that article was to a large extent in conflict with the provision in the last sentence of paragraph (3) of article 16, which precluded a party from contesting an affirmative ruling by the arbitral tribunal on its jurisdiction until the final award on the merits was made. There was some support for retaining the provision on concurrent court control for the sake of a speedy and cost-saving settlement of any controversy about the arbitral tribunal's jurisdiction. However, the prevailing view was in favour of deleting article 17 since it might have adverse effects throughout the arbitral proceedings by opening the door to delaying tactics and obstruction and because it was not in harmony with the principle underlying article 16 that it was initially and primarily for the arbitral tribunal to decide on its competence, subject to ultimate court control.

56. As to the way of providing ultimate court control over the power of an arbitral tribunal to decide on its jurisdiction, there was some support for the view that the arbitral tribunal may make the ruling on its jurisdiction in the form of an award, which could then be reviewed by the court in setting aside proceedings under article 34. The proponents of that view were divided on whether this approach should be expressly regulated in the model law. The prevailing view, however, was to allow the ultimate court control only after the final award on the merits was made, as provided for in the last sentence of paragraph (3) of article 16.

#### *Article 18*

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

*"Article 18. Power of arbitral tribunal to order interim measures*

"Unless otherwise agreed by the parties, the arbitral tribunal may, at the request of a party, order the taking of any interim measure [of protection it considers necessary in respect of the subject-matter of the dispute]. The arbitral tribunal may require of a party or the parties security for the costs of such measure."

58. The Working Group adopted that article, subject to the revision of the first sentence as follows: "Unless otherwise agreed by the parties, the arbitral tribunal may, at the request of a party, order the other party or the parties to take any interim measure of protection which the arbitral tribunal considers necessary in respect of the subject-matter of the dispute".

59. The words "the other party or the parties" were inserted in order to make clear that the power of the arbitral tribunal, which was derived from the parties, was limited to the parties and that, therefore, such orders could not be addressed to third persons.

## CHAPTER V. CONDUCT OF ARBITRAL PROCEEDINGS

#### *Article 19*

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

*"Article 19. Determination of rules of procedure*

*"(1) Subject to the [mandatory] provisions of this Law, the parties are free to agree on the procedure to be followed by the arbitral tribunal in conducting the proceedings.*

*"(2) Failing such agreement, 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."*

61. The Working Group adopted that article, subject to the deletion of the word "mandatory" in paragraph (1) and the addition, at the end of that paragraph, of the words "provided that the parties are treated with equality and that each party is given a full opportunity of presenting his case".

62. That addition to paragraph (1) was designed to emphasize the importance of the principles of equality and the right to be heard which should be observed not only by the arbitral tribunal but also by the parties when laying down any rules of procedure.

63. It was noted, with reference to the question raised in the note prepared by the secretariat (A/CN.9/WG.II/WP.50, para. 14; reproduced in this Yearbook part two, II, B, 3, c), that the freedom of the parties to agree on the procedure should be a continuing one throughout the arbitral proceedings, as was provided in paragraph (1), and should not be limited, for example, to the time before the first arbitrator was appointed.

#### *Article 20*

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

*"Article 20. Place of arbitration*

*"(1) The parties are free to agree on the place of arbitration. Failing such agreement, the place of arbitration shall be determined by the arbitral tribunal.*

*"(2) Notwithstanding the provisions of paragraph (1) of this article, the arbitral tribunal may, unless otherwise agreed by the parties, meet at any place it considers appropriate for consultation among its members, for hearing witnesses, experts or the parties,*

or for inspection of goods, other property, or documents."

65. The Working Group adopted that article.

#### *Article 21*

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

**"Article 21. Commencement of arbitral proceedings**

"Unless otherwise agreed by the parties, the arbitral proceedings [shall be deemed to] commence on the date on which a request that a [particular] [specified] dispute be referred to arbitration is received by the respondent [provided that such a request identifies the claim]."

67. The Working Group adopted that article in the following modified form:

"Unless otherwise agreed by the parties, the arbitral proceedings in respect of a particular dispute commence on the date on which a request that that dispute be referred to arbitration is received by the respondent."

#### *Article 22*

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

**"Article 22. Language**

"(1) The parties are free to agree on the language or languages to be used in the arbitral proceedings. Failing such agreement, the arbitral tribunal shall determine the language or languages to be used in the proceedings. This agreement or determination, unless otherwise specified therein, shall apply to any written statement by a party, any hearing [of witnesses, experts or the parties], and any award, decision or other communication by the arbitral tribunal.

"(2) The arbitral tribunal may order that any documentary evidence shall be accompanied by a translation into the language or [one of the] languages agreed upon by the parties or determined by the arbitral tribunal."

69. The Working Group adopted that article, subject to the deletion, in paragraph (1), of the words "of witnesses, experts or the parties" and, in paragraph (2), of the words "one of the".

70. While some concern was expressed that the provisions contained in the last sentence of paragraph (1) and in paragraph (2) were too detailed for a model law, the prevailing view was that those provisions were useful in view of the great practical importance of the question of language and in that they drew the attention of the parties to different instances in which the agreed or determined language could affect their position in the proceedings.

#### *Article 23*

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

**"Article 23. Statements of claim and defence**

"(1) Within the period of time agreed by the parties or determined by the arbitral tribunal, the claimant shall state the facts supporting his claim, the points at issue and the relief or remedy sought, and the respondent shall state his defence in respect of these particulars. The parties may annex to their statements all documents they consider to be relevant or may add a reference to the documents or other evidence they will submit.

"(2) [During the course of the arbitral proceedings] either party may amend or supplement his claim or defence unless the arbitral tribunal considers it inappropriate to allow such amendment having regard to the delay in making it or prejudice to the other party or any other circumstances."

72. The Working Group adopted that article, including, in paragraph (2), the words "During the course of the arbitral proceedings".

73. It was noted that the provision of paragraph (1) which referred to the "claim" should also apply to a counter-claim. As to whether this understanding should be expressed in that provision, it was agreed that the same question arose in respect of a number of articles of the draft of the model law and that it should therefore be considered at a later stage in a general manner.<sup>7</sup>

#### *Article 24*

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

**"Article 24. Hearings and written proceedings**

"(1) Subject to any contrary agreement by the parties, the arbitral tribunal shall decide whether to hold oral hearings or whether the proceedings shall be conducted on the basis of documents and other materials. However, if a party so requests, 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.

"(2) In order to enable the parties to be present at any hearing and at any meeting of the arbitral tribunal for inspection purposes, they shall be given sufficient notice in advance.

"(3) All statements, documents or other information supplied to the arbitral tribunal by one party shall be communicated to the other party. Also any expert report or other document, on which the arbitral tribunal may rely in making its decision, shall be communicated to the parties."

<sup>7</sup>See decision below, para. 196.

75. The Working Group adopted that article, subject to the modification of paragraph (1) and (2) in the following form:

"(1) Subject to any contrary agreement by the parties, the arbitral tribunal shall decide whether to hold oral hearings or whether the proceedings shall be conducted on the basis of documents and other materials.

"(1 bis) Notwithstanding the provisions of paragraph (1) of this article, if a party so requests, the arbitral tribunal may, at an appropriate stage of the proceedings, hold hearings for the presentation of evidence or for oral argument.

"(2) The parties shall be given sufficient advance notice of any hearing or any meeting of the arbitral tribunal for inspection purposes."

76. The Working Group was agreed that the last sentence of paragraph (1) was ambiguous in that it allowed the following conflicting interpretations: (a) a party has a right to request a hearing only if the parties have not agreed that the proceedings be conducted on the basis of documents and other materials and, as a result, it was for the arbitral tribunal to decide on the mode of the proceedings; (b) a party has a right to request an oral hearing even if the parties have agreed on written proceedings.

77. Divergent views were expressed as to which was the appropriate rule in terms of policy. Under one view, full effect should be given to an agreement by the parties that the arbitral proceedings be conducted without hearings even if a party later requested a hearing. The prevailing view was that the right of a party to request a hearing was of such importance that the parties should not be allowed to exclude it by agreement.

78. The proponents of the prevailing view were divided on whether the arbitral tribunal had to follow such a request by a party and hold hearings or whether it should have discretion in that regard. Under one view, the right of a party to request a hearing was so fundamental that the arbitral tribunal should have to comply with it. Under another view, which the Working Group adopted after deliberation, a certain control by the arbitral tribunal was desirable and the proper wording for the provision was therefore that the arbitral tribunal "may hold" hearings, if a party so requested.

79. It was noted that paragraph (1) (second sentence) referred to "hearings for the presentation of evidence by witnesses, including expert witnesses" and that that reference was too limited because it did not cover other types of evidence, for example, cross-examination or testimony of a party. The Working Group was agreed that, instead of enumerating all possible types of evidence recognized in various legal systems, a general formula was preferable and that, therefore, the reference should merely read: "hearings for the presentation of evidence".

80. It was observed that paragraph (2), in addition to establishing the requirement of advance notice, could be understood as dealing with the procedural rights of the parties at a hearing or at a meeting for inspection purposes and that such a regulation was insufficient and too restrictive. In order to meet that concern, the Working Group decided to revise the provision so as to retain only the requirement of advance notice.

#### *Article 25*

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

*"Article 25. Default of a party*

*"Unless otherwise agreed by the parties, if, without showing sufficient cause,*

*"(a) the claimant fails to communicate his statement of claim in accordance with article 23 (1), the arbitral proceedings shall be terminated;*

*"(b) the respondent fails to communicate his statement of defence in accordance with article 23 (1),*

*"Variant A: the arbitral proceedings shall continue;*

*"Variant B: the arbitral tribunal shall continue the proceedings without treating such failure as an admission of the claimant's allegations;*

*"Variant C: the arbitral tribunal shall treat this as a denial of the claim and continue the proceedings;*

*"(c) any party fails [to comply with a request by the arbitral tribunal] to appear at a hearing, or to produce documentary evidence, the arbitral tribunal [may] [shall] continue the proceedings [and may make the award on the evidence before it]."*

82. The Working Group adopted that article, including, in subparagraph (b), the wording of variant B, and subparagraph (c) in the following modified form:

*"(c) any party fails to appear at a hearing, or to produce documentary evidence, the arbitral tribunal may continue the proceedings and make the award on the evidence before it."*

83. As regards the three variants presented in subparagraph (b), the Working Group, after deliberation, adopted the wording of variant B. That wording, while according certain discretion to the arbitral tribunal, contained a limitation which was considered useful in view of the fact that under many national laws on civil procedure default of the defendant in court proceedings was treated as an admission of the claimant's allegations.

84. It was suggested that the provision should be more elaborate and provide some guidance concerning certain procedural issues (e.g., how to establish the default and in what manner to conduct the proceedings and make the award). The Working Group, after deliberation, was agreed that a model law need not contain detailed procedural rules in that respect.

**Article 26**

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

*"Article 26. Expert appointed by arbitral tribunal"*

"(1) Unless otherwise agreed by the parties before the appointment of the first arbitrator, the arbitral tribunal may appoint one or more experts to report to it on specific issues to be determined by the tribunal.

"(2) The [expert may, within his terms of reference, require a party to give him] [arbitral tribunal may require a party to give the expert] any relevant information or to produce, or to provide access to, any relevant documents, goods or other property for his inspection.

"(3) The expert shall, after delivery of his written or oral report, participate in a hearing where the parties have the opportunity to interrogate him and to present expert witnesses in order to testify on the points at issue."

86. The Working Group adopted that article, subject to the deletion, in paragraph (1), of the words "before the appointment of the first arbitrator" and, in paragraph (2), the deletion of the words "expert may, within his terms of reference, require a party to give him" and, before the first word of paragraph (3), the addition of the words "If a party so requests or if the arbitral tribunal considers it necessary".

87. There was some support for retaining, in paragraph (1), the words "before the appointment of the first arbitrator" since that would ensure that an arbitrator, when accepting his mandate, would know about the restriction on his power to appoint an expert. However, the prevailing view was that the freedom of the parties to restrict that power of the arbitral tribunal was paramount and should not be subject to such a time-limit.

88. As regards paragraph (2), the Working Group was agreed that it was more appropriate that the arbitral tribunal itself, and not the expert, should require any relevant information or materials.

89. As regards paragraph (3), the purpose of the modification was to make clear that a hearing with the expert had not to be held in each and every case but only where a party so requested or where, without such a request, the arbitral tribunal considered it necessary.

evidence. The request shall [be in the language of the court, include a certified copy of the arbitration agreement and] specify:

"(a) The names and addresses of the parties and the arbitrators;

"(b) The general nature of the claim and the relief sought;

"(c) The [necessary information on the] evidence to be obtained, in particular

"(i) the name and address of any person to be heard as witness or expert witness and a statement of the subject-matter of the testimony required;

"(ii) the description of any document to be produced or property to be inspected.

"(2) The court may, within its competence and according to its rules on taking evidence [, including provisions on admissibility and on enforcement procedures], execute the request either by taking the evidence itself or by ordering that the evidence be provided directly to the arbitral tribunal. If so [suggested] [demanded] in the request, the court may transmit the request to a competent court of a foreign State [where assistance in obtaining evidence is required].

"[(3) Where a foreign court transmits to a competent court of this State a request for assistance in taking evidence relating to arbitral proceedings in that foreign State, the court of this State shall treat such request as having been made by that foreign court itself.]"

91. The Working Group adopted that article in the following modified form:

"(1) In arbitral proceedings held in this State or under this Law, the arbitral tribunal or a party with the approval of the arbitral tribunal may request from a competent court of this State assistance in taking evidence. The request shall specify:

"(a) the names and addresses of the parties and the arbitrators;

"(b) the general nature of the claim and the relief sought;

"(c) the evidence to be obtained, in particular,

"(i) the name and address of any person to be heard as witness or expert witness and a statement of the subject-matter of the testimony required;

"(ii) the description of any document to be produced or property to be inspected.

"(2) The court may, within its competence and according to its rules on taking evidence, execute the request either by taking the evidence itself or by ordering that the evidence be provided directly to the arbitral tribunal."

92. The Working Group, in considering whether a provision along the lines of article 27 should be retained

**Article 27**

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

*"Article 27. Court assistance in taking evidence"*

"(1) The arbitral tribunal or a party with the approval of the arbitral tribunal may request from a competent court of this State assistance in taking

in the model law, discussed the intended purpose and possible effect of that article.

93. There was some support for the view that that article, since it formed part of a law on arbitration, could not and should not attempt to alter the existing law of a State concerning court assistance in taking evidence. For example, where that law contained rules for court assistance to other courts but not to arbitral tribunals, article 27 would not open the door to court assistance in aid of arbitration. Accordingly, the effect of the provision was limited to recognizing the right to request court assistance as a part of accepted arbitral procedure.

94. There was wide support for the view that the provision had effect beyond the realm of arbitral procedure and that the right to request court assistance under article 27 carried with it the expectation that there were circumstances under which the national law gave the possibility of obtaining assistance by courts. While article 27, thus, was designed to change, for example, a national law which envisaged court assistance only to other courts but not to arbitral tribunals, it did not attempt to interfere with national rules on civil procedure concerning the taking of evidence and the organization of the judicial system including court competence.

95. In the light of that understanding, divergent views were expressed as to whether article 27 should be retained. Under one view, the article should be deleted since the envisaged involvement of courts was contrary to the private nature of arbitration and was regulated in a way which interfered with the internal procedural law. Under another view, the article should be retained in its entirety, though with certain modifications. It was pointed out in support of that view that the provision was useful in that it would provide the possibility of assistance in obtaining evidence which the arbitral tribunal itself could not obtain since it lacked means of compulsion. In the context of international commercial arbitration such assistance should be provided not only in arbitrations which were held in the State where the court was located but also in arbitrations held abroad (as envisaged in the second sentence of paragraph (2) and in paragraph (3)). Under yet another view, article 27 should be retained only in so far as it dealt with court assistance in arbitrations within the same State. It was stated in support of that view that, while court assistance as such was useful, its extension to foreign arbitral tribunals could not be appropriately dealt with by a model law.

96. That latter view was adopted by the Working Group as a compromise. Accordingly, it was decided to retain, with some modifications, paragraph (1) and the first sentence of paragraph (2).

97. The Working Group was agreed that it was desirable to express that limited scope of application of the article by adding, before the first word of paragraph (1), the words "In arbitral proceedings held in this State or under this Law". It was understood that that

decision was subject to later review in the context of the general deliberation on the territorial scope of application of the model law.<sup>8</sup>

98. As regards, in paragraph (1), the words "or a party with the approval of the arbitral tribunal", it was agreed that that wording reflected a compromise between the two conflicting views that court assistance would be rendered only upon request by the parties or exclusively upon request by the arbitral tribunal.

99. As regards, in paragraph (1), the words "be in the language of the court", the Working Group decided to delete them because such a provision was either redundant or in possible conflict with national regulations on the use of languages in courts.

100. As regards, in paragraph (1), the words "include a certified copy of the arbitration agreement and", the Working Group decided to delete them since that requirement was unnecessarily burdensome in some circumstances, and in other circumstances, for which it seemed to be intended, not sufficient because it did not establish proof of the authority of the arbitrators.

101. The Working Group was agreed that, in paragraph (1) (c), the words "necessary information on the" and, in paragraph (2), the words "including provisions on admissibility and on enforcement procedures" were redundant and should be deleted.

## CHAPTER VI. MAKING OF AWARD AND TERMINATION OF PROCEEDINGS

### Article 28

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

#### "Article 28. Rules applicable to substance of dispute

"(1) The arbitral tribunal shall decide the dispute in accordance with such rules of law as [are chosen] [may be agreed] 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 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 rule which it considers applicable.

"(3) The arbitral tribunal shall decide *ex aequo et bono* or as *amicable compositeur* only if the parties have expressly authorized it to do so."

103. The Working Group adopted that article, subject to the retention, in paragraph (1), of the words "are chosen" and the deletion of the words "may be agreed".

<sup>8</sup>See discussion below, paras. 165-168.

104. An observation was made that, in paragraph (2), the expression "considers" might be construed as giving too wide a discretion to the arbitral tribunal in finding the conflict of laws rules and that it was, therefore, desirable to use another expression. However, the Working Group decided to retain the present wording in view of the fact that the same wording had been adopted in other legal texts on arbitration.

#### *Article 29*

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

*"Article 29. Decision-making by panel of arbitrators*

"In arbitral proceedings with more than one arbitrator, any award, including interim [, interlocutory] and partial award, and any other decision of the arbitral tribunal shall be made, unless otherwise agreed by the parties, by a majority of all its members. However, the parties or the arbitral tribunal may authorize a presiding arbitrator to decide questions of procedure [on his own]."

106. The Working Group adopted that article in the following modified form:

"In arbitral proceedings with more than one arbitrator, any decision of the arbitral tribunal shall be made, unless otherwise agreed by the parties, by a majority of all its members. However, the parties or the arbitral tribunal may authorize a presiding arbitrator to decide questions of procedure."

107. The Working Group was of the view that that article should only deal with the majority principle in the making of decisions in arbitral proceedings and that it should not attempt to define the term "award". It was, therefore, decided to consider at a later stage whether a definition of "award" should be included in another appropriate article of the model law.<sup>9</sup>

108. There was some support for deleting the last sentence of that article because it might create controversies in cases where it was not certain whether a question was one of procedure or one of substance. However, the Working Group decided to retain the provision because the parties or the arbitrators may use it in order to make an arbitration more expedient and efficient.

#### *Article 30*

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

*"Article 30. Settlement*

"(1) If, during arbitral proceedings, the parties settle the dispute, the arbitral tribunal shall terminate the proceedings and, if requested by the parties and

not objected to by the arbitral 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 31 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."

110. The Working Group adopted that article, subject to the replacement, in paragraph (2), of the words "executory force" by the word "effect".

#### *Article 31*

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

*"Article 31. Form and contents of award*

"(1) The award shall be made in writing and shall be signed by the arbitrator or arbitrators. In arbitral proceedings with more than one arbitrator, the signatures of the majority of all members of the arbitral tribunal shall suffice, provided that the reason for any omitted signature is stated.

"(2) The award shall state the reasons upon which it 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 30.

"(3) The award shall state its date and the place of arbitration as determined in accordance with article 20 (1). The award shall be deemed to have been made at that place.

"(4) After the award is made, a copy signed by the arbitrators in accordance with paragraph (1) of this article shall be delivered to each party."

112. The Working Group adopted that article.

#### *Article 32*

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

*"Article 32. Termination of proceedings*

*"Variant A:*

"(1) The arbitral proceedings are terminated:

"(a) by the making of the final award which disposes of all claims submitted to arbitration; or

"(b) by an agreement of the parties that the arbitral proceedings are to be terminated at a specified date [or after expiry of a specified period of time]; or

"(c) by an order of the arbitral tribunal in accordance with paragraph (2) of this article.

"(2) After having given suitable notice to the parties, the arbitral tribunal shall issue an order for the termination of the arbitral proceedings

<sup>9</sup>See discussion below, paras. 192-194.

"(a) when the claimant withdraws his claim, unless the respondent objects thereto and the arbitral tribunal recognizes a legitimate interest on his part in obtaining a final settlement of the dispute; or

"(b) if for any other reason the continuation of the proceedings becomes unnecessary or inappropriate.

[Where the arbitral tribunal fails to issue an order of termination, any party may request from the Court specified in article 6 a ruling on the termination of the proceedings.]

"(3) The mandate of the arbitral tribunal terminates with the termination of the arbitral proceedings, subject to the provisions of articles 33 and 34 (4)."

*"Variant B:*

"(1) The arbitral proceedings are terminated either by the final award or by agreement of the parties or by an order of termination [by the arbitral tribunal] [which the arbitral tribunal may issue when the continuation of the proceedings appears unnecessary or inappropriate].

"(2) The mandate of the arbitral tribunal terminates with the termination of the arbitral proceedings, subject to the provisions of articles 33 and 34 (4)."

114. The Working Group adopted that article, based on variant B, in the following modified form:

"(1) The arbitral proceedings are terminated either by the final award or by agreement of the parties or by an order of the arbitral tribunal in accordance with paragraph (2) of this article.

*"(2) The arbitral tribunal*

"(a) shall issue an order for the termination of the arbitral proceedings when the claimant withdraws his claim, unless the respondent objects thereto and the arbitral tribunal recognizes a legitimate interest on his part in obtaining a final settlement of the dispute;

"(b) may issue an order of termination when the continuation of the proceedings becomes for any other reason unnecessary or inappropriate.

"(3) The mandate of the arbitral tribunal terminates with the termination of the arbitral proceedings, subject to the provisions of articles 33 and 34 (4)."

115. While there was some support for the more elaborate draft provisions presented in variant A, the Working Group, after deliberation, decided in favour of variant B, for the sake of simplicity.

116. As regards termination of the proceedings by an order of the arbitral tribunal, the Working Group adopted the more explicit wording "which the arbitral tribunal may issue when the continuation of the proceedings appears unnecessary or inappropriate" as well as the provision contained in paragraph (2) (a) of variant A, in order to give some indication of the reasons for an order of termination.

*Article 33*

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

*"Article 33. Correction and interpretation of awards and additional awards*

"(1) Within thirty days of 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 of the date of the award, make such corrections on its own initiative; and

"(b) to give [, within thirty 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, within thirty days of receipt of the award, the arbitral tribunal to make an additional award as to claims presented in the arbitral 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 make that additional award [within sixty days of receipt of the request].

"(3) The provisions of article 31 shall apply to a correction or interpretation of the award or to an additional award."

118. The Working Group adopted that article in the following modified form:

"(1) Within thirty days of 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, within thirty days, in the award any errors in computation, any clerical or typographical errors or any errors of similar nature;

"(b) to give, within thirty days, an interpretation of a specific point or part of the award; such interpretation shall form part of the award.

"(2) The arbitral tribunal may correct any error of the type referred to in paragraph (1) (a) of this article on its own initiative within thirty days of the date of the award.

"(3) Unless otherwise agreed by the parties, a party, with notice to the other party, may request, within thirty days of receipt of the award, the arbitral tribunal to make an additional award as to claims presented in the arbitral proceedings but omitted from the award. The arbitral tribunal shall make the additional award within sixty days, if it considers the request to be justified.

"(4) The arbitral tribunal may extend, if necessary, the period of time within which it shall make a correction, interpretation or an additional award under paragraph (1) or (3) of this article.

"(5) The provisions of article 31 shall apply to a correction or interpretation of the award and to an additional award."

119. Divergent views were expressed as to whether the article should prescribe a period of time during which the arbitral tribunal would have to dispose of a request by a party for a correction or interpretation or an additional award. Under one view, it was not appropriate to fix any period of time. It was pointed out in support of that view that there may be circumstances in which the arbitral tribunal would be unable, for good reasons, to comply with a fixed time-limit. Furthermore, rigid periods of time may create uncertainty as to the validity of actions taken after their expiration and would raise questions as to the sanctions for non-compliance.

120. Under another view, time-limits were necessary in order to ensure timely disposal of a party's request and to limit the duration of uncertainty about the definitive content of the award. It was also pointed out that time-limits were needed in view of the provision of article 34 (3) which set a time-limit for an application for setting aside of an award.

121. Under yet another view, a general formula was preferable which would, for example, require the arbitral tribunal to act "promptly" or "without delay".

122. The Working Group, after deliberation, adopted as a compromise the following solution. Article 33 would set fixed periods of time (of 30 days for a correction or interpretation and of 60 days for an additional award) and would empower the arbitral tribunal to extend these periods of time, if necessary under the circumstances.

123. The Working Group was agreed that these periods of times would commence to run when the arbitral tribunal received the request for a correction, interpretation or an additional award. While it was suggested to express that understanding in the text by adding, after the respective time-period, the words "of receipt of the request", the Working Group decided that there was no need for such an explicit statement since the correct answer obtained clearly from the current text.

124. It was noted that a party requesting a correction, interpretation or an additional award had to give notice to the other party in order to give that party the opportunity to express its views concerning that request. It was suggested that a reasonable period of time during which that party could reply should be taken into account for the calculation of the period of time during which the arbitral tribunal should dispose of the request. While the Working Group did not consider it necessary to lay down an elaborate time schedule in that respect, it was understood that the arbitral tribunal should allow sufficient time for a reply.

125. As regards paragraph (2), it was noted that that provision empowered the arbitral tribunal to make an additional award only in cases where the omission could be rectified without any further hearings and evidence. The Working Group, after deliberation, decided not to retain that requirement because it was unduly restrictive in that it excluded a considerable number of cases where at least a hearing, if not further evidence, was necessary before making the additional award.

## CHAPTER VII. RE COURSE AGAINST AWARD

### *Article 34*

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

"Article 34. *Application for setting aside as exclusive recourse against arbitral award*

"(1) Recourse to a court against an arbitral award made [in the territory of this State] [under this Law] may be made only by an application for setting aside in accordance with paragraphs (2) and (3) of this article.

"(2) An arbitral award may be set aside by the Court specified in article 6 only if

"(a) the party making the application furnishes proof that:

"(i) the parties to the arbitration agreement referred to in article 7 were, under the law applicable to them, 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

"(ii) the party making the application was not given proper notice of the appointment of the arbitrator(s) or of the arbitral proceedings or was otherwise unable to present his case; or

"(iii) the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, only that part of the award which contains decisions on matters not submitted to arbitration may be set aside; or

"(iv) the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the [mandatory provisions of this Law and the] agreement of the parties or, failing such agreement, was not in accordance with this Law; or

"(b) the Court finds that:

- "(i) the subject-matter of the dispute is not capable of settlement by arbitration under the law of this State; or
- "(ii) the award or any decision contained therein is in conflict with the public policy of this State.

"(3) An application for setting aside may not be made after three months have elapsed from the date on which the party making that application had received the award in accordance with article 31 (4) [or, if a request had been made under article 33, from the date on which that request had been disposed of by the arbitral tribunal].

"(4) The Court, instead of setting aside the award, [may order, where appropriate, that the arbitral proceedings be continued] [may authorize the continuation of arbitral proceedings where this would permit an omission or other procedural defect to be cured without having to set aside the award]."

127. The Working Group adopted that article, subject to the addition, at the end of paragraph (1), of the words "or by a request to refuse recognition or enforcement in accordance with article 36",<sup>10</sup> and subject to the replacement of the words "mandatory provisions of this Law and the", in paragraph (2)(a)(iv), by the words "provisions of this Law from which the parties cannot derogate and the", and subject to the deletion, in paragraph (3), of the words "in accordance with article 31 (4)", and subject to the revision of paragraph (4) as follows: "The Court, when asked to set aside an award, may, where appropriate and so requested by a party, suspend the setting aside proceedings for a period of time determined by it in order to give the arbitral tribunal an opportunity to resume the arbitral proceedings or to take such other action as in the arbitral tribunal's opinion will eliminate the grounds for setting aside".

128. While there was some support for the suggestion to place article 34 after the provisions on recognition and enforcement, the Working Group decided to retain the existing order of those articles.

129. It was noted that article 34 regulated the recourse against an arbitral award without defining the term "award" or specifying what types of awards would be covered. In order to achieve the necessary clarification, the Working Group decided to include in the model law a general definition of the term "award" or, at least, to specify what types of awards would be subject to setting aside under article 34. A suggestion for later consideration was to allow recourse against any award deciding on the substance of the dispute.<sup>11</sup>

130. It was observed that paragraph (1), by presenting the application for setting aside as exclusive recourse against awards, appeared to disregard the right of a party under article 36 to raise objections against the

recognition or enforcement of an award. Although that right was exercised in reply to an initiative by the other party, the Working Group was agreed that, for the sake of clarity, paragraph (1) should make reference to that other type of recourse.<sup>12</sup>

131. As regards the words "[in the territory of this State] [under this Law]", the Working Group was agreed that it was premature to decide on the specific scope of application of article 34 before having discussed the territorial scope of application of the model law in general.<sup>13</sup>

132. As regards paragraph (2) (a) (i), there was considerable support for substituting the words "a party to the arbitration agreement referred to in article 7 lacked the capacity to conclude the agreement" for the words "the parties to the arbitration agreement referred to in article 7 were, under the law applicable to them, under some incapacity" since the latter wording was seen as containing an incomplete and inappropriate conflict of laws rule. The prevailing view, however, was to retain the current wording which was identical to the one in article V (1) (a) of the 1958 New York Convention.

133. There was some support for deleting the reference, in paragraph (2) (a) (i), to the law applicable to the validity of the arbitration agreement and, thus, to state as reason for refusal merely that "the arbitration agreement is not valid". It was pointed out, in support of that view, that the reference did not set forth a complete system of conflicts rules and had given rise to some difficulties. The prevailing view, however, was to retain the current wording as an acceptable and satisfactory provision which was identical to the one adopted in the 1958 New York Convention.

134. As regards paragraph (2) (a) (iii), the Working Group was agreed that the drafting of that provision, in particular its second part, could be improved. It was suggested, for example, to replace the words "only that part of the award which contains decisions on matters not submitted to arbitration may be set aside" by the words "that part of the award which contains decisions on matters submitted to arbitration need not be set aside".

135. As regards paragraph (2) (a) (iv), the Working Group adopted the policy underlying the words "mandatory provisions of this Law and the arbitration agreement" since a mandatory provision of that law, by definition, would prevail over any procedural agreement by the parties which was in conflict with such provision. However, it was agreed to redraft that portion of the provision so as to avoid the expression "mandatory" which was not understood in all legal systems as meaning "from which the parties cannot derogate".

136. As regards paragraph (2) (b) (i), it was noted that that provision made the law of the forum determine the arbitrability of the subject-matter of the dispute. It was

<sup>10</sup>See, however, decision below, para. 197.

<sup>11</sup>See discussion below, paras. 192-194.

<sup>12</sup>See, however, decision below, para. 197.

<sup>13</sup>See discussion below, paras. 165-171.

suggested that such a rule, while appropriate in the context of recognition and enforcement (art. 36 (1) (b) (i)), was not appropriate in setting aside proceedings since here the effect of a finding of non-arbitrability was not limited to the State of the forum but extended to all other States by virtue of article 36 (1) (a) (v). Such global effect should obtain only from a finding that the subject-matter of the dispute was not capable of settlement by arbitration under the law applicable to that issue which was not necessarily the law of the State of the setting aside proceedings. It was, therefore, suggested to delete the provision of paragraph (2) (b) (i). The result of that deletion, which received considerable support, would be to limit the court control under article 34 to those cases where non-arbitrability of a certain subject-matter formed part of the public policy of that State (para. (2) (b) (ii)) or where the court regarded arbitrability as an element of the validity of an arbitration agreement (para. (2) (a) (i)), although some proponents of that suggestion sought the more far-reaching result of excluding non-arbitrability as a reason for setting aside. Another suggestion was to delete, in paragraph (2) (b) (i), merely the reference to "the law of this State" and, thus, to leave open the question as to which was the law applicable to arbitrability.

137. The Working Group, in discussing those suggestions, was agreed that the issues raised were of great practical importance and, in view of their complex nature, required further study. The Working Group, after deliberation, decided to retain, for the time being, the provision of paragraph (2) (b) (i) in its current form so as to invite the Commission to reconsider the matter and to decide, in the light of comments by Governments and organizations, on whether the present wording was appropriate or whether the provision should be modified or deleted.

138. As regards paragraph (3), the Working Group reaffirmed its decision to delete the words "in accordance with article 31 (4)". As regards the words "or, if a request had been made under article 33, from the date on which that request had been disposed of by the arbitral tribunal", there was considerable support for deleting those words since they might open the door for dilatory tactics by a party and because an unbreakable time-limit for applications for setting aside was desirable for the sake of certainty and expediency. The prevailing view, however, was to retain those words since they presented the reasonable consequence of article 33 which allowed a party to request a correction, interpretation or an additional award. It was also pointed out that the periods of time contained in article 33 enabled the arbitral tribunal to minimize the risk of dilatory tactics and provided a basis for calculating the possible extension of the time-limit prescribed in paragraph (3) of article 34.

139. As regards paragraph (4), the Working Group adopted the policy underlying that provision since remission, though not known in all legal systems, could be a useful device for curing procedural defects without having to set aside the award. It was noted that the wording "instead of setting aside the award" was not

felicitous since it could be understood as upholding the validity of the award for the time during which the arbitral tribunal dealt with the case remitted to it. It was also noted that it was misleading to speak of a "continuation of the arbitral proceedings" since these were terminated by the final award and, apart from that, regard should be had to the fact that the arbitral tribunal may have to repeat an earlier phase of the proceedings. The Working Group was agreed that the wording set forth above (para. 127) would meet those concerns.

## CHAPTER VIII. RECOGNITION AND ENFORCEMENT OF AWARDS

### *Article 35*

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

#### *"Article 35. Recognition and enforcement"*

"(1) An arbitral award [within the scope of article 1 (1)] [made within or outside the territory of this State] shall be recognized as binding, subject to the provisions of article 36.

"(2) To obtain enforcement, an application shall be made in writing to the competent court, accompanied by the duly authenticated original award or a duly certified copy thereof, and the original arbitration agreement referred to in article 7 or a duly certified copy thereof. If the award or agreement is not made in an official language of this State, the party applying for enforcement of the award shall supply a duly certified translation of these documents into such language.\*"

\*The conditions set forth in this paragraph are intended to set maximum standards. It would, thus, not be contrary to the harmonization to be achieved by the model law if a State retained even less onerous conditions [for enforcement of awards made in that State or under the law of that State].

141. The Working Group adopted that article in the following modified form:

"(1) An arbitral award, irrespective of the country in which it was made, shall be recognized as binding and, upon application in writing to the competent court, shall be enforced subject to the provisions of this article and of article 36.

"(2) The party relying on an award or applying for its enforcement shall supply the duly authenticated original award or a duly certified copy thereof, and the original arbitration agreement referred to in article 7 or a duly certified copy thereof. If the award or agreement is not made in an official language of this State, the party shall supply a duly certified translation thereof into such language.

"(3) Filing, registration or deposit of an award with a court is not a pre-condition for its recognition or enforcement in this State."

142. Divergent views were expressed as to whether the model law should contain provisions on the recognition and enforcement of both domestic and foreign awards. Under one view, it was not appropriate to retain in the model law provisions which would regulate recognition and enforcement of foreign awards, in view of the existence of widely adhered to multilateral treaties such as the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. It was pointed out that those States which had not ratified or acceded to that Convention should be invited to do so but that a State which decided not to adhere to that Convention was unlikely to adopt the almost identical rules laid down in articles 35 and 36. It was further pointed out that provisions on recognition and enforcement of foreign awards were not needed by those States which adhered to the 1958 New York Convention. In addition, such provisions in the model law might cast doubt on the effect of the reciprocity reservation made by many member States and may create other difficulties in the application of this Convention. Yet another advantage of not covering foreign awards was that the remaining provisions could be better tailored to domestic awards without the need for harmony with the 1958 New York Convention.

143. The prevailing view, however, was to retain provisions covering both domestic and foreign awards. The main reason in support of that view was that in international commercial arbitration the place of arbitration (and of the award) should be of limited importance and that, therefore, such awards should be recognized and enforced in a uniform manner, irrespective of their place of origin. Provisions in the model law covering also foreign awards could prove useful to States which had not adopted the legal régime of the 1958 New York Convention. They could also be of supplementary assistance to States which adhered to the 1958 New York Convention or a similar convention, by providing a régime for non-convention awards. It was pointed out that any possible conflict between the two régimes would be avoided or settled by the proviso expressed in article 1 (1) according to which the model law yielded to treaty law.

144. The Working Group noted that article 35 would apply to awards from all countries without any restriction such as a requirement of reciprocity. A suggestion was made to meet the concerns of those States which were not prepared to adopt such an unrestricted provision by incorporating into the draft text some kind of reciprocity mechanism. The Working Group, after deliberation, decided not to adopt that suggestion for substantive and technical reasons. It was pointed out, for example, that a model law on international commercial arbitration should not promote the use of territorial links and that it was technically difficult, although not impossible, to provide in a model law a workable mechanism of reciprocity. The Working Group was agreed that a State which wanted to apply article 35 only on the basis of reciprocity should express this restriction in its legislation, specifying the basis or connecting factor and the technique used by it.

145. The Working Group was agreed that the words between square brackets in paragraph (1) were in line with its above policy decisions but that it sufficed to use the words "irrespective of the country in which it was made". The Working Group was also agreed to express the idea, implicit in paragraph (1), that arbitral awards should not only be recognized as binding but also enforced.

146. The Working Group was agreed that a distinction should be drawn between recognition standing alone and enforcement. While an award would be enforced only upon application by a party, recognition was an abstract legal effect which could obtain automatically without necessarily being requested by a party.

147. As regards paragraph (2), the Working Group was agreed that the documents referred to therein should also be supplied by a party which relied on an award. As to the footnote annexed to that paragraph, the Working Group decided to delete the words "for enforcement of awards made in that State or under the law of that State".

148. The Working Group considered the issues raised in the note prepared by the Secretariat (A/CN.9/WG.II/WP.50, paras. 27-29; reproduced in this *Yearbook*, part two, II, B, 3, c). As regards the suggestions to express the notion that an award should be recognized as binding "between the parties" and to express the starting point of such recognition, the Working Group was agreed that there was no need for express statements. The Working Group adopted the third suggestion which was to express in the model law that filing, registration or deposit of an award was not a pre-condition for its recognition or enforcement under article 35.

#### *Article 36*

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

"Article 36. *Grounds for refusing recognition or enforcement*

"(1) Recognition or enforcement of an arbitral award [made within or outside the territory of this State] may be refused only:

"(a) at the request of the party against whom it is invoked, if that party furnishes to the competent court where recognition or enforcement is sought proof that:

"(i) the parties to the arbitration agreement referred to in article 7 were, under the law applicable to them, 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 the country where the award was made; or

"(ii) the party against whom the award is invoked was not given proper notice of the

appointment of the arbitrator(s) or of the arbitral proceedings or was otherwise unable to present his case; or

- "(iii) the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the 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
- "(iv) 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; or
- "(v) the award has not yet become binding on the parties or has been set aside or suspended by a court of the country in which, or under the law of which, that award was made; or
- "(b) if the court finds that:
  - "(i) the subject-matter of the dispute is not capable of settlement by arbitration under the law of this State; or
  - "(ii) the recognition or enforcement of the award would be contrary to the public policy of this State.

"(2) A party, against whom recognition or enforcement of an award made [in the territory of this State] [under this Law] is sought during the period of time referred to in article 34 (3), may raise any objection in accordance with paragraph (1) of this article only by an application for setting aside to the Court specified in article 6.

"[(3) Where a party seeks recognition, but not enforcement, of an award before an authority other than a court, the other party may request the Court specified in article 6 to order refusal of recognition in accordance with paragraph (1) of this article.]

"[(4) If an application for setting aside or suspension of an award has been made to a court referred to in paragraph (1) (a) (v) or (2) of this article, the court where recognition or enforcement is sought may, if it considers it proper, adjourn its decision and may also, on the application of the party claiming recognition or enforcement of the award, order the other party to give appropriate security.]

150. The Working Group adopted that article, subject to the replacement, in the opening phrase of paragraph (1), of the words "made within or outside the territory of this State" by the words "irrespective of the country in which it was made", and subject to the deletion of paragraphs (2) and (3) and, in paragraph (4), of the words "or (2)".

151. As regards the words placed between square brackets in the opening phrase in paragraph (1), the Working Group was agreed that the same words as used in article 35 (1) should be used here.

152. The Working Group noted that the idea underlying paragraph (2) was to avoid double control based on identical reasons during the period of time within which a party could apply for setting aside. There was considerable support for this policy which would prevent conflicting decisions of, on the one side, the court of enforcement and, on the other side, the court requested to set aside the award. However, the Working Group, after deliberation, was agreed that the system envisaged under paragraph (2) was not an appropriate one. The Working Group therefore decided to delete paragraph (2), on the understanding that any suggestion for a more acceptable system could be considered by the Commission.

153. The Working Group considered a proposal to insert, after paragraph (2), a new paragraph (2 bis) as follows:

"(2 bis) If an application for setting aside the award has not been made within the time-limit prescribed in article 34 (3), the party against whom recognition or enforcement thereafter is sought may not raise any other objections than those referred to in this article, paragraph (1), subparagraphs (a) (i) or (v) or (b)."

Divergent views were expressed as to whether such a provision should be incorporated in the model law. Under one view, it was desirable to adopt a provision along these lines which would reduce the grounds for refusal of recognition and enforcement in those cases where a party had not made an application for setting aside during the time-limit prescribed therefor. It was pointed out that the provision was useful in that it induced a party to raise objections based on the procedural irregularities covered by article 34 (2) (a) (ii), (iii) and (iv) during the relatively short time-limit set forth in article 34 (3). While some proponents of that view thought that such a provision should apply to recognition and enforcement of only domestic awards, others were in favour of including also foreign awards, in which case the cut-off period was the period of time for requesting setting aside as prescribed in the law of the country where the award was made.

154. The prevailing view, however, was not to adopt such a provision. It was pointed out that the intended preclusion unduly restricted the freedom of a party to decide on how to raise its objections. In view of the different purposes and effects of setting aside and of invoking grounds for refusal of recognition or enforcement, a party should be free to avail itself of the alternative system of defences which was recognized by the 1958 New York Convention and should be maintained in the model law. It was further pointed out that if the provision were limited to recognition and enforcement of domestic awards it would not be consistent with the policy of the model law to treat awards in a uniform manner irrespective of their place of origin.

155. As regards paragraph (3), the Working Group decided that there was no need for including such a provision which dealt with a rather infrequent occurrence and interfered with the internal system of a State concerning the relationship between the administrative branch and the judiciary.

## CHAPTER I. GENERAL PROVISIONS

### *Article 1*

156. The text of article 1 as considered by the Working Group was as follows:

#### *"Article 1. Scope of application"*

"(1) This Law applies to international commercial\* arbitration, subject to any multilateral or bilateral agreement which has effect in this State.

"(2) [An] arbitration is international if:

"(a) the parties to an arbitration agreement have, at the time of the conclusion of that agreement, their places of business in different States; or

"(b) one of the following places is situated outside the [territory of the] State in which the parties have their places of business:

"(i) the place of arbitration as determined in the arbitration agreement;

"(ii) any place where a [substantial] [the preponderant] part of the [characteristic] obligations of the [commercial relationship] [transaction] are to be performed or the place with which the subject-matter of the dispute is most closely connected.

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

\*The term 'commercial' should be given a wide interpretation so as to cover matters arising from all relationships of a commercial nature, irrespective of whether the parties are 'commercial persons' (merchants) under any given national law. Relationships of a commercial nature include, but are not limited to, the following transactions: any trade transaction for the supply or exchange of goods; distribution agreement; commercial representation or agency; factoring; leasing; construction of works; consulting; engineering; licensing; investment; financing; banking; insurance; exploitation agreement or concession; joint venture and other forms of industrial or business co-operation; carriage of goods or passengers by air, sea, rail or road."

157. The Working Group adopted that article, subject to the deletion, in the first sentence of the footnote to paragraph (1), of the words "irrespective of whether the parties are 'commercial persons' (merchants) under any given national law", and subject to the modification of paragraph (2) in the following form:

"(2) An arbitration is international if:

"(a) the parties to an arbitration agreement have, at the time of the conclusion of that agreement, their places of business in different States; or

"(b) one of the following places is situated outside the State in which the parties have their places of business:

"(i) the place of arbitration if determined in, or pursuant to, the arbitration agreement;

"(ii) any place where a substantial part of the obligations of the commercial relationship is to be performed or the place with which the subject-matter of the dispute is most closely connected;

or

"(c) the subject-matter of the arbitration agreement is otherwise related to more than one State."

158. As regards the content of the footnote to paragraph (1), concern was expressed that the words "irrespective of whether the parties are 'commercial persons' (merchants) under any given national law" might be interpreted as dealing with the issue of State immunity. The Working Group noted that those words were not intended to touch upon that sensitive issue but were incorporated for the sole purpose of clarifying that the commercial nature was not dependent on the qualification of the parties as merchants since some national laws used that qualification for distinguishing between commercial and civil relationships. While there was support for maintaining those words for that very purpose, the Working Group, after deliberation, decided to delete them in order to meet the above expressed concern. It was understood that the deletion did not change the meaning of the first sentence of the footnote.

159. As regards the form of the footnote, the Working Group was agreed that the technique of a footnote was not an ideal one. It was nevertheless maintained as an intermediate solution between the approach of attempting to incorporate in the text of article 1 or 2 a definition of the term "commercial" and the mere inclusion in the report of the content of the footnote. It was observed that the footnote could provide guidance to the legislature of a State when adopting the model law but was unlikely to be reproduced in the national enactment of the model law.

160. As regards paragraph (2), divergent views were expressed concerning the test of internationality. Under one view, an arbitration was international only if the requirement set forth in subparagraph (a) was met, which was the test used in the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980; *Yearbook 1980*, part three, I, B). Under another view, a text comprising the criteria referred to in subparagraphs (a) and (b) was appropriate, subject to minor modifications in the wording of subparagraphs (b) (i) and (ii). The prevailing view, however, was to further widen the scope of the term "international". To that effect, various suggestions were made.

161. One proposal was to use as a criterion significant foreign ownership or substantial control. The Working Group did not adopt that proposal in view of the controversial and sensitive nature of the issue and the practical difficulties in devising a workable test.

162. Another suggestion was to use a general formula such as "involving international commercial interests". The Working Group did not adopt that proposal on the ground that it was too vague for a model law. Another suggestion was to combine that general formula with the element of stipulation of the parties, as follows: "if it involves international commercial interests and the parties so agree". While there was considerable support for that proposal, the Working Group did not accept it, for the time being, on the ground that it combined a flexible formula with the requirement of an agreement by the parties.

163. Yet another suggestion was to add a new subparagraph (c) to cover all other cases where the subject-matter of the arbitration agreement was related to more than one State. The Working Group, after deliberation, adopted that proposal since it presented a widely acceptable formula to achieve the desired widening of the test of internationality.

164. As regards paragraph (3), there was some support for replacing the criterion used therein by the "principal place of business", which was regarded as a clearer criterion. The prevailing view, however, was to retain paragraph (3) in its present form which was modelled on the 1980 Vienna Sales Convention.

#### *Territorial scope of application of the model law*

165. In the context of article 1, the Working Group discussed the question of territorial scope of application of the model law on the basis of a note by the secretariat (A/CN.9/WG.II./WP.49; reproduced in this *Yearbook*, part two, II, B, 3, b), in particular the question whether the parties had a right to exclude the applicability of the procedural law of the place of arbitration by agreeing on a foreign procedural law. In discussing that question, it was understood that the working assumption in the preparation of the model law had been that the model law would govern arbitrations which took place in the State of the model law. However, that assumption did not exclude the possibility of including in the model law a provision which would give the parties an autonomy in choosing the procedural law governing the arbitration.

166. Some support was expressed for the view that the parties should have the autonomy to subject an arbitration to a procedural law other than the law of the place of arbitral proceedings. It was pointed out that arbitral proceedings should not be linked exclusively to the procedural law of the territory where such proceedings took place since the parties might have a legitimate interest to subject an arbitration to a

particular procedural law while having equally legitimate interest in conducting arbitral proceedings in a State other than the State of the governing procedural law.

167. However, the view prevailed that the place of arbitration should be the exclusive determining factor for the applicability of the model law. It was stated in support of that view that the exclusive territorial criterion provided a clearer answer to the question as to which law governed an arbitration and which courts had the competence to intervene in the arbitral proceedings. It was further stated that, if the parties had the autonomy to choose a procedural law governing arbitration, a court of the place of arbitration might nevertheless consider itself competent to intervene in arbitral proceedings and that, if the intervening court would have to apply the chosen procedural law, this may lead to difficulties where the remedies prescribed in the applicable procedural law were essentially different from the remedies prescribed in the law of the place of arbitration.

168. The Working Group decided not to deal expressly in this article with a criterion for the delimitation of the scope of application of the model law. The Working Group decided not to review individual articles where this issue might be of particular relevance except for article 34.

169. The Working Group discussed the words placed between the two sets of square brackets in paragraph (1) of article 34. It was noted that the decision on those words had been deferred until the Working Group discussed the territorial scope of application of the model law in general (see para. 131, above).

170. Under one view, the words "in the territory of this State" should be retained and the words "under this Law" should be deleted, since this would be consistent with the prevailing view on the territorial scope of application of the model law. Under another view, the words "under this Law" should be retained and the words "in the territory of this State" should be deleted because that would be acceptable in a State which did not allow the autonomy in choosing a procedural law governing an arbitration as well as in a State which allowed such autonomy. Under yet another view, the two sets of words should be retained without square brackets. This would make it clear that the courts of the State of the model law would not be competent to set aside an award unless it was made in that State and under the law of that State. There was also a view that the words between both sets of square brackets should be deleted in order not to prejudge, in that article, the questions of competence of a court and of applicable law for setting aside an award.

171. However, in the light of the importance of the matter, the view prevailed that the draft text should retain both sets of the words within square brackets.

*Article 2*

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

*"Article 2. Definition and rules of interpretation*

"For the purposes of this Law:

"(a) 'arbitral tribunal' means a sole arbitrator or a panel of arbitrators;

"(b) 'court' means a body or organ of the judicial system of a country;

"(c) where a provision of this Law leaves the parties free to determine a certain issue, such freedom includes the right of the parties to authorize a third party, including an institution, to make that determination;

"(d) where a provision of this Law refers to the fact that the parties have agreed or that they may agree or in any other way refers to an agreement of the parties, such agreement includes any arbitration rules referred to in that agreement;

"(e) any written communication is deemed to have been received if it is delivered to the addressee personally or if it is delivered at his place of business, habitual residence or mailing address, or, if none of these can be found after making reasonable inquiry, then at the addressee's last-known place of business or residence. The communication shall be deemed to have been received on the day it is so delivered."

173. The Working Group adopted that article, subject to the replacement of the words "or residence", at the end of the first sentence of subparagraph (e), by the words "habitual residence or mailing address".

*Article 3*

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

*"Article 3. Mandatory provisions*

"The parties may not derogate from the following provisions of this Law: articles . . ."

175. The Working Group decided to delete that article and to insert, in articles 2 (e), 23 (2) and 26 (2) and (3), the words "unless otherwise agreed by the parties".

176. The Working Group was agreed that the model law should not contain a provision like article 3, wherein all mandatory provisions would be listed, for the reasons set forth in document A/CN.9/WG.II/WP.50, paragraph 9. As suggested in that note by the secretariat, the Working Group was agreed that the non-mandatory character of articles 2 (e), 23 (2) and 26 (2) and (3) should be expressed in those provisions by words such as "unless otherwise agreed by the parties". It was noted that the non-mandatory character of a considerable number of other provisions was already expressed in the current text.

177. It was understood that that decision, i.e. to delete article 3 and to express, in articles 2 (e), 23 (2) and 26 (2) and (3), the non-mandatory character of these provisions, did not mean that all those provisions of the model law which did not express their non-mandatory character were necessarily of mandatory nature. It was noted that the Commission, when reviewing the draft model law in the light of comments by Governments and organizations, may wish to express also in other provisions their non-mandatory character. While there was some support for the view that it should be left to arbitrators and judges to determine the character of the provisions which did not express their non-mandatory character, the prevailing view, adopted by the Working Group, was that it was desirable to express the non-mandatory character in all provisions of the final text which were intended to be non-mandatory.

*Article 4*

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

*"Article 4. Waiver of right to object*

"A party who knows [or ought to have known] that any provision of this Law [from which the parties may derogate] [or any requirement under the arbitration agreement] has not been complied with and yet proceeds with the arbitration without stating his objection to such non-compliance without delay [or, if a time-limit is provided therefor, within such period of time] shall be deemed to have waived his right to object."

179. The Working Group adopted that article, including all the words which had been placed between square brackets.

180. Some support was expressed for deleting the article since it was too rigid and because the determination of a waiver or estoppel situation was better left to arbitrators and judges who, under the model law, were generally accorded discretion. The prevailing view, however, was to retain the provision.

181. Divergent views were expressed as to the scope of the effect of a waiver. Under one view, the rule in article 4 would have effect only for and during the arbitral proceedings. The prevailing view, however, was that its effect extended to the post-award stage, i.e. setting aside proceedings and recognition or enforcement (articles 34 and 36).

182. As regards the wording of the article, divergent views were expressed on the limitation contained in the words "from which the parties may derogate". Under one view, the waiver rule should operate in respect of non-compliance of any provision of law, whether mandatory or not. Under another view, only fundamental procedural defects should be excluded from its operation (e.g., violation of public policy or non-arbitrability). The prevailing view, however, was to retain in article 4 the demarcation line between non-mandatory and mandatory provisions.

*Article 5*

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

*"[Article 5. Scope of court intervention]*

"In matters governed by this Law [concerning the arbitral proceedings or the composition of the arbitral tribunal, courts may exercise supervisory or assisting functions only if] [, no court shall intervene except where] so provided in this Law.]"

184. The Working Group adopted that article in the following modified form:

"In matters governed by this Law, no court shall intervene except where so provided in this Law."

185. Divergent views were expressed as to whether that article should be retained. Under one view, the article should be deleted since it unduly limited the supervision and assistance by courts and infringed on the sovereign policy decision of a State as to the extent of control exercised by its courts. The prevailing view, however, was to retain that article since it was beneficial to international commercial arbitration by providing certainty to the parties and the arbitrators about the instances in which court supervision or assistance was to be expected.

186. The Working Group, after deliberation, adopted the latter view, but was agreed that that decision was a tentative one which the Commission was invited to reconsider in the light of the comments by Governments and international organizations.

187. It was noted that article 5 did not itself take a stand on the extent of court supervision but merely required that any instance of court involvement be expressed in the model law. It was, thus, possible to include, in addition to the various provisions already now envisaging court involvement, yet another provision for certain instances if the Commission saw a need therefor.

188. It was further understood that the introductory words of article 5, "In matters governed by this Law", had a meaning which was narrower than the term "international commercial arbitration" used in article 1 (1) in that it limited the scope of application of article 5 to those matters which were in fact governed by or regulated in the model law. Article 5 would, for example, not exclude court control or assistance in those matters which the Working Group had decided not to deal with in the law (e.g., capacity of parties to conclude arbitration agreement; impact of State immunity; competence of arbitral tribunal to adapt contracts; enforcement by courts of interim measures of protection ordered by arbitral tribunal; fixing of fees or request for deposit, including security for fees or costs; time-limit for enforcement of awards).

*Article 6*

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

*"Article 6. Special court for certain functions of arbitration assistance and supervision*

"The Court with jurisdiction to perform the functions referred to in articles 11 (3), (4), 13 (3), 14, 17 (1), [32 (2) Variant A] and 34 (3) shall be the... (blanks to be filled by each State when enacting the model law)."

190. The Working Group adopted that article, subject to the deletion of the word "Special" in the heading to that article and the replacement of the words "17 (1), [32 (2) Variant A] and 34 (3)" by the words "and 34 (2)".

## B. Other issues

### 1. Headings

191. The Working Group decided to retain the headings of chapters as forming part of the model law. As regards the headings of the individual articles, the Working Group decided to retain them for the mere purpose of easy reference. It was agreed to express that understanding, in a footnote or by other means, as follows: "Headings to individual articles are provided for easy reference but they are not to be relied on in interpreting the text of the article".

### 2. "Award"

192. The Working Group was agreed that it was desirable for the model law to define the term arbitral "award", in particular for purposes of determining which kinds of decisions would be subject to recourse under article 34. The Working Group considered the following proposal: "award" means a final award which disposes of all issues submitted to the arbitral tribunal and any other decision of the arbitral tribunal which finally determine any question of substance or the question of its competence or any other question of procedure but, in the latter case, only if the arbitral tribunal terms its decision an award.

193. While there was wide support for the first part of the proposed definition, i.e. up to the word "substance", serious concerns were expressed as regards the latter part, in particular the last portion referring to decisions on questions of procedure.

194. The Working Group noted that a definition of "award" had important implications to a number of provisions of the model law and was of special relevance to the issues dealt with in articles 34 and 16. Since there was not sufficient time for considering in depth those complex questions, the Working Group decided not to include a definition in the model law to be adopted by it and to invite the Commission to consider the matter.

### 3. Reference to conciliation

195. A suggestion was made to include in the model law a reference to conciliation along the following lines: "Conciliation can be used as an additional method of settling disputes where parties so wish". The Working Group was agreed that, if the Commission were to decide that the model law should be accompanied by a preamble, such preamble could include the above reference.

### 4. Counter-claim

196. The Working Group decided to delete, in article 16 (2), the words "or, with respect to a counter-claim, in the reply to the counter-claim", on the understanding that any provision of the model law referring to the claim would apply, *mutatis mutandis*, to a counter-claim.

### 5. Reference in article 34 to article 36

197. The Working Group noted that the term "recourse" in article 34 (1) had, in a number of languages, the connotation of an initiative or action by a party such as an "appeal". Since that meaning did not fully correspond with the raising of objections envisaged under article 36, the Working Group decided not to retain the reference to that article in article 34 (1).

### 6. Conflict of laws issues

198. With reference to the conflict of laws issues discussed in document A/CN.9/WG.II/WP.49, paragraphs 28 to 41 (reproduced in this Yearbook, part two, II, B, 3, b), the Working Group considered whether any general conflict of laws rules should be prepared as part of the model law.

## 2. Draft text of a model law on international commercial arbitration as adopted by the Working Group (A/CN.9/246—Annex)

### CHAPTER I. GENERAL PROVISIONS

#### Article 1. Scope of application\*

(1) This Law applies to international commercial\*\* arbitration, subject to any multilateral or bilateral agreement which has effect in this State.

\* Article headings are for reference purposes only and are not to be used for purposes of interpretation.

\*\*The term "commercial" should be given a wide interpretation so as to cover matters arising from all relationships of a commercial nature. Relationships of a commercial nature include, but are not limited to, the following transactions: any trade transaction for the supply or exchange of goods; distribution agreement; commercial representation or agency; factoring; leasing; construction of works; consulting; engineering; licensing; investment; financing; banking; insurance; exploitation agreement or concession; joint venture and other forms of industrial or business co-operation; carriage of goods or passengers by air, sea, rail or road.

199. The Working Group was divided on whether such conflicts rules should be included in the model law. Under one view, it was desirable to include rules on the law applicable to the validity of the arbitration agreement in order to have a comprehensive law dealing with all important aspects of arbitration. Under another view, it was desirable to include in the model law rules on conflict of procedural laws since that issue was directly connected with the subject-matter dealt with in the model law.

200. Under yet another view, it was not appropriate to include in a model law on arbitration any conflicts rules. It was pointed out in support of that view that such rules were normally contained in other laws of a State and that there was less need for such rules in the model law in view of the decision of the Working Group not to include a provision on the territorial scope of its application. It was further noted that the Hague Conference on Private International Law was considering the preparation of a convention on the law applicable to the validity of arbitration clauses.

201. The Working Group was agreed that harmonization of conflicts rules relating to arbitration was desirable but that it was not appropriate to envisage inclusion of conflicts rules in the model law, which the Commission was expected to adopt in 1985. It was understood that the Commission may wish to consider the matter and decide on its possible future course of action, in particular, as regards the co-ordination of work between it and the Hague Conference on Private International Law.

### C. Other business

202. It was noted that the draft text of the model law would be sent to Governments and international organizations for comments so that the Commission could take those comments into account before adopting its final text.

#### (2) An arbitration is international if:

- (a) the parties to an arbitration agreement have, at the time of the conclusion of that agreement, their places of business in different States; or
- (b) one of the following places is situated outside the State in which the parties have their places of business:
  - (i) the place of arbitration if determined in, or pursuant to, the arbitration agreement;
  - (ii) any place where a substantial part of the obligations of the commercial relationship is to be performed or the place with which the subject-matter of the dispute is most closely connected; or
  - (c) the subject-matter of the arbitration agreement is otherwise related to more than one State.

(3) For the purposes of paragraph (2) of this article, 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. If a party does not have a place of business, reference is to be made to his habitual residence.

#### *Article 2. Definitions and rules of interpretation*

For the purposes of this Law:

(a) "arbitral tribunal" means a sole arbitrator or a panel of arbitrators;

(b) "court" means a body or organ of the judicial system of a country;

(c) where a provision of this Law leaves the parties free to determine a certain issue, such freedom includes the right of the parties to authorize a third party, including an institution, to make that determination;

(d) where a provision of this Law refers to the fact that the parties have agreed or that they may agree or in any other way refers to an agreement of the parties, such agreement includes any arbitration rules referred to in that agreement;

(e) unless otherwise agreed by the parties, any written communication is deemed to have been received if it is delivered to the addressee personally or if it is delivered at his place of business, habitual residence or mailing address, or, if none of these can be found after making reasonable inquiry, then at the addressee's last-known place of business, habitual residence or mailing address. The communication shall be deemed to have been received on the day it is so delivered.

#### *Article 4. Waiver of right to object*

A party who knows or ought to have known that any provision of this Law from which the parties may derogate or any requirement under the arbitration agreement has not been complied with and yet proceeds with the arbitration without stating his objection to such non-compliance without delay or, if a time-limit is provided therefor, within such period of time, shall be deemed to have waived his right to object.

#### *Article 5. Scope of court intervention*

In matters governed by this Law, no court shall intervene except where so provided in this Law.

#### *Article 6. Court for certain functions of arbitration assistance and supervision*

The Court with jurisdiction to perform the functions referred to in articles 11 (3), (4), 13 (3), 14 and 34 (2) shall be the . . . (blanks to be filled by each State when enacting the model law).

## CHAPTER II. ARBITRATION AGREEMENT

#### *Article 7. Definition and form of arbitration agreement*

(1) "Arbitration agreement" is an agreement by the parties to submit to arbitration, whether or not

administered by a permanent arbitral institution, all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not. An arbitration agreement may be in the form of an arbitration clause in a contract or in the form of a separate agreement.

(2) The arbitration agreement shall be in writing. An agreement is in writing if it is contained in a document signed by the parties or in an exchange of letters, telex, telegrams or other means of telecommunication which provide a record of the agreement. The reference in a contract to a document 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 part of the contract.

#### *Article 8. Arbitration agreement and substantive claim before court*

(1) A court before which an action is brought in a matter which is the subject of an arbitration agreement shall, if a party so requests not later than when submitting his first statement on the substance of the dispute, refer the parties to arbitration unless it finds that the agreement is null and void, inoperative or incapable of being performed.

(2) Where, in such case, arbitral proceedings have already commenced, the arbitral tribunal may continue the proceedings while the issue of its jurisdiction is pending with the court.

#### *Article 9. Arbitration agreement and interim measures by court*

It is not incompatible with the arbitration agreement for a party to request, before or during arbitral proceedings, from a court an interim measure of protection and for a court to grant such measure.

## CHAPTER III. COMPOSITION OF ARBITRAL TRIBUNAL

#### *Article 10. Number of arbitrators*

(1) The parties are free to determine the number of arbitrators.

(2) Failing such determination, the number of arbitrators shall be three.

#### *Article 11. Appointment of arbitrators*

(1) No person shall be precluded by reason of his nationality from acting as an arbitrator, unless otherwise agreed by the parties.

(2) The parties are free to agree on a procedure of appointing the arbitrator or arbitrators, subject to the provisions of paragraphs (4) and (5) of this article.

(3) Failing such agreement,

(a) in an arbitration with three arbitrators, each party shall appoint one arbitrator, and the two arbi-

trators thus appointed shall appoint the third arbitrator; if a party fails to appoint the arbitrator within thirty days after having been requested to do so by the other party, or if the two arbitrators fail to agree on the third arbitrator within thirty days of their appointment, the appointment shall be made, upon request of a party, by the Court specified in article 6;

(b) in an arbitration with a sole arbitrator, if the parties are unable to agree on the arbitrator, he shall be appointed, upon request of a party, by the Court specified in article 6.

(4) Where, under an appointment procedure agreed upon by the parties,

(a) a party fails to act as required under such procedure; or

(b) the parties, or two arbitrators, are unable to reach an agreement expected of them under such procedure; or

(c) an appointing authority fails to perform any function entrusted to it under such procedure,

any party may request the Court specified in article 6 to take the necessary measure, unless the agreement on the appointment procedure provides other means for securing the appointment.

(5) A decision on a matter entrusted by paragraph (3) or (4) of this article to the Court specified in article 6 shall be final. The Court, in appointing an arbitrator, shall have due regard to any qualifications required of the arbitrator by the agreement of the parties and to such considerations as are likely to secure the appointment of an independent and impartial arbitrator and, in the case of a sole or third arbitrator, shall take into account as well the advisability of appointing an arbitrator of a nationality other than those of the parties.

#### Article 12. *Grounds for challenge*

(1) When a person is approached in connection with his possible appointment as an arbitrator, he shall disclose any circumstances likely to give rise to justifiable doubts as to his impartiality or independence. An arbitrator, from the time of his appointment and throughout the arbitral proceedings, shall without delay disclose any such circumstances to the parties unless they have already been informed of them by him.

(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 an arbitrator appointed by him, or in whose appointment he has participated, only for reasons of which he becomes aware after the appointment has been made.

#### Article 13. *Challenge procedure*

(1) The parties are free to agree on a procedure for challenging an arbitrator, subject to the provisions of paragraph (3) of this article.

(2) Failing such agreement, a party who intends to challenge an arbitrator shall, within fifteen days of the

constitution of the arbitral tribunal or after becoming aware of any circumstance referred to in article 12 (2), whichever is the later, send a written statement of the reasons for the challenge to the arbitral tribunal. Unless the challenged arbitrator withdraws from his office or the other party agrees to the challenge, the arbitral tribunal shall decide on the challenge.

(3) If a challenge under any procedure agreed upon by the parties or under the procedure of paragraph (2) of this article is not successful, the challenging party may request, within fifteen days after having received notice of the decision rejecting the challenge, the Court specified in article 6 to decide on the challenge, which decision shall be final; while such a request is pending, the arbitral tribunal, including the challenged arbitrator, may continue the arbitral proceedings.

#### Article 14. *Failure or impossibility to act*

If an arbitrator becomes *de jure* or *de facto* unable to perform his functions or for other reasons fails to act, his mandate terminates if he withdraws from his office or if the parties agree on the termination. Otherwise, if a controversy remains concerning any of these grounds, any party may request the Court specified in article 6 to decide on the termination of the mandate, which decision shall be final.

#### Article 14 bis

The fact that, in cases under article 13 (2) or 14, an arbitrator withdraws from his office or a party agrees to the termination of the mandate of an arbitrator does not imply acceptance of the validity of any ground referred to in article 12 (2) or 14.

#### Article 15. *Appointment of substitute arbitrator*

Where the mandate of an arbitrator terminates under article 13 or 14 or because of his withdrawal from office for any other reason or because of the revocation of his mandate by agreement of the parties or in any other case of termination of his mandate, 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.

### CHAPTER IV. JURISDICTION OF ARBITRAL TRIBUNAL

#### Article 16. *Competence to rule on own jurisdiction*

(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. A party is not precluded from raising such a plea by the fact that he has appointed, or participated in the appointment of, an arbitrator. A plea that the arbitral tribunal is exceeding the scope of its authority shall be raised promptly after the arbitral tribunal has indicated its intention to decide on the matter alleged to be beyond the scope of its authority. The arbitral tribunal may, in either case, admit a later plea if it considers the delay justified.

(3) The arbitral tribunal may rule on a plea referred to in paragraph (2) of this article either as a preliminary question or in an award on the merits. 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.

#### *Article 18. Power of arbitral tribunal to order interim measures*

Unless otherwise agreed by the parties, the arbitral tribunal may, at the request of a party, order any party to take such interim measure of protection as the arbitral tribunal may consider necessary in respect of the subject-matter of the dispute. The arbitral tribunal may require any party to provide security for the costs of such measure.

### CHAPTER V. CONDUCT OF ARBITRAL PROCEEDINGS

#### *Article 19. Determination of rules of procedure*

(1) Subject to the provisions of this Law, the parties are free to agree on the procedure to be followed by the arbitral tribunal in conducting the proceedings.

(2) Failing such agreement, the arbitral tribunal may, subject to the provisions of this Law, conduct the arbitration in such manner as it considers appropriate. The power conferred upon the arbitral tribunal includes the power to determine the admissibility, relevance, materiality and weight of any evidence.

(3) In either case, the parties shall be treated with equality and each party shall be given a full opportunity of presenting his case.

#### *Article 20. Place of arbitration*

(1) The parties are free to agree on the place of arbitration. Failing such agreement, the place of arbitration shall be determined by the arbitral tribunal.

(2) Notwithstanding the provisions of paragraph (1) of this article, the arbitral tribunal may, unless otherwise agreed by the parties, meet at any place it considers appropriate for consultation among its members, for hearing witnesses, experts or the parties, or for inspection of goods, other property, or documents.

#### *Article 21. Commencement of arbitral proceedings*

Unless otherwise agreed by the parties, the arbitral proceedings in respect of a particular dispute commence on the date on which a request for that dispute to be referred to arbitration is received by the respondent.

#### *Article 22. Language*

(1) The parties are free to agree on the language or languages to be used in the arbitral proceedings. Failing such agreement, the arbitral tribunal shall determine the language or languages to be used in the proceedings. This agreement or determination, unless otherwise specified therein, shall apply to any written statement by a party, any hearing and any award, decision or other communication by the arbitral tribunal.

(2) The arbitral tribunal may order that any documentary evidence shall be accompanied by a translation into the language or languages agreed upon by the parties or determined by the arbitral tribunal.

#### *Article 23. Statement of claim and defence*

(1) Within the period of time agreed by the parties or determined by the arbitral tribunal, the claimant shall state the facts supporting his claim, the points at issue and the relief or remedy sought, and the respondent shall state his defence in respect of these particulars. The parties may annex to their statements all documents they consider to be relevant or may add a reference to the documents or other evidence they will submit.

(2) Unless otherwise agreed by the parties, either party may amend or supplement his claim or defence during the course of the arbitral proceedings, unless the arbitral tribunal considers it inappropriate to allow such amendment having regard to the delay in making it or prejudice to the other party or any other circumstances.

#### *Article 24. Hearings and written proceedings*

(1) Subject to any contrary agreement by the parties, the arbitral tribunal shall decide whether to hold oral hearings or whether the proceedings shall be conducted on the basis of documents and other materials.

(2) Notwithstanding the provisions of paragraph (1) of this article, if a party so requests, the arbitral tribunal may, at any appropriate stage of the proceedings, hold hearings for the presentation of evidence or for oral argument.

(3) The parties shall be given sufficient advance notice of any hearing and of any meeting of the arbitral tribunal for inspection purposes.

(4) All statements, documents or other information supplied to the arbitral tribunal by one party shall be communicated to the other party. Also any expert report or other document, on which the arbitral tribunal may rely in making its decision, shall be communicated to the parties.

### Article 25. Default of a party

Unless otherwise agreed by the parties, if, without showing sufficient cause,

(a) the claimant fails to communicate his statement of claim in accordance with article 23 (1), the arbitral proceedings shall be terminated;

(b) the respondent fails to communicate his statement of defence in accordance with article 23 (1), the arbitral tribunal shall continue the proceedings without treating such failure as an admission of the claimant's allegations;

(c) any party fails to appear at a hearing or to produce documentary evidence, the arbitral tribunal may continue the proceedings and make the award on the evidence before it.

### Article 26. Expert appointed by arbitral tribunal

(1) Unless otherwise agreed by the parties, the arbitral tribunal

(a) may appoint one or more experts to report to it on specific issues to be determined by the arbitral tribunal;

(b) may require a party to give the expert any relevant information or to produce, or to provide access to, any relevant documents, goods or other property for this inspection.

(2) Unless otherwise agreed by the parties, if a party so requests or if the arbitral tribunal considers it necessary, the expert shall, after delivery of his written or oral report, participate in a hearing where the parties have the opportunity to interrogate him and to present expert witnesses in order to testify on the points at issue.

### Article 27. Court assistance in taking evidence

(1) In arbitral proceedings held in this State or under this Law, the arbitral tribunal or a party with the approval of the arbitral tribunal may request from a competent court of this State assistance in taking evidence. The request shall specify:

(a) the names and addresses of the parties and the arbitrators;

(b) the general nature of the claim and the relief sought;

(c) the evidence to be obtained, in particular,

(i) the name and address of any person to be heard as witness or expert witness and a statement of the subject-matter of the testimony required;

(ii) the description of any document to be produced or property to be inspected.

(2) The court may, within its competence and according to its rules on taking evidence, execute the request either by taking the evidence itself or by ordering that the evidence be provided directly to the arbitral tribunal.

## CHAPTER VI. MAKING OF AWARD AND TERMINATION OF PROCEEDINGS

### Article 28. Rules applicable to substance of dispute

(1) The arbitral tribunal shall decide the dispute in accordance with such rules of law as are chosen 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 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 *ex aequo et bono* or as *amiable compositeur* only if the parties have expressly authorized it to do so.

### Article 29. Decision making by panel of arbitrators

In arbitral proceedings with more than one arbitrator, any decision of the arbitral tribunal shall be made, unless otherwise agreed by the parties, by a majority of all its members. However, the parties or the arbitral tribunal may authorize a presiding arbitrator to decide questions of procedure.

### Article 30. Settlement

(1) If, during arbitral proceedings, the parties settle the dispute, the arbitral tribunal shall terminate the proceedings and, if requested by the parties and not objected to by the arbitral 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 31 and shall state that it is an award. Such an award has the same status and effect as any other award on the merits of the case.

### Article 31. Form and contents of award

(1) The award shall be made in writing and shall be signed by the arbitrator or arbitrators. In arbitral proceedings with more than one arbitrator, the signatures of the majority of all members of the arbitral tribunal shall suffice, provided that the reason for any omitted signature is stated.

(2) The award shall state the reasons upon which it 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 30.

(3) The award shall state its date and the place of arbitration as determined in accordance with article 20 (1). The award shall be deemed to have been made at that place.

(4) After the award is made, a copy signed by the arbitrators in accordance with paragraph (1) of this article shall be delivered to each party.

### Article 32. *Termination of proceedings*

(1) The arbitral proceedings are terminated by the final award or by agreement of the parties or by an order of the arbitral tribunal in accordance with paragraph (2) of this article.

#### (2) The arbitral tribunal

(a) shall issue an order for the termination on the arbitral proceedings when the claimant withdraws his claim, unless the respondent objects thereto and the arbitral tribunal recognizes a legitimate interest on his part in obtaining a final settlement of the dispute;

(b) may issue an order of termination when the continuation of the proceedings for any other reason becomes unnecessary or inappropriate.

(3) The mandate of the arbitral tribunal terminates with the termination of the arbitral proceedings, subject to the provisions of articles 33 and 34 (4).

### Article 33. *Correction and interpretation of awards and additional awards*

(1) Within thirty days of 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;

(b) to give an interpretation of a specific point or part of the award.

The arbitral tribunal shall make the correction or give the interpretation within thirty days of receipt of the request. The interpretation shall form part of the award.

(2) The arbitral tribunal may correct any error of the type referred to in paragraph (1) (a) of this article on its own initiative within thirty days of the date of the award.

(3) Unless otherwise agreed by the parties, a party, with notice to the other party, may request, within thirty days of receipt of the award, the arbitral tribunal to make an additional award as to claims presented in the arbitral proceedings but omitted from the award. The arbitral tribunal shall make the additional award within sixty days, if it considers the request to be justified.

(4) The arbitral tribunal may extend, if necessary, the period of time within which it shall make a correction, interpretation or an additional award under paragraph (1) or (3) of this article.

(5) The provisions of article 31 shall apply to a correction or interpretation of the award or to an additional award.

## CHAPTER VII. RE COURSE AGAINST AWARD

### Article 34. *Application for setting aside as exclusive recourse against arbitral award*

(1) Recourse to a court against an arbitral award made [in the territory of this State] [under this Law] may be made only by an application for setting aside in accordance with paragraphs (2) and (3) of this article.

(2) An arbitral award may be set aside by the Court specified in article 6 only if:

(a) the party making the application furnishes proof that:

(i) the parties to the arbitration agreement referred to in article 7 were, under the law applicable to them, 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

(ii) the party making the application was not given proper notice of the appointment of the arbitrator(s) or of the arbitral proceedings or was otherwise unable to present his case; or

(iii) the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, only that part of the award which contains decisions on matters not submitted to arbitration may be set aside; or

(iv) the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties, unless such agreement was in conflict with a provision of this Law from which the parties cannot derogate, or, failing such agreement, was not in accordance with this Law; or

(b) the Court finds that:

(i) the subject-matter of the dispute is not capable of settlement by arbitration under the law of this State; or

(ii) the award or any decision contained therein is in conflict with the public policy of this State.

(3) An application for setting aside may not be made after three months have elapsed from the date on which the party making that application had received the award or, if a request had been made under article 33, from the date on which that request had been disposed of by the arbitral tribunal.

(4) The Court, when asked to set aside an award, may, where appropriate and so requested by a party, suspend the setting aside proceedings for a period of time determined by it in order to give the arbitral tribunal an opportunity to resume the arbitral proceedings or to take such other action as in the arbitral tribunal's opinion will eliminate the grounds for setting aside.

## CHAPTER VIII. RECOGNITION AND ENFORCEMENT OF AWARDS

### Article 35. *Recognition and enforcement*

(1) An arbitral award, irrespective of the country in which it was made, shall be recognized as binding and, upon application in writing to the competent court, shall be enforced subject to the provisions of this article and of article 36.

(2) The party relying on an award or applying for its enforcement shall supply the duly authenticated original award or a duly certified copy thereof, and the original arbitration agreement referred to in article 7 or a duly certified copy thereof. If the award or agreement is not made in an official language of this State, the party shall supply a duly certified translation thereof into such language.\*

(3) Filing, registration or deposit of an award with a court of the country where the award was made is not a pre-condition for its recognition or enforcement in this State.

### Article 36. *Grounds for refusing recognition or enforcement*

(1) Recognition or enforcement of an arbitral award, irrespective of the country in which it was made, may be refused only:

(a) at the request of the party against whom it is invoked, if that party furnishes to the competent court where recognition or enforcement is sought proof that:

(i) the parties to the arbitration agreement referred to in article 7 were, under the law applicable to them, 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 the country where the award was made; or

\*The conditions set forth in this paragraph are intended to set maximum standards. It would, thus, not be contrary to the harmonization to be achieved by the model law if a State retained even less onerous conditions.

- (ii) the party against whom the award is invoked was not given proper notice of the appointment of the arbitrator(s) or of the arbitral proceedings or was otherwise unable to present his case; or
  - (iii) the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the 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
  - (iv) 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; or
  - (v) the award has not yet become binding on the parties or has been set aside or suspended by a court of the country in which, or under the law of which, that award was made; or
- (b) if the court finds that:
- (i) the subject-matter of the dispute is not capable of settlement by arbitration under the law of this State; or
  - (ii) the recognition or enforcement of the award would be contrary to the public policy of this State.
- (2) If an application for setting aside or suspension of an award has been made to a court referred to in paragraph (1) (a) (v) of this article, the court where recognition or enforcement is sought may, if it considers it proper, adjourn its decision and may also, on the application of the party claiming recognition or enforcement of the award, order the other party to provide appropriate security.

### 3. Working papers submitted to the Working Group at its seventh session

- (a) *Composite draft text of a model law on international commercial arbitration: note by the secretariat*  
(A/CN.9/WG.II/WP.48)

## CONTENTS

	<i>Page</i>
INTRODUCTORY NOTE.....	220
COMPOSITE DRAFT TEXT OF A MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION .....	220

	<i>Page</i>
<b>CHAPTER I. GENERAL PROVISIONS .....</b>	220
Article 1. Scope of application .....	220
Article 2. Definitions and rules of interpretation .....	220
Article 3. Mandatory provisions .....	221
Article 4. Waiver of right to object .....	221
Article 5. Scope of court intervention.....	221
Article 6. Special court for certain functions of arbitration assistance and supervision .....	221
<b>CHAPTER II. ARBITRATION AGREEMENT.....</b>	221
Article 7. Definition and form of arbitration agreement .....	221
Article 8. Arbitration agreement and substantive claim before court .....	221
Article 9. Arbitration agreement and interim measures by court .....	221
<b>CHAPTER III. COMPOSITION OF ARBITRAL TRIBUNAL.....</b>	221
Article 10. Number of arbitrators .....	221
Article 11. Appointment of arbitrators .....	221
Article 12. Grounds for challenge.....	222
Article 13. Challenge procedure .....	222
Article 14. Failure or impossibility to act .....	222
Article 15. Appointment of substitute arbitrator .....	222
<b>CHAPTER IV. JURISDICTION OF ARBITRAL TRIBUNAL.....</b>	222
Article 16. Competence to rule on own jurisdiction .....	222
Article 17. Concurrent court control .....	223
Article 18. Power of arbitral tribunal to order interim measures .....	223
<b>CHAPTER V. CONDUCT OF ARBITRAL PROCEEDINGS.....</b>	223
Article 19. Determination of rules of procedure .....	223
Article 20. Place of arbitration .....	223
Article 21. Commencement of arbitral proceedings .....	223
Article 22. Language.....	223
Article 23. Statements of claim and defence .....	223
Article 24. Hearings and written proceedings .....	223
Article 25. Default of a party.....	224
Article 26. Expert appointed by arbitral tribunal .....	224
Article 27. Court assistance in taking evidence .....	224
<b>CHAPTER VI. MAKING OF AWARD AND TERMINATION OF PROCEEDINGS .....</b>	224
Article 28. Rules applicable to substance of dispute.....	224
Article 29. Decision-making by panel of arbitrators .....	224
Article 30. Settlement .....	224
Article 31. Form and contents of award .....	225
Article 32. Termination of proceedings .....	225
Article 33. Correction, interpretation and completion of award.....	225
<b>CHAPTER VII. RE COURSE AGAINST AWARD .....</b>	225
Article 34. Application for setting aside as exclusive recourse against arbitral award	225
<b>CHAPTER VIII. RECOGNITION AND ENFORCEMENT OF AWARDS .....</b>	226
Article 35. Procedural conditions of recognition and enforcement .....	226
Article 36. Grounds for refusing recognition or enforcement .....	226

## INTRODUCTORY NOTE

1. This working paper contains the composite draft text 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 sixth session (Vienna, 29 August - 9 September 1983).<sup>1</sup> The draft text is preceded by a comparative table of numbers of draft articles showing on which previous draft articles the revised articles of the composite text are based.

**Comparative table of numbers of draft articles**

Article in composite draft (WP.48)	Previous draft article (A/CN.9/245; reproduced in this Yearbook, part two, II, A, 1)	Article in composite draft (WP.48)	Previous draft article (A/CN.9/245; reproduced in this Yearbook, part two, II, A, 1)
1	I, I bis (e)	18	XIV
2 (a)-(d)	I bis (a)-(d)	19	XV
2 (e)	—	20	XVI
3	I ter	21	B
4	I quater	22	D
5	III	23	C
6	V	24	XVII (1) (a), (2), (3)
7	II	25	XVIII
8 (1)	IV (1)	26	XVII (4), (5), (1) (b)
8 (2)	XIII (4)	27	E
9	IV (1)	28	XIX (1), (2), (4)
10	XIII (4)	29	XX
11 (1)	IV (2)	30	XXI
11 (2)-(5)	VIII	31	XXII
12 (1), (2)	IX	32	F
12 (3)	—	33	XXIV
13	X	34 (1)	XXIX
14	XI	34 (2)-(4)	XXX
15	XII	35	XXV, XXVI
16	XIII	36	XXVII, XXVIII
17	—		

2. It may be noted that the secretariat did not prepare any explanatory footnotes to the composite draft text, which represents a direct implementation of the Working Group's decisions on the individual previous draft articles. However, the secretariat will submit to the Working Group two further notes. One, to be published as document A/CN.9/WG.II/WP.49 (reproduced in this *Yearbook*, part two, II, B, 3, b), will deal with the territorial scope of application and related issues, including questions of conflict of laws. The other note, to be published as document A/CN.9/WG.II/WP.50 (reproduced in this *Yearbook*, part two, II, B, 3, c), will contain some annotations on articles of the composite draft and deal with a variety of issues which the Working Group may wish to consider, or reconsider, in its overall review of the draft model law.

3. Finally, it may be noted that the headings of chapters and of articles are presented by the secretariat in an attempt to facilitate reference. The Working Group may wish to consider which headings should be retained in the final draft.

<sup>1</sup>"Report of the Working Group on International Contract Practices on the work of its sixth session" (A/CN.9/245) paras. 12-220; reproduced in this *Yearbook*, part two, II, A, 1.

## Composite draft text of a model law on international commercial arbitration

### CHAPTER I. GENERAL PROVISIONS

#### Article 1. Scope of application

(1) This Law applies to international commercial\* arbitration. Its provisions are subject to any multi-lateral or bilateral agreement entered into by this State.

(2) [An] arbitration is international if:

(a) the parties to an arbitration agreement have, at the time of the conclusion of that agreement, their places of business in different States; or

(b) one of the following places is situated outside the [territory of the] State in which the parties have their places of business:

- (i) the place of arbitration if determined in the arbitration agreement;
- (ii) any place where [a substantial] [the preponderant] part of the [characteristic] obligations of the [commercial relationship] [transaction] are to be performed or where its centre of activity or its subject-matter is located.

(3) For the purposes of paragraph (2), 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. If a party does not have a place of business, reference is to be made to his habitual residence.

#### Article 2. Definitions and rules of interpretation

For the purposes of this Law:

(a) "arbitral tribunal" means a sole arbitrator or a panel of arbitrators;

(b) "court" means a body or organ of the judicial system of a country;

(c) where a provision of this Law grants the parties freedom to determine a certain issue, such freedom includes the right of the parties to authorize a third person or institution to make that determination;

(d) where a provision of this Law refers to the fact that the parties have agreed or that they may agree or in any other way refers to an agreement of the parties, such agreement includes any arbitration rules referred to in that agreement;

(e) any written communication is deemed to have been received if it is physically delivered to the

\*The term "commercial" should be given a wide interpretation so as to cover matters arising from all relationships of a commercial nature, irrespective of whether the parties are "commercial persons" (merchants) under any given national law. Relationships of a commercial nature include, but are not limited to, the following transactions: any trade transaction for the supply or exchange of goods; distribution agreement; commercial representation or agency; factoring; leasing; construction of works; consulting; engineering; licensing; investment; financing; banking; insurance; exploitation agreement or concession; joint venture and other forms of industrial or business co-operation; carriage of goods or passengers by air, sea, rail or road.

addressee or if it is delivered at his place of business, habitual residence or mailing address, or, if none of these can be found after making reasonable inquiry, then at the addressee's last-known place of business or residence. The communication shall be deemed to have been received on the day it is so delivered.

#### **Article 3. Mandatory provisions**

The parties may not derogate from the following provisions of this Law: articles . . .

#### **Article 4. Waiver of right to object**

A party who knows [or ought to have known] that any provision of this Law [from which the parties may derogate] [or any requirement under the arbitration agreement] has not been complied with and yet proceeds with the arbitration without stating his objection to such non-compliance without delay [or, if a time-limit is provided therefor, within such period of time] shall be deemed to have waived his right to object.

#### **[Article 5. Scope of court intervention]**

In matters governed by this Law [concerning the arbitral proceedings or the composition of the arbitral tribunal, courts may exercise supervisory or assisting functions only if] [, no court shall intervene except where] so provided in this Law.]

#### **Article 6. Special court for certain functions of arbitration assistance and supervision**

The Court with jurisdiction to perform the functions referred to in articles 11 (3), (4), 13 (3), 14, 17 (1), [32 (2) Variant A] and 34 (3) shall be the . . . (blanks to be filled by each State when enacting the model law).

## **CHAPTER II. ARBITRATION AGREEMENT**

#### **Article 7. Definition and form of arbitration agreement**

(1) "Arbitration agreement" is an agreement by the parties to submit to arbitration, whether or not administered by a permanent arbitral institution, all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not. An arbitration agreement may be in the form of an arbitration clause in a contract or in the form of a separate agreement.

(2) The arbitration agreement shall be in writing. An agreement is in writing if it is contained in a document assigned by the parties or in an exchange of letters, telex, telegrammes or other means of tele-communication which provide a record of the agreement. The reference in a contract to a document 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 term of the contract.

#### **Article 8. Arbitration agreement and substantive claim before court**

(1) A court, before which an action is brought in a matter which is the subject of an arbitration agreement, shall, if a party so requests not later than when submitting his first statement on the substance of the dispute, refer the parties to arbitration unless it finds that the agreement is null and void, inoperative or incapable of being performed.

(2) Where, in such case, arbitral proceedings had already commenced, the arbitral tribunal may continue the proceedings while the issue [of its jurisdiction] is pending with the court [unless the court orders a stay or suspension of the arbitral proceedings].

#### **Article 9. Arbitration agreement and interim measures by court**

It is not incompatible with the arbitration agreement for a party to request, before or during arbitral proceedings, from a court an [interim measure of protection] [interim measure or a measure of conservation] and for a court to grant such measure.

## **CHAPTER III. COMPOSITION OF ARBITRAL TRIBUNAL**

#### **Article 10. Number of arbitrators**

(1) The parties are free to determine the number of arbitrators.

(2) Failing such determination, the number of arbitrators shall be three.

#### **Article 11. Appointment of arbitrators**

(1) No person shall be by reason of his nationality or citizenship precluded from acting as an arbitrator, unless otherwise agreed by the parties.

(2) The parties are free to agree on a procedure of appointing the arbitrator or arbitrators, subject to the provisions of paragraphs (4) and (5) of this article.

(3) Failing such agreement,

(a) in an arbitration with three arbitrators, each party shall appoint one arbitrator, and the two arbitrators thus appointed shall appoint the third arbitrator; if a party fails to appoint the arbitrator within thirty days after having been requested to do so by the other party, or if the two arbitrators fail to agree on the third arbitrator within thirty days from their appointment, the appointment shall be made, upon request of a party, by the Court specified in article 6;

(b) if, in an arbitration with a sole arbitrator, the parties are unable to agree on the arbitrator, he shall be appointed, upon request of a party, by the Court specified in article 6.

(4) Where, under an appointment procedure agreed upon by the parties,

(a) a party fails to act as required under such procedure; or

(b) the parties, or two arbitrators, are unable to reach an agreement expected from them under such procedure; or

(c) an appointing authority fails to perform any function entrusted to it under such procedure,

any party may request the Court specified in article 6 to take the necessary measure instead, unless the agreement on the appointment procedure provides other means for securing the appointment.

(5) A decision on a matter entrusted by paragraph (3) or (4) to the Court specified in article 6 shall be final. The Court, in appointing an arbitrator, shall have due regard to any qualifications required of the arbitrator by agreement of the parties and to such considerations as are likely to secure the appointment of an independent and impartial arbitrator and, in the case of a sole or third arbitrator, shall take into account as well the advisability of appointing an arbitrator of a nationality or citizenship other than those of the parties.

#### Article 12. *Grounds for challenge*

(1) When a person is approached in connection with his possible appointment as an arbitrator, he shall [without delay] disclose any circumstances likely to give rise to justifiable doubts as to his impartiality or independence. An arbitrator, from the time of his appointment and thereafter, shall without delay 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.

(3) The fact that, in cases under article 13 (2) or 14, an arbitrator withdraws from his office or a party agrees to the termination of the mandate of an arbitrator does not imply acceptance of the validity of any ground referred to in [that provision] [paragraph (2) of this article or in article 14].

#### Article 13. *Challenge procedure*

(1) The parties are free to agree on a procedure for challenging an arbitrator, subject to the provisions of paragraph (3) of this article.

(2) Failing such agreement, a party who intends to challenge an arbitrator shall, within fifteen days after knowing any circumstance referred to in article 12 (2), send a written statement of the reasons for the challenge to the arbitral tribunal. Unless the challenged

arbitrator withdraws from his office or the other party agrees to the challenge, the arbitral tribunal shall decide on the challenge.

(3) If a challenge under any procedure agreed upon by the parties or under the procedure of paragraph (2) is not successful, the challenging party may request, within fifteen days [after having received the decision rejecting the challenge], from the Court specified in article 6 a decision on the challenge which shall be final; while such a request is pending, the arbitral tribunal, including the challenged arbitrator, may continue the arbitral proceedings.

#### Article 14. *Failure or impossibility to act*

If an arbitrator [fails to act or becomes *de jure* or *de facto* unable to perform his functions] [becomes *de jure* or *de facto* unable to perform his functions or for other reasons fails to act], his mandate terminates if he withdraws from his office or if the parties agree on the termination. Otherwise, if a controversy remains concerning any of these grounds, any party may request from the Court specified in article 6 a decision on the termination of the mandate which shall be final.

#### Article 15. *Appointment of substitute arbitrator*

[Where the mandate of an arbitrator terminates under article 13 or 14 or because of his resigning for any other reason,] 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.

### CHAPTER IV. JURISDICTION OF ARBITRAL TRIBUNAL

#### Article 16. *Competence to rule on own jurisdiction*

(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. 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 arbitral tribunal has indicated its intention to [deal with] [decide on] the matter alleged to be outside the terms of reference. 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 an award on the merits. [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.]

#### *Article 17. Concurrent court control*

(1) [Notwithstanding the provisions of article 16,] a party may [at any time] request the Court specified in article 6 to decide whether or not there exists a valid arbitration agreement and [, if arbitral proceedings have commenced,] whether or not the arbitral tribunal has jurisdiction [with regard to the dispute referred to it].

(2) While such issue is pending with the Court, the arbitral tribunal may continue the proceedings [unless the Court orders a stay or suspension of these proceedings].

#### *Article 18. Power of arbitral tribunal to order interim measures*

Unless otherwise agreed by the parties, the arbitral tribunal may, at the request of a party, order any interim measure [of protection it deems necessary in respect of the subject-matter of the dispute]. The arbitral tribunal may require of a party or the parties security for the costs of such measure.

### CHAPTER V. CONDUCT OF ARBITRAL PROCEEDINGS

#### *Article 19. Determination of rules of procedure*

(1) Subject to the [mandatory] provisions of this Law, the parties are free to agree on the procedure to be followed by the arbitral tribunal in conducting the proceedings.

(2) Failing such agreement, 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 20. Place of arbitration*

(1) The parties are free to agree on the place of arbitration. Failing such agreement, the place of arbitration shall be determined by the arbitral tribunal.

(2) Notwithstanding the provisions of the preceding paragraph, the arbitral tribunal may, unless otherwise agreed by the parties, meet at any place it considers appropriate for consultation among its members, for hearing witnesses, experts or the parties, or for inspection of goods, other property, or documents.

#### *Article 21. Commencement of arbitral proceedings*

Unless otherwise agreed by the parties, the arbitral proceedings [shall be deemed to] commence on the date at which a request that a [particular] [specified] dispute be referred to arbitration is received by the respondent [provided that such a request identifies the claim].

#### *Article 22. Language*

(1) The parties are free to agree on the language or languages to be used in the arbitral proceedings. Failing such agreement, the arbitral tribunal shall determine the language or languages to be used in the proceedings. This agreement or determination, unless otherwise specified therein, shall apply to any written statement by a party, any hearing [of witnesses, experts or the parties], and any award, decision or other communication by the arbitral tribunal.

(2) The arbitral tribunal may order that any documentary evidence shall be accompanied by a translation into the language or [one of the] languages agreed upon by the parties or determined by the arbitral tribunal.

#### *Article 23. Statements of claim and defence*

(1) Within the period of time stipulated by the parties or determined by the arbitral tribunal, the claimant shall state the facts supporting his claim, the points at issue and the relief or remedy sought, and the respondent shall state his defence in respect of these particulars. The parties may annex to their statements all documents they deem relevant or may add a reference to the documents or other evidence they will submit.

(2) [During the course of the arbitral proceedings] either party may amend or supplement his claim or defence unless the arbitral tribunal considers it inappropriate to allow such amendment having regard to the delay in making it or prejudice to the other party or any other circumstances.

#### *Article 24. Hearings and written proceedings*

(1) Subject to any contrary agreement by the parties, 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, 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.

(2) In order to enable the parties to be present at any hearing and at any meeting of the arbitral tribunal for inspection purposes, they shall be given sufficient notice in advance.

(3) All statements, documents or other information supplied to the arbitral tribunal by one party shall be communicated to the other party. Also any expert report or other document, on which the arbitral tribunal may rely in making its decision, shall be communicated to the parties.

### Article 25. *Default of a party*

Unless otherwise agreed by the parties, if, without showing sufficient cause for the failure,

(a) the claimant fails to communicate his statement of claim in accordance with article 23 (1), the arbitral proceedings shall be terminated;

(b) the respondent fails to communicate his statement of defence in accordance with article 23 (1),

*Variant A:* the arbitral proceedings shall continue;

*Variant B:* the arbitral tribunal shall continue the proceedings without treating such failure as an admission of the claimant's allegations;

*Variant C:* the arbitral tribunal shall treat this as a denial of the claim and continue the proceedings;

(c) any party fails [to comply with a request by the arbitral tribunal] to appear at a hearing, or to produce documentary evidence, the arbitral tribunal [may] [shall] continue the proceedings [and may make the award on the evidence before it].

### Article 26. *Expert appointed by arbitral tribunal*

(1) Unless otherwise agreed by the parties before the appointment of the first arbitrator, the arbitral tribunal may appoint one or more experts to report to it on specific issues to be determined by the tribunal.

(2) The [expert may, within his terms of reference, require a party to give him] [arbitral tribunal may require a party to give the expert] any relevant information or to produce, or to provide access to, any relevant documents, goods or other property for his inspection.

(3) The expert shall, after delivery of his written or oral report, participate in a hearing where the parties have the opportunity to interrogate him and to present expert witnesses in order to testify on the points at issue.

### Article 27. *Court assistance in taking evidence*

(1) The arbitral tribunal or a party with the approval of the arbitral tribunal may request from a competent court of this State assistance in taking evidence. The request shall [be in the language of the court, include a certified copy of the arbitration agreement and] specify:

(a) the names and addresses of the parties and the arbitrators;

(b) the general nature of the claim and the relief sought;

(c) the [necessary information on the] evidence to be obtained, in particular

- (i) the name and address of any person to be heard as witness or expert witness and a statement of the subject-matter of the testimony required;
- (ii) the description of any document or other property to be inspected.

(2) The court may, within its competence and according to its rules on taking evidence [, including provisions on admissibility and on enforcement procedures], execute the request either by taking the evidence itself or by ordering that the evidence be provided directly to the arbitral tribunal. If so [suggested] [demanded] in the request, the court may transmit the request to a competent court of a foreign State [where assistance in obtaining evidence is required].

[(3) Where a foreign court transmits to a competent court of this State a request for assistance in taking evidence relating to arbitral proceedings in that foreign State, the court of this State shall treat such request as having been made by that foreign court itself].

## CHAPTER VI. MAKING OF AWARD AND TERMINATION OF PROCEEDINGS

### Article 28. *Rules applicable to substance of dispute*

(1) The arbitral tribunal shall decide the dispute in accordance with such rules of law as [are chosen] [may be agreed] 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 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 *ex aequo et bono* or as *amicable compositeur* only if the parties have expressly authorized it to do so.

### Article 29. *Decision-making by panel of arbitrators*

In arbitral proceedings with more than one arbitrator, any award including interim [, interlocutory] and partial award, and any other decision of the arbitral tribunal shall be made, unless otherwise agreed by the parties, by a majority of all its members. However, the parties or the arbitral tribunal may authorize a presiding arbitrator to decide questions of procedure [on his own].

### Article 30. *Settlement*

(1) If, during arbitral proceedings, the parties settle the dispute, the arbitral tribunal shall terminate the proceedings and, if requested by the parties and not objected to by the arbitral 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 31 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.

**Article 31. Form and contents of award**

(1) An award shall be made in writing and shall be signed by the arbitrator or arbitrators. In arbitral proceedings with more than one arbitrator, the signatures of the majority of all members of the arbitral tribunal shall suffice, provided that the reason for any missing signature is stated.

(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 30.

(3) An award shall state its date and the place of arbitration as determined in accordance with article 20 (1). The award shall be deemed to have been made at that place.

(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.

**Article 32. Termination of proceedings***Variant A:*

(1) The arbitral proceedings are terminated:

(a) by the making of the final award which constitutes or completes the disposition of all claims submitted to arbitration; or

(b) by an agreement of the parties that the arbitral proceedings are to be terminated at a specified date [or after expiry of a specified period of time]; or

(c) by an order of the arbitral tribunal in accordance with paragraph (2) of this article.

(2) After having given suitable notice to the parties, the arbitral tribunal shall issue an order for the termination of the arbitral proceedings

(a) when the claimant withdraws his claim, unless the respondent objects thereto and the arbitral tribunal recognizes a legitimate interest on his part in obtaining a final settlement of the dispute; or

(b) if for any other reason the continuation of the proceedings becomes unnecessary or inappropriate.

[Where the arbitral tribunal fails to issue an order of termination, any party may request from the Court specified in article 6 a ruling on the termination of the proceedings.]

(3) The mandate of the arbitral tribunal terminates with the termination of the arbitral proceedings, subject to the provisions of articles 33 and 34 (4).

*Variant B:*

(1) The arbitral proceedings are terminated either with the final award or by agreement of the parties or by an order of termination [by the arbitral tribunal] [which the arbitral tribunal may issue when the continuation of the proceedings appears unnecessary or inappropriate].

(2) The mandate of the arbitral tribunal terminates with the termination of the arbitral proceedings, subject to the provisions of articles 33 and 34 (4).

**Article 33. Correction, interpretation and completion of award**

(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 thirty 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, within thirty days after the receipt of the award, the arbitral tribunal to make an additional award as to claims presented in the arbitral 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 make that additional award [within sixty days after the receipt of the request].

(3) The provisions of article 31 shall apply to a correction or interpretation of the award or to an additional award.

**CHAPTER VII. RE COURSE AGAINST AWARD****Article 34. Application for setting aside as exclusive recourse against arbitral award**

(1) Recourse to a court against an arbitral award made [in the territory of this State] [under this Law] may be made only by an application for setting aside in accordance with paragraphs (2) and (3) of this article.

(2) An arbitral award may be set aside by the Court specified in article 6 only if

(a) the party making the application furnishes proof that:

(i) the parties to the arbitration agreement referred to in article 7 were, under the law applicable to them, 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

(ii) the party making the application was not given proper notice of the appointment of the arbitrator(s) or of the arbitral proceedings or was otherwise unable to present his case; or

(iii) the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, only that part of the award which contains

- decisions on matters not submitted to arbitration may be set aside; or
- (iv) the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the [mandatory provisions of this Law and the] agreement of the parties or, failing such agreement, was not in accordance with this Law; or
- (b) the Court finds that:
  - (i) the subject-matter of the dispute is not capable of settlement by arbitration under the law of this State; or
  - (ii) the award or any decision contained therein is in conflict with the public policy of this State.
- (3) An application for setting aside may not be made after three months have elapsed from the date on which the party making that application had received the award in accordance with article 31 (4) [or, if a request had been made under article 33, from the date on which that request had been disposed of by the arbitral tribunal].
- (4) The Court, instead of setting aside the award, [may order, where appropriate, that the arbitral proceedings be continued] [may authorize the continuation of arbitral proceedings where this would permit an omission or other procedural defect to be cured without having to set aside the award].

## CHAPTER VIII. RECOGNITION AND ENFORCEMENT OF AWARDS

### Article 35. Procedural conditions of recognition and enforcement

- (1) An arbitral award [within the scope of article 1 (1)] [made within or outside the territory of this State] shall be recognized as binding, subject to the provisions of article 36.
- (2) To obtain enforcement, an application shall be made in writing to the competent court, accompanied by the duly authenticated original award or a duly certified copy thereof, and the original arbitration agreement referred to in article 7 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 enforcement of the award shall supply a duly certified translation of these documents into such language.\*

### Article 36. Grounds for refusing recognition or enforcement

- (1) Recognition or enforcement of an arbitral award [made within or outside the territory of this State] may be refused only:

\* The conditions set forth in this paragraph are intended to set maximum standards. It would, thus, not be contrary to the harmonization to be achieved by the model law if a State retained even less onerous conditions [for enforcement of awards made in that State or under the law of that State].

- (a) at the request of the party against whom it is invoked, if that party furnishes to the competent court where recognition or enforcement is sought proof that:
  - (i) the parties to the arbitration agreement referred to in article 7 were, under the law applicable to them, 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 the country where the award was made; or
  - (ii) the party against whom the award is invoked was not given proper notice of the appointment of the arbitrator(s) or of the arbitral proceedings or was otherwise unable to present his case; or
  - (iii) the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the 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
  - (iv) 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; or
  - (v) the award has not yet become binding on the parties or has been set aside or suspended by a court of the country in which, or under the law of which, that award was made; or
- (b) if the court finds that:
  - (i) the subject-matter of the dispute is not capable of settlement by arbitration under the law of this State; or
  - (ii) the recognition or enforcement of the award would be contrary to the public policy of this State.
- (2) A party, against whom recognition or enforcement of an award made [in the territory of this State] [under this Law] is sought during the period of time referred to in article 34 (3), may raise any objection in accordance with paragraph (1) of this article only by an application for setting aside to the Court specified in article 6.
- (3) Where a party seeks recognition, but not enforcement, of an award before an authority other than a court, the other party may request the Court specified in article 6 to order refusal of recognition in accordance with paragraph (1) of this article.]
- (4) If an application for setting aside or suspension of an award has been made to a court referred to in paragraph (1) (a) (v) or (2) of this article, the court where recognition or enforcement is sought may, if it considers it proper, adjourn its decision and may also, on the application of the party claiming recognition or enforcement of the award, order the other party to give suitable security.

(b) *Model law on international commercial arbitration: territorial scope of application and related issues: note by the secretariat (A/CN.9/WG.II/WP.49)*

### INTRODUCTORY NOTE

1. The model law, by providing in article 1 that it applies to international commercial arbitration, defines its scope of application in substantive terms. However, it does not define the territorial scope of its provisions. While the question of territorial scope was tentatively discussed by the Working Group in respect of some articles,<sup>1</sup> it was agreed to discuss the question in more detail and with regard to the complete set of draft provisions at the seventh session of the Working Group.<sup>2</sup>

2. The general assumption in the preparation of the model law has been that it essentially applies to arbitrations taking place in the State of the model law. The Working Group may wish to express this principle in the model law. However, it may need to be qualified in two respects.

3. Firstly, it may be useful to decide whether the place of arbitration is the exclusive factor in determining the applicability of the model law or whether the parties have a right to agree on the procedural law applicable to the arbitration. This aspect is discussed under A, below.

4. Secondly, there may be provisions in the model law which require a special delimitation of their scope of application different from the general delimitation of the scope of application of the model law. This aspect is discussed under B, below.

5. In this section possible conflicts of procedural laws, which may arise as a result of a given delimitation of the scope of application of the model law, are also discussed. Possible ways of dealing with such conflicts are discussed under C, below.

#### A. POSSIBLE CRITERION FOR DELIMITING THE SCOPE OF APPLICATION OF PROVISIONS ON ARBITRAL PROCEDURE

6. The basic criterion, common to all legal systems, for determining the applicability of procedural law on arbitration is a territorial one. While it appears that in most legal systems the territorial criterion is applied strictly, it is supplemented by an autonomy criterion in some other systems.

7. Under the strict territorial criterion, the place of arbitration is the exclusive determining factor for the applicability of the law of a State. Under this approach,

a State (State A) does not give effect to an agreement by the parties that an arbitration taking place in State A is to be governed by the procedural law of another State (State B). State A also does not give effect to an agreement by the parties that an arbitration taking place in State B is to be governed by the procedural law of State A.

8. Under the territorial criterion supplemented by the autonomy criterion, the place of arbitration determines the applicability of the law unless the parties have agreed otherwise. Under this approach, the law of a State (State A) applies to an arbitration if the arbitration takes place in State A provided that the parties have not agreed to subject the arbitration to the procedural law of another State (State B), in which case State A considers that the arbitration is governed by the procedural law of State B. The law of State A also applies to an arbitration if the parties have agreed to subject the arbitration to the procedural law of State A even if the arbitration does not take place in State A.

9. It may be noted in this connection that the 1958 New York Convention, while applying the territorial criterion for its application, recognizes the possibility that a State may allow the parties to subject an arbitration to a procedural law different from the law of the place of arbitration. For legal systems which allow such an autonomy of parties, article I (1) of the Convention provides that the Convention also applies to the awards made in the State of recognition and enforcement but not considered as domestic in that State. Furthermore, article V (1) (e) of the Convention envisages the situation where the competent authority of a State sets aside an award, i.e. an award considered as domestic in that State, which was made outside that State but under the procedural law of that State.

10. A reason in favour of the strict territorial criterion is the simplicity in its application since in most cases it can easily be ascertained which procedural law governs an arbitration. Furthermore, the court assistance or supervision is easily accessible to the parties and to the arbitral tribunal since the place of arbitration determines the court competence to provide such assistance or supervision.

11. On the other hand, there is advantage in not preventing the parties from subjecting an arbitration to a procedural law other than the law of the place of arbitration. The parties may have an interest in being able to agree on the place of arbitration in State A, for example, because of the convenience of participants, cost of proceedings or the availability of evidence. Yet, the parties may prefer that the arbitration is governed by the procedural law of State B rather than the law of State A.

12. It may be noted that, under the model law, the arbitral tribunal is not bound to conduct the entire

<sup>1</sup>E.g. articles V and XXX. See "Report of the Working Group on International Contract Practices on the work of its sixth session" (A/CN.9/245) paras. 148 and 191 (reproduced in this Yearbook, part two, II, A, 1).

<sup>2</sup>Ibid., paras. 149 and 191.

arbitral proceedings in the State of the place of arbitration. Under article 20 (2), the arbitral tribunal may decide to meet outside the State of the place of arbitration for consultations, hearings or inspection of goods or documents.

13. In addition to the territorial criterion, whether or not supplemented by the autonomy criterion, the Working Group may wish to provide a criterion for determining the applicability of the model law in cases where the place of arbitration or the law governing the arbitration has not been agreed upon or determined. The reason for this is that a party may need court assistance before the competence of the court to grant such assistance has been established by an agreement on the place of arbitration or on the governing procedural law. The model law could provide, for example, that in the absence of a factor determining the applicability of the model law, a party may rely on the model law, including its provisions on the assistance of the court specified in article 6, if his place of business or residence is in the State of the model law. (For a discussion on the possibility of a conflict created by such a provision see paragraphs 33 and 34, below.)

## B. SPECIAL CONSIDERATIONS WITH REGARD TO PROVISIONS ON COURT ASSISTANCE AND SUPERVISION

14. It may be useful to consider which provisions of the model law dealing with court assistance and supervision should have the same scope of application as the model law in general and which provisions should have a special delimitation of the scope of application. On the basis of such consideration the Working Group may wish to decide whether in a particular case an express provision on the scope of application is needed.

### *1. Provisions on court assistance and supervision which should have the same scope of application as the model law in general*

15. It is submitted that the provisions dealing with the following instances of court assistance and supervision are directed to the courts of the State of the model law and relate to arbitrations which are governed by the procedural law of that State whose court is to decide on the matter:

- (a) Control over the validity of an arbitration agreement (article 17);
- (b) Review of a decision by an arbitral tribunal that it has jurisdiction (article 16 (3));
- (c) Appointment of an arbitrator (article 11);
- (d) Challenge of an arbitrator (article 13);
- (e) Termination of the mandate of an arbitrator (article 14);
- (f) Setting aside of an award (article 34).

16. If the Working Group adopts the strict territorial criterion, the court specified in article 6 would be

competent to make a decision in a matter mentioned in the previous paragraph if the place of arbitration is in the State of the model law.

17. If the Working Group adopts the territorial criterion supplemented by the autonomy criterion, the court specified in article 6 would be competent to make a decision in a matter mentioned in paragraph 15 when the place of arbitration is in the State of the model law, unless the parties have subjected the arbitration to a foreign procedural law. The court would also be competent to make such a decision if the parties have subjected the arbitration to the procedural law of the State of the model law even if the arbitration does not take place in that State.

### *2. Provisions on court assistance and supervision which should have a special delimitation of scope of application*

18. Some provisions in the model law dealing with court assistance and supervision are of such a nature that they may require a different scope of application than the model law in general. These provisions are discussed below.

#### *(a) Referral of parties to arbitration because of existence of arbitration agreement (article 8 (1))*

19. Under article 8 (1), a court before which an action is brought in a matter which is the subject of a valid arbitration agreement, refers the parties to arbitration. This provision is directed to the courts of the State of the model law; however, it is submitted that the arbitration agreement which is the ground for referral of the parties to arbitration may be any arbitration agreement irrespective of the place of arbitration or the law governing the arbitration. The reason for such universal recognition of arbitration agreements is that an arbitration agreement can only be effective if it prevents the parties from bringing an action before a court in any State.

#### *(b) Granting of interim measure (article 9)*

20. Article 9 expresses the principle of compatibility of an arbitration agreement with a request to a court for an interim measure. There are two aspects of this principle.

21. One aspect is that it applies to courts of the State of the model law requested to grant an interim measure and provides that a court shall not refuse to grant such a measure on the ground that there is an arbitration agreement. In this respect the scope of application of the rule should be the same as the rule of article 8 (1) mentioned in paragraph 19.

22. The other aspect is that the rule expresses the principle according to which a request by a party for an interim measure should not be construed as a waiver of the arbitration agreement. This principle should apply irrespective of whether such a request is made to a court in the State of the model law or to a court in any other State.

## (c) Assistance in taking evidence (article 27)

23. Article 27 deals with the assistance of the courts of the model law to arbitrations, in paragraphs (1) and (2) to arbitrations governed by the procedural law of that State and in paragraph (3) to arbitrations not governed by that procedural law. In this respect the scope of application of this article is wider than the general scope of application of the model law.

24. Assistance to arbitrations not governed by the procedural law of the State where the assistance is to be given may be subject to stricter conditions than the assistance to arbitrations governed by that law. The reason is that a foreign procedural law may be different from the law of the State where assistance is to be given and that the courts of that State do not have supervisory powers over such arbitrations. It is, therefore, suggested that, for the purpose of assistance in taking evidence, the distinction between arbitrations governed by the procedural law of the State where assistance is to be given and arbitrations not governed by that procedural law should follow the general scope of application of the model law.

## (d) Recognition and enforcement of arbitral awards (articles 35 and 36)

25. The prevailing view in the Working Group was that the model law should regulate recognition and enforcement of awards governed by the procedural law of the State where recognition and enforcement are sought, i.e. domestic awards, as well as recognition and enforcement of awards not governed by that law, i.e. foreign awards.<sup>3</sup> In this respect the scope of application of this article is wider than the general scope of application of the model law.

26. The Working Group was also of the view that there was no convincing reason for providing different rules for domestic and foreign awards and it was therefore decided that a uniform regime should be adopted for both categories of awards.<sup>4</sup>

27. However, in view of the tentative nature of this decision,<sup>5</sup> it might be useful to discuss a criterion for distinguishing between domestic and foreign awards, such as the criterion consistent with the one to be adopted for the delimitation of the scope of application of the model law. This would mean that an award made in a domestic arbitration, i.e. arbitration governed by the model law of the State of recognition and enforcement, would be recognized and enforced under procedures for domestic awards, and that an award made in a foreign arbitration, i.e. arbitration not governed by the model law of the State of recognition and enforcement, would be recognized and enforced under procedures for foreign awards.

## C. CONFLICT OF LAWS ISSUES

## 1. Conflict of laws created by a delimitation of scope of application of the model law

28. A conflict of procedural laws and the resulting conflict of court competence may arise if the criterion for the delimitation of the scope of application of the model law adopted in a State is different from the criterion for the delimitation of the scope of application of the procedural law on arbitration adopted in another State.

29. For example, if a State does not permit the parties to subject an arbitration taking place in that State to a foreign procedural law, while the State of the chosen procedural law accepts the choice, the courts of both States might consider themselves competent to supervise the arbitration (positive conflict of competence). In such a case it would also be uncertain which procedural law the arbitral tribunal and the parties have to follow.

30. On the other hand, if a State permits the parties to subject an arbitration taking place in that State to a foreign procedural law, while the State of the chosen procedural law does not accept the choice, the courts of both States might decline to supervise the arbitration (negative conflict of competence) and it would also be uncertain which is the governing procedural law.

31. The Working Group may wish to consider whether it would be useful to include in the model law a provision designed to mitigate the effects of positive and negative conflicts of court competence.

32. The effects of a positive conflict of competence may be mitigated by authorizing the court of the State of the model law to decline its competence in respect of an arbitration when a foreign court may take up or has taken up an issue in respect of that arbitration. The effects of negative conflicts of competence may be mitigated by giving a right to the court of the State of the model law to assume the competence in respect of an arbitration when a foreign court has declined to decide an issue in respect of that arbitration.

33. In paragraph 13, above, it has been suggested that a criterion for determining the applicability of the model law may be provided for cases where the place of arbitration or the law governing the arbitration has not been agreed upon or determined. The suggested solution was that the model law should be applicable if a party has his place of business or residence in the State of the model law. Under this solution it may happen that a party relies on the model law in his State for the purpose of, for example, the appointment of the sole arbitrator, while the other party relies for the same purpose on the law in his State (which may or may not have adopted the model law). The consequence may be conflicting court decisions or that the two different laws contain provisions which conflict in substance.

<sup>3</sup>Ibid., para. 129.

<sup>4</sup>Ibid., paras. 135 and 139.

<sup>5</sup>Ibid., paras. 133 and 140.

34. A way of dealing with the problem may be to provide that the request by the claimant or by the most diligent party pre-empts the right of the other party to rely on his law. Such a provision would eliminate conflicts where each party is from a State which has adopted the model law. In situations where one of the two potentially applicable laws is not the model law, such a provision may reduce the possibility of conflicting situations, without, however, eliminating them.

## 2. *Conflict of laws governing validity of arbitration agreement*

35. The model law provides in the procedure for setting aside an award and in the procedure for recognition and enforcement of an award a rule on the law governing the validity of arbitration agreements (articles 34 (2) (a) (i) and 36 (1) (a) (i)). In both cases the chosen law is primarily applicable, while if no choice is made, different solutions are given for each of the cases just referred to. In setting aside, the applicable law is the law of the court which is to decide the issue of setting aside, and in recognition and enforcement, it is the law of the place of the making of the award.

36. Since these conflict rules might be regarded as applicable only in the context of articles 34 and 36, the Working Group may wish to consider the usefulness of a general rule which would also apply to the time before the making of the award or even before the commencement of arbitral proceedings.

37. As to the content of the conflict rules in articles 34 and 36, it may be noted that both rules would lead to the same result if the Working Group adopts the strict territorial criterion in delimiting the scope of application of the model law. If in such a case a general rule on the law governing the arbitration agreement were adopted, the governing law should be the law to which the parties have subjected the arbitration agreement or, failing any indication thereon, the law of the place of arbitration.

38. If, however, the Working Group decides that the parties should be allowed to subject the arbitration to a

law different from the law of the place of arbitration, a conflict between the two rules might arise. If the parties have subjected the arbitration to a law different from the law of the place of the making of the award, in the setting-aside procedure the validity of the arbitration agreement would be governed by the law which governs the arbitration and not by the law of the State where the award was made. In the same arbitration, but in the recognition and enforcement procedure, the validity of the arbitration agreement would be governed by the law of the State where the award was made.

39. Therefore, if the parties were to be given the autonomy to subject their arbitration to a procedural law different from the law of the place of arbitration, the Working Group may wish to consider aligning the two conflict rules. To achieve the alignment, article 36 (1) (a) (i) would have to be modified to the effect that, if the award is not made in the State of the law which governs the arbitration, the arbitration agreement would be governed by the law governing the arbitration. If, at the same time, a general rule on the law governing the validity of the arbitration agreement were to be adopted, it is submitted that the governing law should be the law to which the parties have subjected the arbitration agreement or, failing any indication thereon, the law which governs the arbitration.

40. Furthermore, it may be noted that no solution has been provided for cases where the parties have not subjected the arbitration agreement to a law and it cannot be ascertained where the award is to be made. Since the question of the validity of an arbitration agreement may arise before these connecting factors are established, the Working Group may wish to consider whether it would be useful to include in the conflict rule a provision on a supplementary connecting factor.

41. As to the question which connecting factor might be included in the conflict rule, no ideal solution has been found to date. However, it appears that it would not be contrary to the expectation of the parties if, failing the first two connecting factors, the arbitration agreement is governed by the law which governs the contract in relation to which the dispute has arisen.

## (c) *Composite draft text of a model law on international commercial arbitration: some comments and suggestions for consideration: note by the secretariat (A/CN.9/WG.II/WP.50)*

### INTRODUCTORY NOTE

1. This Working Paper contains some comments and suggestions which the Working Group may wish to consider during its deliberations on the composite draft text of a model law on international commercial arbitration. The composite draft text is contained in document A/CN.9/WG.II/WP.48 (reproduced in this Yearbook, part two, II, B, 3, a).

2. Most of the comments and suggestions apply to more than one draft article. They deal, for example,

with the operation and effect of a given rule in the context of other relevant provisions or, generally speaking, deal with the inner consistency and practical workability of the various draft provisions.

### SOME COMMENTS AND SUGGESTIONS FOR CONSIDERATION

#### A. *Model law as "lex specialis" (articles 1, 5, 34, 36)*

3. It seems to be clear and accepted that the model law is designed to establish a special legal régime for

international commercial arbitration which, in the States adopting it, would prevail over any other municipal law on arbitration. The Working Group may wish to consider whether this principle of *lex specialis* is sufficiently covered by the words, "This Law applies to international commercial arbitration" (article 1 (1)), or whether it should be made more explicit.

4. If an explicit rule to that effect were envisaged, it could state that the application of other national provisions of law dealing with arbitration is excluded by "the provisions of this Law" or, preferably, "this Law in respect of all matters dealt with herein". The latter wording (or words of similar import) could help to clarify that the model law is not a self-contained and self-sufficient legal system which would exclude the application of all other national provisions of law dealing with arbitration.

5. The suggested qualification could help to draw attention to the fact that there are certain matters or aspects of arbitration not governed by the Law. As an illustration, one need only recall a number of issues which the Working Group decided not to settle in the model law: arbitrability of subject-matter of dispute, capacity of parties to conclude arbitration agreement, impact of State immunity, enforcement by courts of interim measures granted by arbitral tribunal, competence of arbitral tribunal to adapt contracts, fixing of fees and request for a deposit, time-limit for enforcement of award. However, as these examples show, it would not always be an easy task to determine whether a certain issue is governed by the model law, though possibly not expressly regulated, or whether it is not dealt with therein and thus governed by another law.

6. It is submitted that similar considerations apply with regard to draft article 5, although to a more limited extent, since the distinction between matters governed by the Law and those not governed thereby is relevant there only in respect of possible court supervision or assistance.

7. Finally, the recognition of the fact that certain provisions of a national law other than the model law may be applicable might lead to a modification of article 34 (2) (a) (iv). The Working Group may wish to consider whether the conference in that sub-paragraph to "this Law" is too narrow and whether it should be replaced by the words "law of this State". It may be noted that, in the parallel provision of article 36 (1) (a) (iv), the reference is to "the law of the country where the arbitration took place" (which, in the domestic setting, does not restrict the test of compliance to the model law).

#### B. Listing of mandatory provisions (article 3)

8. Draft article 3 is designed to clarify, in one place, from which provisions of the model law the parties may not derogate. Such centralisation by means of a list of all mandatory provisions would make it unnecessary to include in the non-mandatory provisions such wording as "unless otherwise agreed by the parties".

9. However, there are certain difficulties and other considerations which cast some doubt on the appropriateness and need for such approach. Firstly, a considerable number of provisions are obviously by their content of a mandatory nature. Secondly, there are a number of provisions granting freedom to the parties, accompanied by suppletive rules failing agreement by the parties; here the question of mandatory nature seems to be a philosophical one and equally redundant. Thirdly, with respect to some draft articles only a part of the provision (e.g. a time-limit) is non-mandatory. Fourthly, in respect of some of the provisions already decided to be non-mandatory, the Working Group was of the view that this should, for the sake of emphasis, be expressed in the individual provision, despite the general listing in article 3. Fifthly, it is suggested that, in addition to the provisions already decided to be non-mandatory and drafted accordingly, i.e. articles 11 (1), 15, 18, 20 (2), 21, 24 (1), 25, 26 (1), 29, 33 (2), there are only few further provisions which may be regarded as non-mandatory and, if so, could be easily marked as such by adding the words "unless otherwise agreed by the parties"; articles 2 (e), 23 (2), and possibly article 26 (2), (3).

#### C. Scope and effect of waiver rule (articles 4, 34, 36)

10. The Working Group may wish to consider, in the light of its decision on which provisions of the model law are to be mandatory, whether the present restriction of the operation of the waiver rule to non-mandatory requirements of the law should be maintained. If only the provisions mentioned in paragraph 9 above were to be non-mandatory, the restriction might be regarded as too narrow. A wider operation of the waiver rule could, for example, be achieved by excluding from its scope only any fundamental procedural defects such as violations of public policy, including arbitrability of the subject-matter of the dispute.

11. The Working Group may also wish to consider clarifying the effect of a waiver by virtue of article 4. While it is obvious that a party would be precluded from raising his objection during the further stages of the arbitral proceedings, it is not immediately clear whether that party is also precluded from invoking the non-compliance in an application for setting aside or for refusing recognition or enforcement of the award. It is submitted that a waiver under article 4 should have such extensive effect and that this interpretation may be expressed either in article 4 or in articles 34 and 36. It may be noted, however, that in the latter case the effect of the waiver rule would be further extended in that its inclusion in article 36 would also apply to foreign arbitral awards made under a procedural law other than the model law.

#### D. Arbitration agreement and agreements by the parties on arbitral procedure (articles 4, 7, 19)

12. The Working Group may wish to consider the relationship between the term "arbitration agreement"

and the various references in the model law to agreements by the parties relating to the composition of the arbitral tribunal or to the arbitral procedure. While arbitration agreements frequently contain such procedural stipulations, in particular by reference to standard arbitration rules, it is not uncommon to agree on most or at least some procedural issues only when a dispute arises, or even during the arbitral proceedings, that is, long after the conclusion of the agreement to submit future disputes to arbitration. This varied practice leads to two suggestions for consideration by the Working Group.

13. The first idea is to use the term "arbitration agreement" as defined in article 7 (1) in its literal and rather narrow sense, i.e. agreement to submit disputes to arbitration. This basic agreement would be the foundation of the arbitral tribunal's jurisdiction, to the exclusion of court jurisdiction, irrespective of whether it is accompanied by any agreement on the procedure. The term "arbitration agreement" should then not be used when the emphasis is on the procedural stipulations (as, e.g., in article 4). An important practical consequence of such interpretation would be that article 7 (2) would require written form only for that basic agreement, including any later determination or modification of the claims or dispute submitted, but not for any procedural agreements by the parties.

14. The second idea would be to require that the parties conclude any agreement on the arbitral procedure, if not already included in the arbitration agreement, before the first or sole arbitrator is appointed. The reason for such time-limit would be that the rules of procedure should be clear when that procedure starts and that any arbitrator should know from the beginning under what rules he is expected to perform his function. It may be recalled that this very reason led the Working Group to include this time-limit in article 26 (1). The suggestion here would be to adopt the same limit on a more general level, for example, in the basic provision of article 19 (1), possibly with the proviso "unless otherwise provided in this Law".

#### *E. Effect of failure to invoke existence or non-existence of valid arbitration agreement (articles 8, 16, 17, 34, 36)*

15. The Working Group may wish to consider the effect of a party's failure to invoke the arbitration agreement in the case of article 8 (1) or, conversely, to plead in the case of article 16 (2) that the arbitral tribunal lacks jurisdiction. In the first case, there may be some doubt as to whether failure to make a timely request of referral to arbitration should preclude a party from relying on the arbitration agreement in other contexts or forums since, for example, its recognition or its scope in terms of arbitrability of the subject-matter may vary from one place to another. However, for the sake of preventing parallel proceedings and conflicting decisions, one might consider treating the failure to request referral as a waiver of the right to rely anywhere on the arbitration agreement. This would

then, for example, bind the court which is asked under article 17 to decide whether or not there exists a valid arbitration agreement.

16. In the reverse case, i.e. article 16 (2), the answer seems to be less difficult. It is submitted that a party who fails to raise the plea as required under article 16 (2) should be precluded from raising objections with respect to the existence or validity (or scope) of the arbitration agreement also in other contexts, including the court control envisaged under article 17 and, in particular, the post-award stage (i.e. articles 34 (2) (a) (i) and 36 (1) (a) (i)). However, such waiver by submission should be subject to certain limits such as public policy including arbitrability.

#### *F. Court control of arbitral tribunal's jurisdiction (articles 16, 17)*

17. Where the arbitral tribunal has ruled on a plea referred to in article 16 (2) as a preliminary question and has decided that it has jurisdiction, such ruling may be contested, according to paragraph (3) of that article, only in an action for setting aside the arbitral award. The secretariat has placed this provision between square brackets, not because it wished to indicate any doubts as to the appropriateness of this very rule, but in order to invite reconsideration of the relationship between this rule and article 17.

18. From a formal point of view, the two provisions deal with different matters since article 16 (3) provides recourse to a court only against a ruling of the arbitral tribunal while article 17 envisages direct resort. However, from a substantive point of view and for all practical purposes, these two provisions deal with the same issue and are, it is submitted, in conflict with each other. There would seem to be two possible approaches to avoid any conflict.

19. One possibility is to delete the last sentence of article 16 (3). In this case, one may consider adding to article 17 (2) the device adopted in article 13 (3) for accelerating matters, i.e. that the court's decision shall be final. The other possibility is to exclude the concurrent court control under article 17 to the extent it would be in conflict with article 16 (3). Article 17 would, then, be limited to those cases where the arbitral proceedings have not yet commenced or where they have been terminated by a ruling of the arbitral tribunal that it lacks jurisdiction. Where the proceedings have been terminated by a final award which is based on a ruling that the arbitral tribunal has jurisdiction, the court control would be exercised in the proceedings governed by article 34 and articles 35 (2) and 36.

#### *G. Suspension of award (articles 33, 34, 36)*

20. The draft model law refers to the procedural possibility of a suspension of the award only indirectly in article 36 (1) (a) (v) and (4), stating certain legal

consequences of a suspension or an application for suspension. The Working Group may wish to consider adding a positive provision which would grant a right to request suspension of an award made under this law. Such a right may be appropriate in conjunction with the right to request a correction under article 33 (1) (a), possibly in conjunction with the right to request an interpretation under article 33 (1) (b), and certainly in conjunction with an application for setting aside under article 34.

#### H. Additional award requiring further hearings or evidence (articles 33, 34)

21. Article 33 (2) envisages the making of an additional award as to claims presented in the arbitral proceedings but omitted from the award only where such omission can be rectified without any further hearings or evidence. The question therefore remains what would happen in those cases where further evidence or hearings are required.

22. From a practical point of view, the suggested answer would be that the arbitral tribunal could still be entitled or required to make the additional award since it did not completely fulfill the mandate entrusted to it. If this view were adopted, it would mean that the restriction contained in article 33 (2) would be abolished, although this provision might be retained for the residual purpose of setting a time-limit of sixty days for these restricted cases. A supplementary consideration would be to include in article 34 a provision to the effect that the award may be set aside if the points dealt with therein cannot be separated from the points omitted. In this context, the possibility of remission under article 34 (4) may prove to be a very useful device.

23. The need for an express rule on this question becomes apparent when one looks at the present draft provisions. It is at least a possible interpretation of articles 33 (2) and 34 that omission of a claim requiring further hearings or evidence constitutes a ground for setting aside the award, irrespective of whether the omitted points can be separated from the points dealt with in the award. The omission could then be rectified by the arbitral tribunal if the award would be remitted to it for completion. If, however, the court would not remit the award but would set it aside, a problem of general relevance arises which is treated in the following section (paragraphs 24-26).

#### I. Effect of setting aside on arbitration agreement (articles 32, 34)

24. The Working Group may wish to consider the question how a party may pursue his claim after the award has been set aside under article 34. Where lack of a valid arbitration agreement was the ground for setting aside, the answer would be that the party may resort to a court. If the award was set aside for other reasons, there are essentially two possible solutions.

25. One possibility would be to conclude that arbitration did not work and to refer the parties to court litigation without, of course, taking away the (here probably more theoretical than practical) option of concluding a new arbitration agreement.

26. The other possibility would be to re-activate the original arbitration agreement or to regard it as still operative, on the ground that the final award, which under article 32 would terminate the mandate of the arbitral tribunal, has been set aside and, thus, cannot have this terminating effect. However, in order to limit the risk of repeated futile arbitrations, one might consider adopting the recent innovation in Austrian law (sect. 595 (2) Code of Civil Procedure) according to which the arbitration agreement becomes invalid if an arbitral award on the matter has been set aside twice.

#### J. Recognition of award as binding (article 35 (1))

27. The Working Group may wish to consider supplementing the provision of article 35 (1) in three respects. The first would be to add after the words "shall be recognized as binding" the words "between the parties". This would clarify that a decision which is founded on an arbitration agreement between two (or more) parties cannot bind other persons. It would also help to convey the idea of *res judicata*, without using that term which is not known in all legal systems although the concept seems to be commonly shared.

28. The second suggestion would be to indicate the exact point of time from which an award shall be recognized as binding. While it may be in the interest of a party to be bound by an award only from the date of the receipt of such award, it might be preferable, for the sake of certainty, to use the date of the award, referred to in article 31 (3). In this context, consideration might be given to expressing the idea, accepted in substance by the Working Group, that an award would not be binding (and may not be set aside) if, and as long as, it is subject to appeal before arbitrators, i.e. an arbitral tribunal of second instance, as often envisaged in commodity arbitrations.

29. The third suggestion for consideration would be to state that registration or deposit of an award in the country of origin is not a requirement for recognition and enforcement under the model law. While this rule might already be inferred from the above suggested provision that an award is binding from its date, an express statement may be advisable in view of the fact that a foreign procedural law may require such registration or deposit. It is even advisable in respect of awards made under the model law since registration or deposit is not expressly regulated, in fact not even mentioned, therein (see article 31). An express statement would help to clarify that this fact should not be regarded as an intentional gap to be filled by another municipal law but as a positive regulation to the effect that registration or deposit is not a pre-condition for recognition or enforcement. This clarification would, thus, help to avoid the uncertainty alluded to earlier (in paragraph 5 above).

K. *Possible separate treatment of foreign and of domestic awards (articles 35, 36)*

30. Finally, it may be recalled that the Working Group decided to consolidate the previous draft articles XXV and XXVI as well as articles XXVII and XXVIII so as to have uniform rules covering domestic and foreign arbitral awards alike. However, in view of the tentative nature of the policy decision as regards uniform treatment, observations were made on the

draft articles in case a separate régime were to be retained, at least as an option for the time being. Nevertheless, the secretariat did not prepare alternative draft provisions for such separate treatment since their eventual wording could be easily deduced from draft provisions already existing, i.e. article 35 for domestic and foreign awards, article 36 for foreign awards and previous draft article XXVII, as modified by the Working Group (A/CN.9/245, paras. 140 and 141; reproduced in this *Yearbook*, part two, II, A, 1), for domestic awards.

### III. NEW INTERNATIONAL ECONOMIC ORDER

#### A. Report of the Working Group on the New International Economic Order on the work of its fifth session (New York, 23 January-3 February 1984) (A/CN.9/247)<sup>a</sup>

#### CONTENTS

	<i>Paragraphs</i>
INTRODUCTION .....	1-11
FORMAT OF THE LEGAL GUIDE .....	12-23
VARIATION CLAUSES .....	24-42
ASSIGNMENT .....	43-54
SUSPENSION OF CONSTRUCTION.....	55-60
TERMINATION .....	61-85
INSPECTION AND TESTS .....	86-97
FAILURE TO PERFORM.....	98-126
DAMAGES .....	127-131
OTHER BUSINESS AND FUTURE WORK.....	132-134

#### INTRODUCTION

1. At its eleventh session (in 1978) 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.<sup>1</sup> At its twelfth session the Commission designated member States of the Working Group.<sup>2</sup> At its thirteenth session the Commission decided that the Working Group should be composed of all States members of the Commission.<sup>3</sup> The Working Group consists of the following 36 States: 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.

2. At its first session (in 1980) 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.<sup>4</sup> 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.<sup>5</sup>

3. The studies<sup>6</sup> prepared by the secretariat were examined by the Working Group at its second and third sessions, in 1981 and 1982.<sup>7</sup> At its third session the Working Group requested the secretariat, pursuant to a decision of the Commission at its fourteenth session,<sup>8</sup> to commence the drafting of a legal guide on contractual provisions relating to contracts for the supply and construction of large industrial works.<sup>9</sup> The legal guide

<sup>a</sup>For consideration by the Commission see Report, chapter V (part one, A, above).

<sup>1</sup>Report 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).

<sup>2</sup>Report 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).

<sup>3</sup>Report 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).

<sup>4</sup>See A/CN.9/176, para. 31 (*Yearbook 1980*, part two, V, A).

<sup>5</sup>See A/CN.9/WG.V/WP.4 and Add.1-8 (*Yearbook 1981*, part two, IV, B, 1), and A/CN.9/WG.V/WP.7 and Add.1-6 (*Yearbook 1982*, part two, IV, B).

<sup>6</sup>See A/CN.9/198, paras. 11-80 (*Yearbook 1981*, part two, IV, A), and A/CN.9/217, paras. 13-129 (*Yearbook 1982*, part two, IV, A).

<sup>7</sup>Report 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).

<sup>8</sup>See A/CN.9/217, para. 130 (*Yearbook 1982*, part two, IV, A).

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.<sup>7</sup>

4. At its fourth session (in 1983) the Working Group examined a draft outline of the structure of the legal guide and some sample draft chapters prepared by the secretariat<sup>8</sup> and requested the secretariat to proceed expeditiously with the preparation of the legal guide.<sup>10</sup>

5. The Working Group held its fifth session in New York from 23 January to 3 February 1984. All the members of the Working Group were represented with the exception of the Central African Republic, Peru, Senegal and the United Republic of Tanzania.

6. The session was attended by observers of the following States: Argentina, Benin, Canada, Chile, Colombia, Democratic People's Republic of Korea, Finland, Honduras, Indonesia, Liberia, Netherlands, Nicaragua, Republic of Korea, Suriname, Switzerland, Thailand, Turkey and Venezuela.

7. The session was also attended by observers from the following international organizations:

(a) United Nations organs: Centre for Transnational Corporations, United Nations Industrial Development Organization and United Nations Institute for Training and Research;

(b) Specialized agency: World Bank;

(c) Other intergovernmental organizations: Asian-African Legal Consultative Committee, European Economic Community;

(d) Non-governmental organizations: International Bar Association, International Federation of Consultative Engineers, International Chamber of Commerce.

8. The Working Group elected the following officers:

Chairman: Leif SEVON (Finland)\*

Rapporteur: Peter Kihara MATHANJUKI (Kenya).

9. The Working Group had before it draft chapters of the legal guide on drawing up international contracts for construction of industrial works, on "Termination" (A/CN.9/WG.V/WP.9/Add.5; *Yearbook 1983*, part two, IV, B), and on "Inspection and tests", "Failure to perform", "Damages", "Liquidated damages and penalty clauses", "Variation clauses", "Assignment" and "Suspension of construction" (A/CN.9/WG.V/WP.11 and Add.1-8; reproduced in this *Yearbook*, part two, III, B), together with a document discussing some aspects of the format of the guide (A/CN.9/WG.V/WP.11/Add.9; *idem*).

10. The Working Group adopted the following agenda:

1. Election of officers
2. Adoption of the agenda
3. Consideration of draft chapters of the legal guide for drawing up international contracts for the construction of industrial works
4. Other business
5. Adoption of the report

11. The Working Group reaffirmed the importance of this project in the context of the new international economic order and agreed that the draft chapters should be examined keeping in view its objectives.

#### FORMAT OF THE LEGAL GUIDE

12. The Working Group discussed various issues concerning the format of the legal guide (A/CN.9/WG.V/WP.11/Add.9).

13. A view of general nature was expressed that the guide should more clearly bring out that it only contained recommendations to the parties, and that it should avoid stating that the parties "must" or be "obliged to" include certain provisions in their contract. However, the use of such words may be necessary in the illustrative provisions of the guide.

14. According to one view, chapter summaries were disadvantageous in that it would be difficult in such summaries to reflect the balance achieved in the text of the chapter, and in that a summary of complex legal issues and discussions could produce misleading results. The prevailing view, however, was that chapter summaries would be of great help to businessmen, contract administrators and others who had to be aware of the principal issues covered by a particular type of contract clause, but who did not require the detailed information contained in the text of the chapter.

15. It was suggested that the general approach adopted in the present set of draft chapters for summaries should be followed. In this regard, it was suggested that it would be useful for the chapter summaries to contain references to paragraphs of the text of the chapter where particular issues referred to in the summaries were used, as well as cross-references to other relevant chapters.

#### *Index*

16. It was generally agreed that the legal guide should contain a detailed alphabetical index with references to the text of the guide.

#### *Check-lists and table of contents*

17. It was suggested that a check-list for each chapter might be useful, if it were detailed enough to make the

\*The Chairman was elected in his personal capacity.

<sup>8</sup>See A/CN.9/WG.V/WP.9 and Add. 1-4 (*Yearbook 1983*, part two, IV, B).

<sup>10</sup>See A/CN.9/234, paras. 51-52 (*Yearbook 1983*, part two, IV, A).

reader aware of the points discussed in the chapter. According to another view, however, a detailed table of contents could serve the same purpose. It was generally agreed that the secretariat should consider whether it would be possible to structure a table of contents in such a way as to enable it to serve as a check-list as well, taking into account that the legal guide will also have a detailed index.

#### *Illustrative provisions*

18. With respect to illustrative provisions, the view was expressed that such provisions should not normally be included if they merely repeated what was contained in the text. Nevertheless, it was recognized that it might be desirable to include illustrative provisions on some issues even if the provisions in substance set forth what was contained in the text, because of the importance of such issues. It was suggested that, in principle, illustrative provisions should be included only for the purpose of illustrating the drafting needed to cover a complex issue, or making an issue in the text easier to understand.

19. It was also suggested that the relationship among the various illustrative provisions contained in a chapter be clarified, to enable the reader to know whether two or more illustrative provisions were intended to be or could be used together.

20. The view was expressed that illustrative provisions expressed in clear language could be useful in that they could make it easier for businessmen, contract draftsmen and administrators, particularly from developing countries, to formulate contractual provisions.

21. The suggestion was made that the legal guide should make it clear that the illustrative provisions should not necessarily be regarded as models for inclusion in particular contracts. There was a general view that the guide should present alternative illustrative provisions when it was appropriate and useful to do so.

22. It was suggested that illustrative provisions should be placed in footnotes at locations in the chapter containing the issues which are illustrated.

23. It was proposed that the guide should contain instructions for its use.

#### VARIATION CLAUSES

24. The Working Group considered the draft chapter on variation clauses (A/CN.9/WG.V/WP.11/Add.6). A suggestion was made that the chapter would gain in clarity if the kinds of variations to which it related were specified at the beginning of the chapter.

25. The Working Group discussed whether variations of the work to be performed under the contract should be possible only with the consent of both parties, or

whether the purchaser should be able to order variations unilaterally. The secretariat was requested to consider whether the result should depend upon the type of works contract involved.

26. It was recognized that an appropriate balance should be struck between the principle of *pacta sunt servanda* and the desirability of permitting variations of the contract when they were necessary or desirable due to the complex and long-term character of works contracts. Some support was expressed for the approach taken in the draft chapter, according to which the purchaser should be able to vary the contract unilaterally, subject to certain conditions designed to protect the interests of the contractor. In this regard, it was noted that purchasers from developing countries have a particular interest in being able to order variations because, due to their lack of experience of works contracts, they are often not able to foresee at the time of concluding a contract all circumstances which may arise during construction. According to another view, the consent of both parties should be required for all variations.

27. Certain intermediate approaches were suggested. According to one, the legal guide would make no recommendation as to whether the purchaser should be able to order variations unilaterally, or whether all variations should require the consent of both parties. The guide would recommend, however, that if the parties chose to permit unilateral variations, the contract should contain provisions dealing with such issues as the effect of the variation on the contract price, time for performance and other contract terms, the scope of variations which may be ordered, the right of the contractor to object to variations, and procedures to be followed with respect to ordering and objecting to variations.

28. According to another intermediate approach, the consent of both parties would normally be required for a variation, but it would be recognized that in some situations the parties might wish to permit the purchaser unilaterally to order variations. If so, the contract should contain provisions dealing with the issues mentioned in the previous paragraph.

29. It was suggested that the scope of variations which may be ordered unilaterally by the purchaser should be restricted. Various suggestions were made for achieving this, such as permitting unilateral variations only if they have no impact on the contract price, or only up to a specified percentage of the contract price, or providing quantitative limits to certain types of variations (e.g., permitting variations of the production capacity of the works only up to a certain limit), or specifying in the contract which contractual provisions may be varied. Other suggestions included permitting unilateral variations only as to the construction of the works, and not as to the supply of equipment or materials to be incorporated in the works, or limiting the period during which unilateral variations may be made. It was noted that the limitation of unilateral variations to those

"within the overall scope of the works" would become clearer when considered in relation to chapter IX of the legal guide ("Scope and quality of works").

30. With respect to the grounds on which the contractor should be able to object to a unilateral variation by the purchaser, various formulations were proposed as alternatives to the ground of "substantial prejudice" referred to in the draft chapter. Those included "unreasonably more work", "unreasonably additional cost", "undue burden" and "undue inconvenience".

31. A suggestion was made that the contract should set forth specific circumstances which would entitle the contractor to object, rather than setting forth general standards. A further suggestion was that the legal guide might propose alternative formulations of the grounds entitling the contractor to object to a unilateral variation by the purchaser.

32. A view was expressed that if the variation clause contained a list of specific circumstances which would entitle the contractor to object, the list should be only illustrative, since contractors would not agree to have their ability to object restricted to circumstances contained in an exhaustive list.

33. With respect to the time within which the contractor should be required to notify the purchaser of his objection, the view was expressed that a single time period was unrealistic. One view suggested that the contract should provide for two time periods, one within which the contractor must notify his objection, and a further period within which the contractor would be obligated to calculate and notify the purchaser of the effect of the variation on the price and time for performance, and provide the purchaser with information pertinent thereto. According to another view, the time for notification should depend upon the nature of the variation, and this period should be agreed to by the parties after the variation had been proposed.

34. With respect to the consequences of a failure by the contractor to give a timely notification, the view was expressed that a loss of the right to object and to obtain adjustments in the contract price and time for performance was too harsh. It was suggested that the legal guide should propose alternatives to these consequences. One alternative might be to obligate the contractor to pay damages to the purchaser to compensate for any loss caused by the failure to give a timely notification. Another alternative might be to obligate the contractor to perform the variation, but to allow him to obtain appropriate adjustments in the price and time for performance.

35. A suggestion was made that if the contractor objected to a unilateral variation by the purchaser, the contract should require the parties to attempt to resolve the issue themselves through negotiations. It was suggested that if the parties failed to resolve the issue, the contract should provide for it to be resolved quickly by an independent third party available on site, who possessed the knowledge and experience necessary to

resolve such issues. The view was expressed that the identity of the independent third party should be specified in the contract itself. A further view was expressed that a dispute concerning the effect of the variation on the price and time for performance should be resolved separately from a dispute over whether the variation should be performed.

36. With respect to the question of whether the contractor should be obligated to perform a variation pending the settlement of a dispute concerning the variation, one view suggested that it was too burdensome to require the contractor to perform the variation pending the settlement of the dispute. Another view suggested that the independent third party who is to settle the dispute should be empowered to require the contractor to perform if he makes a *prima facie* finding that the purchaser is entitled to order the variation unilaterally. According to another view, however, this could be unduly burdensome for the contractor if it is ultimately determined that the purchaser is not entitled to order the variation unilaterally. Suggestions were made that the independent third party should be empowered to condition the contractor's performance of the variation pending settlement of the dispute upon the purchaser's providing a security for the payment of the increased price which may be occasioned by the variation.

37. The view was expressed that the issue of variations proposed by the contractor was inadequately dealt with in the chapter. A reference was made to a situation which sometimes occurs in practice, in which a contractor makes an unreasonably low bid, and then during construction demands variations which he claims to be necessary for the proper functioning of the works and which result in a substantially higher contract price. It was suggested that the solution to such problems may lie in the negotiation of proper and reasonable contracts by the purchaser, assisted by the legal guide.

38. Two alternative approaches were suggested with respect to the role of a consulting engineer. Under one approach, a consulting engineer would be empowered to settle disputes concerning variations, whether or not he had been engaged by or was an agent of one of the parties. It was suggested that this approach is sometimes followed in practice. Under the other approach, even if there were a consulting engineer involved in the project, such disputes should be resolved by an independent third party.

39. With respect to guidelines for determining the effect of a variation on the contract price, it was suggested that such guidelines should be more concrete and should be expressed in quantitative terms.

40. The Working Group discussed the illustrative provisions contained in the draft chapter. It agreed that the illustrative provisions would be redrafted so as to correspond with changes to be made in the text of the chapter.

41. With respect to paragraph (4) of the illustrative provision in footnote 1, it was suggested that an alternative provision be added requiring the written agreement of both parties for any variation which would produce an increase or decrease in the contract price in excess of a specified percentage.

42. It was suggested that it be made clear that the list of circumstances in the illustrative provision in footnote 2 was open-ended and not exhaustive. It was also suggested that it be made clear that the list of circumstances need not be adopted as a whole in a particular contract. The view was also expressed that terminology other than "substantially prejudice" should be used in paragraph (a) of this illustrative provision. With respect to paragraph (c), it was suggested that an alternative provision be added whereby the contractor would be obligated to perform a variation involving the doing of work which he does not normally do only if a subcontractor whom he has already employed can perform the variation. It was suggested that the illustrative provision in footnote 4 make no recommendation as to the exact number of days within which the contractor must dispatch his notification of objection and claims to the purchaser.

## ASSIGNMENT

43. The Working Group discussed the draft chapter on assignment (A/CN.9/WG.V/WP.11/Add.7). It was generally agreed that rather than using the term "assignment" an attempt should be made to use a neutral term, such as "transfer", which does not carry with it special legal meanings under particular legal systems. A suggestion was made that the chapter should state that it deals only with assignments by act of a party, and not by operation of law.

44. It was suggested that the chapter should advise the parties to consider the positions of third parties in relation to assignments. In this regard, a suggestion was made that the chapter should advise an assigning party to consider whether, under applicable law, the consent of his guarantor was needed for an assignment since under some legal systems an assignment without such consent discharged the guarantor.

45. A view was expressed that the chapter should distinguish between assignments of the contract as a whole, assignments of specific rights and assignments of specific obligations.

46. It was generally agreed that an assignment of the contract as a whole should not be permitted without the consent of the other party. It was also generally agreed that an assignment of most specific rights and obligations should also not be permitted without the consent of the other party, although, in accordance with contracting practice, an assignment by the contractor of his right to receive payments, in order to obtain financing, should be permitted without the consent of the purchaser. A view was expressed that

assignments without the consent of the other party should be permitted in other cases as well, such as an assignment of the completed works by the purchaser. According to one view consent should be required in these cases as well.

47. It was suggested that the chapter should mention issues concerning succession, merger and reorganization and should call to the attention of the parties that the issues in connection with such events would be settled under the applicable law. In this regard, the secretariat noted that some of these issues might be explored when the legal issues associated with joint ventures and consortia in the context of industrial contracts was later considered by the Working Group.

48. With respect to assignment of a contract by one State organ or enterprise to another, it was suggested that the chapter should point out that when a Government was a party to the contract, the Government might decide which organ or enterprise was to administer the contract and that this should be reflected in the contract. It was also suggested that the chapter should point out that in some cases under the applicable law an assignment might be subject to the approval of a State authority and should advise the parties to examine the applicable law in this regard.

49. It was suggested that the chapter should point out that the rights of an assignee would in some cases be governed by mandatory provisions of the applicable law and should advise the parties to ascertain the extent to which their ability in their contract to affect the rights of an assignee may be restricted.

50. For cases in which the contractor is able to assign his right to receive payments without the consent of the purchaser, it was suggested that the chapter propose two alternative means of protecting the interests of the purchaser. The first means would require the contractor to notify the purchaser of the assignment. The second means would, in addition to the notice requirement, entitle the purchaser to object to the assignment on reasonable and substantial grounds.

51. It was suggested that the chapter should mention that when a contract requires notice of an assignment to be given to the non-assigning party, the assignee might wish to ensure that such notice has been given. In this regard, however, the view was expressed that the contract could not deal with this issue. Rather, the assignee should explore his obligations and position under applicable law and take such actions as were necessary to protect his position.

52. It was noted that the consequence recommended in the draft chapter of an unauthorized assignment, e.g., that the non-assigning party should be entitled to disregard the assignment, may not be possible under applicable law. It was suggested that alternative consequences should be added, such as a right of the non-assigning party to damages, or termination. A view was expressed that the consequences of an improper assign-

ment should be dealt with in connection with the discussion of means to protect the rights of the non-assigning party.

53. It was agreed that in the illustrative provision in footnote 3 of the draft chapter, the period of time therein specified should be deleted. It was also suggested that an illustrative provision should be added under which, if the contractor were permitted to assign his right to payments, this should be conditioned upon his undertaking to procure the assignee's consent to the right of the purchaser to set off sums owed to the purchaser by the contractor against payments to be made to the assignee.

54. It was generally agreed to delete the illustrative provision in footnote 8 of the draft chapter.

#### SUSPENSION OF CONSTRUCTION

55. The Working Group considered the draft chapter on suspension of construction (A/CN.9/WG.5/WP.11/Add.8). A question was raised whether the topic of suspension should not be dealt with in a separate chapter, but rather in other chapters where the topic was relevant, e.g., in the chapter on termination. It was agreed that it would be preferable to discuss the topic in a separate chapter.

56. It was suggested that the guide should propose that in respect of suspension for convenience by the purchaser, it should be required that the suspension should be effective only if exercised in good faith. The view was expressed, however, that the requirement of good faith was a general principle which might be equally applicable in other chapters and that it should be dealt with separately. Furthermore, it was noted that such a requirement might not be in accordance with the concept of suspension for convenience under which the purchaser was not obliged to indicate reasons for suspension. It was agreed, therefore, that it was unnecessary to make reference to good faith in this context.

57. In connection with the treatment in the contract of suspension by the purchaser on specific grounds, it was suggested that parties might wish to include in the contract either a complete list of grounds for suspension, or only examples of such grounds.

58. It was agreed that the view set forth in paragraph (13) was unnecessary. It was also agreed that the question of compensating the contractor for loss of profit in respect of the contract affected by the suspension should be dealt with in paragraph (12). It was suggested that compensation should be payable for such loss of profit.

59. It was suggested that the guide should not express the view set forth in paragraph (17) that the contractor should be entitled to suspend the construction in cases of failure to perform certain obligations by the pur-

chaser. According to another view, such a provision in the contract was admissible. It was agreed to mention in the guide the possibility of specifying in the contract situations in which the contractor might suspend the contract due to the failure to perform certain obligations by the purchaser, e.g., in case the purchaser fails to fulfil his obligation to supply a design to be used for the construction by the contractor. It was suggested that such a right of the contractor should be limited to cases where the design was to be supplied by the purchaser during construction.

60. It was suggested that paragraph (7) in the illustrative clause set forth in footnote 2 should include a reference to the costs of demobilization and remobilization, including housing and transportation.

#### TERMINATION

61. The Working Group discussed the draft chapter on termination (A/CN.9/WG.V/WP.9/Add.5). The secretariat informed the Working Group that this chapter would be redrafted in a style corresponding to the other draft chapters which were before the Working Group at the present session. In particular, the text would be shortened and would be presented in a less normative style, and illustrative provisions and a summary would be added.

62. A suggestion was made that the chapter should clearly state that it dealt only with the termination of a contract by a party and not with the validity of contracts under applicable law, since the latter issue was outside the scope of the legal guide. It was also suggested that the chapter should stress that, if events occur which may give rise to a right of termination, it would be desirable for the parties to attempt negotiation or conciliation before resorting to termination, which should be regarded as a remedy of last resort.

63. Partial termination was discussed and the difficulties with respect to the matter were considered. It was agreed that the parties in drafting contract provisions with respect to partial termination should consider it carefully. According to one view a discussion of partial termination would be inadvisable.

64. With respect to termination by the purchaser for a breach by the contractor, it was suggested that, rather than permitting termination if the contractor does not remedy the breach within a certain time after being notified by the purchaser to do so, the contractor should be able to avoid termination if he begins to remedy the breach within the period and progresses in accordance with a mutually agreed schedule. According to another view, both these possibilities should be presented in the chapter as alternatives.

65. A suggestion was made that the treatment of termination for abandonment of the contract by the contractor and for delay by the contractor should be placed in separate sections.

66. There was a difference of opinion as to whether the purchaser should be able to terminate for delay by the contractor only if the delay was serious. According to one view, the chapter should recommend to the parties to set forth the circumstances of delay which would justify termination, without regard to their seriousness. According to another view, the contract should be terminable only if the delay was serious.

67. It was suggested that the purchaser should be able to terminate if there was one long delay of a specified period, or an accumulation of shorter delays totalling a specified period, at the purchaser's option.

68. Since the validity and effects of an assignment of the contract as a whole by the contractor in violation of the contract vary among legal systems, a suggestion was made that the chapter should recommend to the parties that they determine the effects of such an assignment by reference to the law applicable to the contract. One view was expressed that if such an assignment was not valid under applicable law, it should not be possible to terminate the contract for such an assignment. According to another view, however, the contract should be terminable even if the purported assignment was not valid, since the purported assignment could indicate a lack of interest by the contractor in performing the contract. However, it was acknowledged that a provision that the contract might be terminable in such cases could be retained.

69. In addition to permitting the purchaser to terminate if the contractor improperly purported to assign the contract as a whole, it was suggested that the purchaser should also be able to terminate if the contractor improperly purported to assign specific rights and obligations under the contract.

70. In addition to permitting the purchaser to terminate if the contractor violated a provision of the contract or applicable law prohibiting subcontracting without the purchaser's consent, it was suggested that the purchaser should be able to terminate if the contractor violated other restrictions on the ability to subcontract. In this connection, it was suggested that the chapter should mention that restrictions on the ability of the contractor to subcontract might be imposed by applicable law, in addition to restrictions set forth in the contract itself.

71. A suggestion was made that even if the contract did not permit termination for trivial breaches, it should be made clear that the purchaser's other remedies in respect of such breaches were not prejudiced. It was also suggested that a failure to exercise the right of termination in one instance should not prejudice a party's right to terminate in other instances.

72. With respect to termination due to the bankruptcy of a party, it was suggested that the chapter mention that in some legal systems a contract could not be terminated when a party was bankrupt, and the parties should be advised to explore carefully the applicable

law in this regard. It was suggested that, if permitted by applicable law, the contract should be terminable if a party entered receivership.

73. A suggestion was made that termination in the event of bankruptcy or similar proceedings should be permitted only after allowing a period of time which would allow the party affected to take steps to have the proceedings dismissed or stayed.

74. According to one view, the treatment of termination for convenience should be deleted from the chapter, since termination should be resorted to only as a last resort. According to another view, however, this treatment should be retained because, due to the high cost to the purchaser of terminating for convenience, it would in fact be used only as a last resort. In addition, according to this view, a provision permitting termination for convenience benefited both parties by providing an orderly and certain procedure for such a termination in the limited areas when it became necessary, without having to rely on applicable law.

75. It was suggested that the chapter should make it clear that the consequence of termination for convenience, particularly with respect to the costs of such termination to the purchasers, would be different from the consequences of termination by the purchaser on grounds of a breach by the contractor or circumstances not within the responsibility of either party.

76. With respect to termination by the contractor for interference by the purchaser with the contractor's work, it was suggested that the contract specify types of interference which would give rise to a right of termination.

77. It was agreed that the treatment in the chapter of termination when performance was prevented by the actions of a State should be deleted and that the chapter should merely state that the validity of the exercise of jurisdiction by a State and its consequences under national law were beyond the scope of the legal guide.

78. It was suggested that the chapter should mention the possibility of enabling the non-terminating party to ask the party entitled to terminate whether he would do so, thus reducing the uncertainty as to the continuance of the contract. However, it was noted that such a provision may not be suited to all situations in which the right of termination existed under a works contract, since, for example, in cases of delay by the contractor, the purchaser might wish to postpone the decision of whether to terminate in order to see whether the work would resume. Furthermore, if the purchaser renounced his right to terminate, and thought the contractor failed to perform or cure defects, the purchaser may be left without a remedy.

79. A suggestion was made that the legal guide should deal in general with issues related to the giving of notice in works contracts. It was suggested that the chapter

should advise the parties to consider the possibility of notice being given to a representative of a party on site.

80. With respect to the hiring of a new contractor to replace a terminated contractor, it was suggested that the chapter refer to the fact that the surety under a performance bond sometimes provided a new contractor, and that a cross-reference be made to the chapter dealing with performance bonds.

81. A suggestion was made that in addition to being obligated to deliver existing drawings and descriptive documents to the purchaser, a contractor, upon termination of the contract, should be obligated to create and deliver such necessary drawings or descriptive documents that have not yet been created.

82. It was suggested that in connection with the treatment of payments to be made to a contractor when the contract is terminated, reference should be made to any obligation on the part of the contractor to mitigate his losses. A suggestion was made that when the contract is terminated due to circumstances within the responsibility of the purchaser, or for convenience, the purchaser should reimburse the contractor for his costs incidental to the termination only to the extent that they are not already included in the contract price.

83. With regard to the losses in respect of which a purchaser would be entitled to be compensated in the event of termination, it was suggested that reference be made to the possibility of limiting such damages to a liquidated sum.

84. With respect to the treatment in the chapter of the question whether the contractor should be entitled to be compensated for his lost profit on the terminated portion of the contract when the contract was terminated for convenience by the purchaser, differing views were expressed. According to one view, the contractor should be compensated for his lost profit on the contract in question, since the contractor may have foregone other contracting opportunities in anticipation of completing the contract in its entirety. Another view suggested that the contractor should be compensated for some of his lost profit through the payment of a premium or penalty by the purchaser. On the other hand, it was suggested that if the purchaser had to compensate the contractor for his lost profit, termination for convenience would be deprived of its purpose. A further view suggested that rather than making any recommendation on the question, the chapter should merely advise the parties to consider whether and to what extent the contractor should be entitled to his lost profit, and how this profit should be calculated. It was also suggested that the chapter should note that in international practice, while under some works contracts the contractor was not entitled to his lost profits, under other contracts he was so entitled. A suggestion was made that the practice in this regard should be investigated further by the secretariat.

85. It was suggested that the chapter should deal with the question whether the contractor should be able to

terminate even after the purchaser made a delayed payment, and whether the purchaser should be able to terminate even after the contractor had completed performance after delay.

## INSPECTION AND TESTS

86. The Working Group considered the draft chapter on inspection and tests (A/CN.9/WG.V/WP.11/Add.1). There was agreement that certain parts of the chapter should be redrafted with a greater emphasis on suggestions as to what parties might include in their contract. Suggestions were also made for improving the terminology used in the draft chapter.

87. It was pointed out that the phrase "inspection and tests" was uniformly used throughout the chapter. It was noted, however, that in respect of some situations to which the phrase was applied, only the term "inspection" was relevant, while in respect of others only the term "tests" should be used. It was also observed that the guide should indicate that the kinds of inspection and tests might differ in various situations and might also differ depending on the type of contract concluded by the parties.

88. The view was expressed that the section on "general remarks" did not sufficiently clarify the distinctions between inspections and tests during manufacture, building and erection, and those upon completion. It was suggested that the differing functions of these inspections and tests, and their different legal consequences, should be amplified.

89. It was observed that, while all testing requirements did not need to be expressly specified in the contract documents, it was nevertheless advisable that they should be specified in as much detail as was appropriate. Such a course would reduce possible disputes at a later stage.

90. There was general agreement that inspection by the purchaser's personnel during manufacture may give such personnel an opportunity to acquaint themselves with certain aspects of the plant. The view was expressed, however, that improper operation of equipment by the purchaser's personnel during such inspection might lead to defects in the equipment and might, therefore, diminish the contractor's responsibility for providing equipment free of defects.

91. The question of possible restrictions on the purchaser's access to sites of manufacture because of the need to protect confidential information was discussed. It was observed that, in addition to the factors which might restrict access noted in the chapter, the public law in the country of manufacture relating to secrecy might restrict access. However, the view was expressed that confidentiality should not be unduly overemphasized so as to unnecessarily limit participation by the purchaser in inspection and tests. It was also noted that the contracts under discussion always involved to a certain degree a transfer of technology, and concern was

expressed that restrictions on access might hinder the transfer of technology. It was noted in that connection that the legal guide would contain a separate chapter on the transfer of technology and that that issue could be addressed therein.

92. In regard to tests additional to or different from those originally specified in the contract, it was suggested that the contract should provide that such tests should only be permitted with the consent of both parties, but that the contract should also provide that consent could not be unreasonably withheld. It was further suggested that what was to be regarded as standard practice should be clarified in the contract. The view was expressed that if a requirement by the purchaser of additional or modified tests caused delay and consequent loss to the contractor, he should be compensated for such loss. The view was expressed that the attention of the parties should be drawn to the fact that the practice as to the tests might change after the conclusion of the contract and that, therefore, the contract should deal therewith in one way or another.

93. Suggestions were made in regard to the section dealing with inspection of shipments relating to payments and passing of risks. Concern was expressed that, if such inspection were made by third parties, confidential information might be wrongfully divulged. It was stated, however, that this might be prevented by providing that the inspection was to be made by an agent of the party entitled to inspect. Furthermore, it was noted that inspections of the kind referred to would mainly be visual inspections to ascertain shortages or breakages, as in a normal sale of goods transaction, and would not involve the operation of machinery or inspection of technical documents. The view was also expressed that the relationship between inspection and the passing of risks should be clarified. The passing of risks occurred by operation of law and was unconnected with inspection. It was noted, however, that under certain contracts for the supply of machinery or equipment, the responsibility of the supplier for the condition and quality of the goods might end with the shipment, and that the contract might provide that the risk of loss of or damage to the goods passed to the purchaser after inspection. In that connection, it was pointed out by the secretariat that the passing of risk and the transfer of property would be dealt with in detail in two separate chapters. It was also noted that inspection of the packing of goods was often important and should be mentioned.

94. The view was expressed that the chapter should provide more detailed suggestions as to certain procedural aspects of inspection and tests. Additional information should be supplied as to possible methods of collaboration between the parties in the keeping and production of records of the work done and in verifying and preserving the records of inspection and tests.

95. In regard to mechanical completion tests, it was observed that the chapter should mention the possibility of performing certain tests even before the date fixed for completion, as sometimes occurred in practice. In regard to performance tests, it was observed that, in

exceptional cases, those were conducted by the purchaser, and that the chapter should deal with the issues which might arise in such cases.

96. There was general agreement that the secretariat should add some illustrative provisions relating to situations dealt with in the chapter where the procedures envisaged were complex and needed to be clearly described.

97. A suggestion was made that the summary of this chapter should refer to the availability of international inspection services and standards.

#### FAILURE TO PERFORM

98. The Working Group considered the draft chapter on failure to perform (A/CN.9/WG.5/WP.11/Add.3). It was suggested that the chapter should be drafted in a style which would give more guidance to the parties and should present various options and examples where appropriate.

99. It was decided that, in the light of the issues covered by the chapter, an appropriate title to it would be "Delay, defects and other failures to perform". It was suggested that an introductory section of the chapter should clarify the system of remedies proposed and their interrelationship. Various suggestions were made for the elaboration of certain paragraphs to clarify the situations covered by them. The inclusion of more cross-references to other chapters was recommended.

100. Some suggestions were made in respect of the terminology to be used; for example, different terms should be used to describe equipment to be incorporated in the works and equipment of the contractor used for effecting the construction. It was suggested that some issues dealt with in the chapter might more appropriately be dealt with in other chapters. For example, the issues of the quality of the equipment and services to be supplied and the standards for performance and functioning of the works discussed in paragraphs (12) to (15) might be discussed in the chapter entitled "Scope and quality of works".

101. It was suggested that this chapter should deal only with the remedies available to the purchaser in case of a breach of a quality guarantee and that the nature and scope of the guarantee should be dealt with in another chapter, for example in the chapter entitled "Scope and quality of works" or the one entitled "Completion, take-over and acceptance". It was agreed that the secretariat should find a more appropriate place in the legal guide for the treatment of the guarantee in the light of the discussion.

102. It was suggested that this chapter should include a consolidated description of the main categories of delay by either party and should have, if necessary, cross-references to other chapters. One view was that the issue of the delay of the purchaser to pay the price should be dealt with in the chapter entitled "Price".

103. A suggestion was made to exclude from the category of delay in construction by the contractor not only cases where the failure of the contractor to perform was due to the lack of co-operation of the purchaser, but also cases where such failure was due to the acts of other contractors employed by the purchaser.

104. A view was expressed that "delay" should not always be the essence of non-performance of contracts of this type. Obligations to perform contract and its breach would give rise to liability not only as provided under the contract but also as dictated by the applicable law.

105. It was suggested that the issue of liability of the contractor for failure in the training of the purchaser's personnel should not be discussed in paragraph (21) of this chapter, but should rather be discussed in the chapter entitled "Training".

106. It was noted that in cases of partial take-over there may be several guarantee periods in respect of different parts of the works. It was agreed that it was not appropriate to indicate in the legal guide any specific guarantee period (even in the form of an example) and that parties should be advised to determine the length of such a period in the light of the relevant factors mentioned in the guide. According to one view, the legal guide should state that the parties should take into consideration usages in different industries.

107. With respect to a manufacturer's guarantee, the view was expressed that assignment of such a guarantee to the purchaser may not be permitted by the applicable law. A suggestion was made that one way of overcoming this difficulty might be for the contractor to act as the agent of the purchaser in procuring the equipment from the manufacturer.

108. The view was expressed that the legal guide should stress that the parties should take into account the rules of the applicable law in determining the remedies to be available in case of a failure to perform. It was noted that enforcing performance by the contractor was often not available or practicable as a legal remedy. However, it was desirable that in the case of a failure to perform by the contractor the purchaser should, in the first instance, request him to effect proper performance.

109. With respect to the suggested obligation of the contractor not to take from the site defective equipment at least partially paid for by the purchaser without his approval, it was pointed out that in some cases defective equipment had to be repaired in the contractor's country and removal should be possible if a financial guarantee was procured.

110. Under one view, the purchaser should bear certain consequences if he inspects equipment during manufacture and does not object to their quality. It was suggested that, for example, he should be considered to

have accepted the quality if defects were discoverable by the inspection. Under another view, however, during manufacture the purchaser only participates in tests carried out by the contractor, and if the defects are discoverable they should be discovered and cured by the contractor. It was suggested that the legal guide should suggest that when the purchaser does not discover the defects, he should not lose any of his rights arising from such defects. If the purchaser discovers defects, he should be obliged to notify them to the contractor.

111. A suggestion was made that the distinction between defects which entitle the purchaser not to take over the works and other defects should be elaborated. It was suggested that some defects causing a reduction of the production capacity of the works to a specified percentage should not be considered as serious defects. It was generally agreed that the parties should be advised to specify as precisely as possible the situations where the purchaser was not obliged to take over the works.

112. It was suggested that in cases of non-performance for whatever reason, the parties should have opportunity through a process of constant interaction to agree on mutually acceptable alternatives before resorting to remedies such as cure of defects, price reduction or termination. Further, it was suggested that the guide should provide for a clear analysis of remedies available in case of non-performance due to defects discovered during the manufacture or construction, during the guarantee period and during the post-guarantee period.

113. A view was expressed that price reduction may not be appropriate as a remedy as it might give rise to bargaining between the parties. Under another view, however, price reduction was frequently used in works contracts as a remedy and, in some situations, might be the only remedy which was practicable. The question was raised whether, instead of the term "value", another term might be used in connection with the calculation of the price reduction. It was also suggested that the relationship between price reduction and damages should be clarified.

114. It was suggested that the remedies available in respect of defects discovered and notified after the take-over but during the guarantee period might be more limited in comparison with the remedies available in respect of defects discovered at taking over, e.g., price reduction may be excluded.

115. It was suggested that the time within which the purchaser might exercise the remedies of cure of defects by employing a new contractor, price reduction and termination should be clarified. A reasonable opportunity should be given to the contractor to cure the defects, and if he fails to do so the purchaser should notify him of his choice of remedy. It was suggested that paragraph (63) should be redrafted to make clearer the situation when the purchaser was entitled to change a choice of the remedy.

116. A view was expressed that in some cases it was important to the purchaser for defects to be cured immediately. It was suggested that in such cases the purchaser should be able to hire a new contractor immediately to cure the defects, at the expense of the first contractor, rather than being required to notify the first contractor of the defects and to give him an opportunity to cure them. It was also suggested that the purchaser should be permitted in some cases to cure the defects himself.

117. A discussion was held concerning the remedy of permitting the purchaser to hire a new contractor to cure defects caused by the first contractor. It was suggested that the chapter should alert the purchaser to the fact that under some performance bonds the hiring of a new contractor was subject to the consent of the surety.

118. It was agreed that the costs of hiring a new contractor should be borne by the first contractor. However, different views were expressed concerning whether the efforts by the new contractor to cure the defects should be at the risk of the first contractor. According to one view, the first contractor should not bear this risk. Another view suggested that it might be appropriate for the first contractor to bear this risk in the case of a separate contract dealing with a part of the works (e.g., a contract for electrical or mechanical work), but it would not be appropriate in a contract for the construction of the entire works. A third view suggested that the first contractor should bear the risk of all defects in work performed by him unless he proved that the defect was caused by the new contractor. In such a case, the first contractor and the new contractor should each be responsible for his own defects. It was also suggested that the original contractor and the contractor engaged by the purchaser could be jointly liable as regards defects. According to another view this should only be the case where the defects could not be attributable to either of these contractors. A suggestion was made that the chapter should provide various alternatives with respect to this question, including the bearing of risk by the first contractor, but that in connection with the latter alternative reference should be made to contract forms or general conditions which contain that alternative.

119. Reference was made to the possibility mentioned in paragraph (72) that the liability of the contractor for the purchaser's lost profit might be limited to cases in which the contractor intentionally caused a delay, or performed with defects intentionally or with knowledge that defects would result. A view was expressed that such a limitation on the recovery of lost profits by the purchaser was excessive. A suggestion was made that the chapter present, as alternatives, this limitation together with the ability of the purchaser to recover his lost profits fully. Another suggestion was made that the section on damages for failure to perform be removed from the chapter and included in the chapter entitled "Damages".

120. With respect to the obligation of the purchaser to pay interest when he fails to make a payment on the due date, a view was expressed that the purchaser should be obligated to pay interest even when his failure to pay on time was due to an exempting impediment. A different view was also expressed in this regard. As to the interest rate to be applied, one view suggested that the contract merely refer to applicable law, while another view suggested that the contract provide a specific rate or formula for determining the rate. A suggestion was made that the rate or formula should be one used in the particular industry involved. A further suggestion was that the interest rate should be related to the contractor's borrowing rate.

121. Reference was made to the obligations of the purchaser to notify the contractor of defects discovered during the guarantee period. Differing opinions were expressed as to the consequence of a failure by the purchaser to give such notice in time. According to one view, in the event of such a failure the purchaser should lose his rights with respect to the contractor's defective performance, while, according to another view, he should not lose his rights, but he should be obligated to compensate the contractor for losses caused by a failure to give timely notice. It was suggested that the chapter should present both these approaches as alternatives. It was also suggested, however, that the purchaser should lose his rights if he does not give notice within the guarantee period. With respect to whether the consequences of a failure to notify in time should arise if the purchaser does not dispatch a notice in time, or whether they should arise if the notice is not received by the contractor in time, it was suggested that both these approaches should be presented in the chapter as alternatives.

122. It was agreed that the summary of the chapter should be redrafted so as to correspond with changes in the text. A suggestion was made that the summary refer to two types of situations which might be considered delay, i.e. performance which occurred late, and performance which had not occurred at all.

123. It was agreed that the illustrative provisions should be redrafted so as to correspond with changes in the text. It was suggested that, in the illustrative provision in footnote 1, it should be made clear that the contractor's guarantee covered only equipment, materials and supplies which were incorporated in the works. A suggestion was made that the illustrative provision in footnote 2 make it clear that it was not intended to be an exhaustive list of exclusions from the guarantee, but merely illustrations, and that the parties could choose such of those exclusions mentioned which were useful or appropriate to their contract.

124. A suggestion was made for the addition to the illustrative provision in footnote 3 of an optional provision for a maximum guarantee period. A suggestion was also made for the addition of an optional provision under which the guarantee period would be suspended when the works were incapable of operation and resumed when they became capable of operation. It was also suggested that it be made clear that when a

part of the works was repaired or replaced, a new guarantee period would cover only that part, and not the entire works.

125. Various suggestions were made concerning the desirability of including in the illustrative provision in footnote 10 specific figures as to the percentage of price reduction to which the purchaser would be entitled. One suggestion was that the figures should be omitted, as they might not be appropriate in some contracts and could mislead readers of the legal guide. Another suggestion was that the figures should be placed in square brackets. It was agreed that the secretariat should consider the best way to deal with this question, including the possibility of a text or verbal description of different methods of price reduction, such as a progressive, degressive or proportional reduction. It was suggested that the illustrative provision should note that this mechanism for determining a price reduction was useful only for turn-key contracts.

126. Various other suggestions were made for improving the drafting of the illustrative provisions.

#### DAMAGES

127. The Working Group held an exchange of general observations on the draft chapter on damages (A/CN.9/WG.5/WP.11/Add.4). The view was expressed that there was a need to emphasize the limitations on the contractor's liability which existed in practice in relation to works contracts. Thus the liabilities of the contractor under quality guarantees, his liabilities covered by various forms of insurance and his extra-contractual liabilities were all, in practice, subject to certain forms of limitation. Under another view, however, the chapter should stress that the purchaser was likely to suffer serious loss by failure of performance on the part of the contractor, and the legal guide should indicate that he should be compensated for such losses. It was observed that one approach to resolve that difference of views was to distinguish between direct losses (in respect of which liability should in principle be unlimited) and indirect losses (in respect of which the parties should be advised to provide in their contract for a proper limitation of liability). It was also suggested that the parties should consider an overall limitation of liability on part of both parties. Discussion continued and it was decided to revert to this issue at the next session of the Working Group.

128. There was general agreement that it would be advantageous to include in the chapter an introductory section which would mention methods other than damages of compensating the purchaser for loss (e.g., insurance, performance bonds and guarantees, liquidated damages) and would indicate the interrelationship between these various methods. Thereafter, the chapter could deal with various possible approaches to settling the question of recovery of damages and indicate the relative advantages and disadvantages of each approach, as well as the impact of the various approaches on other methods of obtaining compensation (e.g., a

restricted liability for damages may necessitate the taking out of insurance with a wide coverage). The parties should also be advised to consider the applicable law relating to damages and the extent to which it might be desirable or possible to modify the impact of such law by agreement. The chapter would, therefore, indicate the risks the purchaser might bear under different contractual arrangements and the techniques which he might adopt to cover such risks.

129. The view was expressed that the terminology used in the chapter should be clarified and, in particular, that attention should be paid to the terms "liability" and "responsibility" and to the distinction between "compensation" and "damages". It was noted that the distinction between "compensation" and "damages" resulted in certain sections of the chapter (e.g., the section relating to mitigation of losses) not applying to cases where compensation and not damages was payable, and that this might not always be advisable.

130. A view was expressed that no suggestions should be made in the guide that the parties should provide for a limitation of liability of the contractor to compensate any loss caused by him to the purchaser.

131. It was agreed that the Working Group should, at its next session, continue its deliberations on the basis of the draft chapter, which would then be examined in detail.

#### OTHER BUSINESS AND FUTURE WORK

132. There was general agreement in the Working Group that the work on the legal guide should proceed as quickly as possible and that two sessions of the Working Group should, whenever feasible, be held every year in order to expedite the work. The Secretary of the Commission informed the Working Group that, subject to approval by the Commission, the sixth session of the Working Group could be held at Vienna from 10 to 21 September 1984 and the seventh session in New York in February 1985.

133. The Working Group was informed that, due to the limited capacity of the Arabic Translation Service at Vienna, it had been impossible to provide the Arabic version of documents for the present session of the Working Group, but that all efforts would be made to provide Arabic translation of documents starting from the next session. The Working Group welcomed this information and agreed that the availability of the Arabic version of documents would be highly desirable, particularly in the light of the objective sought in the preparation of the legal guide.

134. At the close of the session, the Working Group expressed its appreciation to its Chairman, Leif Sevon, for his assistance and guidance. Appreciation was also expressed on behalf of the Group of 77 which recognized the value of the Chairman's services from the point of view of developing countries.

**B. Working papers submitted to the Working Group on the New International Economic Order at its fifth session**

Draft legal guide on drawing up international contracts for construction of industrial works: draft chapters: report of the Secretary-General (A/CN.9/WG.V/WP.11 and Add. 1 to 9)

CONTENTS

	<i>Paragraphs</i>
[A/CN.9/WG.V/WP.11]	

INTRODUCTION .....	1-5
--------------------	-----

[A/CN.9/WG.V/WP.11/Add.1]	
---------------------------	--

**CHAPTER XIII. INSPECTION AND TESTS**

SUMMARY

A. General remarks .....	1-9
B. Inspection and tests during production .....	10-24
1. Function and effects .....	10-11
2. Access for purchaser's representatives to places of production, and facilities to be provided by contractor .....	12-14
3. Time for tests and prior notification .....	15-17
4. Additional or modified test requirements .....	18-19
5. Unsuccessful tests .....	20
6. Test reports and certificates .....	21-23
7. Costs .....	24
C. Inspection of shipments relating to payments and passing of risk .....	25-26
D. Inspection and tests during building and erection .....	27-31
E. Inspection and tests upon completion .....	32-46
1. Types of tests .....	32-33
2. Mechanical completion tests .....	34-38
3. Performance tests .....	39-46

[A/CN.9/WG.V/WP.11/Add.3]	
---------------------------	--

**CHAPTER XXX. FAILURE TO PERFORM**

SUMMARY

A. General remarks .....	1-5
B. Determination of failure to perform .....	6-18
1. Determination of delay .....	6-9
2. Determination of defective construction .....	10-18
C. Quality guarantee .....	19-33
1. Defects covered by guarantee .....	19-26
2. Guarantee period .....	27-32
(a) Length of guarantee period .....	28
(b) Commencement of guarantee period .....	29-31
(c) Extension of guarantee period .....	32
3. Manufacturer's guarantee .....	33
D. Remedies for failure to perform .....	34-77
1. Purchaser's remedies .....	34-73
(a) Delay in construction .....	34-38
(i) Delay before scheduled date for completion .....	36-37
a. Delay before commencement of construction .....	36
b. Delay after commencement of construction .....	37
(ii) Delay after scheduled date for completion .....	38

	Paragraphs
(b) Defective construction .....	39-69
(i) Defects discovered during construction .....	41-49
(ii) Defects discovered during take-over or notified during guarantee period .....	50-51
a. Refusal to take over .....	52-53
i. Requiring performance without defects .....	54
ii. Termination of contract .....	55
b. Remedies in respect of defects in works taken over .....	56-69
i. Remedies at time of discovery or notification of defects in works taken over .....	57-69
aa. Cure of defects by contractor .....	57-58
bb. Price reduction .....	59-61
ii. Remedies after expiration of time given to contractor for curing defects in works taken over .....	62-69
aa. Cure of defects by employing new contractor ....	64-67
bb. Price reduction .....	68
cc. Termination of contract .....	69
(c) Damages for failure to perform .....	70-72
(d) Delay in payment by contractor .....	73
2. Contractor's remedies for purchaser's failure to pay .....	74-77
E. Purchaser's remedies in respect of defects not covered by contractor's liability	78
F. Procedure for claims in respect of defects notified during guarantee period ...	79-82
G. Defects notified after expiration of guarantee period .....	83

## [A/CN.9/WG.V/WP.11/Add.4]

## CHAPTER XXXI. DAMAGES

## SUMMARY

A. General remarks .....	1-3
B. Liability for damages .....	4-10
C. Extent of damages .....	11-15
1. Mitigation of losses .....	11
2. Reduction of scope or amount of recovery .....	12-15
(a) Unforeseeable losses .....	12-13
(b) Indirect or consequential losses .....	14
(c) Damages limited by amount .....	15
D. Personal injury and damage to property of third persons.....	16-18

## [A/CN.9/WG.V/WP.11/Add.5]

## CHAPTER XXXIII. LIQUIDATED DAMAGES AND PENALTY CLAUSES

## SUMMARY

A. General remarks .....	1-4
B. Liquidated damages and penalty clauses and applicable law .....	5-8
C. Increasing effectiveness of liquidated damages or penalty clauses .....	9-11
D. Ceiling on recovery of agreed sum .....	12-14
E. Obtaining agreed sum .....	15
F. Liquidated damages and penalty clauses for delay .....	16-20
G. Termination of contract and liquidated damages and penalty clauses .....	21

## [A/CN.9/WG.V/WP.11/Add.6]

## CHAPTER XXXV. VARIATION CLAUSES

## SUMMARY

A. General remarks .....	1-6
--------------------------	-----

	Paragraphs
B. Variations ordered by purchaser .....	7-22
1. Scope of variations .....	8-9
2. Right of contractor to object to variations .....	10-14
3. Procedure .....	15-22
(a) Variations to be in writing .....	16
(b) Response by contractor and ensuing procedure .....	17-22
(i) Notification by contractor .....	17
(ii) Failure of contractor to notify .....	18
(iii) Contractor's concurrence with variation but not of its effects	19
(iv) Contractor's objection to or proposal to alter variation .....	20
(v) Performance of variation pending settlement of dispute .....	21-22
C. Variations proposed by contractor .....	23-24
D. Role of engineer .....	25-26
E. Guidelines for effect of variations on contract price .....	27-32

[A/CN.9/WG.V/WP.11/Add.7]

#### CHAPTER XXXVI. ASSIGNMENT

##### SUMMARY

A. General remarks .....	1-2
B. Assignment of contract .....	3
C. Assignment of specific contractual rights and obligations .....	4-7
D. Provisions to safeguard interests of parties.....	8-12
1. Preservation of rights of non-assigning party .....	9-10
2. Consent to be in writing .....	11
3. Notification of assignment .....	12
E. Consequences of improper assignment .....	13

[A/CN.9/WG.V/WP.11/Add.8]

#### CHAPTER XXXVII. SUSPENSION OF CONSTRUCTION

##### SUMMARY

A. General remarks .....	1-5
B. Suspension by purchaser .....	6-15
1. Suspension by purchaser for convenience .....	6-7
2. Suspension on specified grounds .....	8
3. Some suggestions on contents of suspension clause .....	9-15
C. Suspension by contractor .....	16-20

[A/CN.9/WG.V/WP.11/Add.9]

#### FORMAT OF THE LEGAL GUIDE

INTRODUCTION .....	1-2
I. CHAPTER SUMMARIES .....	3-7
II. CHECK-LIST .....	8-9
III. TABLE OF CONTENTS AT BEGINNING OF EACH CHAPTER.....	10
IV. POSSIBLE ARRANGEMENTS .....	11
V. ILLUSTRATIVE AND MODEL PROVISIONS .....	12-15
VI. SPACE FOR NOTES BY USERS OF GUIDE .....	16

[A/CN.9/WG.V/WP.11]

### Introduction

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.<sup>1</sup> 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 contracts for the supply and construction of large industrial works and suggest possible solutions to assist parties, in particular from developing countries, in their negotiations.<sup>2</sup>

2. After having completed at its second<sup>3</sup> and third<sup>4</sup> sessions the consideration of a study submitted by the secretariat of clauses used in contracts for the supply and construction of large industrial works,<sup>5</sup> the Working Group requested the secretariat to prepare a few sample chapters and an outline of the structure of the guide.<sup>6</sup> In compliance with this request the secretariat submitted to the fourth session of the Working Group a draft outline of the structure of the legal guide and some sample draft chapters.

3. At its fourth session the Working Group discussed the draft outline of the structure of the guide and draft chapters on "Choice of contract type", "Exemptions" and "Hardship clauses"<sup>7</sup> while the discussion on the chapter "Termination"<sup>8</sup> was postponed to the fifth session. There was general agreement that the draft outline of the structure of the guide was on the whole acceptable. It was generally recognized that, as the work progressed, some rearrangement of chapters might become necessary and the secretariat was given the discretion to do so, if needed. While the draft chapters were on the whole considered to be acceptable, it was suggested that certain portions of the chapters needed rearrangement or redrafting in the light of the discussion. There was general agreement in the Working Group on the need to prepare the guide expeditiously.<sup>9</sup> These conclusions of the Working Group were approved by the Commission at its sixteenth session.<sup>10</sup>

<sup>1</sup>A/CN.9/198, para. 92 (*Yearbook 1981*, part two, IV, A).

<sup>2</sup>Report 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).

<sup>3</sup>A/CN.9/198 (*Yearbook 1981*, part two, IV, A).

<sup>4</sup>A/CN.9/217 (*Yearbook 1982*, part two, IV, A).

<sup>5</sup>A/CN.9/WG.V/WP.4 and Add. 1-8 (*Yearbook 1981*, part two, IV, B, 1), A/CN.9/WG.V/WP.7 and Add. 1-6 (*Yearbook 1982*, part two, IV, A).

<sup>6</sup>A/CN.9/217, paras. 132-133 (*Yearbook 1981*, part two, IV, A).

<sup>7</sup>A/CN.9/WG.V/WP.9 and Add. 1-4 (*Yearbook 1983*, part two, IV, B).

<sup>8</sup>A/CN.9/WG.V/WP.9/Add.5 (*Yearbook 1983*, part two, IV, B).

<sup>9</sup>A/CN.9/234 (*Yearbook 1983*, part two, IV, A).

<sup>10</sup>Report of the United Nations Commission on International Trade Law on the work of its sixteenth session, *Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17* (A/38/17), paras. 90-92 (*Yearbook 1983*, part one, A).

4. With regard to the question of title to be given to the legal guide, the sample chapters submitted to the fourth session were entitled "Legal Guide on drawing up contracts for construction of industrial works". The Working Group agreed that the term "international" should be added to in the title to qualify the term "contracts" and that the omission of the term "large" originally used in the title in connection with the term "industrial works" was justified. However, the issue whether the term "contracts for construction of industrial works" or the term "contracts for supply and construction of industrial works" should be used for the title remains open and it may be advisable to settle it in the future after the definition of the term "construction" has become well-settled as the preparation of the guide progresses.

5. The present report contains in its addenda the following draft chapters prepared by the secretariat: "Inspection and tests", Add.1; "Failure to perform: delay", Add.2; "Failure to perform: defective construction", Add.3; "Damages", Add.4; "Liquidated damages and penalty clauses", Add.5; "Variation clauses", Add.6; "Assignment", Add.7 and "Suspension of construction", Add.8 as well as a note on the format of the guide, Add.9.

[A/CN.9/WG.V/WP.11/Add.1]

### Chapter XIII. Inspection and tests

#### Summary

The contract should specify clearly the requirements and procedures for inspection and tests, and their legal effects. Inspection and tests during production, building and erection (paragraphs 2, 3 and 7) should be distinguished from those upon completion.

Provisions on tests during production, building and erection should take into account inspection and tests required under national regulations in the countries where the works are being erected, and where equipment is produced (paragraphs 4-6).

Tests during production should be regarded as a part of the contractor's obligation of quality control. Therefore, an expression by the purchaser of satisfaction with such tests should not release the contractor from the obligation to demonstrate on completion that the works conform to the contract specifications (paragraph 10).

The purchaser's representatives should, to the extent possible, be assured a right of access to places where the plant and its components are produced, so that they can inspect them during production (paragraphs 12-14). The contractor should be obligated to give reasonable advance notice of the performance of tests (paragraphs 15 and 16). The contract should permit the purchaser to modify the tests to be performed by the contractor, or to require the contractor to perform tests not specified in the contract, and should establish who is to bear the

costs of such tests and whether they should entitle the contractor to additional time to perform the contract (paragraphs 18 and 19). Unsuccessful tests should be repeated at the contractor's expense, and without entitling the contractor to additional time to perform the contract (paragraph 20). The contract should contain provisions concerning the issuance, notification, and legal effects of reports and certificates of tests (paragraphs 21-23). The costs of inspection and tests during production should in principle be borne by the contractor (paragraph 24).

The contract should establish procedures concerning inspection and tests during building and erection (paragraphs 27-31).

Inspection and tests to be performed upon completion of the works should include mechanical completion tests (to demonstrate that the works has been properly completed), and performance tests (to determine whether the works meets the performance requirements stipulated in the contract). The contract should clearly set forth the steps to be included in the mechanical completion tests, and the procedures connected therewith (paragraphs 34-36). The contract should permit the purchaser to modify such tests and to require the performance of tests in addition to those specified in the contract (paragraph 37). The contract should establish procedures concerning the conduct of performance tests (paragraphs 39-43), and should establish which party is to bear costs associated with such tests (paragraph 44).

\* \* \*

#### A. General remarks

1. It is important for a works contract to specify clearly the requirements and procedures for inspection and tests, and their legal effects. Procedures should be established to ascertain whether the works constructed conform to the contractual requirements. The procedures should relate not only to visual inspection of the works but should also provide for a variety of tests to be performed. The precise nature, scope and timing of the inspection and tests provided for by the contract will, of course, depend upon the nature of the works to be constructed. However, inspection and tests should normally be carried out not only upon completion of the work but throughout the construction process.

2. Inspection and tests during production, building and erection serve a purpose different from those upon completion. This difference should be borne in mind when drafting the corresponding contract provisions.

3. Tests during production, building and erection are not, in principle, conceived to demonstrate that the contractor has met his obligations. Consequently a failure of the purchaser to detect and notify a defect should not deprive him from relying later on such a defect. These tests rather constitute part of the contractor's obligations to construct the works and to observe certain rules on quality control. The purchaser may also wish to satisfy himself that production is proceeding in accordance with the agreed time-schedule.

4. A number of countries, especially those in which industry is highly developed, have issued legal regulations which require that industrial installations and many of their components be inspected and tested by public authorities or private institutions. In some areas, and in particular in the field of nuclear energy, such inspection and tests may also be prescribed at an international level.

5. Such inspection and tests prescribed by national legal regulations which relate primarily to safety, health and environmental standards in principle are applicable irrespective of whether they are provided for in the contract or not. Nevertheless, consideration should be given to them when drafting the contract. This applies first of all to inspection and tests required by national legal regulations at the place where the works is built (see chapter XXXIX, "Applicable law"). In addition, inspection and tests required in the countries where equipment and components are produced should also be considered. Where they apply to the production of equipment and components, the contractor has to provide such inspection and tests independently of any stipulation in the contract. It is, nevertheless, important for the purchaser to take account of them in specifying the contractual requirements for inspection and tests; in fact where certain quality control requirements have to be met under legal requirements in the producer's country, additional contractual provisions on testing such quality requirements may not be necessary, and it may be sufficient for the contractor to show that the inspection and tests required in the country of production have been properly performed.

6. On the other hand, where such inspection and tests are only required immediately prior to operating a plant or certain components, the legal regulations in the contractor's country may not be directly applicable. The purchaser may therefore wish to stipulate that these inspection and tests should also be performed in his own country. Some of the institutions carrying out inspection and tests under national legal regulations in countries with a high degree of industrial development can also perform these services abroad; in cases where a new industry is built up in the purchaser's country it may be preferable, at an initial stage, to have certain inspection and tests carried out by an experienced foreign institution. The necessary arrangements can be made directly between the purchaser and the institution, and in that case the contract should provide that the respective regulations on inspection and tests are to be observed as if they were regulations in the purchaser's country. Alternatively, the contract could provide that the necessary arrangements are to be made by the contractor.

7. In some cases inspection and tests may be required with respect to equipment and materials supplied by the purchaser. The contractor should be required to make such inspection and tests as soon as feasible after such equipment and materials have been supplied to him. The contract should deal with the consequences of the contractor's failure to discover defects (see chapter XXX, "Failure to perform").

8. Particular attention should be paid to specifying inspection and tests upon completion (see section D, below). With respect to tests during production and erection, a more flexible approach might be adopted. These latter tests may be regarded as a part of the contractor's own quality control system, and it may be sufficient for the purchaser to satisfy himself that this quality control system is adequate. Excessive inspection and testing requirements, like other interferences with the contractor's methods of production and work, are likely to increase the cost of the works.

9. However, not all testing requirements need to be specified expressly in the contract documents. A number of technical standards prepared by national or international standardization institutions also specify testing requirements. Consequently, before specifying the testing requirements in the contract documents it should be determined whether the technical standards which are made applicable already contain such requirements. The contract may also provide that certain requirements under national legal regulations of the contractor's country or a third country should be applied.

#### **B. Inspection and tests during production**

##### **1. Function and effects**

10. The contract should expressly state that the performance of tests during production, and an expression of satisfaction by the purchaser's representative during the course of such tests, do not release the contractor from the obligation to demonstrate by tests on completion that the works conform to the contract specifications (see chapter XXX, "Failure to perform").

11. Inspection during the production process may give to the purchaser's personnel an opportunity to acquaint themselves with certain aspects of the plant. If the purchaser wishes to secure this training effect, the contract should specify that the right to attend tests during production is not limited to the purchaser's engineer or other personnel supervising the construction of the plant, but also extends to other persons whom the purchaser may choose (see, however, paragraph 12, below).

##### **2. Access for purchaser's representatives to places of production, and facilities to be provided by contractor**

12. Because of the purchaser's interest in inspecting the plant and its components during production, it is usual for works contracts to provide that the purchaser's representatives should during working hours have access to all places where the plant or its components are produced. Difficulties in applying this principle arise primarily in two areas. One area relates to questions of confidentiality; the contractor may wish to protect the confidential know-how of certain production processes, or he may be under an obligation to preserve such confidentiality either under contractual arrangements with other firms, such as licensors, or under arrangements with certain clients, especially when he

also performs certain contracts for government authorities in sensitive areas. In such cases the only possibility for according to the purchaser some form of inspection might consist in retaining a specialized engineering firm in the contractor's country. Such a firm could provide the necessary guarantees of confidentiality.

13. The second area relates to subcontractors and suppliers. Not infrequently, the contractor's subcontractors and suppliers, in particular where they are specialists in high technology products, refuse to allow access to their premises to the purchaser. As subcontractors have no contractual relationship with the purchaser, the right of access may be provided through the main contract between the purchaser and the contractor, by requiring the contractor to include such a right of access in his contracts with subcontractors.

14. Where the purchaser has a right of access at least to the contractor's premises, the contract should also specify what facilities are to be provided to the purchaser's representatives to enable them to carry out their inspection. Such facilities may consist in particular of office space, and in the supply of samples for independent testing by the purchaser or institutions retained by him.

##### **3. Time for tests and prior notification**

15. Production tests form part of the contractor's manufacturing programme. Consequently, it is usual for the contractor to fix the times for these tests. However, it is rare for these times to be fixed in the schedule of the contract itself, except possibly in respect of some critical major items.

16. The contract should specify that the purchaser has the right to delegate a representative to observe the tests and their results. In order to enable the purchaser to exercise this right, the contractor should be obligated to advise him in advance of the time when certain tests will be performed. The contract should provide a reasonable period of notice to be given to the purchaser. In developed countries this period of notice normally is relatively short, i.e. a week or two. Where the purchaser is in a distant developing country, the period of notice might have to be longer, to allow the purchaser to make the necessary travel, visa and other arrangements for his representatives to attend the tests.

17. In the case of certain important parts of equipment, it might be advisable to allow the contractor to proceed with the work only after these parts have been inspected by the purchaser's representatives, subject, of course, to arrangements protecting the contractor's interests in case the purchaser unreasonably delays inspection.

##### **4. Additional or modified test requirements**

18. It may not be possible to set out in the contract all production tests required. Certain tests not specified in the contract may, for a variety of reasons (such as

technological developments subsequent to the conclusion of the contract), become necessary during the production process. The purchaser should therefore reserve for himself the right to require tests not specified in the contract, or require modifications to the test procedures. The contractor should be obliged to perform such additional or modified tests, but he should have the right to disclaim liability for damage to the equipment caused by such tests, where such tests create a risk for the equipment.

19. The contract should provide that the costs of such additional or modified tests, and whether they should give a right to the contractor to additional time to perform the contract, should be determined by reference to standard practice in the industry. The contractor should be paid his additional costs and be granted additional time only if such tests are not standard practice in the industry. When determining what is standard practice, account should also be taken of the particular conditions under which the plant will be operated in the purchaser's country (e.g. humid conditions).

#### *5. Unsuccessful tests*

20. If the tests have been unsuccessful they should be repeated. In structuring his time schedule the contractor should take into account the possibility or likelihood of having to repeat the tests. The contractor should not be granted additional time to perform the contract if unsuccessful tests have to be repeated, and he should be required to bear all costs of unsuccessful tests. For the purchaser's remedies in cases of defects discovered during production, see chapter XXX, "Failure to perform".

#### *6. Test reports and certificates*

21. The contract should require all tests to be recorded, and such records should include the procedures which were followed and the quantified test results. When a test has been attended by representatives of the purchaser, the test report should also be signed by these representatives. However, such signature should constitute only an acknowledgement that the test procedures and readings have been correctly recorded.

22. When a test is not attended by representatives of the purchaser, the contractor should be obligated to transmit the test reports immediately to the purchaser. If the purchaser has been given proper notice of the tests, the procedures and results recorded in the reports should in principle be deemed to be correct.

23. When inspection or tests are performed by an independent testing institution, the institution normally issues a certificate or a similar document. The contract should obligate the contractor to transmit such certificates to the purchaser either immediately after they have been issued or as part of the documentation submitted to the purchaser prior to take-over of the plant.

#### *7. Costs*

24. The costs of inspection and tests during production should in principle be borne by the contractor, except for the costs of the purchaser's representatives. The costs to be borne by the contractor should also include labour, materials, electricity, fuel and other items necessary for the proper conduct of such tests, as well as the costs of such tests performed by subcontractors.

#### *C. Inspection of shipments relating to payments and passing of risk*

25. There are certain inspection and tests which have a function in connection with payments and the passing of risk. This applies in particular to inspection prior to shipment. When certain payments are made upon shipment of the equipment, or where the risk in respect of such equipment passes at this stage, inspection is sometimes carried out by the purchaser's representatives. However, it is normally more economical for the inspection to be carried out by a specialized firm at the place of production or shipment.

26. Inspection of shipped equipment may also be made upon arrival of the shipment at the site. Again, this is done primarily for payment purposes. Such inspection may also be required in order to preserve possible claims against the carrier in case the equipment has been damaged during transport. The costs of such inspection and tests should in principle be borne in the same manner as the costs of inspection and tests during production.

#### *D. Inspection and tests during building and erection*

27. The discussion concerning inspection and tests during production also applies to a large extent to inspection and tests during building and erection on site. However, some additional aspects should be considered.

28. During building and erection, the purchaser will usually have appointed a representative to observe or supervise the work. Normally the problems of confidentiality to which reference has been made above (see paragraph 12) do not occur at this stage, and the period of notice to be given to the purchaser can be considerably shorter.

29. Even where the purchaser's representative regularly is present on the site, the contractor should be obligated to keep complete records of his work, and to produce them to the purchaser's representative upon request.

30. In addition, the purchaser or his representative should have the right during building and erection to inspect all work which cannot be inspected later. This applies in particular to work which is being covered up as building progresses.

31. When the works are to be erected not by the contractor but by the purchaser, and the contractor is to provide only assistance and supervision of erection, the contractor should be responsible for specifying and performing inspection and tests of the works. Here, too, the contract should be obligated to prepare and keep records of such inspection and tests.

#### *E. Inspection and tests upon completion*

##### *1. Types of tests*

32. The contract should provide for procedures by which the works are inspected and tested by the purchaser, so that the contractor can demonstrate, and the purchaser can satisfy himself before take-over, that the works have been constructed in accordance with the contract. These inspection and tests in all cases concern the proper mechanical operation of the works. Such tests are referred to herein as mechanical completion tests (see also chapter XIV, "Completion, take-over and acceptance of works").

33. For certain types of works, and in particular in the case of processing plants, the contract may provide for tests to be conducted to determine whether the works meet the performance requirements stipulated in the contract. In this Guide such tests are referred to as performance tests. The latter type of tests may be performed together with the mechanical completion tests before the purchaser takes over the works.

##### *2. Mechanical completion tests*

34. Since the objective of mechanical completion tests is to demonstrate that the works has been properly completed and that the component parts are in proper mechanical order, mechanical completion tests should be commenced only after construction has been completed and the contractor has notified the purchaser of this completion, and has requested that the purchaser initiate procedures to take over the works.

35. The mechanical completion tests consist of a variety of steps, and often may require a considerable amount of time. It is desirable that they be set out clearly in the contract. These tests should include such of the following as are appropriate in a particular contract:

- Visual inspection of the works and its components;
- Checking and calibration of instruments;
- Safety tests;
- Dry runs;
- Mechanical operation of the works and its various components;
- Inspection of the technical documentation which the contractor has to supply for operation and maintenance of the works, (e.g. as-built plans, reports and certificates, and list of spare parts);
- Inspection of the stock of spare parts and materials which the contractor may have to deliver with the works.

36. During mechanical completion tests, the contractor should normally remain responsible for the works (see chapter XIV, "Completion, take-over and acceptance of works"). Consequently, the tests should be conducted by the contractor, but in the presence of and in co-ordination with the purchaser or his engineer. The purchaser may undertake a number of responsibilities, such as supplying raw materials and utilities for consumption in the works during the tests. Moreover, where the works are connected to other installations of the purchaser, e.g. a power plant which feeds the purchaser's installations or transmission lines, the purchaser may undertake additional responsibilities for specifying and supervising those aspects of the mechanical completion tests which relate to these other installations. All these aspects should be clearly specified in the contract.

37. As in the case of tests during production, the purchaser may require additional or modified testing procedures, and the principles discussed above with respect to the costs of such procedures, and their effect on the time for the contractor's performance of the contract (see paragraphs 18-19, above) also apply here, as do the principles concerning repetition of tests (see paragraph 20, above). Thus, except as indicated in paragraph 19, above, the costs of the tests should be borne by the contractor. However, the purchaser should normally bear the costs of raw materials, utilities and fuel which he is obligated to supply, as well as the costs of his own personnel.

38. Particular problems may arise when the tests are delayed for causes not attributable to the contractor. As the tests are a prerequisite for the take-over of the works by the purchaser, and thereby affect such issues as payments to the contractor and acceptance of the works by the purchaser (see chapter XIV, "Completion, take-over and acceptance of works"), it is in the contractor's interest that take-over and acceptance not be held up by a delay in the tests. A provision may be included in the contract to the effect that if a delay exceeds a certain period of time, all those tests which can be performed should be carried out; others may be simulated.

##### *3. Performance tests*

39. Performance tests are of particular importance in works contracts. Their purpose is to show that the works meets the performance standards specified in the contract, not only with respect to the output and its qualities, but also for a number of other parameters, such as consumption of feedstock or other materials and energy, as well as with respect to the performance of the works under a variety of conditions. In view of the importance of these tests, the procedures to be followed should be described carefully in the contract documents. But, because of the variations which have to be allowed for, such description is particularly difficult.

40. The document describing performance test procedures should state the test procedures for the operation of the works as contemplated at the time when the contract is entered into. It should state the duration of the tests, the criteria for performance, the methods of measurement and analysis, the tolerances, and the number of times unsuccessful tests should be repeated.

41. However, it is not sufficient to specify the details for the performance tests in those cases in which the works operates as specified in the contract. In fact, it is not infrequent that, due to variations in the course of design and construction of the works, and due to differences in feedstock, materials and energy supply, the parameters for the performance of the works as finally constructed differ from those specified originally. For example, during the course of construction of the plant the purchaser may decide on a different source for raw materials and feedstock, or his own raw materials and feedstock may have characteristics different from those originally considered. Such differences obviously affect the performance and the output of the works, and the performance tests schedule, to the extent possible, should provide for adjustments in those cases.

42. For a number of reasons, it may occur that the tests do not proceed as scheduled. This may be due to defects in the works itself, in its design or in the technology used; it may be due to defects in design or construction of other parts of the works which have not been supplied by the contractor; it may be due to the feedstock, material or energy not conforming to contract specifications; or it may be due to differences in the conditions under which the works is operating, such as outside temperature or humidity. For these and similar reasons, the test procedures themselves may have to be modified.

43. Where such situations lead to short interruptions (e.g. where conditions of extreme humidity require a postponement of the tests), these interruptions should not normally extend the duration of the performance tests unless these tests and the process of the works make uninterrupted performance an absolute prerequisite. Where these situations lead to a longer interruption of the tests, the contract should provide for the duration of the tests to be adjusted accordingly or for all or part of the tests to be repeated. Such prolongation or repetition should normally be provided for irrespective of the cause of the interruption. However, this cause may be taken into account when dealing with the costs of the ensuing prolongation or repetition; thus the contractor should bear the costs if the cause is attributable to him, and otherwise should be reimbursed his costs by the purchaser.

44. With respect to other costs, their allocation should also generally depend on who has caused them. Accordingly, costs for corrections and adjustments which the contractor wishes to make before the performance tests are conducted should in principle be borne by the contractor, unless he shows that the need for such corrections or adjustments is due to some cause attributable to the purchaser.

45. The test procedures, readings and results should normally be recorded and evaluated jointly by the parties and form the subject of test reports. Any differences concerning the readings or the evaluation of the tests should be reflected in the report. In case of such differences, the contract should provide that either party may call immediately upon a neutral expert to make the necessary assessment of the facts.

46. If the contract is a product-in-hand contract (see chapter II, "Choice of contract type"), the testing procedures must be designed so as to reflect the nature of the obligations particular to this type of contract. The performance guarantees by the contractor in these contracts relate not only to the technical performance of the works, but also to the success of the training he is obligated to provide. As this latter aspect is determined primarily not by technical but by human capacities, appropriate test procedures should be specified (see chapter XXIII, "Training").

[A/CN.9/WG.V/WP.11/Add.3]

### Chapter XXX. Failure to perform<sup>a</sup>

#### *Summary*

Failure to perform covers two types of situations, i.e. delay and defective performance. Delay applies to situations where a party fails to perform his obligations under the contract in time. Defective performance applies to cases where the performance is effected with defects (paragraph 2).

In determining whether there is delay in the construction of the works on the part of the contractor it is useful for the contract to provide for a time-schedule and to indicate which periods for performance under the time-schedule are to be obligatory (paragraphs 6-8). The determination of defects should depend upon the quality of the work required by the contract, and upon the type of contract (paragraphs 10-18).

It is advisable to agree upon a quality guarantee (paragraphs 19-23). In principle, the contractor should be responsible for all defects discovered and notified during the guarantee period. It may be reasonable, however, to exclude certain defects from the scope of guarantee (paragraphs 19-26). The guarantee period should be long enough to enable discovery of all potential defects in the works (paragraphs 28-32). Its length should depend upon the nature of the works and the extent and character of the contractor's participation in the construction.

<sup>a</sup>It had originally been decided to divide chapter XXX into parts A "Failure to perform: delay" and B "Failure to perform: defective construction". As noted in document A/CN.9/WG.V/WP.11/Add.2 it was subsequently found preferable to deal with delay and defective construction in one chapter entitled "Failure to perform". That chapter (chapter XXX) was contained in addendum 3.

The remedies for delay to which the purchaser should be entitled may depend on whether the delay occurs before or after the construction commences, or after the scheduled date for completion. These remedies should include requiring performance by the contractor, termination, or completion of the works at the expense and risk of the original contractor. In requiring performance, the contractor should be given a reasonable or specified time to perform. If the contractor still fails to perform within the period of time, the purchaser should be entitled to terminate the contract (paragraphs 34-38).

The remedies for defective construction should depend upon the nature of the defects and the time when they are discovered. It is advisable to distinguish between defects discovered during construction of the works, defects discovered during taking over or notified during the guarantee period and defects notified after its expiration (paragraph 39).

During the construction of the works, the purchaser's remedies should in substance be limited to the right to stop defective construction and to claim cure of defects. In some exceptional cases, the purchaser may be entitled even to terminate the contract (paragraphs 41-49).

If serious defects (for example, those which prevent a proper operation of the works) are discovered at the time of taking over, the purchaser should be entitled to refuse to take over the works and he should have rights analogous to those he has when the contractor fails to complete the works in time. The defects which will entitle the purchaser to refuse to take over the works should be defined in the contract. If other defects are discovered or if the purchaser does not exercise his right to refuse to take over the works, the purchaser should be entitled to claim cure of defects by the contractor or an adequate price reduction if the defects are not curable. If the contractor fails to cure defects within a reasonable time or time specified in the contract, the purchaser should be entitled to do so through a new contractor reasonably employed by him at the expense and risk of the contractor, or to claim an adequate price reduction. In some situations the purchaser should be entitled to terminate the contract (paragraphs 50-69). The contractor should not generally be responsible for defects discovered or notified after the expiration of the guarantee period (paragraph 83).

The contractor should be obligated to cure even those defects for which he is not responsible at the expense of the purchaser, if the defects are notified during the guarantee period and the contractor is asked by the purchaser to cure the defects (paragraph 78).

In addition to the above-mentioned remedies, the purchaser may be entitled to damages, liquidated damages or penalties. The parties may wish to limit the liability of the contractor for loss of profits to certain instances of delay and defective performance.

If the purchaser fails to pay the contract price or any portion thereof on the date when it is due, the contractor should be entitled to require payment,

suspend the construction of the works or terminate the contract. In addition, the contractor should be entitled to interest.

The parties should agree upon an appropriate procedure to be followed for claims arising from defects, in order to facilitate a choice of remedy by the purchaser, to accelerate the cure of defects, and to prevent excessive loss being caused to either party (paragraphs 79-82).

\* \* \*

#### A. General remarks

1. Strict adherence to contract terms relating to the performance of obligations is particularly important in works contracts, as the failure to adhere to these terms may have serious consequences. The issues of whether there is a failure of performance and, if so, what are the legal consequences of such failure, are frequently the cause of long and complicated disputes. It is therefore advisable to agree upon clear contractual stipulation relating to these issues.
2. Failure to perform covers two types of situations, i.e. delay and defective performance. Delay applies to situations where a party fails to perform his obligations under the contract in time. In such situations a party will be in delay until he performs at a later stage, or until the contract is terminated. Defective performance applies to situations where the performance is effected with defects.
3. This chapter deals only with the failure to perform the main obligations of the parties, i.e. the contractor's obligation to construct the works and the purchaser's obligation to pay the contract price. As regards the other main obligations of the purchaser, the obligation to take over the works is discussed in chapter XIV, "Completion, take-over and acceptance of works". The failure of the contractor to perform certain obligations after completion of the construction, e.g. to provide management services and technical advisory services and to maintain and repair, are discussed in the chapters dealing with these obligations, i.e. chapter XVIII, "Management services", chapter XIX, "Maintenance and repairs" and chapter XX, "Technical advisory services". In addition to the main obligations the parties have a number of auxiliary obligations (such as to notify certain events) and the legal effects of failures to perform such obligations are discussed in relevant chapters, e.g. chapter XXXII, "Exemptions" and chapter XXXVIII, "Termination".
4. Infringement of a right (in particular a right based on industrial property or other intellectual property) of a third party, which is characterized under some legal systems as a "legal defect" is dealt with in chapter XXII, "Transfer of technology" and chapter XXV, "Transfer of property".
5. The parties should agree in particular upon the defects in the works for which the contractor would be

responsible, the guarantee period for the quality of the works, the procedure for the notification of defects and the purchaser's remedies. The provisions on these issues should be carefully harmonized with the contractual provisions on the scope and quality of the works (see chapter IX, "Scope and quality of works"), on inspection and tests (see chapter XIII, "Inspection and tests"), as well as on completion, take-over and acceptance (see chapter XIV, "Completion, take-over and acceptance of works"). The contractual provisions on passing of risks (see chapter XXIV, "Passing of risks") and damages (see chapter XXXI, "Damages") should also be taken into consideration when drafting the provisions relating to defects.

## B. Determination of failure to perform

### 1. Determination of delay

6. It is advisable for the parties to provide for a time-schedule for the overall progress of construction. The contract should indicate which periods for performance under the time-schedule are to be obligatory. Failure to comply with the obligatory periods as specified in the contract should constitute delay.

7. If the construction involves several contractors, the parties preparing a time-schedule should take into consideration the aspects of the works which required the co-ordination of the contractors. Where co-ordination among several contractors is required for the completion of a particular portion of the works, the time-schedule of the contractors applying to such portion should be made obligatory.

8. Although the time-schedule in a turnkey contract need not be as stringent as when separate contractors are employed, the timely performance of those portions of the works which are considered critical should be obligatory. For example, the purchaser may wish to obligate the contractor to complete a portion of the works at a specified date so that he can operate the completed portion profitably, independently of other uncompleted portions. If the contractor fails to perform in time there may be delay.

9. When the time for performance is postponed due to certain events, e.g. when a contractor fails to perform at the time originally fixed because the construction is varied or suspended, there should be no liability for delay (see chapter XXXV, "Variation clauses" and chapter XXXVII, "Suspension of construction"). There should also be no liability for delay when the failure of a party to perform in time is caused by the other party, e.g. where the performance of the contractor is dependent on the co-operation of the purchaser, and the purchaser fails to co-operate with him.

### 2. Determination of defective construction

10. Defective construction includes both cases where defects are discovered in works which are completed

and cases where, during the construction, it is discovered that there are defects in the equipment, material or plant, or that the contractor is using incorrect methods of construction which would result in defects.

11. The determination of defects in the works for which a contractor should be responsible under a works contract will depend on the nature of the particular contract and the performance due from the contractor under it. The contractor should be responsible only for the failure to perform his obligations in accordance with the terms of the contract. In this connection the extent of the responsibility for the construction assumed by the contractor may be relevant.

12. If the contractor assumes responsibility for the entire design and construction of the works, putting it into operation, and handing over to the purchaser works capable of operation in accordance with the contract (i.e. in a turnkey contract), the works should be considered defective in particular in all cases where the contractor fails to fulfil this obligation. All equipment and services needed for the completion and appropriate operation of the works in accordance with the contract, even if not expressly provided in the contract specifications, should be supplied by the contractor (see chapter II, "Choice of contract type").

13. A different situation may exist regarding the extent of the contractor's responsibility when two or more contractors participate in the construction, and the purchaser is to co-ordinate the construction of the works as a whole. A contractor who is not the supplier of the works design should assume responsibility for the proper functioning of equipment and the quality of materials which he supplies. Such a contractor should not, however, be responsible for the suitability of his supplies for integration within the works, so long as the equipment or materials conform to the contract specifications.

14. Since the existence of defects will be determined by reference to the contractual terms, it is advisable for the contract to stipulate as clearly as possible the standards for performance and functioning of the works to be supplied by the contractor, in particular in respect of the quantity and quality of expected production, and the consumption of power and raw materials (see chapter IX, "Scope and quality of works"). As regards the quality of the works, requirements should be specified in terms of operating capability rather than only design, materials or workmanship. By employing this functional approach, the contractor would be liable for a failure of the equipment or works to obtain this capability without a need for the purchaser to prove that the defects resulted from faulty design, material or workmanship. Even if the purchaser used the separate contracts approach (see chapter II, "Choice of contract type"), it may be necessary or advisable to require a certain operating capability if it is possible to do so with respect to that part of the works to be supplied by the separate contractor.

15. In respect of some supplies, however, this functional approach to the definition of defects may not be possible (for example, in case of supplies of materials to be used for construction). In such cases the responsibility of the contractor should be based upon the lack of conformity with the qualitative features described in the contract. Such qualitative features might include design, workmanship, material and fabrication. This responsibility should, however, be included even if the functional approach is used for the determination of defects (see second sentence of illustrative provision in footnote 1), as some defects may be irrelevant to the capability of the works to operate (e.g. lack of painting in administrative buildings, or low-grade metal used resulting in shortening of service life of the works).

16. The contractor should not be responsible for defects arising from a design or equipment or materials supplied or instructions given by the purchaser for the construction. The parties may, however, agree that the contractor's responsibility in these cases is to be excluded only if the contractor could not have been reasonably expected to discover the defective nature of the design or equipment or materials at the time when they were used by him or of the instructions at the time when they were followed by him, in constructing the works. If the latter approach is adopted the contractor should not be responsible if he discovers these defects in time, informs the purchaser immediately thereof and disclaims his responsibility for them. In such cases the contractor should be entitled to suspend the construction (see chapter XXXVII, "Suspension of construction") relating to the use of the design, equipment or materials or observance of the instructions, until the defects are cured by the purchaser, or until the purchaser notifies his decision that the design, equipment or materials should be used, or that instructions should be followed.

17. During the time when the contractor bears the risk of loss of or damage to equipment or materials or the works, he should be responsible for defects caused by events covered by this risk. The time when the risk passes may depend upon the type of works contract; in most cases the passing of risks occurs at the time of take-over (see paragraph 40, below, and chapter XXIV, "Passing of risks").

18. The complex and long-term nature of the execution of a works contract makes it advantageous to give the purchaser the right to check the quality of the equipment, materials or plant even before taking over the works (i.e. during construction), in order to prevent construction which would result in defective works (see paragraphs 41-49, below).

### C. Quality guarantee

#### I. Defects covered by guarantee

19. All works contracts should include a quality guarantee under which the contractor assumes responsibility for defects discovered and notified before the

expiry of a guarantee period specified in the contract. In principle, the guaranteee should cover all defects for which the contractor would have been responsible if they had been discovered during take-over of the works.<sup>1</sup> The parties may, however, wish to exclude from the guaranteee the following defects.

20. *Defects as result of normal wear and tear:* The parties may wish to exclude from the guaranteee defects which are the result of normal wear and tear, since the purpose of the quality guarantee is not to prolong the normal service life of the works.

21. *Defects caused by faulty use or maintenance:* Guaranteees are usually given subject to the appropriate use and maintenance of the works by the purchaser, and in particular the scrupulous observance of instructions given by the contractor for the operation of the works. On the other hand, the instructions given by the contractor for use and maintenance should be sufficiently detailed, taking into account conditions in the purchaser's country and the training of the personnel who will operate and maintain the works. In addition, defects caused by faulty use or maintenance should not be excluded if the contractor trained the purchaser's personnel and assumed the responsibility for their ability to operate and maintain the works (see chapter XXIII, "Training").

22. *Defects caused by defective design, equipment or material supplied or defective instruction given by purchaser:* The guaranteee should not cover defects which are a result of the defective nature of design, equipment or materials supplied or defective instructions given by the purchaser if the contractor fulfils his obligation to discover and notify their defective nature in time (see paragraph 16, above).

23. *Defects caused by improper repairs or alterations by purchaser or person employed by him:* The quality guaranteee of the contractor should not operate if the quality of the works is changed by an improper repair or alteration carried out without the contractor's consent by the purchaser or by a person employed by him. A dispute may arise later whether defects occurring after the employment of such person are defects for which the contractor is responsible. Accordingly, the purchaser may find it advisable to choose the remedy of curing the defects at the expense and risk of the original contractor (see paragraphs 64-67, below).

24. However, if the purchaser chooses the remedy of curing the defects by a new contractor at the expense and risk of the original contractor defects which may be

<sup>1</sup>Illustrative provision

"The contractor guarantees that at the time of take-over and during the guarantee period, the works will be capable of operation in accordance with the contract, and that all equipment, materials or other supplies used by him in constructing the works will conform with the drawings, specifications, plans and all other terms of the contract, and that all plans, technical data and documents supplied by him are correct and complete. In addition the contractor shall be responsible for any faulty or improper design, production, material or workmanship in the supplies effected by him."

the result of an improper repair by the new contractor should not be excluded from the guarantee.

**25. Defects in respect of which price reduction has been claimed:** If the purchaser is entitled to a price reduction, and claims this remedy, the defects in respect of which the reduction is claimed should be excluded from the guarantee after the time of notification of the choice of such remedy; by choosing this remedy, the purchaser accepts the works with the defects in return for the price reduction.

**26. Defects as result of risk borne by purchaser:** The guarantee should be excluded in respect of defects which are caused by events covered by the risk borne by the purchaser. This exclusion would operate in respect of all defects caused by an accidental event or by a third person for whom the contractor is not responsible after passing of the risk of loss of or damage to equipment, materials, plant or works to the purchaser. However, defects caused by the contractor or a person employed by him even after passing of the risk should of course not be covered by the risk borne by the purchaser, and should not be excluded from the guarantee (see chapter XIV, "Passing of risks").<sup>2</sup>

## 2. Guarantee period

27. The responsibility of the contractor for defects discovered after the take-over of the works by the purchaser should be limited to a specified period of time, i.e. to a guarantee period. While on the one hand the guarantee gives assurances and safeguards to the purchaser in regard to the quality of the work, on the other hand the specified period limits in a reasonable manner the time during which the contractor is responsible for the defects.

### (a) Length of guarantee period

28. Several factors may be relevant in determining what length of time would be reasonable for the guarantee period, such as the extent and character of the contractor's participation in the construction (in

<sup>2</sup>Illustrative provision

"The guarantee shall not cover defects:

"(a) arising from normal wear and tear;

"(b) arising from the purchaser's faulty maintenance or from an alteration carried out by the purchaser or another person employed by him, without the contractor's consent in writing;

"(c) caused by the defective nature of design, equipment, or materials supplied, or instructions given, by the purchaser, if the contractor fulfils his obligation to discover and notify their defective nature in time;

"(d) caused by an improper repair by the purchaser or by a person employed by him; however, if the contractor is required to cure a defect, and fails to cure it within a reasonable time, and the purchaser employs a third person to cure the defects at the expense and risk of the contractor, the guarantee shall cover defects in the work executed by such third person;

"(e) for which a price reduction has been claimed by the purchaser; or

"(f) caused by an event covered by the risk of loss of or damage to the works borne by the purchaser."

particular, whether the contractor was solely responsible for the construction, or whether his participation in the construction was limited), the nature of the works, in particular whether the equipment supplied is of a complex nature, and the difficulty of discovering defects. The guarantee period should be long enough to enable the purchaser to discover all defects for which the contractor may be responsible. On the other hand, it should not result in making the contractor responsible for the maintenance of the works, which may be the consequence of too long a guarantee period.

### (b) Commencement of guarantee period

29. In cases where a single contractor is responsible for the construction of the whole works, the guarantee period should commence to run on the date when the works are taken over by the purchaser. However, if the purchaser breaches the contract by refusing to take over the works, and the contract in such circumstances provides for a presumed take-over, the guarantee period should start to run on the date of the presumed take-over. When the purchaser refuses to take over and the contract does not provide for a presumed take-over, the parties may wish to agree that the guarantee period commences to run from the date when the performance tests have been successfully carried out. For cases where the purchaser unjustifiably prevents the performance tests from being carried out, the contract may stipulate that the guarantee period will commence to run when a written notice to that effect has been sent by the contractor to the purchaser.

30. In cases where several contractors participate in the construction of the works and the equipment supplied by a contractor cannot be put into operation until the entire works are capable of operation, it is advisable to agree that the guarantee period will commence to run from the date when the works are capable of operation.

31. The contractor may, however, be reluctant to accept the putting into operation of the equipment at the commencement of the guarantee period. A long period may elapse between his performance and the performance of other contractors needed to put the works into operation together with the equipment. This may result in the contractor's responsibility existing for an unforeseeable period of time. One approach to resolve this difficulty may be to add to a normal guarantee period, which would commence to run at the date of putting the equipment into operation, an additional period of time during which the construction would be normally completed, and to provide for a guarantee period consisting of both these periods commencing to run from the date of take-over of the equipment. Even if the putting into operation of the works took longer than anticipated the guarantee period would not be extended and would expire within the specified period of time from the date of take-over. Another approach may be to specify that the guarantee period commences to run at the date of putting the equipment into operation, but cannot in any event exceed a specified longer period from the date of take-over of the equipment.

(c) *Extension of guarantee period*

32. The guarantee period given by the contractor should be extended by any period of time during which the works could not be operated as a result of a defect covered by the guarantee. This extension should cover the whole works if no part thereof could be operated, or a part thereof if only that part could not be operated. In relation to defective supplies which have been repaired or replaced, a new guarantee period should commence from the time when the works can be operated after cure of defects. The length of such a period should in principle be the same as that originally applicable to the defective part.<sup>3</sup> The parties may wish to consider whether it is advisable to agree upon a maximum guarantee period which would apply in any event, to be computed from the date of take-over or acceptance of the works.

3. *Manufacturer's guarantee*

33. If equipment to be used by the contractor in constructing the works is supplied by manufacturers or other persons to the contractor, guarantees are usually given by such suppliers. It is advisable to agree that the contractor should inform the purchaser of such guarantees after they have been granted and that he should assign to the purchaser all the rights which may arise from such guarantees, whenever possible. An alternative approach may be to agree that the guarantee given by the contractor will not expire in respect of equipment covered by a manufacturer's guarantee before the expiration of such guarantee.

D. *Remedies for failure to perform*

1. *Purchaser's remedies*

(a) *Delay in construction*

34. The purchaser's remedies for delay in construction should include requiring the contractor to perform, termination (see chapter XXXVIII, "Termination") and completion of the construction of the works by a new contractor at the expense and risk of the original contractor (see paragraph 38, below). In requiring the contractor to perform, a reasonable or specified period should be given to him. If the contractor still fails to perform within this period of time the purchaser should be entitled to terminate the contract. However, during this period the purchaser should not be entitled to terminate the contract.

<sup>3</sup> *Illustrative provision*

"The guarantee period shall cease to run during any period during which the works are not capable of being operated due to a defect covered by the guarantee given by the contractor. If only a part of the works becomes incapable of being operated, the guarantee period shall cease to run only in respect of that part. If defective supplies are repaired or replaced by the contractor, or by a new contractor at the risk of the contractor, a new guarantee period of the same length as the original one shall commence in respect of these supplies from the time that the works can be operated after cure of the defects."

35. In addition to these remedies the purchaser may be entitled to damages (see chapter XXXI, "Damages"), or to liquidated damages or penalties (see chapter XXXIII, "Liquidated damages and penalty clauses"). However, the purchaser should be entitled to damages only if the contractor was not prevented from performing by an exempting impediment (see chapter XXXII, "Exemptions"). Other remedies (i.e. requiring performance, termination, completion of construction by employing a new contractor at the expense and risk of the original contractor) should be available even in cases where the contractor is in delay due to an exempting impediment.

(i) *Delay before scheduled date for completion*

a. *Delay before commencement of construction*

36. If the contractor fails to commence construction at the time stipulated in the contract, the purchaser should be entitled to require performance. If the contractor still fails to perform within a reasonable or specified period of time given, the purchaser should be entitled to terminate the contract (see chapter XXXVIII, "Termination"). If the contractor expresses his intention to abandon the contract the purchaser should be entitled to terminate the contract without giving the contractor an additional period for performance.

b. *Delay after commencement of construction*

37. If the contractor fails to meet the obligatory periods of time set out in the time-schedule, the purchaser should be entitled to require the contractor to perform and, if the contractor still fails to perform within a reasonable or specified period of time given, the purchaser should be entitled to terminate the contract in respect of the delayed portion. However, the parties may wish to permit the purchaser to terminate only in certain situations, e.g. when the contractor has, without justification, stopped work for a period of time (see chapter XXXVIII, "Termination"). If the contractor terminates the contract only in respect of the delayed portion of the construction, and employs a new contractor to complete that portion, the original and the new contractor would simultaneously be working at the site. This may lead to difficulties. Accordingly, the parties may wish to provide that the purchaser is also entitled to terminate the contract in respect of all portions of the construction not yet completed.

(ii) *Delay after scheduled date for completion*

38. If the contractor fails to complete the works on the date scheduled in the contract, the purchaser should be entitled to require the contractor to perform and complete the construction. If the contractor still fails to complete within a reasonable or specified period of time given, the purchaser should be entitled to terminate the contract in respect of the delayed portion. The parties may wish to stipulate, as an alternative, the right to complete the construction by employing a new contractor at the expense and risk of the original contractor. The consequences of this remedy should be the same as the consequences of the analogous remedy of cure of defects by employing a new contractor at the expense

and risk of the original contractor (see paragraphs 63-67, below).

(b) *Defective construction*

39. The purchaser's remedies for defective construction may depend on the stage when defective construction is discovered (i.e. during the construction, at taking-over and during the guarantee period, or after its expiration) and on the nature of the defects (i.e. defects preventing the works' operation in accordance with the contract, such as reducing their capacity, lowering the quality of products, increasing consumption of raw materials, or defects not preventing the works' operation in accordance with the contract). Depending on these factors, the purchaser's remedies may include the right to order stoppage of defective construction (see paragraphs 42 and 43, below), the right to refuse to take over defective works (see paragraphs 52 and 53, below), the right to require the contractor to cure defects at his expense by repair or replacement (see paragraphs 42, 54, 57 and 58, below), the right to cure defects by a new contractor employed by the purchaser at the expense and risk of the original contractor (see paragraphs 64-67, below) or the right to a price reduction (see paragraphs 59, 60 and 68, below). The contract may also be made terminable in certain situations (see paragraphs 48, 49, 55 and 69, below). In addition to these remedies the purchaser may be entitled to damages (see paragraphs 70-72, below), or to liquidated damages or a penalty (see chapter XXXIII, "Liquidated damages and penalty clauses").

40. During a certain period, the contractor will, under the contract or the applicable law, bear the risk of loss of or damage to equipment, materials, plant or the works. Such risk may include damage caused by accidental events, or the acts of a third party for whose acts the purchaser is not responsible. The consequences of the contractor bearing such risk is that, if an event covered by the risk occurs and causes damage resulting in a defect, the contractor must nevertheless effect performance free of defects (e.g. repair or replace defective equipment). If the contractor fails to effect performance free of defects, the purchaser would have all the remedies mentioned in the preceding paragraph even if the failure was due to an exempting impediment, with the important exception that he should not have the remedy of damages. The reason for this distinction is that the purpose of the remedies other than damages is to restore an equivalence between the price and the value of the performance effected by the contractor. Sums paid by the contractor to the purchaser in order to restore such an equivalence either directly or in the form of a set-off against the price to be paid by the purchaser, are considered to be price reduction and not damages.

(i) *Defects discovered during construction*

41. The purchaser should have the right during the construction to inspect the design and the equipment and materials to be used, and the way in which the erection and other services are effected (see chapter XIII, "Inspection and tests"). Even if such inspection is effected and defective construction is not discovered by

the purchaser, he should not lose any of his rights arising from the failure of performance by the contractor. If the purchaser waives his right of inspection, or if he inspects but has no objections to the quality of the inspected design, equipment, materials or services, he should not be deemed to have approved their quality, unless otherwise agreed.

42. If the purchaser discovers during the construction that the equipment being produced or services being effected do not conform to those required by the contract, he should be entitled to order stoppage of the defective construction and to demand that the construction be effected in accordance with the contract.<sup>4</sup>

43. If the purchaser asks the contractor to stop construction which the purchaser considers to be defective, the contractor should be obliged to do so even if he considers the construction to be in accordance with the contract. The purchaser should also be entitled to order stoppage of construction in cases where it may not be possible to discover defects without an interruption of the construction. If it turns out later that the construction is not defective, the contractor should have the same rights from the date of interruption of the construction as in cases where the purchaser suspends the construction for his convenience (see chapter XXXVII, "Suspension of construction").

44. Some contracts oblige the contractor to check the quality during the production of the equipment and the erection of the works. However, such provision may be important only in cases where the responsibility of the contractor for third persons employed by him for the construction is limited (e.g. only to an appropriate choice of subcontractors). It is, however, preferable to provide for the full responsibility of the contractor for persons employed by him for performance of his obligations (see chapter XXVIII, "Third parties employed in execution of contract"). If the latter approach is adopted such an obligation to check may not be necessary. However, such an obligation is of course different from an obligation of the contractor to procure a certificate of inspection issued by an inspection body (see chapter XIII, "Inspection and tests").

45. In some cases it may be advisable to agree that the contractor shall check whether the equipment, materials or services supplied by third parties employed by the purchaser are appropriate for the construction. If the contractor fails to discover and notify in time defects which he could reasonably be expected to discover, he should be liable for damages. In some kinds of works contracts (in particular semi-turnkey contracts), the parties may wish to agree that such failure may make the contractor liable to the same extent as for defects in

*<sup>4</sup>Illustrative provision*

"The purchaser shall be entitled to check the production of any equipment and the construction of the works and to order stoppage of any production or construction which results or would result in defects in the works. The contractor shall discontinue such production or construction, and shall expeditiously replace or repair any defective supplies already effected, or any defective part of the plant."

his performance. In such cases, the purchaser should, however, be obliged to assign to the contractor the rights the purchaser may have against third parties employed by him as a result of the failure of such third parties which the contractor was obliged to check.

46. If the purchaser exercises his right to order stoppage of defective construction the contractor should be obliged to proceed with proper construction. The contractor should not be entitled to any postponement of the time for his performance, and all costs connected with the interruption of the defective construction should be borne by the contractor.

47. The contractor should be free to choose the way in which the defects are to be remedied. He may either repair defective equipment or materials or replace them. The purchaser may wish to stipulate in the contract that defective equipment or material for which he has paid at least in part cannot be taken from the site without his approval or without being replaced by new equipment or materials.

48. If the contractor fails within a reasonable time to remedy defects which would prevent the works from operating in accordance with the contract, or if he declares that he will not cure them, or if the contractor persists with defective construction, the purchaser should be entitled to terminate the contract (see chapter XXXVIII, "Termination").

49. Special provisions may be required in some contracts in respect of defects in the design. Such provisions are advisable in contracts where a contractor supplies a design for the whole or part of the construction and both he and other contractors are to participate in the construction under that design. In these situations defects in the design may affect not only the construction to be executed by the supplier of the design, but also the construction to be executed by other contractors. The purchaser may suffer serious losses due to the need to suspend or vary contracts concluded with other contractors, and his remedies should be appropriate to cover these consequences. The contractor should expeditiously make good the defects in the design. If he fails to do so within a reasonable time the purchaser should be entitled to employ a new contractor to cure the defects at the expense and risk of the original contractor. Alternatively the purchaser should be entitled to terminate the contract.

(ii) *Defects discovered during take-over or notified during guarantee period*

50. When the contractor finishes the construction he should be entitled to have the works taken over by the purchaser. Before the take-over the purchaser should have the right to check the quality of the works and to have the contractor cure defects which are then discovered. For this purpose performance tests are usually carried out.

51. If defects are discovered during take-over the purchaser should have the remedies which are discussed

in paragraphs 52-69. The contractor should also have the same remedies in respect of defects notified during the guarantee period. However, after the works have been taken over, the purchaser should not be able to reverse the take-over.

a. *Refusal to take over*

52. If the contractor fails to demonstrate through a successful performance test that the works are free of serious defects, the purchaser should be entitled to refuse to take over the works. When a defect is to be considered serious should be defined in the contract. If the needs of the purchaser do not require a different approach, the parties may wish to define them as defects preventing the works from being capable of operation in accordance with the contract.<sup>5</sup> Some defects which under this approach would entitle the purchaser to refuse to take over the works may, however, be acceptable to the purchaser if the price is adequately reduced. The parties may therefore stipulate that for such defects the purchaser's only remedy is to claim a price reduction (see paragraph 61, below).

53. Upon refusal by the purchaser to take over the works, his consequent remedies should be analogous to those which he has in cases where the contractor is in delay (see paragraph 38, above). This approach is based on the consideration that in both cases the purchaser is prevented from operating the works in accordance with the contract and that a precise borderline between delay in construction and defective construction may be difficult to draw. In case of refusal to take over the works the purchaser should have the following consequent remedies.

i. *Requiring performance without defects*

54. The contractor should be obliged to cure the discovered defects, and to prove through further performance tests stipulated in the contract that his performance is in accordance with the contract. If during the repeated performance tests the defects discovered during the previous performance tests or new defects of a serious character appear, the purchaser should again be entitled to refuse to take over the works and to require performance without defects.<sup>6</sup> If no further performance tests are specified in the contract, additional tests should be held within a reasonable time.

<sup>5</sup>*Illustrative provision*

"If the contractor fails to prove through a successful performance test that the works are capable of being operated in accordance with the contract, the purchaser shall be entitled to refuse to take over the works. After the take-over occurs, the purchaser shall not be entitled to reverse the take-over."

<sup>6</sup>*Illustrative provision*

"If the purchaser refuses to take over the works, the contractor shall be obliged to cure the discovered defects expeditiously and to prove through new performance tests that the works are capable of operation in accordance with the contract. If during the repeated performance tests the same defects or new defects preventing the works from being operated in accordance with the contract appear, the purchaser shall again be entitled to refuse to take over the works."

## ii. Termination of contract

55. If during the final performance tests provided for in the contract defects are discovered which entitle the purchaser to refuse to take over the works, he should, as an alternative to the right to require performance without defects, have the right to terminate the contract.<sup>7</sup> The extent to which the contract may be terminated and the effects of termination are discussed in chapter XXXVIII, "Termination".

### b. Remedies in respect of defects in works taken over

56. If the purchaser takes over the works because he was not entitled to refuse to do so, or if he has decided not to exercise his right of refusal, he should have the following remedies in respect of defects discovered during taking-over or notified before the expiration of the guarantee period.

#### i. Remedies at time of discovery or notification of defects in works taken over

##### aa. Cure of defects by contractor

57. In the first instance, the purchaser's sole remedy should be to require cure of the defects. The contractor should be obliged to cure the defects expeditiously after they are discovered during taking over, or after their notification during the guarantee period.<sup>8</sup> Either the time-limit for curing defects should be specified in the contract, or the contract should provide that the defects are to be cured within a reasonable time. If the contractor fails to do so, within the time given to him by the purchaser, the purchaser should have the remedies mentioned in paragraphs 62-69, below.

58. If the contractor is obliged to cure the defects, he should be responsible for making an appropriate, complete and timely cure. He may repair or replace defective equipment. If the cause of the defects lies in a defective design supplied by the contractor, he should be obliged to cure the design and also to replace equipment which is not in accordance with a proper design. In order to protect adequately the purchaser's interest, it may be advisable to stipulate that equipment or material to be replaced by the contractor may be taken from the site only after having been replaced by new equipment or material without defects, or with the purchaser's consent.

##### <sup>7</sup>Illustrative provision

"If the contractor fails to prove through the final performance test specified in the contract that the works are capable of being operated in accordance with the contract the purchaser shall be entitled either to claim that the defects be cured and performance without defects be proved through additional performance tests within a reasonable period of time or to terminate the contract. The remedy chosen by the purchaser shall not be changed without the consent of the contractor. The purchaser shall be entitled to such alternative remedies also in the case of a failure of any additional performance tests."

##### <sup>8</sup>Illustrative provision

"If defects are discovered at the time of take-over and the purchaser does not refuse to take over the works, or defects covered by the guarantee are discovered and notified before the expiration of the guarantee period, the contractor shall be obliged to cure the defects expeditiously."

### bb. Price reduction

59. The purchaser should have this remedy to the exclusion of the remedy of cure only in two cases. The purchaser should be entitled to a price reduction regardless of whether or not the price or any part of the price of the defective equipment or material has been paid.

60. Firstly, he should have it when the defects are not curable. An appropriate formula for calculating the price reduction may be to provide that it should be equal to the difference between the value which the works without defects would have had, and the value of the defective works at the time of discovery of the defects.<sup>9</sup> The parties may wish to provide for the latter point of time in order to prevent the purchaser from delaying his choice of the remedy and speculating on possible changes in the values of the works. If the values prevailing at the time of the conclusion of the contract are adopted, changes in the price level occurring during the period of time which elapses till the discovery of defects would not be taken into account.

61. Secondly, the purchaser should have this remedy when the contract provides that for certain defects the purchaser's only remedy is price reduction. Such defects should be precisely defined in the contract (for example, in terms of a percentage of reduction production capacity). Furthermore, parties should agree upon a precise method of determining the price reduction, if possible by using a mathematical formula.<sup>10</sup>

#### ii. Remedies after expiration of time given to contractor for curing defects in works taken over

62. If the contractor is obliged to cure the defects, he should be entitled to a reasonable time to do so. If within such reasonable time given to him by the purchaser he fails to cure the defects, the purchaser should be entitled alternatively to do so through a new contractor employed by him at the original contractor's expense and risk (see paragraphs 64-67, below), to claim a price reduction (see paragraph 68, below), or to terminate the contract in certain situations (see paragraph 69, below). When, after the lapse of the reasonable time given for cure, the purchaser notifies the contractor of his choice of one of the latter remedies, the contractor should be obliged to discontinue his attempts to cure the defects.

##### <sup>9</sup>Illustrative provision

"The purchaser who has taken over the works shall be entitled to a price reduction if the defects discovered during take-over cannot be cured. The price reduction shall be equal to the difference between the value which the works without defects would have had, and the value of the defective works, at the time of the discovery of the defects."

<sup>10</sup>For example, the parties may agree that the purchaser should take over the works with a lower production capacity if the difference does not exceed 5 per cent of the agreed capacity. In such a case the parties may agree that the purchaser should be entitled to the following price reduction:

Reduced production not exceeding	Price reduction
1 per cent	2 per cent
2 per cent	4 per cent
3 per cent	6 per cent
4 per cent	8 per cent
5 per cent	10 per cent

63. The purchaser should be permitted to change a choice of one of the latter remedies mentioned in the preceding paragraph for another of the latter remedies mentioned therein only with the consent of the contractor. However, in case the purchaser chooses the option of employing a new contractor to cure the defects at the expense and risk of the original contractor and the new contractor fails to cure the defects, the purchaser should be entitled to a price reduction or to terminate the contract.<sup>11</sup>

*aa. Cure of defects by employing new contractor*

64. If the contractor fails to cure the defects, it may be advisable in some cases to use this remedy instead of price reduction or termination of the contract, in particular if a turnkey contract has been concluded. If price reduction is claimed, or if the contract is terminated in respect of a defective portion of the works, the original contractor would not be liable to cure the defects, and the purchaser must usually employ a new contractor to cure them. The new contractor may hesitate to assume responsibility for ensuring the proper operation of the works since he did not effect the entire construction and each contractor would only be responsible for the construction effected by him. Furthermore, defects resulting from improper construction by the new contractor would not be covered by the guarantee given by the original contractor. Such a division of responsibility between the original contractor and the new contractor may be avoided by employing the new contractor at the expense and risk of the original contractor.

65. If the purchaser chooses the remedy of curing defects by a new contractor at the expense and risk of the original contractor, he should be obliged to make a reasonable selection of a new contractor and to agree with him reasonable contractual terms. The original contractor should be obliged to pay all costs reasonably incurred by the purchaser, including the price to be paid to the new contractor. The risk connected with a failure by the new contractor reasonably chosen by the purchaser to perform his obligations should be borne by the original contractor. The guarantee for defects granted by the original contractor should cover not only defects not cured by the new contractor but also those caused by him. However, if the original contractor paid costs incurred by the purchaser in employing the new

*<sup>11</sup>Illustrative provisions*

"(1) If the contractor fails to cure the defects in the works taken over by the purchaser [within a reasonable time] [within . . . days] given to him by the purchaser, the purchaser shall be entitled:

- "(a) to an adequate price reduction;
- "(b) to cure the defects through a new contractor employed by him at the expense and risk of the contractor; or
- "(c) to terminate the contract if the defects are incurable and the works are not capable of being operated in accordance with the contract.

"(2) The remedy chosen by the purchaser shall not be changed without the consent of the contractor. However, if the purchaser chooses to employ a new contractor to cure the defects at the expense and risk of the original contractor and the new contractor fails to cure them, the purchaser shall be entitled, either to terminate the contract if the works are not capable of being operated in accordance with the contract, or to a price reduction."

contractor under this remedy, the purchaser should be obliged to assign to him rights he may have against the new contractor due to the failure of the latter to perform, and the purchaser should remain obliged to pay him the price agreed upon in the contract.<sup>12</sup>

66. If the purchaser chooses the remedy of curing the defects by a new contractor, the original contractor should be obliged to stop his efforts to cure the defects and to leave the site to enable the cure by the new contractor. The contract should stipulate when the original contractor is obliged to stop (for example, the day when the original contractor is notified of the choice of this remedy by the purchaser or a later date determined by the purchaser).

67. Before the cure of defects the contractor should be obliged not to remove any of his equipment or material which is at the site if it can be used in curing the defects. Reasonable use of such equipment and materials should be permitted in order to speed up the cure of the defects.

*bb. Price reduction*

68. The purchaser should be entitled to claim a price reduction as an alternative to the cure of the defects by a new contractor, or in cases where it turns out that defects were not cured by the new contractor. The price reduction should consist of the difference between the value which the works without defects would have had and the value of the defective works at the time the purchaser claims the price reduction. This approach also takes into consideration changes in the value of the works between the time of conclusion of the contract and the time of claiming the price reduction. If the defects are curable the price reduction should be equal to the costs which would normally be incurred in curing such defects.<sup>13</sup>

*cc. Termination of contract*

69. Termination of the contract should be available only in limited cases. Thus it may be available when the contractor fails to cure defects or when a new contractor employed by the purchaser to cure the defects at the expense and risk of the original contractor fails to do so, and as a result of the defects the works are unable to be operated in accordance with the contract (see

*<sup>12</sup>Illustrative provision*

"If the purchaser employs a new contractor to cure the defects, provided the selection of such new contractor and the terms of the contract with him are reasonable, the purchaser shall be entitled to all costs reasonably incurred by him. If the performance by the new contractor is defective, the contractor shall be responsible for such defects to the same extent as if he had effected such performance. To the extent to which the contractor paid costs incurred by the purchaser in employing the new contractor, the purchaser shall assign any rights he may have against the new contractor to the contractor."

*<sup>13</sup>Illustrative provision*

"The price reduction shall be equal to the difference between the value which the works without defects would have had and the value of the defective works at the time the purchaser claims the price reduction. If the defects are curable the price reduction shall be equal to the cost which would normally be incurred in curing the defects."

footnote 11, above). The parties may even wish to limit this remedy to certain specified cases (for example, if the capacity of the works does not achieve a certain percentage of the capacity specified in the contract). The extent to which the contract may be terminated and the effects of termination are discussed in chapter XXXVIII, "Termination".

(c) *Damages for failure to perform*

70. In addition to the remedies discussed in the previous paragraphs, the purchaser should be entitled to be compensated for losses caused by his failure to perform, unless the failure was due to an exempting impediment (see chapter XXXI, "Damages" and chapter XXXII, "Exemptions"). The extent of damages may depend upon the other remedies chosen by the purchaser, and should of course not include compensation for losses covered by such remedies.

71. The purchaser may be entitled to be compensated for costs which he incurs as a result of delay (e.g. salaries paid to the purchaser's personnel) or the cure of defects by repair or replacement effected by the contractor (e.g. the cost of laying a new concrete platform where the contractor has to replace a defective machine and it is the purchaser's obligation to lay the new platform on which a new machine is to be installed). The purchaser may also recover damages for losses suffered through his liability to pay compensation to a third person which arises because of failure to perform by the contractor. Such compensation to a third person may take the form of damages payable to him (for example, due to breach of an obligation to enable the third person to start erection on a particular date) or compensation payable to the third person as the result of variation or suspension of the third person's obligations, or termination of a contract for the purchaser's convenience necessitated by the failure to perform by the contractor (see chapter XXXV, "Variation clauses", chapter XXXVII, "Suspension of construction" and chapter XXXVIII, "Termination").

72. The extent to which compensation should be paid for loss of profits is debatable. Compensation for loss of profits usually has no practical importance when delay occurs before the date scheduled for completion or when defects are discovered during construction since the loss of profits will be suffered by the purchaser only when the works cannot be operated properly on the date scheduled for completion. However, cure of defects discovered during construction may result in delay in the completion of the construction and loss of profits may be caused. The parties may wish to stipulate that the contractor is liable to the purchaser for loss of profits only in cases when the contractor intentionally causes the delay. In the case of defective construction the parties may wish to limit liability for loss of profits to cases where the contractor intentionally performed with defects, or where he constructed the works with knowledge that defects would result. The parties may also wish to use other approaches to limit liability for loss of profits (see chapter XXXI, "Damages").

(d) *Delay in payment by contractor*

73. The contractor may be obliged to pay a sum of money to the purchaser, e.g. to pay costs incurred by the purchaser in employing a new contractor for completion of the construction or cure of defects at his expense and risk (see paragraph 65, above). If the contractor fails to perform this obligation in time he should be liable to pay interest and damages to the same extent as the purchaser is liable when he fails to pay the price (see paragraphs 74-76, below).

2. *Contractor's remedies for purchaser's failure to pay*

74. The payment conditions in a contract will often determine when the contract price or a part thereof is to be paid. If the purchaser fails to pay the contract price or a part thereof on the date when it is due, the contractor should be entitled to require payment, suspend the construction of the works (see chapter XXXVII, "Suspension of construction") or terminate the contract (see chapter XXXVIII, "Termination"). In addition, the contractor should be entitled to interest in the event of the failure of the purchaser to make payment on the due date, if the applicable law permits. The parties should consider whether the interest payable by the purchaser should be governed by the applicable law or regulated in the contract. However, there may be mandatory rules under the applicable law with regard to interest, such as restrictions on the interest rate. If parties provide for the payment of interest in the event of failure to make payment by the purchaser, the contract should state the time during which interest is to be payable, for example, interest may be payable from the date of failure to make payment, as the money to be paid to the contractor could earn interest from that date. The parties should stipulate whether, in addition, damages should be payable for loss suffered which is not covered by the interest.

75. The parties may wish to consider whether interest should be due in cases where an exempting impediment prevents the purchaser from paying the contract price. Parties may wish to provide that interest is payable in such cases in order to prevent the purchaser from benefiting from the use of the money which should have been paid to the contractor. Damages for loss suffered which is not covered by the interest should not be payable if the delay in payment is caused by an exempting impediment (see chapter XXXII, "Exemptions").

76. The interest rate may be determined so as to safeguard against the fluctuation of interest rates in the market between the time payment is due and the actual time when payment is made. However, it may not be possible to predict accurately what the interest rate will be at the time payment becomes due. It is therefore not advisable to stipulate a specific rate of interest, but to provide for a formula. One approach is to base the interest rate on some banking rate (e.g. the London Inter-bank Offering Rate) at the time payment is due, without stipulating a particular rate in the contract. Other possible approaches to determining the interest rate include providing either the interest rate for the

time being prevailing in the purchaser's country, or that for the time being prevailing in the contractor's country, during the time when the purchaser is in delay in payment. If the rate prevailing in the contractor's country is to apply, the purchaser might be tempted to delay payment when the rate prevailing in his own country is higher than the rate prevailing in the contractor's country. If the rate prevailing in the purchaser's country is to apply, there would be no such inducement. However, if the latter approach is adopted, and the rate prevailing in the contractor's country is higher than the rate prevailing in the purchaser's country, the contractor might regard the approach as unfair. Such possible unfairness might be mitigated by permitting the contractor to sue for damages for the loss caused by the difference in interest rates. Yet another approach may be to link the interest rate to that prevailing in the country in whose currency the payment is to be made (see chapter XXXI, "Damages", paragraph 10). Parties must in any event agree on which of the many interest rates prevailing in a country is to apply. One rate which might be adopted is the official discount rate in a country.

77. The rules applicable to the obligation to pay interest and damages should apply also to the purchaser's failure to make payment other than payment of the price.

#### *E. Purchaser's remedies in respect of defects not covered by contractor's liability*

78. The parties may wish to agree that the contractor is obligated at the purchaser's request to cure as soon as possible defects for which he is not responsible, at the expense of the purchaser, if they are notified during the guarantee period. The extent to which the contractor may be obliged to cure, at the expense of the purchaser, defects which appear after the expiration of the guarantee period are dealt with in chapter XIX, "Maintenance and repairs".

#### *F. Procedure for claims in respect of defects notified during guarantee period*

79. This section deals only with the procedure for claims relating to defects discovered and notified during the guarantee period. The procedure to be followed during the construction period is discussed in chapter XIII, "Inspection and tests". The procedure relating to defects discovered at taking-over is dealt with in chapter XIV, "Completion, take-over and acceptance of works".

80. The purchaser should be obliged to notify the contractor as soon as possible in writing of any defect which may be discovered during the guarantee period. The failure to give such a notification, or to give it in time, should not result in a loss of the purchaser's rights arising from the defective performance. The purchaser should, however, be liable to compensate the contractor for losses caused by the non-receipt of such a notice.

81. The notice of defects should specify the defects and the date of their discovery. It should also specify the nature and extent of damage to the purchaser's property caused by the defects. The contractor should be given an opportunity of inspecting the defects notified.

82. The contractor should inform the purchaser in writing within a period of time to be stipulated in the contract whether he contests the existence of the defects or the coverage thereof under the guarantee. Even if the contractor denies his responsibility for the defects, he should be obliged to take immediate steps to cure the defects informing the purchaser of the time he needs to cure the defects if he is required by the purchaser to do so. If the contractor later proves that he is not responsible for the defects, he should be entitled to the costs reasonably incurred in curing the defects (see paragraph 78, above).

#### *G. Defects notified after expiration of guarantee period*

83. The contractor should not be responsible for any defects which are discovered or notified after the expiration of the guarantee period. Under the applicable law or where parties so provide in the contract, there may be some exceptions to this principle (for example, the contractor may be responsible for defects discovered by the purchaser after the expiration and the guarantee period if the contractor knew of these defects at the time of his performance, or if he fraudulently concealed the defects).

[A/CN.9/WG.V/WP.11/Add.4]

### **Chapter XXXI. Damages**

#### *Summary*

The contract should provide that a party who has failed to perform any obligation under the contract is liable for damages unless the failure was due to an exempting impediment.

The contract should specify the types of losses to be compensated and the extent of damages to be paid. A determination of these factors should take into consideration the long term and complex nature of works contracts and the large losses which may be caused by the breach. The parties may also wish to provide for methods to reduce the scope or amount of damages payable, such as excluding compensation for losses which are unforeseeable, excluding compensation for indirect or consequential losses, and limiting the amount of damages. The extent of damages payable may also depend upon the nature of the breach and the time when it occurs. It is advisable to obligate the aggrieved party to mitigate his losses resulting from the breach through appropriate measures reasonable under the circumstances.

The issue of the liability to pay damages for personal injury and for damage caused to property of third persons need not be settled in the contract. The parties may, however, wish to agree upon the internal allocation of risks between them to be paid to third persons.

\* \* \*

#### A. General remarks

1. An important consequence of a failure to perform which constitutes a breach of contract<sup>1</sup> is that the party in breach must pay damages to the other party to compensate him for losses suffered as a result of the breach. The applicable law will usually determine when a failure to perform constitutes a breach of contract, and under what circumstances the aggrieved party is entitled to damages. However, the approaches to these issues under various legal systems may differ. The legal rules on some matters relating to liability may be mandatory, while on other matters they may be capable of modification by the parties. Under some legal systems, mandatory rules may prevent the parties from excluding liability or reducing the extent of recoverable damages.

2. Damages as conceived in this Guide do not include compensation payable to the other party for reasons which do not constitute a failure to perform (see chapter XXXV, "Variation clauses", chapter XXXVII, "Suspension of construction", and chapter XXXVIII, "Termination"). Damages should also be distinguished from other remedies which the purchaser may have in case of defective construction, such as price reduction (see chapter XXX, "Failure to perform").

3. It may be noted that under some liquidated damages or penalty clauses the liability to pay an agreed sum may exist regardless of whether the failure constitutes a breach of contract (see chapter XXXIII, "Liquidated damages and penalty clauses"). The payment of interest arising from the failure of a party to make timely payment should also be distinguished from damages in that interest should be paid regardless of whether or not the failure was due to an exempting impediment (see chapter XXX, "Failure to perform").

#### B. Liability for damages

4. As a general principle, the contract should provide that the party who is in breach of contract is obligated to compensate the other party for losses suffered as a result of the breach. This rule should apply to the failure to perform any obligation by either party. However exceptions thereto may be agreed upon in the contract for some cases.<sup>2</sup>

<sup>1</sup>Failures to perform due to exempting impediments are not considered to be breaches of contract (see chapter XXXII, "Exemptions").

<sup>2</sup>Illustrative provision

"Unless otherwise provided in this contract, a party who fails to perform any obligation under this contract shall be liable for damages unless the failure was due to an exempting impediment."

5. The contract may provide that the aggrieved party is entitled to be compensated for all losses caused by the breach, except for certain losses which are excluded. A more restrictive approach may be to provide that the aggrieved party is entitled to be compensated only for certain types of losses expressly mentioned.

6. In determining what losses are to be compensated by damages the parties may wish to consider in particular the following types of losses:

(a) Diminution in the value of assets of the aggrieved party (e.g. damage to equipment owned by the purchaser as a result of defects in other equipment supplied by the contractor);

(b) Costs reasonably incurred by the aggrieved party as a result of a breach by the other party (e.g. wages and overhead expenses of the purchaser during the time when the works are not capable of being operated);

(c) Payments which the aggrieved party makes to a third party because of a liability to make such payments which arises due to the breach;

(d) Loss of profits which would have accrued to the aggrieved party if the contract had been properly performed (see paragraph 8, below).

7. When the aggrieved party is liable to pay compensation to a third party due to a breach by the other party, the payments to be made to the third party could be substantial. Therefore, when the aggrieved party is entitled to recover from the party in breach damages in respect of such payments, he may wish to obtain these damages before making payment to the third party. On the other hand, if the aggrieved party's actual payment to the third party is less than the amount of damages received from the party in breach the aggrieved party will be unjustly enriched. The parties should consider whether the rules of the law applicable to the contract or rules of procedure which will be applicable to the settlement of a dispute arising from the contract resolve these problems satisfactorily. If not, the parties may wish to provide for payment to be made directly by the party in breach to the third party in the name of the aggrieved party. Another approach may be to provide that the damages must be repaid to the extent to which the aggrieved party fails to prove within a certain period of time that he discharged his obligation towards the third party.

8. It may often be difficult to determine the amount of lost profits; furthermore, this amount could potentially be very large. As a result, contractors are reluctant to assume unlimited liability for lost profits. In addition, such unlimited liability may not be insurable. One approach to limiting liability may be to compensate for loss of profits under a liquidated damages or penalty clause. Another approach may be to restrict liability for lost profits only to certain cases of delay or defective performance (see chapter XXX, "Failure to perform"). Yet another approach may be for the contract to limit compensation for loss of profits to a certain amount or to loss of profits suffered during a limited period of

time after a breach. Such limitation could result in a lower contract price since the contractor's liability insurance costs (which he would normally include in the price), or his financial reserves to cover liability risks could be lower.

9. A breach of contract may result in some benefits or savings to the aggrieved party (for example, he may save certain costs in the operation of the works which he would have incurred if there were no breach). These benefits and savings should be taken into account in determining the losses to be compensated. However, it may be noted that when the aggrieved party receives insurance indemnification for the losses suffered the claim for damages may be subjected to subrogation by or assignment to the insurer to the extent of losses indemnified.

10. The party in breach should generally be obliged to compensate the other party by paying a sum of money equivalent to the losses suffered. As a general principle, the contract may require damages to be paid in the same currency in which the price is to be paid. However, in some cases, in particular if the price is to be paid in a currency which is not freely convertible, the contract may provide for damages to be paid in the currency in which the loss has been suffered (e.g. if the aggrieved party is obliged to pay compensation to a third party in a freely convertible currency, the damages in respect of the payment of such compensation should be paid to the aggrieved party in the freely convertible currency).

### C. Extent of damages

#### 1. Mitigation of losses

11. The parties may wish to provide in the contract that the aggrieved party must endeavour to mitigate the losses resulting from the breach of contract. If the aggrieved party fails to fulfill his obligation to mitigate his losses he should not be entitled to compensation for losses which could have been prevented if he had fulfilled this obligation. However, the party should be obligated to take only measures which can reasonably be expected to mitigate the losses and which are reasonable for a party in his position to take (for example, he should not be obligated to take any measures which might endanger his own commercial reputation or which are too onerous). If the aggrieved party takes such measures he should be able to recover his losses in full including costs reasonably incurred in taking such measures, even if the measures were unsuccessful.<sup>3</sup>

##### <sup>3</sup>Illustrative provision

"A party who suffers losses as a result of a breach by the other party shall take all measures which he can reasonably be expected to take to mitigate the losses. If he fails to take such measures any losses which could have been prevented thereby shall not be recoverable. If he takes such measures he shall be entitled to recover the full extent of his losses, including costs reasonably incurred by him in taking such measures, even if such measures were not successful in mitigating the losses."

#### 2. Reduction of scope or amount of recovery

##### (a) Unforeseeable losses

12. The contract may exclude recovery by the aggrieved party for losses which the party in breach could not have been expected to foresee. The relevant time for determining the foreseeability of a loss may be the time of the conclusion of the contract,<sup>4</sup> or the date of the breach. Because of the long-term character of a works contract the parties may wish to stipulate that the date of the breach of contract is the relevant date to determine foreseeability. Such a stipulation would expand the scope of recovery since a particular type of loss may become foreseeable between the times of the conclusion and the breach of the contract.

13. If the parties provide that unforeseeable losses are not to be recoverable they should provide an objective test to determine unforeseeability, for example, losses which are not foreseeable by a reasonable person in the same position as the party in breach.<sup>5</sup>

##### (b) Indirect or consequential losses

14. Some works contracts exclude from recovery compensation for indirect or consequential losses. However, the terms "indirect" and "consequential" are vague and could give rise to differing interpretations. Therefore, these terms should be defined if they are to be used in the contract. The parties may wish to specify the types of losses which are not to be compensable, without using these terms. For example, the parties may wish to exclude from recovery losses suffered by the aggrieved party as a result of a liability which the aggrieved party has assumed towards a third person even in cases where no loss was caused (e.g. if the contractor undertakes to pay to a subcontractor an agreed sum as liquidated damages or a penalty if the erection of the equipment cannot be commenced in time due to the purchaser's failure to co-ordinate construction, and the sub-contractor did not suffer any loss). If the contract excludes from recovery losses which are unforeseeable, this will in many cases also exclude recovery for indirect or consequential losses, since such losses are often unforeseeable. In such cases an additional clause excluding indirect and consequential losses from damages may therefore be superfluous.

##### (c) Damages limited by amount

15. Some works contracts limit the extent of recoverable damages to a certain amount. Such an amount may be determinable as a percentage of the price of the works, or a sum may be specified in the contract. In contracts in which the exact price is not known at the

<sup>4</sup>This approach was adopted in the United Nations Convention on Contracts for the International Sale of Goods, Vienna (1980), annex I, article 74, (A/CONF. 97/18; Yearbook 1980, part three, I, B).

<sup>5</sup>Illustrative provision

"Unless otherwise provided in the contract, damages shall not exceed the amount of the loss which the party in breach foresaw or could have been reasonably expected to foresee at the time of [the conclusion of the contract] [the breach of the contract] in the light of the facts and matters of which he then knew or could reasonably have been expected to know."

time of the making of the contract (for example, in the case of a cost-reimbursable contract) a combination of these approaches may be used, for example, by limiting damages to the greater of the percentage or the specified sum. A liquidated damages or penalty clause can also serve as a limitation upon the extent of recovery (see chapter XXXIII, "Liquidated damages and penalty clauses"). Parties may, however, wish to exclude a limitation of the extent of recoverable damages in certain types of breach of the contract (e.g. in cases where a loss results from an act or omission of the party in breach done with the intent to cause such loss).

#### **D. Personal injury and damage to property of third persons**

16. Defective construction may result in death or personal injury to the employees of the purchaser or to other third persons, or in damage to their property. The issues concerning damages in such cases are complex, and may be governed not by the law applicable to the contract, but rather by other mandatory rules. The contract cannot affect the liability of the contractor or the purchaser to compensate third persons who are not parties to the contract. The parties may, however, wish to provide for the internal allocation of risks between them in respect of damages to be paid to third parties due to death or personal injury or damage to their property, and to provide for insurance against such risks (see chapter XXVI, "Insurance").

17. If a person suffers personal injury or damage to his property as a result of the construction, and brings a claim against the purchaser, the contract should obligate the contractor to indemnify the purchaser against such a claim to the extent of the purchaser's liability, if the injury or damage was caused by the contractor's failure to use proper skill and care in constructing the works. The contractor should also be obligated to indemnify the purchaser against claims arising from such a failure by persons employed by the contractor to perform the contractor's obligations under the works contract.

18. The purchaser against whom a claim is made in respect of injury or damage to property of a third person should be obligated to notify the contractor of such a claim, and to permit him, if he wishes, to participate in all negotiations for the settlement of the claim and to join in legal proceedings, to the extent permitted by the law of the country where the action is brought.

[A/CN.9/WG.V/WP.11/Add.5]

#### **Chapter XXXIII. Liquidated damages and penalty clauses**

##### *Summary*

Liquidated damages and penalty clauses provide that, upon a failure of performance by one party, the other

party is entitled to an agreed sum of money from the party failing to perform. Such clauses have certain advantages. Since the agreed sum is recoverable without the need to prove that losses have been suffered, the costs and uncertainty associated with the proof of losses are removed. The sum also often serves as the limit of liability of that party (paragraph 2).

Most legal systems have some mandatory rules on liquidated damages and penalty clauses. Under some systems, agreed sums intended to coerce performance are invalid. Under other systems, the agreed sum may be reduced in certain circumstances (paragraph 5). There are also rules, which are often not mandatory, on the following questions: whether damages can be recovered in addition to the agreed sum for losses not compensated by the agreed sum; and whether, in addition to recovering the agreed sum, there can be enforcement of the performance in respect of which there has been a failure (paragraphs 6 and 7). The normal rule under most legal systems is that, for an agreed sum to be payable by a party, that party must not only fail to perform, but such failure must constitute a breach of contract. However, the contract may provide that the agreed sum should be payable even if there is no liability for the failure of performance (paragraph 8).

Parties should decide upon the objectives which they wish to attain by these clauses, and fix the amount of the sum accordingly. Because of the long-term nature of works contracts, such objectives are more difficult to achieve in these contracts. A sum which may be of a sufficient amount to compensate for a particular failure in the light of conditions existing at the time the contract is made may be insufficient if the failure occurs after the lapse of a considerable period. When the applicable law so permits, parties may find it beneficial to provide for the payment of agreed sums which exert a moderate pressure on the contractor to perform. Harsh penalties may not be useful and under many legal systems such penalties are also likely to be set aside or reduced in legal proceedings (paragraphs 9 and 11). A technique often adopted to limit liability is to place a ceiling on the agreed sums payable. Parties may also decide that the limitation is to be excluded in defined circumstances (e.g. when the failure consists of an intentional or reckless act) (paragraphs 12 and 14).

The contract should also deal with means to obtain liquidated damages or penalties. In addition to entitling the purchaser to recover the agreed sum, he should be authorized to deduct the agreed sum from sums payable to the contractor (paragraph 15).

Liquidated damages and penalties are most often provided for delay in performance. The contract should clarify the rights of the parties where the failure consists not only of failure to perform in time but of complete failure of performance. Furthermore, the contract should contain mechanisms for fixing new dates for performance if the dates originally fixed for performance by the contractor become inoperative (e.g. owing to failures of performance by the purchaser) (paragraph 16).

The purchaser may wish to provide that liquidated damages or penalties are to be payable, not only when there is delay in completing the whole works, but even when there is delay in completing a specified portion of the works. In such cases the appropriate quantification of the agreed sum requires careful consideration (paragraphs 17 to 20).

The parties may wish to provide for the effect of termination on the right to recover the agreed sum, and on the effect that the provision of a ceiling on recovery should have on the right of termination (paragraph 21).

\* \* \*

#### A. General remarks

1. Liquidated damages and penalty clauses provide that, upon a failure to perform a specified obligation by one party, the other party is entitled to an agreed sum of money from the party failing to perform. Such an agreed sum may serve as a penalty, or as compensation, or both.\* Such clauses are inserted in respect of failures of performance other than failures to make payment, and therefore in works contracts such clauses are usually inserted in respect of failures of performance by the contractor. As regards failures to make payment, it is usual to stipulate for the payment of interest. Interest is dealt with in chapter XXX, "Failure to perform".

2. Liquidated damages and penalty clauses may be included in a works contract for the purpose of achieving one or more of the following purposes:

(a) The sum payable as compensation for failure of performance is agreed at the time the contract is made. Such an agreed sum eliminates the expenses incurred in the proof of loss. Furthermore, because of difficulties sometimes encountered in proving the extent of loss, the amount of damages which might be awarded in legal proceedings may be uncertain. An agreed sum is certain, and this certainty may be of benefit to both parties;

(b) Fixing the agreed sum at an amount higher than that which the contractor might save by not performing his obligations puts pressure on him to perform, rather than breach, his obligations;

(c) The agreed sum is often the limit of liability of the contractor. The contractor is assisted by knowing in advance the maximum liability to which he is likely to be exposed.<sup>1</sup>

\*In many civil law systems the term penalty describes not only an agreed sum intended to coerce performance but also a sum intended only to compensate, and a sum with both these purposes. Studies on the nature and operation of liquidated damages and penalty clauses in international contracts are contained in *Yearbook 1979*, part two, I, A, and *Yearbook 1981*, part two, I, B, I. "Uniform rules on contract clauses for an agreed sum due upon failure of performance" adopted by the Commission are set forth in the Report of the United Nations Commission on International Trade Law on the work of its sixteenth session, *Official Records of the General Assembly, Thirty-eighth session, Annexes*, annex No. I, document A/38/17 (*Yearbook 1983*, part one, A).

<sup>1</sup>Illustrative provision

"(1) If the contractor fails to complete the works on the date fixed for completion, the purchaser shall be entitled to recover from the contractor [\$] for each day of delay which elapses from that date till the date of completion."

3. These considerations can be of special importance in international construction contracts. A purchaser who has to establish his loss in a foreign court, or in an arbitration held away from the country of construction, may incur considerable expenses, and may also be uncertain of the extent of his recovery. Furthermore, purchasers may find it advantageous to stimulate performance. The employment of alternative contractors to complete or cure performance may entail considerable time, expense and disruption. Stimulating performance through an agreed sum may also be advantageous where there are difficulties in the way of directly enforcing performance through court action. Stimulating performance may also be useful when the works form one item in a project, and non-completion or delayed completion of this item can adversely affect the entire project.

4. Liquidated damages and penalty clauses should be distinguished from two other types of clauses which are sometimes found in works contracts, i.e. clauses limiting the amount recoverable and clauses providing alternative obligations. A clause limiting the amount recoverable fixes a maximum amount payable if liability is proved, but not a minimum. A plaintiff must establish the amount of his loss, and if the loss falls below the maximum, only the loss proved is recoverable. In the case of a liquidated damages or penalty clause, in general the sum stipulated is recoverable, without proof of loss. A clause providing an alternative obligation in favour of a contractor gives him the option either of performing a specified obligation or paying an agreed sum. If he chooses to pay the agreed sum, performance cannot be enforced. Under a liquidated damages or penalty clause, however, the obligation to perform may not be discharged by paying the agreed sum.

#### B. Liquidated damages and penalty clauses and applicable law

5. Many legal systems have rules, which are sometimes mandatory, regulating liquidated damages and penalty clauses, and such rules will often restrict what the parties may achieve through such clauses. Under some legal systems, liquidated damages clauses, i.e. clauses by which the parties, at the time of contracting, fix an agreed sum payable as compensation for loss caused by a breach of contract, are valid. In contrast, clauses imposing a penalty are invalid, and the party who fails to perform is liable only for the damages recoverable under the general law. Under other legal systems, however, clauses providing for compensation, or imposing a penalty, or fixing a sum which has both these purposes, are in principle valid. The courts have the power to reduce the agreed sum in specified circumstances e.g. if the amount is grossly excessive in the circumstances, or there has been part performance. Parties by agreement cannot derogate from the power to reduce the agreed sum.

6. The applicable law also regulates the relationship between recovery of the agreed sum and recovery of damages. Since one of the objects of an agreed sum is

to avoid the difficulties of an inquiry into the extent of recoverable damages, most legal systems do not permit the purchaser, in cases where recoverable damages under the ordinary rules exceed the agreed amount, to waive the agreed amount and claim damages. Nor can the contractor, in cases where the amount recoverable as damages is less than the agreed amount, assert that he should only be liable for damages. Under some legal systems, however, where the loss exceeds the agreed sum, the purchaser can, in addition to the agreed sum, recover damages to the extent of the excess, either unconditionally or subject to satisfying certain conditions (for example, that the failure of performance was negligent, or was committed with an intention to cause loss, or that there was an express agreement that damages for such excess was to be recoverable). The purchaser may justify the maintenance of such claims on the ground that he is seeking only to be compensated for loss proved by him which would otherwise not be compensated. The contractor may seek to exclude such claims on the ground that they make his liability exposure uncertain. Parties may therefore wish to regulate these issues in the contract to the extent permitted by the applicable law.<sup>2</sup>

7. The applicable law also regulates, though generally by rules for interpreting the contract made by the parties, the relationship between recovery of the agreed sum and enforcement of performance. Under certain legal systems, enforced performance is not usually granted, and therefore the purchaser will be restricted to claiming the agreed sum. Where enforced performance is granted, however, the normal rules of interpretation are that, where an agreed sum is provided for delay in performance or defective performance other than delay, the purchaser can claim both performance and the agreed sum. It would be advisable for the contract clearly to affirm this rule.<sup>3</sup> The agreed sum normally only compensates for the loss suffered by the purchaser during the period of delay, or during the period which elapses before the defect is cured. Accordingly, the purchaser must, in addition to the agreed sum, be able to claim performance or cure respectively. The provision of an agreed sum for complete non-performance of an obligation is very rarely found in works contracts, because complete non-performance is normally not envisaged by the parties. If such an agreed sum is provided, the contract should clarify its function.

8. The rule in many legal systems is that, for liquidated damages or a penalty to be due, there must not only be the specified failure of performance, but such failure must constitute a breach of contract. Thus, if the failure of performance was caused by an exempting impediment, or by the acts of the other

party, the liquidated damages or penalty would not be due. Parties may wish (e.g. in the interests of certainty) to change the incidence of risks resulting from this rule, and to provide that the contractor must pay liquidated damages or a penalty even if he is not liable for a failure. Such a change would, however, nearly always result in an increase in the price.

### C. Increasing effectiveness of liquidated damages and penalty clauses

9. The effectiveness of such clauses depends on a number of factors. In a long-term contract, it is extremely difficult to estimate at the time of contracting the losses which will be suffered at the time of breach. Fluctuations, for example, in the prices of raw materials or feedstocks used for consumption, of markets for the finished products, or of the cost of labour or materials, may result in the agreed sum being over-compensatory or under-compensatory, or being an effective or ineffective deterrent to breach. From the point of view of the purchaser, the agreed sum should not be fixed at such a level that he will suffer serious uncompensated loss upon failure of performance. A sum which is too low will also reduce the inducement to the contractor to perform properly, or on time. An agreed sum will also be less effective as an inducement to proper or timely performance if the contractor has as a safety margin included in the price at the time of tendering a certain sum which he is prepared to pay by way of liquidated damages or a penalty. The effectiveness of the agreed sum as a remedy will also depend on the ease with which it can be recovered; if it can only be recovered after protracted legal proceedings, it will be less effective (see paragraph 15, below). From the point of view of the contractor, the effectiveness of the agreed sum in limiting his liability exposure will depend on the extent to which it constitutes an absolute limit of liability.

10. A very clear delimitation of the failure of performance for which the agreed sum constitutes compensation or a penalty would be in the interests of both parties. Thus where an agreed sum constitutes compensation for delay in performance by the contractor, the fact that this sum is not to be the purchaser's only compensation when the contractor completely fails to perform should be clarified. Again, as is common practice, when an agreed sum is payable on delay in completion, how delay and completion are defined for this purpose should be clarified. For example, a clear definition of completion is needed to determine the date from which the agreed sum becomes payable (see chapter XIV, "Completion, take-over and acceptance of works").

11. If the applicable law so permits, the purchaser may find it beneficial for the contract to fix an agreed sum for failure of performance by the contractor which both provides reasonable compensation to the purchaser and puts a moderate pressure on the contractor to perform. In determining what sum is reasonable, parties may consider such factors as the loss which might be

<sup>2</sup>Illustrative provision

"(2) Subject to the provision of paragraph (7) of this clause, and without prejudice to any right to recover the sum referred to in paragraph (1) of this clause, no damages are recoverable in respect of the delay in completion referred to in the latter paragraph."

<sup>3</sup>Illustrative provision

"(3) Without prejudice to any right to recover the sum referred to in paragraph (1) of this clause, the purchaser shall be entitled to require the contractor to complete the works."

caused to the purchaser by the failure, the effect of payment of the agreed sum on the financial position of the contractor, and the fact that the sum should be substantial enough to induce the contractor to perform. Harsh penalties should be avoided, as their stipulation in tender requirements may deter some reputable contractors from undertaking the construction, and may also have no special deterrent effect if it can be predicted that in all likelihood they will be reduced in legal proceedings. Furthermore, when accepting the provision of harsh penalties in the contract, contractors may as a counterbalance increase their safety margins in respect of the performances undertaken (e.g. by fixing later dates for completion, or lower guaranteed performance standards or by over-designing the works). Where a legal system permits an agreed sum only to serve as compensation, parties should attempt to estimate as accurately as possible the loss which the purchaser is likely to suffer. Any records relating to the basis of the estimate and the calculations should be preserved, as evidence that the sum was not fixed arbitrarily.

#### D. Ceiling on recovery of agreed sum

12. The liquidated damages or penalties are often fixed by way of increments, a fixed amount being due per unit of delay or per unit by which performance standards are not met. Very often, however, the function of liquidated damages or penalties as imposing a limitation on liability is emphasized by placing a ceiling on the amount to which the agreed sum can increase.<sup>4</sup> A contractor may be unwilling to accept liability without a ceiling, and the provision of a ceiling may tend to a reduction of the price. A purchaser should, however, only agree to a ceiling after careful consideration, as he may suffer serious uncompensated loss after the ceiling is reached. Where a contractor insists on an unreasonably low ceiling, or on unreasonably low agreed sums, the purchaser should consider whether, despite the difficulties and costs associated with recovery under it, he would find it more beneficial to rely on the general law of damages.

13. In regard to a ceiling, parties may wish to consider whether the limitation created by the ceiling should be absolute, or be excluded in certain cases. Parties may wish to consider the insertion of a provision under which the ceiling is excluded, for example, where loss results from a failure committed with the intent to cause loss.<sup>5</sup>

14. What remedies the purchaser might have if delay continues after the ceiling is reached should also be

<sup>4</sup>Illustrative provision

"(4) The amount recoverable under paragraph (1) of this clause shall not exceed a maximum of [\\$]."

<sup>5</sup>Illustrative provision

"(5) The maximum specified in paragraph (4) of this clause shall not apply to a failure to perform with the intent to cause loss."

(This approach to the exclusion of the limitation of liability is also adopted in the United Nations Convention on the Carriage of Goods by Sea, 1978, article 8 (1) (A/CONF.89/13; Yearbook 1981, part three, I, B.).

settled. If the legal system in question permits enforced performance, such a right would exist from the time delay commenced, and would continue even after the ceiling is reached. With respect to the right to recover damages, a possible approach is to provide that, after the ceiling is reached, the purchaser is entitled to recover damages for loss suffered by non-completion after the date on which the ceiling was reached. He should also be entitled to terminate the contract (see paragraph 21, below, and the illustrative provision appended thereto).

#### E. Obtaining agreed sum

15. The liquidated damages or penalty clause should entitle the purchaser to recover from the contractor the agreed sum in the event of failure of performance. Since legal proceedings for recovery entail time and expense, it is normal practice for the contract to authorize the purchaser to deduct the agreed sum from funds of the contractor in the hands of the purchaser (e.g. a deposit) or from funds due from the purchaser to the contractor (e.g. the price). The clause should clarify that deduction is an optional mode of obtaining the agreed sum. Where the same purchaser and contractor have entered into more than one contract with each other, each contract might authorize deduction from funds due under the other contract or contracts.<sup>6</sup> The purchaser can enhance the certainty of obtaining the agreed sum through provisions in the contract that the contractor must arrange for a financial institution to open in favour of the purchaser a guarantee in respect of the performance for failure of which the sum is stipulated, and that in the event of a failure of performance the purchaser can claim the agreed sum from the financial institution.

#### F. Liquidated damages and penalty clauses for delay

16. In works contracts liquidated damages and penalties are most commonly stipulated for delay in performance by the contractor. In some cases, however, difficulties arise under some legal systems because the date originally fixed for performance may become inoperative. This can happen either because of a breach of obligation by the purchaser (e.g. he hands over the site late, or gives necessary drawings or specifications late), or through acts of the purchaser which are not breaches of obligation (e.g. ordering extra work under a variation clause), or through occurrences for which neither party is responsible (e.g. exempting impediments preventing the contractor from performing). The result is that the contractor is only bound to perform within a reasonable time, and the liquidated damages or penalty clause will also be inoperative by reference to the date

<sup>6</sup>Illustrative provision

"(6) Without prejudice to any other remedy to which the purchaser may be entitled for recovery of the sum mentioned in paragraph (1) of this clause, he shall be entitled to deduct such sum, in whole or in part, from any sums due to the contractor, either under this contract, or any other contract between the purchaser and the contractor."

originally fixed for performance. Accordingly the contract should contain a mechanism for fixing a new date for performance (see chapter XXXII "Exemptions", chapter XXXV "Variation clauses" and chapter XXXVII "Suspension of construction").

17. Parties may wish to consider in what circumstances liquidated damages or penalties are to be provided for delay in completion of a portion of the works by a contractor. The purchaser may wish to impose an obligation on the contractor to complete portions of the works by specified dates to ensure steady progress in the construction, even though delay in completion of the portion does not by itself cause him loss. He may also find it advantageous to impose an obligation to complete a particular portion by a specified date if he can enter and use that portion independently of the completion of the rest of the works. It may also be advantageous where one main contractor and some subsidiary contractors are employed. Failure to complete a portion on schedule by the main contractor may result in the purchaser having to pay damages to the subsidiary contractors whose work cannot as a result be started on schedule.

18. The quantification of the agreed sum in such circumstances should depend on the reason why the portion is required to be completed by the specified date. If the obligation is imposed only to ensure steady progress, the agreed sum will assume the character of a penalty, and, if the applicable law permits the imposition of penalties, may be based on a percentage of the value of the delayed portion. Where, however, the portion is required to be completed by the specified date for the other reasons noted in paragraph 17, above, the agreed sum may assume a compensatory character, and be quantified on the basis of the expected loss from the delay.

19. The parties may wish to provide that liquidated damages or penalties are provided both for delayed completion of a portion and for delayed completion of the whole works. In such a case, in order to quantify the agreed sums they would have to identify separately the loss caused by delay in completion of the portion, and delay in completion of the whole works.

20. A related problem arises when liquidated damages or penalties are only specified for delay in completion of the whole works, and on the date specified for completion certain portions are completed, although the whole is still incomplete. In such circumstances one approach may be for the parties to provide that the agreed sum is to be reduced if the contractor can prove that the purchaser's loss was less than the agreed sum. The contractor may be able to prove this, for example, if the purchaser has entered upon the completed portions and is using them. Another approach, however, is not to provide for any reduction of the agreed sum in such circumstances, since the quantification of the reduction may lead to those disputes and difficulties of proof which the agreed sum was intended to eliminate. Furthermore, if the agreed sum is to be reduced in such circumstances to accord with the actual loss suffered by

the purchaser, it might be suggested that it should also be increased if the actual loss suffered by the purchaser exceeds it. The possibility of both increasing and reducing the agreed sum could deprive it of much of its utility.

#### **G. Termination of contract and liquidated damages and penalty clauses**

21. Parties may wish to provide that, where liquidated damages or penalties are stipulated by way of increments with a ceiling on the amount recoverable, no termination by the purchaser is possible in respect of the failure for which liquidated damages or penalties are provided until the ceiling is reached. Parties should also specifically provide for the effect of termination upon the recovery of liquidated damages and penalties, and on the ceiling. It has been suggested that termination should not have a retrospective effect on the contract, and that parties should preserve certain rights and obligations in respect of performances due before termination (see chapter XXXVIII, "Termination"). Accordingly, if a ceiling has been reached, and termination occurs after the ceiling has been reached, the termination would have no practical effect on the operation of the liquidated damages or penalty clause. If, however, termination by the purchaser occurs before the ceiling is reached (e.g., if the purchaser terminates for a failure other than the one for which the agreed sum has been stipulated), the parties may wish to provide that the termination does not affect the right to recover the amount due on the date of termination, but puts an end to the right to recover the agreed sum after termination, and also makes the ceiling inoperative. However, the purchaser should of course be entitled to recover damages for loss suffered by non-performance after the termination.<sup>7</sup>

[A/CN.9/WG.V/WP.11/Add.6]

#### **Chapter XXXV. Variation clauses**

##### *Summary*

Variations are often necessary in an industrial works project. The contract should include a variation clause permitting variations and settling the substantive and procedural conditions under which they may be made. It is usually in the interest of the purchaser to be able to

<sup>7</sup>Illustrative provision

"(7) (a) The purchaser shall not be entitled to terminate the contract on the ground of the delay in completion for which the sum payable under paragraph (1) of this clause is provided, unless the maximum specified in paragraph (4) has been reached;

"(b) If the delay occurs for which the sum payable under paragraph (1) of this clause is provided, and the contract is terminated by the purchaser for reasons other than such delay before the date when the sums payable under paragraph (1) of this clause reach the maximum specified in paragraph (4), this clause shall not be operative after termination, and the purchaser shall be entitled to recover damages from the contractor for loss suffered after that date by failure of completion."

order variations, as long as the contractor is not unduly prejudiced by them (paragraphs 2 and 7). Variations which increase or reduce the equipment, materials or services to be supplied by the contractor should result in commensurate and reasonable adjustments in the contract price, time for performance and other terms as appropriate (paragraphs 4 and 5).

The clause should permit only variations which are within the overall scope of the work (paragraphs 8 and 9). The contractor should be able to object to a variation ordered by the purchaser if performance of it would cause him substantial prejudice (paragraphs 10 to 14).

The variation clause should settle various procedural matters in connection with variations.

- A variation ordered by the purchaser should be in writing (paragraph 16).
- An objection to a variation ordered by the purchaser, a proposed alteration to such a variation, or a contention concerning the consequences of the variation, should be made by the contractor in writing within a stipulated time period (paragraph 17). The parties should attempt to resolve between themselves any dispute concerning the variation or its consequences, failing which the dispute should be admissible for third-party settlement (paragraphs 19 and 20). If the parties disagree with respect to the consequences of the variation, but not its nature, the contractor should be obligated to perform the variation pending the resolution of the issue of the consequences (paragraph 19). If the contractor objects to the variation, or proposes an alteration to it, the variation clause should establish when the variation must be performed pending settlement of the dispute (paragraphs 21 and 22).
- Variations proposed by the contractor should not be executed unless they have been agreed to in writing by both parties (paragraphs 23 to 24).
- If an engineer is to be authorized to act on behalf of the purchaser to order, confirm or consent to variations, or to settle disputes between the parties concerning variations, this authority should be set forth in the variation clause (paragraphs 25 and 26).
- The variation clause should set forth guidelines for determining the effect of a variation upon the contract price. Factors to be taken into account in determining this effect should include increases or decreases in construction costs, overhead and profit, the effect of a variation on other aspects of the contract, and other losses and expenses of the contractor (paragraphs 27 to 31). The parties should be required to keep proper records of the cost and expenses associated with a variation (paragraph 32).

\* \* \*

#### A. General remarks

1. During the course of construction of a complex industrial works project it is usual for situations to be

encountered which make it necessary or advisable to vary certain aspects of the work. These situations most often occur due to problems with the availability of feedstock or materials. They could also result from other unforeseen problems during construction requiring different equipment, materials, or services, from circumstances affecting the expected profitability of the works, or from technological innovation of which the purchaser or contractor wishes to take advantage. In addition, the contractor may seek variations to suit his construction techniques. Variations may be in the form of changes in the performance required under the contract as well as additions to or omissions from that performance.

2. In most cases it will be the purchaser who, upon his own initiative or the advice of his engineer, will seek variations. Two basic approaches are possible. First, variations sought by the purchaser could be permitted only with the consent of the contractor, with a possible exception for variations which do not affect the functioning of the works (e.g. the use of a different colour paint) which the purchaser might be permitted to order without the consent of the contractor. Second, the purchaser could be permitted to order all variations unilaterally, with some exceptions and subject to certain conditions designed to protect the contractor. It is usually in the interest of the purchaser, as the party for whom the works are being built and who is paying for them, to be able to order variations unilaterally. However, under most legal systems the purchaser will be unable to do so unless the contract expressly authorizes such unilateral variations.
3. To enable the purchaser to order variations, therefore, a clause permitting this must be included in the contract. As its essential elements, such a variation clause should authorize the purchaser to make variations, obligate the contractor to execute them, subject to the contractor's right to object in certain circumstances, and settle various procedural matters, such as the requirement that variations be ordered in writing. If an engineer is to have the power to order variations with which the contractor must comply, this authorization should also be set forth in the variation clause.
4. In addition, the variation clause should provide for adjustments in various terms of the contract as appropriate, such as the price and the time for performance by the contractor. The purchaser should be obligated to pay a higher price to compensate the contractor for additional work performed by him pursuant to the variation. Similarly, the purchaser should benefit financially from reductions in equipment, materials or services to be supplied by the contractor resulting from variations. It is important for the variation clause specifically to provide for adjustments of the contract price. This is particularly the case with lump-sum contracts, in which the contract price will remain unchanged notwithstanding variations unless the contract expressly provides for adjustments of the price. In unit-price contracts, variations which change only quantities of units used will automatically produce changes in the total price to be paid by the purchaser in accordance with the number of additional or fewer units used.

However, other expenses or losses accruing to the contractor would not affect the contract price unless the contract so provides. In a cost-reimbursable contract increases or decreases in construction costs will often, but not always, be reflected through commensurate changes in the total price paid by the purchaser. For example, if the contract imposes a price ceiling, increases in construction costs could not cause the total price to exceed the ceiling. Here, too, other expenses or losses of the contractor would not be reflected in price changes unless the contract so provides.

5. An increase or reduction in the equipment, materials or services to be supplied by the contractor may also make it reasonable to extend or reduce the time for performance of the contract by the contractor. Adjustments in other contract terms (e.g. payment conditions, insurance and guarantees) may also be warranted.

6. This chapter discusses clauses for variations which are within the overall scope of the works under the contract. Changes in the overall scope of the works itself, and alterations to the drawings and descriptive documents affecting the overall scope of the contract, are discussed in chapter IX, "Scope and quality of works". Changes in the price are dealt with in this chapter only in connection with variations; other price revisions are discussed in chapter XV, "Price". Renegotiation of the contract in cases of hardship is discussed in chapter XXXIV, "Hardship clauses". For termination by the contractor in cases of exempting impediments see chapter XXXVIII, "Termination".

#### B. Variations ordered by purchaser

7. It is usually advisable for the purchaser to be able to institute variations in respect of the equipment, materials or services to be supplied by the contractor regardless of whether or not the contractor agrees with the variations. However, the variations should be capable of being performed by the contractor, should not impair the performance by the contractor of his other obligations, and should not otherwise cause the contractor undue prejudice.

##### 1. Scope of variations

8. The variation clause should define the scope of the variations which it governs. The following points should be considered in this regard. First, equipment, materials or services which are not specifically provided for in the contract but which the contractor is nevertheless obligated to supply (e.g. when they are ancillary to express contract specifications, necessitated by circumstances which are within the risk assumed by the contractor, or required as a result of the contractor having performed defectively) are not variations, and should therefore not be governed by the variation clause. Nor should the variation clause cover changes in performance which are already provided for in the contract price. In all of these cases, the contractor should be obliged to effect the necessary changes at his own expense and within the original time for performance.

9. Second, the variation clause should permit the purchaser to order only variations which are within the overall scope of the work. Variations which alter the nature of the contract should require the agreement of both parties. As a legal matter, under many legal systems such changes are not valid without mutual agreement. As a policy matter, the contractor should not be compelled to execute work which is fundamentally different from that which he originally agreed to perform.<sup>1</sup>

##### 2. Right of contractor to object to variations

10. There may be reasons why a contractor would not want to execute a variation ordered by the purchaser. For example, a variation which alters or adds to the work which the contractor originally undertook to perform may not be consistent with his usual construction practices, may unduly prolong the completion of the contract and thereby interfere with the performance of his obligations in other projects, or may affect the extent to which he can be bonded by a bonding company. If the contractor has supplied the design for the works and guarantees the output of the works he could be prejudiced if he is compelled to perform a variation which is inconsistent with the design. The contractor should be able to object to a variation if he would suffer substantial prejudice if he were compelled to perform it.

11. The grounds upon which the contractor may object to a variation, and the effect of such an objection, should be formulated so as to balance the right of the purchaser to have the work performed as he wishes with the necessity to protect the contractor from any undue prejudice which the variation may cause him, after taking into consideration the fact that a variation will result in adjustments in the price and time for performance.

##### <sup>1</sup>Illustrative provisions

"(1) The term 'variation' as used in this clause means any alteration to the type or amount of the equipment, materials or services to be supplied by the contractor, whether an amendment of, omission from, or addition thereto.

"(2) This clause does not govern alterations which the contractor is otherwise obligated to execute.

"(3) The purchaser may order variations and the contractor shall execute them subject to the provisions of this clause.

"(4) No variation shall be made which by itself, or together with other variations at any previous time made, alters the general scope of the works under this contract, and in particular the character and nature of the works, without the written agreement of both parties.

"(5) For any variation which increases the equipment, materials or services which the contractor is obligated to supply under this contract, the contractor shall be entitled to a commensurate and reasonable increase in the contract price and in the time for performance of this contract; and for any variation which reduces such equipment, materials or services the purchaser shall be entitled to a commensurate and reasonable reduction in the contract price and in the time for performance of this contract. However, no such adjustment in the contract price or time for performance shall be made to the extent that such increases or reductions in equipment, materials or services have already been accounted for in the contract price or time for performance."

12. The grounds for objection can be formulated in various ways. One approach is to provide simply that the contractor may object to the variation if he would suffer substantial prejudice by performing the variation. For greater certainty, and to reduce the possibility of abuse of the clause by the contractor, the parties may prefer to refer to specific types of prejudice which would entitle the contractor to object.<sup>2</sup>

13. It is also possible to enable the contractor to object to a variation if it, together with all other variations which have previously been ordered, results in an increase or decrease of the contract price by a specified percentage.

14. With respect to the effect of an objection by the contractor, it would be inconsistent with the goal of balance described in paragraph 11, above, for the contractor's objection to constitute a veto. The preferable result is for the parties to discuss and attempt to agree on whether, in view of the prejudice claimed by the contractor, the variation should be required, or whether the variation ordered by the purchaser could be modified so as to take into account the interests of the contractor. If the parties fail to agree, the dispute should be submitted to an independent third party for settlement. The specific procedures to implement this mechanism are discussed in paragraphs 17-22, below.

### 3. Procedure

15. The variation clause should set forth procedural requirements in connection with variations ordered by the purchaser. These requirements should be designed to minimize ambiguities and disputes, minimize interruptions of the work, and protect the interests of both parties.

#### (a) Variations to be in writing

16. The variation clause should require variations governed by it to be in writing. The writing should also advise the contractor of any contention by the purchaser concerning the amount by which the contract price or

##### <sup>2</sup>Illustrative provisions

"The contractor may object to a variation ordered by the purchaser:

"(a) if performance of the variations would prevent or substantially prejudice the contractor from or in fulfilling any of his other obligations under the contract;

"(b) if performance of the variation would require the contractor to act in breach of any enforceable undertaking or agreement with a third party or would cause him to infringe any patent, registered design, copyright or other protected right of any third party;

"(c) if performance of the variation would require the contractor to do work or to exercise skills which are not of the kind the contractor normally does or exercises, unless the variation may be performed by a subcontractor and under the effective supervision of the contractor; or

"(d) if the variation would prevent the achievement of output targets guaranteed by the contractor."

time for performance of the contract should be adjusted, or as to any other adjustments in the contract.<sup>3</sup>

#### (b) Response by contractor and ensuing procedure

##### (i) Notification by contractor

17. A contractor who objects or suggests alterations to a written variation ordered by the purchaser, or who disagrees with the purchaser's contentions concerning adjustments in the price, in the time for performance, or in any other terms of the contract, as a result of the variation, or who contends that adjustments should be made in the price, time for performance, or other contractual terms (e.g. guarantees) because of the variation, should be required so to notify the purchaser within a stipulated time period. The contractor should be required to include in this notification all pertinent information and data so that the purchaser can evaluate the contractor's contentions. If the contractor objects to the variation as ordered by the purchaser but considers that it could be altered so as to accommodate the interests of both parties, he should be required to make such a proposal in his notification, giving all pertinent information.<sup>4</sup>

##### (ii) Failure of contractor to notify

18. If the contractor fails to submit the required notification to the purchaser within the time specified, he should be obligated to perform the variation as ordered by the purchaser, with such adjustments in the price, the time to perform, or other contract terms, as are set forth in the purchaser's variation order.<sup>5</sup>

##### <sup>1</sup>Illustrative provision

"All variations ordered by the purchaser under this clause shall be in writing. Such writing shall contain any contention by the purchaser as to the amount by which the contract price or the time for performance of the contract by the contractor should be adjusted, or as to any other adjustments in the contract."

##### <sup>2</sup>Illustrative provision

"If the contractor objects to a variation ordered in writing by the purchaser, or disagrees with a contention by the purchaser concerning the effect of the variation on the contract price, time for performance, or other terms of the contract, or if as a result of the variation the contractor claims an increase in the contract price or an extension of time to perform the contract, or an adjustment in any other terms of the contract, then within [21] days after receiving a variation order from the purchaser, and before performing the variation, the contractor shall despatch to the purchaser notice in writing of such objection and claims. The notification shall include all information and data pertinent to the objection and claims asserted by the contractor in the notification. If the contractor proposes any alteration of the variation as ordered by the purchaser, this proposal, together with the effect of the variation as altered on the contract price, the time for performance of the contract, and any other terms of contract, and all information and data pertinent thereto, shall be included in the notification."

##### <sup>3</sup>Illustrative provision

"If the contractor fails to despatch to the purchaser a notification as provided in the preceding paragraph within the time provided therein, then upon the expiry of the said time period the contractor shall be obligated to perform the variation as ordered by the purchaser, and the contract price, time for performance of the contract and/or any other terms of the contract shall be adjusted in accordance with the contentions of the purchaser, if any, as set forth in the writing containing the variation."

(iii) *Contractor's concurrence with variation but not its effects<sup>6</sup>*

19. When the contractor submits a timely notification to the purchaser a number of possibilities exist. If the contractor does not object or propose an alteration to the variation, but disagrees with the contentions by the purchaser concerning the effects of the variation on the price, time for performance or other contractual terms, or if the contractor claims an increase in the contract price, an extension of time to perform, or an adjustment in another term of the contract, he should be obligated to perform the variation, and the differences between the parties concerning the adjustments to be made should be settled by the parties, or, failing that, by dispute settlement proceedings.

(iv) *Contractor's objection to or proposal to alter variation*

20. If the contractor proposes an alteration to a variation ordered by the purchaser, the parties should endeavour to settle the variation and its effects, failing which the dispute should be referable for resolution by dispute settlement proceedings. An objection by the contractor to the variation should also be referable for resolution by dispute settlement proceedings.

(v) *Performance of variation pending settlement of dispute*

21. In order to prevent such proceedings from delaying the progress of the work, there should be some mechanism for requiring the contractor to perform the

*\*Illustrative provisions*

"(1) If the contractor does not object, or propose an alteration, to the variation ordered by the purchaser, but in a timely written notification to the purchaser disagrees with a contention by the purchaser concerning the effect of the variation on the contract price, time for performance or other terms of the contract, or claims an increase in the contract price, an extension of time to perform the contract, or an adjustment in any other terms of the contract, the contractor shall be obligated to perform the variation forthwith unless the purchaser orders the contractor to postpone such performance to some future date, and the parties shall endeavour to agree upon the effects of the variation on the contract price, the time for performance of the contract, or other contract terms as a result of the variation. Failing such agreement the dispute may be submitted by either party for resolution in accordance with [the dispute settlement provisions of the contract].

"(2) If the contractor proposes in his notification an alteration of the variation ordered by the purchaser, the parties shall endeavour to agree upon the variation and upon the effects of the variation on the contract price, time for performance of the contract or any other terms of the contract. Failing such agreement the dispute may be submitted by either party for resolution in accordance with [the dispute settlement provisions of the contract].

"(3) If the contractor objects to the variation, the dispute may be submitted by either party for resolution in accordance with [the dispute settlement provisions of the contract].

"(4) Pending settlement of a dispute concerning the nature or scope of a variation, and unless the purchaser orders the contractor to postpone such performance, the contractor shall be obligated to perform the variation forthwith [, if the [arbitrators] [engineer] determine that a delay will prejudice the satisfactory completion of the work or will otherwise significantly prejudice the purchaser]."

variation as ordered by the purchaser pending settlement of the dispute. Either the contractor could always be obligated to perform the variation pending settlement of the dispute, or he could be required to do so if the arbitrators who are to resolve the dispute, or an independent engineer, if any, determine that a delay will prejudice the satisfactory completion of the work or will otherwise prejudice the purchaser.

22. However, in some cases it may be advisable for the purchaser not to insist upon performance of the variation until the disputes relating to the variation (e.g. concerning the price) have been settled. The contract should therefore permit the purchaser to order the contractor to postpone performance of the variation to some future date.<sup>6</sup>

**C. Variations proposed by contractor**

23. There may be cases in which the contractor will wish to propose variations in the work, in order, for example, to facilitate construction, to take advantage of price differentials in materials, or to incorporate innovations.

24. Variations proposed by the contractor should not be executed unless they have been agreed to in writing by both parties.<sup>7</sup> Except in unusual cases the purchaser should be able to receive what he has contracted for even if the contractor considers that a variation would be preferable, and the purchaser should not be compelled to accept price increases or interruptions of the work because of changes in work to which he has not agreed. For those situations in which the contractor, for reasons which do not result from his breach and are not within the risks assumed by him, cannot perform the work as specified in the contract, or if he would be prejudiced if the work is not varied, he may rely on other mechanisms and remedies under the contract, such as exemption, renegotiation, or termination (for discussions of these mechanisms and remedies see chapters XXXII, "Exemptions"; XXXIV, "Hardship clauses"; and XXXVIII, "Termination").

**D. Role of engineer**

25. If an engineer is to play a significant role in the contract on behalf of the purchaser (see chapter XVII, "Consulting engineer"), one of his functions might be to determine the necessity for variation orders and to issue such orders on behalf of the purchaser, and to perform other acts in connection therewith, as described in the preceding paragraphs. The nature and extent of the engineer's authority should be specified in the variation clause in order to avoid questions and disputes about his authority. If any act, such as the

*\*Illustrative provision*

"The contractor may propose variations to the purchaser. No such variation shall be executed unless it has been agreed to in writing by both parties."

signing or confirmation of variation orders, or deciding on variations proposed by the contractor, are to be performed by the engineer, the provisions dealing with such acts should make specific reference to the engineer.

26. In some contracts the engineer might be given an independent role (see chapter XVII, "Consulting engineer"). In such contracts certain functions which the parties consider appropriate for an independent entity might be delegated to the engineer. These might include determining whether the contractor should perform a variation pending the resolution of a dispute concerning the variation, or issuing rulings on objections by the contractor to variations or determining the effects of variations on the contract price, the time for performance, or on another contract term. Such rulings could be subject to review in accordance with the dispute settlement mechanism in the contract.

#### **E. Guidelines for effect of variations on contract price**

27. A variation should often result in a reasonable adjustment of the contract price. It would be useful for the contract to contain guidelines to assist in the determination of the required amount of adjustment of the contract price. These guidelines could assist the parties in reaching agreement on this issue, and could provide criteria to be applied by arbitrators or an engineer when the parties cannot agree.

28. Some contracts may contain a schedule of prices for particular types of work or materials. Such contracts might provide that increases or decreases in specified equipment, materials or services shall be valued in accordance with prices set forth in the schedule. However, it might not always be appropriate to use these prices. For example, prices specified for particular types of work may be based upon the work being performed in a particular sequence, and a variation in this sequence may make the prices inappropriate. In addition, the contractor's overhead and profit may be distributed unevenly among the prices designated for various items, and a valuation of variations in the quantities of particular items based on these prices may take excessive or insufficient account of overhead or profit. Therefore, if variations in items specified in a contract schedule are to be valued in accordance with prices designated in a schedule, provision should be made for departing from these prices in cases where, for reasons similar to those just discussed, these prices would be inappropriate.

29. If the contract contains a schedule of prices for equipment, materials and services and variations occur in items which are not specified in the schedule, the prices designated in the schedule could be used as a basis for the valuation of the variation if it is reasonable to do so (as when the items which are the subject of the variation are analogous to items specified in the schedule).

30. When the contract contains a schedule but it is not employed to determine the adjustment in the contract price, the adjustment should be based upon changes in costs, plus the following additional factors:<sup>8</sup>

(a) Increments for overhead and profit in respect of varied work should be added or deducted, as appropriate;

(b) A variation of one aspect of the contract may affect the prices of other aspects. For example, during an interruption of a particular construction process caused by a variation, the prices of materials to be used in connection with other elements of the work may rise. Such effects should also be taken into consideration;

(c) Other losses and expenses incurred by the contractor, such as losses resulting from an interruption of construction, and expenses incurred for terminating subcontractors if work is omitted, should be taken into consideration.

31. When the contract does not contain a schedule, the adjustment in the contract price should be based upon the factors referred to in paragraph 30, above.

32. In order to facilitate the determination of costs each party should be required to keep and produce appropriate accurate records relating to such costs incurred by him.<sup>9</sup>

#### *<sup>8</sup>Illustrative provisions*

"(1) The following principles shall be applied by the parties, or, if the parties cannot agree, by the [engineer] [arbitrators], in determining the effect of a variation on the contract price.

"(2) If the equipment, materials or services which have been varied are identical in character to and supplied under the same conditions as equipment, materials or services specified in [the schedule], then the prices therein for such equipment, materials, or services shall be applied, unless a party proves that he would suffer substantial prejudice if such prices were applied, in which case the effect of the variation on the contract price shall be based upon such of the factors in paragraph (4), below, as may be appropriate.

"(3) If the equipment, materials or services which have been varied are not of such identical character or executed under such same conditions, the prices in [the schedule] shall be applied whenever reasonable. If a party proves that it is not reasonable to apply such prices then the effect of the variation upon the contract price shall be based upon such of the factors in paragraph (4), below, as may be appropriate.

"(4) The factors referred to in paragraphs (2) and (3), above, are the following:

"(a) the actual cost of varied equipment, materials or services (or, in the case of omitted equipment or materials, the market cost thereof);

"(b) reasonable profit;

"(c) any financial effects of a variation upon other aspects of the work to be performed by the contractor;

"(d) any costs and expenses accruing to the contractor from an interruption of work resulting from a variation;

"(e) any other costs and expenses accruing to the contractor as a result of the variation;

"(f) any other factors which it would be equitable to take into consideration with respect to the variation."

#### *<sup>9</sup>Illustrative provision*

"Each party shall keep and present to the other party, when required, proper records of all costs and expenses incurred by him in connection with all variations."

[A/CN.9/WG.V/WP.11/Add.7]

## Chapter XXXVI. Assignment

### *Summary*

An assignment clause should deal with assignment of the contract (substitution of a third party for a party to the contract), and assignment by a party of certain specific rights and obligations under the contract. Neither party should be able to assign the contract without the consent of the other (paragraph 3). The assignment of specific rights and obligations should in general also require the consent of the other party, but an exception may be made for assignments by the contractor of his right to receive payments from the purchaser (paragraph 6). If such an exception is made the interests of the purchaser may be protected by enabling him to prevent the assignment on reasonable and substantial grounds (paragraph 7).

The assignment clause should contain provisions to ensure that the contractual rights of the non-assigning party are not diminished or extinguished by the assignment. This should be done by making the assignee subject to the same obligations and remedies as was the contracting party (paragraph 9), and by enabling the non-assigning party to subject his consent to conditions (paragraph 10).

The assignment clause should also contain other provisions designed to safeguard the interests of the parties. Such provisions include the following:

- A requirement that a consent to an assignment be in writing (paragraph 11);
- A requirement that the assigning party notify the other party of an assignment (paragraph 12);
- A provision that in the event of violation of the clause the non-assigning party shall be able to disregard the assignment (paragraph 13).

\* \* \*

### *A. General remarks*

1. The concept of assignment as considered in this chapter covers both assignment of the contract in its entirety, whereby a new party is substituted for one of the original parties to the contract, and assignment of certain specific rights and obligations under the contract.<sup>1</sup>

2. Most legal systems contain rules governing the right of a party to assign the contract and certain of his rights and obligations under the contract, as well as the legal effects of an assignment. However, it is usually possible for the parties to supersede these rules by stipulating in the contract the terms and conditions under which an assignment may be made.

<sup>1</sup>Subcontracting, which, strictly speaking, is not an assignment of obligations, is discussed in chapter XXVII, "Third parties employed in execution of contract".

### *B. Assignment of contract*

3. Assignment of the contract by either party without the consent of the other should be prohibited. A contractual relationship between parties to a works contract is usually based upon mutual confidence between the parties. In particular, the purchaser normally selects a contractor because of the contractor's skill and experience, his reputation, his financial strength, and similar factors personal to the contractor. Significant problems could arise for the purchaser if, for example, the contractor were able to assign the contract to a third party which does not possess the same degree of skill and expertise as the contractor. Similarly, the purchaser could suffer if the contractor assigned the contract to a subsidiary which had no assets or financial resources of its own from which damages could be paid to the purchaser in the event of a breach. The substitution of a new party may result in significant disruption of the work programme, as well as of other aspects of the contract. For these reasons, an assignment of the contract should be permitted only with the consent of the non-assigning party.<sup>2</sup>

### *C. Assignment of specific contractual rights and obligations*

4. There are a number of situations in which a party may wish to assign specific rights under the contract without assigning the contract in its entirety. For example, a purchaser may wish to sell his rights to the works to a third party prior to completion, under an arrangement in which the third party is to pay the purchase price to the purchaser, and the purchaser is to remain bound to pay the contract price to the contractor. A contractor may often wish to assign his rights to receive payments under the contract, in order to obtain financing.

5. The assignment of rights should entail that the assignee is subject to the rights and remedies of the non-assigning party affecting the rights assigned. For example, a sale of the plant by the purchaser prior to their completion should be subject to modifications in construction which may be provided for under the hardship or variation clauses of the contract; such sale should also be subject to the exemptions clause. Similarly, an assignment by the contractor of his right to receive payments from the purchaser should be subject to a right of the purchaser to set-off against such sums which the purchaser is to receive from the contractor.

6. For reasons similar to those discussed in connection with the assignment of a contract in its entirety, a party

<sup>2</sup>Illustrative provisions

"(1) For the purposes of the following paragraph an assignment of this contract shall mean an assignment by a party of all his rights and obligations under the contract.

"(2) Neither party to this contract shall assign this contract without the prior consent of the other party."

should not normally be able to assign specific rights and obligations under the contract unless the other party consents to the assignment. An exception to this principle may be made in the case of an assignment by the contractor of his right to receive payment from the purchaser. Contractors often find it necessary to make such an assignment in order to borrow funds or obtain financing needed to purchase equipment and supplies, to pay labour or cover other costs of performing the contract, or to benefit from an export credit guarantee scheme. The parties may consider it appropriate to permit such an assignment without requiring the consent of the purchaser. If so, in the case of assignments for the purpose of borrowing funds or obtaining financing, the parties should consider whether the requirement of consent should be dispensed with for assignments to creditors of all types, or whether it should be dispensed with only in the case of assignments to banks or similar institutions.

7. If such an assignment by the contractor is to be permitted without the consent of the purchaser, the parties may wish to provide a means of protecting the purchaser against substantial prejudice which could result from such an assignment. This could be accomplished by requiring the contractor to notify the purchaser of the proposed assignment, and allowing the purchaser to prevent the assignment if he has reasonable and substantial grounds for doing so.<sup>3</sup> A dispute between the parties as to whether the grounds are reasonable and substantial would be settled under the general dispute settlement provisions of the contract.

#### D. Provisions to safeguard interests of parties

8. There are various provisions which could be incorporated in the assignment clause in order to safeguard the interests of the parties. Examples of such provisions are discussed in the following paragraphs.

##### 1. Preservation of rights of non-assigning party

9. The contract should ensure that the contractual rights of the non-assigning party are not diminished or

##### <sup>3</sup>Illustrative provisions

"(1) Except as provided in the following subparagraphs, neither party shall assign any of his rights or obligations under this contract to a third party without the prior consent of the non-assigning party.

"(2) If the contractor desires to assign his right to receive payments from the purchaser under this contract for the purpose of borrowing funds or obtaining financing [from banks or similar institutions], or to benefit from an export credit guarantee scheme, or for similar purposes, he shall so notify the purchaser in writing, and shall specify in the notice the sums desired to be assigned and the name and address of the assignee.

"(3) The contractor shall be permitted to make the assignment as described in the notice after [14] days following delivery of the notice to the purchaser unless within such [14] day period the purchaser delivers to the contractor, in writing, an objection to the assignment which is based upon reasonable and substantial grounds."

extinguished by the assignment. Two types of provisions should be considered in this regard. First, the contract should ensure that within the scope of the rights assigned, the assignee will be subject to the same contractual obligations and remedies as was the assigning party. In particular, purchasers should be aware that if the contractor assigns his right to receive payments, the purchaser's right to set off sums which are due to him from the contractor against sums which he owes to the contractor and have been assigned to a third party will depend upon applicable law. Since the assignee is not a party to the works contract, under some legal systems he might not be directly bound by provisions in that contract. Therefore, the contract should provide that any assignment made by a party must subject the assignee to the same rights and remedies of the non-assigning party with respect to the subject-matter of the assignment as the latter had with respect to the assigning party.<sup>4</sup>

10. Second, when, as should usually be the case, an assignment is not permitted without the prior consent of the other party, the party giving consent may wish to subject his consent to certain conditions. For example, whether an assignment of the contract relieves the assigning party from the performance of his contractual obligations may vary depending upon the applicable law. A party consenting to an assignment of the contract may wish to do so only on the condition that the assigning party remains jointly and severally liable with the assignee for the performance of those obligations, or that he guarantees the performance of those obligations. Therefore, the contract should provide that an assignment must subject the assignee to any conditions contained in the consent of the non-assigning party.<sup>5</sup>

##### 2. Consent to be in writing

11. The contract should require consent to an assignment to be given in writing. If the consent is subject to conditions, these conditions should also be required to be set forth in writing.<sup>6</sup>

##### <sup>4</sup>Illustrative provision

"Any assignment by a party of his rights under this contract shall be under the express condition that the assignee shall be bound by and subject to the same obligations and remedies under the contract with respect to the assigned rights as was the assigning party. In particular, and without limiting the generality of the foregoing, any assignment by the contractor of his right to receive payments under this contract shall be made subject to the express condition that any set-off which would have been available to the purchaser against such payments to the contractor shall also be available to the purchaser in respect of such payments to be made to the contractor's assignee."

##### <sup>5</sup>Illustrative provision

"When under this clause an assignment is not permitted without the consent of a party to this contract, the consenting party may make his consent subject to conditions, and the assignment must subject the assignee to such conditions."

##### <sup>6</sup>Illustrative provision

"Any consent pursuant to the provisions of this clause shall be given in writing. If a consent is subject to conditions, such conditions shall be set forth in the written consent."

### 3. Notification of assignment

12. It is important for the non-assigning party to know when an assignment has been executed. Even if he has consented to the assignment, it is advisable for him to receive confirmation that the assignment has in fact occurred. The contract should therefore require the assigning party to notify the non-assigning party of the assignment and the date at which it becomes effective, and identify the assignee. The assignee should not be entitled to rights under the contract which have been assigned until the non-assigning party has received such notification.<sup>7</sup>

### E. Consequences of improper assignment

13. The contract should specify the consequences of an assignment which violates the provisions of the assignment clause. In such a case the non-assigning party should be able to disregard the assignment and continue to act, in relation to the contract and the assigning party, as if no assignment had been made.<sup>8</sup>

[A/CN.9/WG.V/WP.11/Add.8]

## Chapter XXXVII. Suspension of construction

### Summary

This chapter deals with situations where the purchaser may order suspension of the construction of works for convenience or on specified grounds and where the contractor may suspend the construction due to a failure of performance by the purchaser.

As no developed doctrine of suspension exists in most legal systems, parties should consider the nature of suspension, the circumstances in which suspension may be invoked and the legal effects of suspension.

The purchaser may be given a right to order suspension for convenience (paragraphs 6 and 7) or

#### *Illustrative provisions*

"(1) In the event of an assignment permissible under this contract, the assigning party shall notify the non-assigning party of the subject-matter of the assignment, the name and address of the assignee and the date at which the assignment becomes effective.

"(2) Until the non-assigning party receives the notification required in the foregoing subparagraph he shall remain entitled to treat only the assigning party as the party to receive the performance or to perform the obligations which are the subject of the assignment."

#### *Illustrative provision*

"If a party makes or purports to make an assignment in violation of any provision of this contract, the non-assigning party shall be entitled to disregard the assignment or purported assignment and to act in relation to the contract and to the assigning party as if the assignment or purported assignment had not been made."

only in certain exhaustively defined circumstances (paragraph 8). When the purchaser orders suspension of construction, the performance of all correlative obligations of the purchaser should be automatically suspended (paragraph 9).

A suspension clause for convenience may have the advantage of allowing the purchaser time to overcome any temporary difficulties he may have rather than resorting to the more drastic remedy of termination of the contract (paragraph 7). However, suspension may also have a disruptive effect on the construction of the works (paragraph 12). Thus, the contractor should be able to terminate the contract if the suspension or cumulative suspensions exceed a specified period (paragraph 14). The purchaser should also be accountable to the contractor for any losses suffered by the contractor, such as costs of rented equipment which are maintained at the site and costs incurred as a consequence of the postponement of the completion of the works (paragraph 12). The contractor should be entitled to an extension of time reasonably commensurate with the suspension period for the completion of works (paragraph 11).

With regard to the contractor, it may be advisable to give him a right of suspension in two circumstances. First, the contractor may be given the right to suspend construction as an alternative to the more drastic remedy of termination in cases where a failure of obligation by the purchaser is serious enough to justify unilateral termination on the part of the contractor (paragraph 16). The second instance is when a failure of performance on the part of the purchaser affects the construction of the works so as to make it unreasonable for the contractor to proceed with the construction (paragraph 17).

The parties may wish to consider whether the exercise of the right to suspend by the contractor for failure of performance by the purchaser should be conditioned upon a written notice being given to the purchaser requiring him to perform within a specified time. However, when a failure of obligation on the part of the purchaser makes it necessary to suspend the construction immediately, the contractor should be permitted to do so by giving written notice of suspension to the purchaser (paragraph 18).

\* \* \*

### A. General remarks

1. This chapter deals with situations where the purchaser<sup>1</sup> may order suspension of the construction of

<sup>1</sup>Where reference is made to the purchaser, it should be noted that such a reference includes the engineer or any person to whom the purchaser has delegated his authority. If the engineer is to exercise an independent function, including the power of ordering suspension and settling ancillary matters, this power should be expressly conferred on him in the contract (see chapter XVII, "Consulting engineer").

works for convenience or on specified grounds and where the contractor may suspend the construction due to a failure of performance by the purchaser.

2. In view of the fact that no developed doctrine of suspension exists in most legal systems, it is important for parties to consider the nature of suspension, the circumstances in which suspension may be invoked and the legal effects of suspension.

3. Suspension may also occur in other contexts, and this is considered elsewhere in the Guide. In cases of exempting impediments, it may be necessary, as a practical measure, to provide for automatic suspension of the obligation to construct the works (see chapter XXXII, "Exemptions"). Where the contractor invokes a hardship clause the contract may be suspended by the mutual agreement of the parties (see chapter XXXIV, "Hardship clauses").

4. A distinction should be made with an order by the purchaser to the contractor to stop construction of work which is defective. Although both suspension and stoppage of construction involve a temporary interruption of construction, the legal effects of such interruptions are different. Stoppage of defective construction may occur where the purchaser orders the contractor to stop using defective materials for the construction of the works. The contractor may have to stop the construction for some time until appropriate materials are obtained. Since the obligation of the contractor to perform is not suspended, the purchaser is not liable to the contractor for losses suffered in the stoppage, and the contractor may be liable for damages resulting from delay in performance (see chapter XXX, "Failure to perform"). For the legal effects of suspension by the purchaser considered in this chapter, see section B, 3.

5. The mechanism of suspension involves a temporary interruption of the construction of the works. During suspension all construction activity to which the order of suspension relates should be temporarily interrupted. However, construction of other parts of the works not affected by the suspension should continue. As the construction is merely suspended and the contract is not terminated, the contractor is under an obligation to resume construction after the suspension period.

## B. Suspension by purchaser

### 1. Suspension by purchaser for convenience

6. The parties may wish to consider whether the purchaser, as a matter of policy, should be given the right to order suspension of the construction of the works for any reason. For example, he may wish to order suspension because of a delay in obtaining credit from a financial institution, or because of a delay in obtaining a licence for the project. He may also wish to suspend for reasons which are too delicate to be revealed. Although the scope of a suspension for convenience clause is wide, it is unlikely that the

purchaser would order suspension capriciously, both because of the high costs ensuing to him of ordering suspension (see paragraph 12, below) and because the date for completion of the works may be postponed (see paragraph 11, below).

7. If the right to order suspension were not available, the purchaser might have to resort to the more drastic remedy of termination in situations where, for the moment, he would have no other choice but to interrupt the construction (see termination for convenience in chapter XXXVIII, "Termination"). On the other hand, suspension may give him time to overcome his difficulties even though at a high cost.

### 2. Suspension on specified grounds

8. The parties may, however, wish to narrow the scope of the purchaser's right to order suspension by providing only an exhaustive list of circumstances where the purchaser may order suspension. Unlike suspension for convenience where the purchaser does not have to state his reasons, under suspension on specified grounds, the purchaser should be required to state the ground justifying the suspension. Therefore, these circumstances must be clearly specified to avoid any uncertainties in interpretation. For example, in a contract where more than one contractor is involved, the delay in construction by one contractor may make it necessary for the purchaser to suspend construction by the other contractors.

### 3. Some suggestions on contents of suspension clause

9. Provision should be made to ensure that the contractor is not prejudiced by the suspension. Certain ancillary matters such as the protection and preservation of the equipment and materials should also be dealt with in the clause. When the purchaser orders suspension, the performance of all correlative obligations of the purchaser should be automatically suspended.

10. Suspension may be either for a definite or indefinite period. The purchaser should be entitled to cease the suspension by written notice to the contractor. Although the contractor is obliged to resume construction immediately the suspension is over, the immediate resumption of the construction may sometimes be difficult as, for example, where the suspension ceases by a notice from the purchaser to that effect. The contractor, for example, may have already cancelled an order for materials because of the prior order of suspension and may have to re-order them. Therefore, the parties may wish to stipulate in the contract for a reasonable time to be given to the contractor to resume work in such cases.

11. The suspension may affect the work schedule and, in some instances, the date of completion of the works. The contractor should be entitled to an extension of time reasonably commensurate with the suspension period for the completion of the works. The contractor

should notify the purchaser in writing of the period of time he considers necessary giving detailed particulars of the need for the extension to complete the works. Any dispute as to the extension of time shall be settled by the dispute settlement mechanism provided for in the contract.

12. While the mechanism of suspension could be useful, it may also have a disruptive effect on the construction of the works. For example, if the contractor employs several subcontractors in the construction of the works, suspension may prevent him from co-ordinating their work. The financial viability of a project may also be jeopardized due to the cost of shutting down and restarting the works. The purchaser should therefore be accountable to the contractor for any losses suffered. However, the determination of the losses could be complicated. The suspension clause may, therefore, include an illustrative list of the usual types of losses in this regard. Such an itemization would also assist the purchaser in determining beforehand the financial implications should he wish to order suspension. Such losses should include costs incurred for the maintenance and protection of the works, equipment and materials; costs in demobilization of personnel and subcontractors; increased costs of equipment and materials; costs of rented equipment which are maintained at the site; costs incurred for the resumption of work; additional overhead costs; and costs incurred as a consequence of the postponement of the completion of the works (for example, the contractor may have to employ another subcontractor at a higher cost to replace the one whose contract has come to an end and who does not wish to renew his service). The clause should also obligate the parties to consult each other on how to reduce the losses.

13. An extension of time to complete the works may prevent the contractor from performing other contracts. The parties should consider whether the purchaser should be obligated to compensate the contractor for profits which the contractor was unable to earn under those contracts.

14. The parties may further agree that if the suspension extends beyond a specified period, the contractor should be entitled to terminate the contract. Extension beyond the specified period may occur either through a single suspension, or through the cumulation of periods of suspension occurring at different times, whether such periods are in respect of the same portion of the construction or different portions. This specified period should not be unduly long. Even though the purchaser is liable for certain losses suffered by the contractor, he may still be prejudiced if he is required to maintain his commitment to the project indefinitely or for a long period. The purpose of stating a specified period is to empower the contractor to terminate the contract if the suspension exceeds this period. The contract should therefore provide the contractor with an option to terminate if the suspension or cumulative suspensions exceed this period. If the contract is terminated, the termination should be regarded as on the same basis as termination for the convenience of the purchaser in

respect of the liability for loss caused by the termination (see chapter XXXVIII, "Termination").<sup>2</sup>

<sup>2</sup>*Illustrative clause*

"(1) The purchaser may at any time order suspension of the construction of the works or any portion thereof by giving written notice to the contractor specifying the construction or any portion thereof to be suspended and the effective date of suspension. The purchaser is not required to state his reasons for the suspension. The suspension shall not affect the validity of the contract."

or

"(1) The purchaser may at any time on any of the grounds specified in the contract order suspension of the construction of the works or any portion thereof. He shall give written notice to the contractor specifying the construction or any portion thereof to be suspended and state the grounds for the suspension and the effective date of suspension. The suspension shall not affect the validity of the contract.

"(2) The contractor shall interrupt the construction or any portion thereof, from the effective date of suspension specified in the notice or as soon as possible. However, he shall continue to perform the unsuspended portion of the construction, if any.

"(3) When the construction of the works or any portion thereof is suspended, the performance of all correlative obligations of the purchaser shall automatically be suspended, and the purchaser shall not be obliged to perform such obligations during the period of suspension.

"(4) The contractor shall take necessary measures needed for the protection and preservation of the equipment and materials on the site during the suspension or, if the purchaser wishes to take such measures, shall inform the purchaser what measures should be taken by him. During the period of suspension, the contractor shall not remove from the site any of the equipment or materials without the consent of the purchaser.

"(5) Suspension may be either for a definite or indefinite period. Subject to paragraph (9), of this clause, the contractor shall resume construction of the suspended construction immediately, or, if that is not possible, within a reasonable time after the suspension ceases whether by the expiry of the specified period or by a written notice from the purchaser. The purchaser shall also resume the performance of his correlative obligations.

"(6) The contractor shall be entitled to an extension of time reasonably commensurate with the period of suspension for the completion of the works. The contractor shall notify the purchaser in writing of the extended period of time he considers necessary giving detailed particulars of the need for the extension to complete the works. Any dispute as to the extension of time shall be settled by [the dispute settlement mechanism provided for in the contract].

"(7) The purchaser shall pay the contractor compensation for any losses suffered by the contractor. Such losses shall include in particular the following: costs incurred for the maintenance and protection of the works, equipment and materials; costs in demobilization of personnel and subcontractors; increased costs of equipment and raw materials; costs of rented equipment which is maintained at the site; costs incurred for the resumption of work; additional overhead costs; and costs incurred as a consequence of the postponement of the completion of the works. The parties shall consult each other regularly during the period of suspension on how to reduce the losses.

"(8) The purchaser shall not be liable to compensate the contractor for profits which the contractor was unable to earn under contracts which he was unable to perform as a result of the extended time needed to complete the works due to the suspension.

"(9) If the suspension or cumulative suspensions continue for a period exceeding [ ] days, the contractor is entitled to terminate the contract, and he is entitled to be compensated as in the case of termination of the contract for convenience by the purchaser for loss caused by the termination. Such cumulative suspensions shall consist of the totality of the periods of suspension occurring at different times, whether such periods are in respect of the same portion of the construction or different portions of construction."

15. The right of suspension for convenience should not be available to the contractor as he is in an entirely different position from that of the purchaser. The contractor is engaged by the purchaser to construct the works and he should complete it despite difficulties, financial or otherwise. Even where there is a failure of performance by the purchaser, it should in principle not be possible for the contractor to resort to suspension, as other remedies, such as damages, would ordinarily be adequate to compensate him for such failure. There are, however, two situations in which suspension may serve a useful function (see paragraphs 16 and 17, below).

### C. Suspension by contractor

16. First, the contractor may be given the right to suspend construction as an alternative to the more drastic remedy of termination in cases where a failure of obligation by the purchaser is serious enough to justify unilateral termination on the part of the contractor. An example where suspension might be used as a remedy is a case of non-payment of a contract sum due from the purchaser. Such non-payment may be considered serious enough to justify termination. The parties may wish to provide for the option of suspension as a possible means of exerting pressure for performance before the contractor exercises the right of termination (see chapter XXXVIII, "Termination").

17. The second instance is when the failure of performance on the part of the purchaser affects the construction of the works or a portion thereof so as to make it unreasonable to proceed with the construction. For example, where the purchaser supplies a defective design and construction based on it endangers the safety of the works or the personnel, it may be necessary for the contractor to suspend the construction until the design is rectified.

18. The parties may wish to consider whether the exercise of the right to suspend should be conditioned upon the contractor giving notice to the purchaser to perform within a specified time the obligation which he has failed to perform. If so, the suspension would only be effected if the purchaser does not comply with the request within the time specified. If, however, a failure of performance on the part of the purchaser makes it necessary to suspend the construction immediately, the contractor should be permitted to do so by giving written notice of the suspension to the purchaser.

19. It would not be practical to require the contractor to specify the suspension period because such suspension should last as long as the failure of obligation of the purchaser persists. However, when the purchaser performs his obligation, the contractor should resume construction immediately or, if that is not possible, within a reasonable time.

20. With regard to the contractor's entitlement to an extension of time for the completion of the works and

the purchaser's obligation to compensate the contractor for losses because of the suspension, see paragraphs 11 and 12, above, respectively. The resort by the contractor to suspension should not deprive him of any other remedies he may have under the contract.<sup>3</sup>

[A/CN.9/WG.V/WP.11/Add.9]

### Format of the legal guide

#### *Introduction*

1. At the fourth session of the Working Group on the New International Economic Order, suggestions were made relating to the format of the legal guide on drawing up international contracts for the construction of industrial works.<sup>1</sup> This note has been prepared in order to assist the Working Group in its consideration of these suggestions and other aspects of the format of the legal guide.

2. At the previous session of the Working Group it was suggested that the guide should be of practical value for at least two categories of persons involved in the negotiation and drafting of works contracts, i.e. lawyers who are involved in actual negotiation and

#### *<sup>3</sup>Illustrative clause*

"(1) Subject to paragraphs (2) and (3) of this clause, the contractor may suspend the construction of the works or any portion thereof when the purchaser fails to perform an obligation which justifies the termination of the contract, or when the failure of performance on the part of the purchaser affects the construction of the works or any portion thereof so as to make it unreasonable to proceed with the construction. The suspension shall not affect the validity of the contract.

"(2) Where the contractor intends to suspend the construction of the works or any portion thereof due to a failure of performance by the purchaser, the contractor shall give the purchaser notice in writing informing him of the failure of performance justifying suspension and requiring him to perform within a specified time. If the purchaser fails to perform within the specified time, the contractor may suspend the construction of the works or any portion thereof immediately by giving written notice of the suspension to the purchaser.

"(3) If, however, a failure of performance on the part of the purchaser makes it necessary to suspend the construction of the works or any portion thereof immediately, the contractor may do so by giving written notice of the suspension to the purchaser.

"(4) The suspension may last as long as the failure to perform the obligation persists. However, it shall in any event come to an end when the purchaser performs his obligation, and the contractor shall resume construction of the suspended construction immediately or, if that is not possible, within a reasonable time. The contractor shall give written notice to the purchaser of the resumption of the construction.

"(5) Identical to footnote 2, paragraph (6).

"(6) Identical to footnote 2, paragraph (7).

"(7) The resort by the contractor to suspension shall not deprive him of any other remedies he may have under the contract."

<sup>1</sup>A/CN.9/234, paras. 15, 16, 25-28 (Yearbook 1983, part two, IV, A).

drafting, and businessmen or administrators who are responsible for initiating and carrying through a project. In order to enhance the practicality of the legal guide, the Working Group may wish to consider the elements of the format discussed below. In addition, it may be noted that the secretariat will consider the appropriate positioning of a glossary and consolidated index to the guide.

### I. Chapter summaries

3. As requested by the Working Group, sample summaries have been included in the draft chapters which have been prepared for the current session.<sup>2</sup> Summaries could serve the needs of businessmen or administrators who need to be aware of the principal issues to be covered by a particular type of contract clause, but who do not require a discussion of the issues in the depth or detail contained in the text of a chapter. For such persons the summaries could set forth the principal issues which should be covered by a clause and the main solutions recommended in the text of the chapter. It is, of course, the lawyers involved in negotiating and drafting the contract for whom the chapter text itself is intended.

4. If the Working Group considers that summaries are useful, it may wish to consider whether they should appear at the beginning or at the end of each chapter. A reader of a chapter may be assisted in understanding the interrelationship among the issues and solutions discussed in the chapter by being presented with a summary of such issues and solutions before he reads the text of the chapter. By the inclusion in the summary of references to paragraphs in the chapter where such items and solutions are discussed, the summary could also assist the reader in locating in the chapter particular issues which are of interest to him. If such a summary is provided at the beginning of a chapter the Working Group may wish to consider whether a table of contents such as that described in paragraph 10, below, would be unnecessary.

5. On the other hand, a summary at the end of the chapter may provide a useful means of enabling one who has read the text to synthesize the information contained in it. Such a summary could also operate in the nature of a check-list of points to be dealt with in the course of negotiating or drafting a works contract. However, if a check-list is provided at the end of each chapter (see paragraph 8, below), a summary at that location may not be needed.

6. Summaries, may, however, have certain disadvantages. In the first place, the attempt to compress the often sophisticated discussion in the text of the chapter for the purposes of a summary may lead to a summary which does not adequately reflect the difficulties in the subjects dealt with. Furthermore, because of the simplification which has to be achieved for the purposes of a

summary, it may contain little that businessmen or administrators in the industrial sector of a country do not already know.

7. If the Working Group were to consider that summaries are not useful, it may wish to consider whether an outline of the contents of each chapter could be included immediately after the title of a chapter and before the main text commences. This approach is sometimes adopted in the "Licensing Guide for Developing Countries" of the World Intellectual Property Organization (WIPO).<sup>3</sup> Such an outline may make unnecessary a table of contents for the chapter (see paragraph 10, below).

### II. Check-list

8. The Working Group may wish to consider the desirability of providing a check-list at the end of each chapter. It could be helpful to lawyers, businessmen and administrators to have a check-list of the issues which should be dealt with in the clauses discussed in each chapter. The check-list could provide references to paragraphs in the chapter where a point mentioned in the check-list is discussed. In addition, cross-references to related matters in other chapters could assist the user of the guide in achieving necessary co-ordination among various provisions and clauses of the contract being negotiated or drafted. Such a check-list could also assist the reader of a chapter in synthesizing information which he has obtained from the chapter.

9. The Working Group may wish to consider whether it might be preferable to provide check-lists instead of summaries or a table of contents at the beginning of each chapter. Check-lists could serve the same purposes as summaries (i.e. to indicate the principal issues to be covered by a clause and the main solutions recommended, and to synthesize information). In addition, because of the concise, telegraphic style in which check-lists can be drafted, it may be possible both to deal with the issues in less space than would be taken by a summary, and also to focus the reader's attention on an issue in a more pointed manner.<sup>4</sup>

<sup>3</sup>The following example of such an outline is the heading to section D of "Part III: Explanatory notes and examples" of the WIPO Guide:

#### "D. SCOPE OF THE LICENCE OR AGREEMENT

"(Identification of the technology necessary for the manufacture of the product or the application of the process or for some other given purpose; description of the technology in terms of time or by reference to specified documentation or designated expertise; rights conferred under the law of industrial property and laws applicable to the use, disclosure and communication of know-how; field of use or activity for which the invention, the industrial design, the know-how, or the trademark may be applied; specification of the territory of manufacture, use or sale; exclusivity and non-exclusivity; acquisition or use of competing technology)."

<sup>4</sup>The WIPO Guide contains a check-list, in addition to outlines of the contents of each chapter (see footnote 3, above). Check-lists are also used in *Guidelines for Contracting for Industrial Projects in Developing Countries* (United Nations publication, Sales No. E.75.II.B.3) and in the *Guide for Drawing up International Contracts on Consulting Engineering, Including some Related Aspects of Technical Assistance* (ECE/TRADE/145).

### **III. Table of contents at beginning of each chapter**

10. The Working Group may wish to consider whether, in addition to the master table of contents which will appear at the beginning of the legal guide, it would be helpful for each chapter to have its own table of contents immediately preceding the text of the chapter. Such an individual table of contents could assist the reader in obtaining a rapid overview of the issues covered by the chapter to which he has turned, as well as enable him to locate particular issues in the chapter. The individual table of contents could be identical to the master table; alternatively, it could be more detailed than the master table.

### **IV. Possible arrangements**

11. In the light of the foregoing discussion, the following arrangements of the chapters appear to be reasonable:

- (a) Outline of contents or table of contents at the beginning of each chapter, followed by the text of the chapter, followed by a check-list; or
- (b) Outline of contents or table of contents at the beginning of each chapter, followed by the text of the chapter, followed by a summary; or
- (c) Summary followed by the text of the chapter, or the text of the chapter followed by a check-list (the table of contents of each chapter being reflected in the master table of contents at the beginning of the legal guide).

### **V. Illustrative and model provisions**

12. The draft chapters prepared for the current session of the Working Group contain illustrative provisions.<sup>5</sup> The Working Group may consider such provisions to be useful as illustrations of issues referred to in the text. These provisions may also serve as examples of how certain solutions discussed in the text, particularly those that are complex or may otherwise present difficulties in drafting, might be structured.

13. The Working Group may consider it inadvisable for illustrative provisions to be drafted to illustrate every issue or represent every solution referred to in the text. Many issues and solutions may be sufficiently clear so as not to require illustration. Moreover, the text will in many cases discuss alternative, and in some cases

<sup>5</sup>As used in the chapters of the legal guide drafted thus far, the word "provision" refers to a portion or section of a contract clause which deals with a particular issue in the clause; "clause" refers to a collection of provisions which deal with a certain major topic under the contract.

conflicting, approaches and solutions. Presenting illustrative provisions for each such analysis or solution could hinder and confuse the reader, rather than assist him.

14. The Working Group may also wish to consider whether it is desirable to include model provisions in the legal guide. These are provisions which would be recommended by the Commission for actual use by parties in their contracts. There are, however, difficulties in drafting such model provisions. The content of a contract provision may depend upon the type of contract in which the provision appears, and on the subject-matter of the contract. In addition, the content may depend on the requirements of the parties with respect to a particular provision (e.g. the scope of an exemption clause may depend on the particular allocation of risks between the parties). The Working Group may therefore wish to authorize the secretariat to include model clauses only when the secretariat considers it feasible to draft such clauses.

15. If the Working Group considers illustrative or model provisions to be desirable, it may wish to consider where in the chapter they should be placed. In the draft chapters prepared for this session of the Working Group, illustrative provisions have been placed in footnotes. Another possibility is to place illustrative or model provisions in the text itself. A disadvantage to the latter approach may be that a provision appearing in the text could interrupt the progress of the reader through the discussion. Moreover, it may be necessary, for drafting reasons or for clarity, to present as a unit provisions on a particular group of issues which are discussed in various locations in the text. It would be undesirable to locate such a unit in all portions of the text in which the issues represented by the provisions are discussed. If, however, the unit is located in one place, the reader may be confused. Such a unit may, however, be located in a footnote after the conclusion of the discussion on the group of issues.

### **VI. Space for notes by users of guide**

16. The Working Group may consider it desirable for each chapter of the legal guide to include blank spaces in which the user could, for example, insert his own notes concerning points to remember, cross-references to other clauses, and rules of law applicable to the contract being negotiated or drafted. To permit notes to be taken immediately adjacent to the relevant portion of the text, it may be desirable for each page of the guide to contain extra-wide margins. As an alternative or additional method of providing space for notes, blank pages could be provided at the end of each chapter.

## IV. INTERNATIONAL TRANSPORT LAW

### A. Liability of operators of transport terminals: report of the Secretary-General (A/CN.9/252)<sup>a</sup>

#### CONTENTS

	<i>Paragraphs</i>
INTRODUCTION .....	1-4
I. SCOPE OF APPLICATION OF UNIFORM RULES.....	5-16
A. Relationship of uniform rules to international transport .....	5-10
B. Types of operators and operations to be governed by uniform rules ...	11-16
II. ISSUANCE OF DOCUMENT .....	17-26
III. STANDARD OF LIABILITY.....	27-29
IV. LIABILITY FOR DELAY.....	30-32
V. LIMIT OF LIABILITY .....	33-39
VI. LIMITATION PERIOD.....	40-41
VII. SECURITY INTEREST IN GOODS.....	42-44
VIII. ISSUES NOT DEALT WITH IN THE PRELIMINARY DRAFT CONVENTION .....	45
IX. FORM AND NATURE OF UNIFORM RULES.....	46-47
X. FUTURE WORK .....	48-49

*Annex I:* SELECTED PROVISIONS OF MAJOR INTERNATIONAL TRANSPORT CONVENTIONS

*Annex II:* TEXT OF PRELIMINARY DRAFT CONVENTION ON OPERATORS OF TRANSPORT TERMINALS<sup>b</sup>

#### INTRODUCTION

1. The Commission, at its sixteenth session, 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; *Yearbook 1983*, part two,

V, C).<sup>1</sup> That report, *inter alia*, described the work of the International Institute for the Unification of Private Law (UNIDROIT) on the liability of international terminal operators, and discussed a preliminary draft Convention on this subject which had been prepared by a UNIDROIT study group.

<sup>a</sup>For consideration by the Commission see Report, chapter IV (part one, A, above).

<sup>b</sup>Reproduced in this *Yearbook*, part two, IV, B, as a separate section.

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its sixteenth session, *Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17 (A/38/17)*, para. 109 (*Yearbook 1983*, part one, A).

2. After considering the report, the Commission decided to include the topic of liability of international terminal operators in its programme of work, to request UNIDROIT to transmit the 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 seventeenth session the decision on the composition of the Working Group. The secretariat was requested to submit to the Commission at its seventeenth session a study of important issues arising from the preliminary draft Convention, and to consider in this study the possibility of broadening the scope of the uniform rules to cover the storage and safekeeping of goods not involved in transport.<sup>2</sup>

3. UNIDROIT has transmitted to the Commission the preliminary draft Convention as adopted by the UNIDROIT Governing Council in May 1983.<sup>3</sup> The text of the preliminary draft Convention is contained in annex II to this study. The present study, prepared in response to the request of the Commission, discusses some of the major issues which arise from the preliminary draft Convention and which may merit consideration in the formulation of uniform rules on the liability of operators of transport terminals (OTTs).

4. Whether or not the application of the uniform rules is limited to operations which are directly related to international transport, it may be desirable in dealing with certain issues (e.g. the standard of liability, limit of liability, and limitation period) to keep in mind approaches which are adopted in international transport conventions. For ease of reference, a table summarizing the approaches adopted in various major international transport conventions is provided in annex I to this study.

## I. Scope of application of uniform rules

### A. Relationship of uniform rules to international transport

5. A principal reason for undertaking to unify the legal rules relating to the liability of OTTs is to fill gaps in the liability régimes left by international transport conventions.<sup>4</sup> These conventions achieve a high degree of uniformity with respect to legal rules governing the liability of carriers for loss of and damage to goods during carriage operations. However, the liability of

<sup>2</sup>*Ibid.*, para. 115.

<sup>3</sup>The preliminary draft Convention, as adopted by the Governing Council of UNIDROIT at its 62nd session in May 1983, is titled "Preliminary draft Convention on Operators of Transport Terminals" (UNIDROIT 1983, study XLIV—document 24; reproduced in this *Yearbook*, part two, IV, B). The term "operators of transport terminals" (OTTs), rather than "international terminal operators", will be used in the balance of this study.

<sup>4</sup>See A/CN.9/236, paras. 28-32 (*Yearbook 1983*, part two, V, C); also, "Explanatory report on the preliminary draft Convention on Operators of Transport Terminals" (UNIDROIT 1983, study XLIV—document 24) (hereinafter referred to as "Explanatory report") paras. 1 and 9-10 (reproduced in this *Yearbook*, part two, IV, C).

non-carrying intermediaries for loss of and damage to goods before and after carriage (which is when such loss and damage most frequently occur), as well as during carriage, remains governed by disparate legal régimes under national legal systems.<sup>5</sup> It has been considered desirable for this liability, too, to be governed by a uniform international legal régime, in order to give due protection to persons with interests in cargo, and to facilitate recourse by carriers, multimodal transport operators, freight forwarders and similar entities against intermediaries when the former are held liable for loss of or damage to goods in the custody of the intermediaries.

6. With these objectives in mind, the drafters of the UNIDROIT preliminary draft Convention restricted its application to operations of OTTs which are related to international carriage (article 2 (b)). However, it has been questioned whether such a restriction is desirable, or whether all operations of OTTs, even if they are not related to international transport, or to transport at all, should be governed by a uniform international legal régime. Within the UNIDROIT study group which prepared the preliminary draft Convention it was suggested, in favour of having the convention govern even operations of OTTs which were not related to international transport, that restricting the scope of the rules to operations related to international transport would make it difficult in some cases to determine when an OTT's operations would be governed by the Convention. For example, goods might be deposited in a terminal by a customer who had not yet determined whether they would be exported and transported internationally, or sold domestically. Even if the customer did know, it might not be known by the OTT. In such circumstances the OTT would not know whether he should take out insurance to cover his liability under the Convention.<sup>6</sup>

7. It might be considered, however, that cases in which a customer depositing goods in a terminal does not know whether they will be carried in international transport are probably not very numerous, and will occur only with respect to goods deposited before transport, rather than during or after transport. In any event, if the application of the uniform rules is to be restricted to operations of OTTs related to international transport, it might be possible to cover those situations in which the OTT does not know whether the goods will be carried in international transport, by obligating the customer to declare to the OTT that the goods are to be carried in international transport, failing which the operations of the OTT would not be governed by the uniform rules. It might also be possible to subject the operations to the uniform rules only if the OTT knew or ought to have known that the goods had been deposited with him in connection with international transport.

<sup>5</sup>See A/CN.9/236, paras. 22-27. See also Ramberg, "Liability of sea terminals—some preliminary thoughts" (International Maritime Committee, Documentation, 1975, II); and D. Hill "Preliminary report on the warehousing contract" (UNIDROIT 1976, study XLIV—document 2).

<sup>6</sup>Explanatory report, para. 33.

8. In connection with the question of whether the uniform rules should apply only to operation of OTTs which are related to international transport, it may also be noted that the safekeeping of goods which is not related to transport, or which is only remotely or tenuously related to transport, usually does not have foreign elements, and for these situations the existence of disparate rules under other national legal systems should create few problems. These transactions might continue to be governed by local law, and there may be no need for international harmonization of the legal rules applicable to them. Moreover, an attempt to unify legal rules which would also be applicable to operations of OTTs unrelated to transport or related only to transport of a purely local nature may encounter significant opposition from OTTs engaged in such operations, as well as from some States, and may unnecessarily jeopardize the international acceptance of uniform rules covering operations related to international transport.

9. If the application of the uniform rules is to be restricted to operations related to international transport, it might be considered advisable for the rules to establish the degree and nature of the relationship required in order for the rules to apply. One possible approach might be to have the rules apply only to operations of an OTT which are performed between the time when the goods are taken over by a carrier from the shipper in one State and the time when the goods are delivered to a recipient in another State. Since this would include periods during which a carrier would be responsible for the goods, this approach would protect the carrier's right of recourse against the OTT. However, under this approach the uniform rules would not apply to some situations in which uniformity in the legal rules governing the operations of OTTs might be thought to be desirable, such as the safekeeping of goods for a shipper before carriage in international transport has begun, and the safekeeping of goods at the end of international transport by an OTT to whom the goods are delivered by a carrier and who acts as agent for the recipient.

10. The preliminary draft Convention is made applicable to operations of OTTs which are "related to carriage in which the place of departure and the place of destination are situated in two different States" (article 2 (b)). The degree and nature of the relationship are not further defined, and such a formulation could give rise to questions in particular cases as to whether the Convention is applicable.

#### B. Types of operators and operations to be governed by uniform rules

11. It may be considered what types of operations performed by an intermediary should be governed by the uniform rules. The preliminary draft Convention applies to operators of transport terminals, i.e. persons acting in a capacity other than that of a carrier who undertake against remuneration the safekeeping of goods before, during or after carriage (article 1 (1)). An

OTT would be responsible for the safekeeping of goods from the time he has taken them in charge until their handing over to the person entitled to take delivery of them (article 3 (1)). During this basic period of responsibility, it appears that the OTT would be responsible for loss of or damage to the goods whether they occurred while the goods were in safekeeping, or during any other operation performed by the OTT with respect to the goods ancillary to safekeeping. In addition, if the OTT has undertaken discharging, loading or stowage of the goods even before or after the basic period of responsibility, he would be responsible for loss or damage occurring during these operations as well (article 3 (2)).

12. On the other hand, it appears that the preliminary draft Convention does not apply to an intermediary (such as a stevedore) who handles the goods before, during or after carriage, but for whom safekeeping does not constitute part of his undertaking.

13. This approach was adopted as a compromise between creating a single, unified legal régime to cover all handling operations taking place at any time before, during and after carriage, whether or not these operations were related to a primary obligation of safekeeping, and restricting such a régime to safekeeping alone. It was based on the desire to fill to the greatest extent possible the gaps left by international transport conventions, and to avoid enabling an OTT to escape the application of the Convention by claiming that the loss or damage occurred during handling operations, rather than safekeeping. It was therefore decided not to restrict the application of the preliminary draft Convention to safekeeping operations alone. On the other hand, it was considered unrealistic at the present time to create a unified régime covering all handling operations, whether or not they were related to safekeeping, and that a single régime may not be suitable for all operations.<sup>7</sup>

14. A related issue may be whether the safekeeping of goods and ancillary operations performed by a freight forwarder (i.e. an intermediary who arranges for transportation of goods for a shipper or consignee and who may perform other services in connection with the transportation) should be covered by the uniform legal rules. In this regard, a distinction may be drawn between a forwarder who acts as a principal in the transport of goods, i.e., one who, in his own name, assumes responsibility for the transport from the point of receipt of the goods to the final destination,<sup>8</sup> and one who merely arranges for transport for the shipper, by entering into a contract with the carrier either on behalf of the shipper<sup>9</sup> or on his own behalf.

15. The activities of a forwarder acting as a principal will in many cases be governed by a combined transport document such as the Combined Transport Bill of Lading issued by the International Federation of

<sup>7</sup>Ibid., paras. 36 and 37.

<sup>8</sup>"Survey of the work of international organizations in the field of transport law: report of the Secretary-General" (A/CN.9/172) paras. 59-62 (Yearbook 1979, part two, V, A).

<sup>9</sup>Ibid., paras. 54 and 55.

Freight Forwarders Associations (FIATA),<sup>10</sup> which has achieved a degree of international uniformity with respect to the liability of forwarders issuing the document. Moreover, the activities of a forwarder acting as a principal will likely be governed by the United Nations Convention on International Multimodal Transport of Goods (1980) (the "Multimodal Convention") when it comes into force.<sup>11</sup> It may therefore be unnecessary for the uniform rules to govern these activities. In this regard, it may be noted that the preliminary draft Convention specifically precludes its application to one acting as a carrier (article 1 (1)),<sup>12</sup> and that the liability of carriers is governed by other conventions.<sup>13</sup> By analogous reasoning the uniform rules might also exclude freight forwarders acting as principals, and perhaps other similar operators, such as multimodal transport operators. However, if a freight forwarder acting as a principal engages and deposits goods with an OTT during the period when the forwarder is responsible for the goods, the operations of the OTT should be governed by the uniform rules in order to preserve the forwarder's right of recourse against the OTT.

16. Where, on the other hand, the forwarder merely arranges for transport for the shipper, he may temporarily store the goods in his own premises. Such operations would not be governed by other international transport conventions. Moreover, although the safekeeping of the goods is not the primary undertaking by forwarders in such cases, safekeeping and related operations (e.g. pick-up and delivery of the goods) are sometimes the major material or physical acts performed by the forwarder (his other tasks being ministerial in nature, such as arranging for carriage and insurance, preparing and receiving shipping documents, and customs clearance), and one during which the goods could suffer actual loss or damage. It may therefore be reasonable to include within the scope of the uniform régime the safekeeping and related operations of freight forwarders who act in this capacity.

<sup>10</sup>This document has been approved by the Joint Committee on Intermodal Transport of the International Chamber of Commerce (ICC), as conforming with the ICC Uniform Rules for a Combined Transport Document.

<sup>11</sup>TD/MT/CONF.16. An exception may be when, after carriage has ended, the forwarder holds the goods in his own facility at the disposal of the consignee, and notifies the consignee of the arrival of the goods, but after a reasonable time the consignee fails to collect them. Under article 14 (2) (b) (ii) of the Multimodal Convention the responsibility of the forwarder may terminate; if so, storage would be subject to rules of national law.

<sup>12</sup>See also Explanatory report, para. 24. It should be noted that under some legal systems after a carrier unloads goods and retains them in his own storage areas and a reasonable time for collection of the goods by one entitled to receive them has elapsed, the carrier ceases to be liable for the goods as a carrier, and is liable only as a bailee. It may be questioned whether, as a consequence of the words "other than that of a carrier" in article 1 (1) of the preliminary draft Convention, a carrier whose situation under the position just described is changed to that of a bailee would be subject to the rules of the Convention. If not, it may be considered whether a carrier in such a position should be made subject to the régime applicable to OTTs.

<sup>13</sup>Pursuant to article 14, the preliminary draft Convention would be subordinate to other international conventions relating to the international transport of goods.

## II. Issuance of document

17. The issues of whether the OTT should be obligated to issue a document in respect of goods taken in charge by him, and if so, the nature and contents of the document, might be considered. Current practice in this regard varies. In some locations documents are not issued by an OTT. In those areas in which documents are issued, the contents and nature of the document, and the time of its issuance, vary considerably.<sup>14</sup>

18. It has been suggested that requiring a document in connection with international terminal operations in addition to the documents covering the carriage of the goods could be an unnecessary hindrance to the rapid movement of goods.<sup>15</sup> On the other hand, it has also been argued that there is no value in establishing a liability régime for OTTs if no document is to be available to prove that the goods have actually been taken in charge.<sup>16</sup> In addition, a document serving as a receipt for goods taken in charge by an OTT may be useful in connection with claims for loss of or damage to the goods. A document could also be useful in connection with obtaining finance against the goods. This is particularly true in international trade, where it is not uncommon for a seller to ship goods to a foreign warehouse, and for either the seller or a buyer to obtain financing against the goods.

19. The drafter of the preliminary draft Convention chose to require the OTT to issue a document only upon request of the customer (article 4 (1)), on the ground that the need for the document would vary according to the circumstances.<sup>17</sup>

20. With regard to the question whether the document should be negotiable, the UNIDROIT study group which prepared the preliminary draft Convention was unsure of the commercial need for a negotiable document. The next provides that the document may be negotiable if the parties so agree and the applicable law so permits (article 4 (4)).<sup>18</sup>

21. Arguments against requiring the OTT to issue a negotiable document include the following. There are many cases in which it is not necessary for the document to be negotiable. The existence of a negotiable transport document may in some cases obviate the need for a negotiable OTT document. The problem of fraud in connection with negotiable transport documents is becoming increasingly serious, and the widespread issuance of negotiable OTT documents could add to this problem. Difficulties could arise if two documents of title for the same goods were to be in effect at the

<sup>14</sup>Explanatory report, para. 41 (reproduced in this Yearbook, part two, IV, C).

<sup>15</sup>Ibid., para. 40.

<sup>16</sup>Ibid., para. 41.

<sup>17</sup>Ibid., para. 42.

<sup>18</sup>This provision was included by UNIDROIT merely for the purpose of stimulating discussion on the issue of negotiability, as the UNIDROIT study group which prepared the preliminary draft Convention felt that it did not have sufficient information to take a final decision on the issue (*ibid.*, para. 46).

same time. There is a growing body of opinion that the speed of modern international transport makes negotiable transport documents, and the costs, time and risks associated with them, unnecessary, and makes non-negotiable documents preferable.<sup>19</sup> In some cases a negotiable document can impede the flow of goods out of a terminal. An example is when goods deposited together are to be released at different times or to different persons. With a non-negotiable document, goods could be released against orders executed by the party to whom the document has been issued.

22. On the other hand, in order to accommodate those situations in which the customer needs or wants a negotiable document, it may be appropriate to require the OTT to issue a negotiable document when the customer requests one (compare article 4 (4) of the preliminary draft Convention).

23. If the uniform rules were to provide for a negotiable document, it might be desirable for provisions to be included dealing with various issues arising from the negotiability of the document, such as the position of a good-faith transferee of the document who relies on an erroneous description of the goods in the document, and an adjustment of rights of a good-faith transferee with the rights of a person entitled to the goods under a transport document.

24. If the OTT is obligated to issue a document, it might also be considered desirable for the uniform rules to specify a time-limit within which he must do so. If the OTT were to be obligated to issue a document in all cases, the time-limit might begin to run from the time he has taken over the goods. The preliminary draft Convention does not specify a time-limit within which the document must be issued.

25. It might also be considered whether it would be desirable for the uniform rules to provide sanctions for a failure of the OTT to issue a document within the time allowed, or whether the consequences of such a failure should be left to existing rules of national law. Possible sanctions might include the payment of compensation to the customer for losses incurred by him due to the OTT's failure, or a presumption that the goods were received by the OTT in good condition or as claimed by the customer. The preliminary draft Convention does not provide for sanctions in the event of a failure of the OTT to issue a document.

26. As to the contents of the document, the preliminary draft Convention requires the document to be dated, to acknowledge receipt of the goods, and to state the date on which the goods were taken in charge by

the OTT (article 4 (1)). The document need not itself indicate the quantity or condition of the goods; however, it must indicate "any inaccuracy or inadequacy of any particular concerning the description of the goods taken in charge as far as this can be ascertained by reasonable means of checking" (article 4 (2)). The document is given *prima facie* evidentiary effect (article 4 (3)). It may be considered whether the document should also indicate the quantity, condition and other relevant particulars concerning the goods, insofar as these can be reasonably ascertained by the OTT. Where a container is used, an OTT will often be unable to examine goods inside the container which has been deposited with him. In such cases, his obligation might be therefore limited to indicating the condition of the container.

### III. Standard of liability

27. Various approaches may be adopted with respect to the standard of liability to which an OTT should be subject. If the operations of an OTT are related to transport, one approach could be to impose on the OTT the same standard of liability as the standard which governs the transport to which the operations are related. Although this approach would facilitate the carrier's right of recourse against the OTT, it could lead to differences in the standards of liability applicable to OTTs whose operations are related to different modes of transport. Moreover, such an approach would be difficult to apply when carriage is effected by two or more different modes of transport.

28. Another approach could be to establish a single standard of liability to apply to all operations of OTTs covered by the uniform rules, regardless of whether they are related to a particular mode of transport. This approach would have the advantage of uniformity. This is the approach adopted by the preliminary draft Convention. The standard adopted is presumed fault (article 6), following the régime under the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg) ("Hamburg Rules"),<sup>20</sup> and the Multimodal Convention (see annex I, *infra*).

29. The following considerations may be relevant to the question of whether this or some other standard may be appropriate. First, the evidence and the means of determining the circumstances relating to loss of or damage to the goods are likely to be within the control of the OTT. It may therefore be appropriate for him to bear the burden of proving that the loss or damage was not due to his fault, rather than requiring the claimant to prove that the loss or damage resulted from the fault of the OTT. Second, the presumed fault standard is the lowest standard employed in most of the major existing international transport conventions (including those not yet in force) (see annex I). If the uniform rules were to adopt a lower standard than this, recourse by carriers

<sup>19</sup>"Co-ordination of work: international transport documents: report of the Secretary-General" (A/CN.9/225), paras. 68-76 (*Yearbook 1982*, part two, VI, B). For mechanisms designed to overcome problems associated with the use of non-negotiable sea-way bills instead of negotiable bills of lading, and in connection therewith the simplification of documents and the role of automatic data processing and other techniques, see *ibid.*, paras. 74-76.

<sup>20</sup>*Official Records of the United Nations Conference on the Carriage of Goods by Sea* (United Nations publication, Sales No. E.80.VIII.1) (*Yearbook 1978*, part three, I, B).

against OTTs would not be fully assured.<sup>21</sup> Third, since in some modes of transport other than carriage by sea it is customary for carriers to store goods in their own facilities, rather than to employ OTTs, the uniform rules will more frequently apply to OTT operations connected with carriage by sea, or with multimodal transport, than to operations connected with other modes of transport. It may therefore be appropriate to employ in the uniform rules governing the operations of OTTs the same standard as that applicable to carriage by sea and multimodal transport. Also for this reason, a standard more strict than presumed fault might be excessive for the purpose of assuring recourse against OTTs by carriers who would principally be affected by the uniform rules.

#### IV. Liability for delay

30. It may be considered whether the uniform rules should deal with the liability of an OTT for delay in handing over the goods. The preliminary draft Convention does not deal with the liability of the OTT for delay, on the ground that the question of delay is relevant essentially to the movement of goods, rather than to stationary goods such as those deposited in a terminal.<sup>22</sup> On the other hand, the operations to be covered by the uniform rules will in any event include those connected with the transport of goods; the question of delay may therefore be relevant from the points of view both of the person entitled to receive the goods and the carrier. The intended recipient of goods in transport will be affected by a delay in an OTT's handing them over (either to a carrier for transport or to the intended recipient) just as he would be by a delay in the transport itself. Under international transport conventions a carrier is responsible for delay in delivery, and he may be liable even if the delay was that of an OTT. The question of the delay of an OTT may therefore be relevant to the carrier from the point of view of his recourse against the OTT if the carrier is held liable for delay.

31. The preliminary draft Convention does, however, provide that if an OTT does not hand over goods within 60 days following a request by the person entitled to receive them, the goods may be treated as lost (article 6 (2)).<sup>23</sup> This would apparently give a claimant a choice as to whether to claim for loss of the goods, which would be governed by the Convention and its limitation of liability, or to claim for delay under national law.

<sup>21</sup>This may be illustrated by the following: a carrier is liable to a shipper upon the basis of presumed fault (such as under the Hamburg Rules or the Multimodal Convention). Goods are damaged while in the custody of an OTT but within the period of the carrier's responsibility for the goods. The standard of liability applicable to the OTT is ordinary negligence, which must be proved by the claimant. In such a case the carrier may be held liable to the shipper or consignee under his stricter standard of liability but his recourse action against the OTT may fail due to an inability to prove that the OTT was negligent.

<sup>22</sup>Explanatory report, para. 55.

<sup>23</sup>Comparable to the Hamburg Rules, article 5 (3).

32. If the uniform rules do not deal with the issue of delay, it will be governed by other rules of national law, under which the liability of an OTT for consequential damages may be extensive, or perhaps by general conditions, which might severely restrict an OTT's liability for delay and thus prejudice recovery by a person entitled to receive the goods and recourse by a carrier. Consideration might therefore be given as to whether the uniform rules should impose liability on an OTT for delay in handing over the goods, and whether they should establish a financial limit to this liability.<sup>24</sup>

#### V. Limit of liability

33. One feature of the preliminary draft Convention that was thought by some members of the UNIDROIT study group to constitute an inducement to OTTs to agree to the higher standard of liability under the Convention is as a limit of liability that would be difficult to break.<sup>25</sup> The limit in the preliminary draft Convention is 2.75 units of account per kilogramme (article 7).<sup>26</sup>

34. Assuming that the uniform rules are to contain financial limits to liability for loss of or damage to the goods, it may be considered whether the limit used in the preliminary draft Convention is appropriate, or whether some other limit should be used. It may be noted, for example, that this limit is lower than limits established in some international transport conventions (see annex I). The preliminary draft Convention adopts the limit contained in the Multimodal Convention<sup>27</sup> because this limit was considered to be the most recent expression of the will of the international community.<sup>28</sup> A further justification for the adoption of this limit might be that the safekeeping of goods in transport by an entity which is not a carrier or an analogous entity (e.g. multimodal transport operator or freight forwarder acting as a principal) may most often occur before, during or after carriage by sea or multimodal transport. It may therefore be appropriate to key the limits of liability of an OTT to the limits to which carriers in these modes of transport would be subject. Adopting the 2.75 units of account limit would enable full recourse against OTTs by carriers subject to the Multimodal Convention, as well as those subject to the

<sup>24</sup>See Hamburg Rules, article 6 (1) (b); Multimodal Convention, article 18 (4).

<sup>25</sup>Explanatory report, para. 13.

<sup>26</sup>The preliminary draft Convention incorporates the unit of account provision (defining the unit of account as the Special Drawing Right of the International Monetary Fund) (article 13), and the expedited procedure for revising the limits of liability (article 17), which were recommended by the Commission at its fifteenth session (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)*, para. 63; *Yearbook 1982*, part one, A). The unit of account provision and two alternative provisions recommended by the Commission for revising limits of liability (i.e. the expedited revision procedure, and revision in accordance with changes in a price index) have also been recommended by the General Assembly for use in international conventions containing limit of liability provisions (resolution 37/107 of 16 December 1982; *Yearbook 1982*, part one, D).

<sup>27</sup>Multimodal Convention, article 18 (1).

<sup>28</sup>Explanatory report, para. 59.

Hamburg Rules and the International Convention for the Unification of Certain Rules of Law relating to Bills of Lading ("Hague Rules") (both under the original Convention and as amended), which impose lower limits of liability.

35. Like a carrier under the Hamburg Rules and a multimodal transport operator under the Multimodal Convention,<sup>29</sup> under the preliminary draft Convention the OTT could agree to higher limits (article 7 (3)). An ability of the OTT to agree to increase his limits to those to which the carrier is subject would protect the ability of the carrier to obtain full compensation from the OTT in a recourse action. It has been suggested, however, that this possibility could make the uniform rules less attractive to OTTs, since they could be subjected to pressure from shipping companies to agree to higher limits.<sup>30</sup>

36. The question may be considered whether, and if so under what circumstances, the limit of liability may be broken. The preliminary draft Convention subjects the OTT to damages in full if the loss or damage "resulted from an act or omission of the OTT done with the intent to cause such loss or damage, or recklessly and with knowledge that such loss or damage would probably result" (article 9 (1)).

37. The liability limits under the Hamburg Rules and the Multimodal Convention are breakable only in the event of the wilful misconduct or recklessness of the carrier.<sup>31</sup> In favour of such an approach it has been suggested that as a general rule insurance carriers prefer limits that are difficult to break, since this enables them to assess their risks accurately and calculate reasonable premiums. This implies that relatively unbreakable limits may result in premiums that are somewhat lower than they would be with easily breakable limits. It has also been suggested that relatively unbreakable limits would be an inducement to OTTs to accept a standard of liability which is more stringent than that to which they are accustomed.<sup>32</sup>

38. In connection with the limit of liability it might further be questioned whether, in addition to the per-kilogramme limit, a total limit of liability per event should be incorporated in the uniform rules. Such a limit may be appropriate for covering cases of excessive damage (e.g. caused by fire or explosion) against which it would be difficult or expensive to insure. If such an approach is adopted it might be desirable for the uniform rules to provide a means of apportioning the available recovery among the various claimants, in the event the total of the damages to which they would be entitled under the per-kilogramme limit exceed the maximum.

<sup>29</sup>Hamburg Rules, article 6 (4); Multimodal Convention, article 18 (6).

<sup>30</sup>Explanatory report, para. 60.

<sup>31</sup>Hamburg Rules, article 8. See also *Official Records of the United Nations Conference on the Carriage of Goods by Sea* (United Nations publication, Sales No. E.80.VIII.1) part II, Summary records of the First Committee, 34th meeting, para. 24; Multimodal Convention, article 21.

<sup>32</sup>Explanatory report, para. 62.

39. It might also be considered whether, as an alternative to the per-kilogramme limit, the uniform rules should include a per-package limit, as do the Hamburg Rules and the Multimodal Convention.<sup>33</sup> An argument against including the per-package limit has been that the goods may arrive in a terminal in the form of a single package, and then be broken up to be transported further to separate destinations.<sup>34</sup>

## VI. Limitation period

40. The limitation period for bringing an action under the preliminary draft Convention is two years from the day on which the goods are handed over by the OTT, or from the time when they may be treated as lost (see paragraph 31, above) (article II). In determining whether this period is appropriate, it may be relevant to consider that it is equal to the periods within which actions must be brought against carriers under the Hamburg Rules and the Multimodal Convention, and is longer than the limitation periods applicable to carriers under other international transport conventions (see annex I). It should be noted, however, that the two-year period applicable to an action against an OTT may in some cases bar a recourse action by a carrier or a multimodal transport operator against an OTT. For example, when goods are handed over by an OTT to a carrier or a multimodal transport operator during transport, the limitation period applicable to an action by a cargo interest against the carrier or multimodal transport operator would commence at the end of the transport; the limitation period applicable to a recourse action by the carrier or multimodal transport operator against the OTT would commence earlier, i.e. when the goods are handed over to the carrier or multimodal transport operator by the OTT. With both types of action subject to the same limitation period, the recourse action against the OTT would be barred before the action against the carrier or multimodal transport operator. It may be considered whether the limitation period in the uniform rules should contain a provision which effectively preserves the ability of a carrier or a multimodal transport operator to bring such a recourse action.

41. The preliminary draft Convention does not deal with the question of interruption or suspension of the limitation period or other related issues.<sup>35</sup> For example, in some legal systems, rules of national law may be applied if the uniform rules are silent as to these issues. In other legal systems the silence of the uniform rules could be interpreted to mean that the limitation period may not be interrupted or suspended, notwithstanding the existence of national legal rules. From the point of view of uniformity in the application of the limitation

<sup>33</sup>Hamburg Rules, article 6 (1); Multimodal Convention, article 18 (1).

<sup>34</sup>Explanatory report, para. 58.

<sup>35</sup>For identification of these issues, see, e.g., Convention on the Limitation Period in the International Sale of Goods (New York, 1974), *Official Records of the United Nations Conference on Prescription (Limitation) in the International Sale of Goods* (United Nations publication, Sales No. E.74.V.8) (Yearbook 1974, part three, I, B).

period, it may be desirable for the uniform rules either to provide detailed rules for the operation of the limitation period, or to provide that these related issues are to be resolved in accordance with national legal rules.

## VII. Security interests in goods

42. The preliminary draft Convention grants the OTT a security interest in goods taken in charge by him for his costs and claims relating to the goods, including the right to retain the goods and the right to sell them to satisfy his claims (article 5).

43. If these rights are exercised by an OTT, they may conflict with and interfere with the rights of the person entitled to receive the goods. It might be considered whether this is an appropriate result. For example, in cases where an OTT engaged by a carrier retains the goods until the carrier pays the OTT's charges, the carrier may be liable for damages to the person entitled to receive the goods. This may constitute sufficient protection to that person. However, when an OTT sells the goods to satisfy his claim against the carrier for unpaid charges, the carrier's liability to pay damages may not constitute adequate protection to the person entitled to receive the goods. On the other hand, if such rights of retention and sale are exercised by an OTT who is engaged by, or acts as agent for, the person entitled to receive the goods, it may not be inappropriate for him to suffer the consequences of the retention or sale, since the claims of the OTT leading to such actions (e.g. non-payment of storage fees) will usually be the responsibility of that person himself. Moreover, it may be noted that such cases will in any event usually occur outside the period of the carrier's responsibility.

44. In connection with conflicts such as these it may be noted that article 14 of the preliminary draft Convention provides, "This Convention does not modify any rights or duties which may arise under any international Convention relating to the international carriage of goods". Another approach might be to leave such matters to national law.

## VIII. Issues not dealt with in the preliminary draft Convention

45. In addition to the question of whether the uniform rules should deal with the liability of an OTT for delay in handing over the goods, a number of other issues relevant to the operations and liability of OTTs are not dealt with in the preliminary draft Convention. These include, for example, the obligations of a customer, such as his obligation to pay the charges of the OTT, and to inform the OTT as to the nature of hazardous goods or instruct him relative to their safekeeping. Nor does it deal with the right of the OTT to dispose of dangerous goods. The preliminary draft Convention also does not deal with the liability of an OTT for his failure to accept goods for safekeeping under a contract with a customer. The intention of the drafters of the

preliminary draft Convention was to produce an outline draft establishing a minimum set of rules governing essentially the liability of OTTs. They anticipated that omitted details, such as those just referred to, could be included in the text at a later stage or, alternatively, could be regulated by standard conditions which could be prepared by an interested commercial organization.<sup>36</sup> In this regard, it may be noted that the International Maritime Committee has been preparing a set of standard conditions to be used by OTTs. The UNCITRAL secretariat has been in contact with the International Maritime Committee and has informed it of the decisions taken by UNCITRAL at its sixteenth session with respect to the topic of the liability of OTTs.

## IX. Form and nature of uniform rules

46. The current great disparity in legal rules governing the liability of OTTs arises from rules of national law, as well as from general conditions employed by OTTs which may not be consistent with the interests of parties under modern commercial conditions. Uniformity in this area might be achieved by providing for uniformity in national law through a convention or model law, and by requiring general conditions to be consistent with these uniform rules. Even if the uniform rules were non-mandatory (see paragraph 47, below), the existence of a formal legal framework could constitute an increased incentive to OTTs to follow them. It could also legitimize provisions of general conditions which are consistent with the uniform rules. This would benefit both customers of OTTs and OTTs themselves, since general conditions alone, even if they were substantially unified, might otherwise be contrary to mandatory rules of national law, and since advantages to OTTs under such unified general conditions (e.g. limits of liability) might otherwise run the risk of being struck down by courts in some legal systems.

47. Another issue is whether the uniform rules contained in a convention or model law should be made applicable to all OTTs within the State which is a party to the convention or which enacts the model law. Within the UNIDROIT study group that prepared the preliminary draft Convention, the view was expressed that if the uniform rules were mandatorily applicable to all OTTs within a State it might be difficult for States to overcome the pressure of professional interests not to adhere to the text. A suggestion was therefore made that States which wished to do so might be permitted to apply the uniform rules only to OTTs who undertook to be bound by them. Those favouring this view considered that under such an approach OTTs could be induced to "opt-in" to the uniform régime by certain incentives, such as a moderate liability régime, a limit to liability which would be difficult to break, a lien over goods deposited with the OTT, and the reduced likelihood that general conditions which conform to the rules would be struck down by a court. However, it was decided not to complicate the preliminary draft Con-

<sup>36</sup>Explanatory report, para. 20.

vention at its present stage by including an "opting-in" provision, but rather to present the uniform rules without prejudice as to the ultimate form which the text would assume.<sup>37</sup> It is submitted that the Commission might also wish to defer its decision on the ultimate form the uniform rules should take until after the working group which will be entrusted with the work of preparing draft texts finalizes its work, at which time the Commission may be in a better position to decide on the matter in the light of developments surrounding the project.

## X. Future work

48. With respect to the procedure to be followed in the elaboration of uniform rules, one approach may be

<sup>37</sup>*Ibid.*, para. 13.

for the working group to which the work is assigned first to review the UNIDROIT preliminary draft Convention with the need in mind to take decisions on the approaches to be adopted with respect to issues discussed in this study, and then to proceed to the preparation of a draft set of uniform rules on the basis of a draft which the secretariat might be requested to prepare after such decisions have been taken.

49. With respect to the working group to which the work should be assigned, it may be noted that the Working Group on International Contract Practices has recently completed its work on a model law on international commercial arbitration, and would be available to commence work on the liability of OTTs in the third quarter of 1984. The working group may be expected to be able to proceed with its work expeditiously, and perhaps complete a set of draft uniform rules during the course of 1985.

## ANNEX I

### Selected provisions of major international transport Conventions

Convention	Standard of liability	Limit of liability for loss of or damage to goods (per kilogramme)*	Limitation period
<i>Carriage by sea</i>			
International Convention for the Unification of Certain Rules of Law relating to Bills of Lading (1924) ("Hague Rules")	Based on duties and immunities in articles 3 and 4; broadly, a duty of reasonable care	No per-kilogramme limit: 100 pounds sterling per package or unit (article 4 (5))	1 year (article 3 (6))
Hague Rules as amended by Protocol done at Brussels on 23 February 1968 ("Hague/Visby Rules")	Essentially as Hague Rules, above	30 Poincaré francs (article 4 (5) (a))	1 year (article 3 (6))
Protocol amending the International Convention for the Unification of Certain Rules of Law Relating to Bills of Lading, 25 August 1924, as amended by the Protocol of 23 February 1968 (1979) (not yet in force)	Not applicable	2 units of account (SDR) (non-IMF members which cannot apply SDR provision may fix limit at 30 monetary units (1 monetary unit equal to 1 Poincaré franc)) (article II)	Not applicable
United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg) ("Hamburg Rules") (not yet in force)	Carrier liable unless he proves that he, his servants or agents took "all measures that could reasonably be required to avoid the occurrence and its consequences" (article 5 (1))	2.5 units of account (SDR) (article 6 (1)) (non-IMF members which cannot apply SDR provision may fix limit at 37.5 monetary units (1 monetary unit equal to 1 Poincaré franc)) (article 26)	2 years (article 20)

<i>Convention</i>	<i>Standard of liability</i>	<i>Limit of liability for loss of or damage to goods (per kilogramme)*</i>	<i>Limitation period</i>
<i>Carriage by air</i>			
Convention for the Unification of Certain Rules relating to International Carriage by Air (1929) ("Warsaw Convention")	Carrier liable (article 18 (1)): (a) unless he proves he and his agents have taken "all necessary measures to avoid the damage or that it was impossible for him or them to take such measures" (article 20 (1)), or (b) unless he proves that the damage was occasioned by negligent pilotage, negligence in handling of aircraft or in navigation, and that in all other respects he and his agents have taken all necessary measures to avoid the damage (article 20 (2))	250 Poincaré francs (article 22 (2))	2 years (article 29)
Warsaw Convention as amended by Protocol done at The Hague on 28 September 1955	Warsaw Convention standard "(a)", above, only (article 20)	250 Poincaré francs (article 22 (2))	2 years (article 29)
Montreal Protocol No. 4 to amend the Warsaw Convention as amended by the Protocol done at The Hague on 28 September 1955 (1975) (not yet in force)	Carrier liable unless he proves that destruction, loss or damage resulted solely from inherent defect etc., defective packing by one other than carrier, his servants or agents, act of war or armed conflict, or act of public authority in connection with entry exit or transit of cargo (article IV)	17 SDRs (non-IMF members which cannot apply SDR provision may fix limit at 250 monetary units (1 monetary unit equal to 1 Poincaré franc)) (article VII)	Not applicable
<i>Carriage by road</i>			
Convention on the Contract for the International Carriage of Goods by Road (CMR) (1956)	Carrier liable (article 17 (1)) unless he proves loss or damage caused by wrongful act or neglect of claimant, by instructions of claimant not resulting from wrongful act or neglect of carrier, by inherent vice, or through "circumstances" which the carrier could not avoid and the consequences of which he was unable to prevent" (article 17 (2)); or unless he proves that loss or damages arose from an enumerated special risk (article 17 (4)) (generally loss or damage is rebuttably presumed to have arisen from a special risk if carrier establishes it could have so arisen (article 18))	25 Germinal francs (article 23 (3))	1 year; 3 years if wilful misconduct (article 32)
Protocol to the Convention on the Contract for the International Carriage of Goods by Road (CMR) (1978)	Not applicable	8.33 units of account (SDR) (non-IMF members which cannot apply SDR provision may fix limit at 25 monetary units (1 monetary unit equal to 1 Germinal franc)) (article 2)	Not applicable
<i>Carriage by rail</i>			
Agreement concerning the International Carriage of Goods by Rail (SMGS) (1966)	Carrier liable unless he proves that loss or damage resulted from circumstances he could not avoid or consequences of which he could not prevent or unless they resulted from other enumerated circumstances (article 22)	Price of goods or declared value (articles 24, 25)	9 months (article 30)
International Convention concerning the Carriage of Goods by Rail (CIM) (1970)	Essentially same as CMR Convention, above (articles 27, 28)	50 Germinal francs (articles 31 (1), 33)	1 year; 2 years if wilful misconduct, fraud, others (article 47)

<i>Convention</i>	<i>Standard of liability</i>	<i>Limit of liability for loss of or damage to goods (per kilogramme)*</i>	<i>Limitation period</i>
Complementary provision concerning method of conversion of gold franc under the CIM Convention (1977)	Not applicable	3 francs = 1 SDR	Not applicable
Appendice B à la Convention relative aux transports internationaux ferroviaires (COTIF) du 19 Mai 1980 (not yet in force)	Same as CIM Convention, above (articles 36, 37)	17 units of account (SDR) (articles 40 (2), 42) (for non-IMF members which cannot apply SDR provision the unit of account equals 3 Germinal francs) (article 7)	Same as CIM Convention (article 58)
<i>Multimodal transport</i>			
United Nations Convention on International Multimodal Transport of Goods (1980) ("Multimodal Convention") (not yet in force)	Essentially same as Hamburg Rules, above (article 16)	2.75 units of account (SDR) (article 18 (1)) (non-IMF members which cannot apply SDR provision may fix limit at 41.25 monetary units (1 monetary unit equal to 1 Poincaré franc)) (article 31)	2 years (article 25)

\*The Poincaré franc referred to in this column consists of 65 1/5 milligrammes of gold of millesimal fineness 900; the Germinal franc consists of 10/31 of a gramme of gold of millesimal fineness 900. The relative values of these units is therefore approximately 1 Germinal franc = 5 Poincaré francs. Most of the Conventions listed in this chart, either in the Conventions themselves or in Protocols, contain equivalences between these units and the SDR; in general, 1 SDR = 15 Poincaré francs or 3 Germinal francs. For cases in which these provisions do not apply (e.g. to a State which is a party to a Convention but not to the Protocol which contains the provision) there is no international agreement on the method of converting the Poincaré or Germinal franc into national currencies. This has led to disparities in the conversion of liability limits expressed in these units.

## ANNEX II

For the text of annex II see the following section B.

## B. Text of preliminary draft Convention on Operators of Transport Terminals<sup>a</sup> (A/CN.9/252, annex II)

### *Preamble*

THE STATES PARTIES TO THE PRESENT CONVENTION,

HAVING RECOGNIZED the desirability of determining by agreement certain rules relating to the rights and duties of operators of transport terminals and in particular to their liability;

HAVE DECIDED to conclude a Convention for this purpose and have thereto agreed as follows:

### *Article I*

#### DEFINITIONS

For the purposes of the application of this Convention:

(1) "Operator of a transport terminal (OTT)" means any person acting in a capacity other than that of a carrier, who undertakes against remuneration the safe-keeping of goods before, during or after carriage, either by agreement or by taking in charge such goods from a shipper, carrier, forwarder or any other person, with a view to their being handed over to any person entitled to take delivery of them.

<sup>a</sup>UNIDROIT 1983, study XLIV, document 24.

(2) "Goods" includes any container, pallet or similar article of transport or packaging, if not supplied by the OTT.

### *Article 2*

#### SCOPE OF APPLICATION

This Convention applies whenever the operations for which the OTT is responsible are:

(a) performed in the territory of a Contracting State, and

(b) related to carriage in which the place of departure and the place of destination are situated in two different States.

### *Article 3*

#### PERIOD OF RESPONSIBILITY

(1) The OTT shall be responsible for the safe-keeping of goods from the time he has taken them in charge until their handing over to the person entitled to take delivery of them.

(2) If the OTT has undertaken to perform or to procure performance of discharging, loading or stowage of the goods, even before their taking in charge or after their being handed over, the period of responsibility shall be extended so as to cover such additional operations also.

### *Article 4*

#### ISSUANCE OF DOCUMENT

(1) The OTT shall, at the request of the other party to the contract issue a dated document acknowledging receipt of the goods and stating the date on which they were taken in charge.

(2) Such a document shall indicate any inaccuracy or inadequacy of any particular concerning the description of the goods taken in charge as far as this can be ascertained by reasonable means of checking.

(3) Such a document is *prima facie* evidence of the contract for the safekeeping of goods and the taking in charge of the goods as therein described.

(4) The document issued by the OTT may, if the parties so agree, and the applicable national law so permits, contain an undertaking by the OTT to deliver the goods against surrender of the document. A provision in the document that the goods are to be delivered to the order of a named person or to order, or to bearer, constitutes such an undertaking.

(5) Nothing in this Convention shall prevent the issuing of documents by any mechanical or electronic means, if not inconsistent with the law of the place where the document is issued.

### *Article 5*

#### SECURITY RIGHTS IN THE GOODS

(1) The OTT shall have a right of retention over the goods he has taken in charge for costs and claims relating to such goods, fees and warehousing rent included. However, nothing in this Convention shall affect the validity under national law of any contractual arrangements extending the OTT's security in the goods.

(2) The OTT shall not be entitled to retain the goods he has taken in charge if a sufficient guarantee for the sum claimed is provided or if an equivalent sum is deposited with a mutually accepted third party or with an official institution in the State where the operations for which the OTT is responsible under this Convention are performed.

(3) The OTT may, after giving timely and adequate notice, sell or cause to be sold all or part of the goods retained by him so as to obtain the amount necessary to satisfy his claim.

### *Article 6*

#### BASIS OF LIABILITY

(1) The OTT is liable for loss resulting from loss of or damage to the goods for which he is responsible under this Convention, unless he proves that he, his servants or agents took all measures that could reasonably be required to avoid the occurrence which caused the loss or damage, and its consequences.

(2) If the OTT does not hand over the goods at the request of the person entitled to take delivery of them within a period of 60 consecutive days following such request, the person entitled to make a claim for the loss of the goods may treat them as lost.

(3) Where fault or neglect on the part of the OTT, his servants or agents combines with another cause to produce loss or damage the OTT is liable only to the extent that the loss or damage is attributable to such fault or neglect, provided that the OTT proves the amount of the loss or damage not attributable thereto.

### *Article 7*

#### LIMIT OF LIABILITY

(1) The liability of the OTT for loss resulting from loss of or damage to goods according to the provisions of article 6 is limited to an amount equivalent to 2.75 units of account per kilogramme of gross weight of the goods lost or damaged.

(2) Unit of account means the unit of account mentioned in article 13.

(3) The OTT may, by agreement, increase the limits of liability provided for in paragraph 1 of this article.

**Article 8****NON-CONTRACTUAL LIABILITY**

(1) The defences and limits of liability provided for in this Convention apply in any action against the OTT in respect of loss of or damage to goods caused by any act or omission within the scope of the OTT's obligations provided for under this Convention, whether the action is founded in contract, in tort or otherwise.

(2) If such an action is brought against a servant or agent of the OTT, such servant or agent, if he proves that he acted within the scope of his employment, is entitled to avail himself of the defences and limits of liability which the OTT is entitled to invoke under this Convention.

(3) Except as provided in article 9, the aggregate of the amounts recoverable from the OTT and from any person referred to in paragraph 2 of this article shall not exceed the limits of liability provided for in this Convention.

**Article 9****LOSS OF THE RIGHT TO LIMIT LIABILITY**

(1) The OTT is not entitled to the benefit of the limitation of liability provided for in article 7 if it is proved that the loss or damage resulted from an act or omission of the OTT done with the intent to cause such loss or damage, or recklessly and with knowledge that such loss or damage would probably result.

(2) Notwithstanding the provisions of article 8, paragraph 2, a servant or agent of the OTT is not entitled to the benefit of the limitation of liability provided for in article 7 if it is proved that the loss or damage resulted from an act or omission of such servant or agent, done with the intent to cause such loss or damage, or recklessly and with knowledge that such loss or damage would probably result.

**Article 10****NOTICE OF LOSS OR DAMAGE**

(1) Unless notice of loss or damage, specifying the general nature of such loss or damage, is given in writing to the OTT not later than the working day after the day when the goods were handed over to the person entitled to take delivery of them, such handing over is *prima facie* evidence of the delivery by the OTT of the goods as described in the document issued by the OTT or, if no such document has been issued, in good condition.

(2) Where the loss or damage is not apparent, the provisions of paragraph 1 of this article apply correspondingly if notice in writing is not given within 15 consecutive days after the day when the goods were handed over to the person entitled to take delivery of them.

(3) If the state of the goods at the time they were handed over to the person entitled to take delivery of them has been the subject of a joint survey or inspection, notice in writing need not be given of loss or damage ascertained during such survey or inspection.

(4) In the case of any actual or apprehended loss or damage the OTT and the person entitled to take delivery of the goods must give all reasonable facilities to each other for inspecting and tallying the goods.

**Article 11****LIMITATION OF ACTIONS**

(1) Any action under this Convention is time-barred if judicial or arbitral proceedings have not been instituted within a period of two years.

(2) The limitation period commences on the day on which the OTT has handed over the goods or part thereof or, in cases where no goods have been handed over, on the last day of the period referred to in article 6, paragraph 2.

(3) The day on which the limitation period commences is not included in the period.

(4) The person against whom a claim is made may at any time during the running of the limitation period extend that period by a declaration in writing to the claimant. This period may be further extended by another declaration or declarations.

(5) Provided that the provisions of another applicable international convention are not to the contrary, a recourse action for indemnity by a person held liable under this Convention may be instituted even after the expiration of the limitation period provided for in the preceding paragraphs if instituted within the time allowed by the law of the State where proceedings are instituted; however, the time allowed shall not be less than 90 days commencing from the day when the person instituting such action for indemnity has settled the claim or has been served with process in the action against himself.

**Article 12****CONTRACTUAL STIPULATION**

(1) Any stipulation in a contract for the safekeeping of goods concluded by an OTT or in any document evidencing such a contract is null and void to the extent that it derogates, directly or indirectly, from the provisions of this Convention. The nullity of such a stipulation does not affect the validity of the other provisions of the contract or document of which it forms a part.

(2) Notwithstanding the provisions of paragraph 1 of this article, the OTT may, by agreement, increase his responsibilities and obligations under this Convention.

*Article 13*

## UNIT OF ACCOUNT AND CONVERSION

(1) The unit of account referred to in article 7 of this Convention is the Special Drawing Right as defined by the International Monetary Fund. The amounts mentioned in article 7 are to be expressed in the national currency of a State according to the value of such currency at the date of judgment or the date agreed upon by the parties. The equivalence between the national currency of a Contracting State which is a member of the International Monetary Fund and the Special Drawing Right is to be calculated in accordance with the method of valuation applied by the International Monetary Fund in effect at the date in question for its operations and transactions. The equivalence between the national currency of a Contracting State which is not a member of the International Monetary Fund and the Special Drawing Right is to be calculated in a manner determined by that State.

(2) The calculation mentioned in the last sentence of paragraph 1 is to be made in such a manner as to express in the national currency of the Contracting State as far as possible the same real value for amounts in article 7 as is expressed there in units of account. Contracting States must communicate to the Depositary the manner of calculation at the time of signature or when depositing their instrument of ratification, acceptance, approval or accession and whenever there is a change in the manner of such calculation.

*Article 14*

## OTHER CONVENTIONS

This Convention does not modify any rights or duties which may arise under any international convention relating to the international carriage of goods.

*Article 15*

## INTERPRETATION OF THE CONVENTION

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

(2) Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based, or in the absence of such principles, in

conformity with the law applicable by virtue of the rules of private international law.

*Article Y*

## REVISION OF THE LIMITATION AMOUNTS AND UNIT OF ACCOUNT

(1) The Depositary shall convene a meeting of a Committee composed of a representative from each Contracting State to consider increasing or decreasing the amounts in article 7:

(a) Upon the request of at least [ ] Contracting States; or

(b) When five years have passed since the Convention was opened for signature or since the Committee last met.

(2) If the present Convention comes into force more than five years after it was opened for signature, the Depositary shall convene a meeting of the Committee within the first year after it comes into force.

(3) Amendments shall be adopted by the Committee by a [ ] majority of its members present and voting.

(4) Any amendment adopted in accordance with paragraph 3 of this article shall be notified by the Depositary to all Contracting States. The amendment shall be deemed to have been accepted at the end of a period of [6] months after it has been notified, unless within that period not less than [one-third] of the States that were Contracting States at the time of the adoption of the amendment by the Committee have communicated to the Depositary that they do not accept the amendment. An amendment deemed to have been accepted in accordance with this paragraph shall enter into force for all Contracting States [12] months after its acceptance.

(5) A Contracting State which has not accepted an amendment shall nevertheless be bound by it, unless such State denounces the present Convention at least one month before the amendment has entered into force. Such denunciation shall take effect when the amendment enters into force.

(6) When an amendment has been adopted by the Committee but the [6] month period for its acceptance has not yet expired, a State which becomes a Contracting State to this Convention during that period shall be bound by the amendment if it comes into force. A State which becomes a Contracting State to this Convention after that period shall be bound by any amendment which has been accepted in accordance with paragraph 4.

### C. Explanatory report on the preliminary draft Convention on the Liability of Operators of Transport Terminals prepared by the secretariat of UNIDROIT: note by the secretariat<sup>a</sup>

#### I. Background to the preliminary draft Convention

1. It was in 1960 that the subject of bailment and warehousing contracts first appeared in UNIDROIT's Work Programme. It had been included therein in the context of combined transport operations since it was here that the lack of uniform rules for the liability of those persons into whose custody goods are entrusted, whether before, during or after the transport operation or operations, had made itself particularly felt. A preliminary report on this aspect of the topic was submitted by Professor Le Gall<sup>1</sup> in 1966 and the Governing Council of UNIDROIT requested the Secretariat to conduct an enquiry among Governments and the appropriate organisations for the purpose of assessing their interest in the subject and of giving greater precision to its scope.

2. The outcome of these enquiries led the Secretariat to the conclusion that a large amount of information assembled by other organisations was becoming available and that the gap mentioned in the preceding paragraph was being fully brought out during the revision work on the 1924 Convention on bills of lading within UNCTAD and UNCITRAL. In fact, during this work some countries, in particular developing countries, suggested that a study should be made of the liability of independent contractors used by maritime carriers, especially warehousemen and storekeepers. A wish was, therefore, expressed by some Governments that UNIDROIT resume its study of the subject and at its 53rd session, held in Rome in February 1974, the Governing Council decided to instruct the Secretariat to update Professor Le Gall's report.

<sup>a</sup>This study was made available to the Commission at its seventeenth session, together with the preliminary draft Convention, but was not reproduced as an UNCITRAL document until later, in time for the eighth session of the Working Group on International Contract Practices (A/CN.9/WG.II/WP.52/Add.1).

The text of the "Explanatory report" was introduced in these terms:

"The mandate of the Working Group in connection with the formulation of uniform rules on the liability of operators of transport terminals is to base its work, *inter alia*, on the Explanatory Report, which has been prepared by the Secretariat of UNIDROIT, on the UNIDROIT preliminary draft Convention on this subject.<sup>1</sup> Copies of the Explanatory Report, which has been issued by UNIDROIT in English and French only, were made available to the Commission at its seventeenth session. As noted in the preliminary agenda for the current session of the Working Group (A/CN.9/WG.II/WP.51), copies in those languages will also be made available at the session of the Working Group. In addition, for the convenience of member States and observers and their representatives, the text of the Explanatory Report,<sup>2</sup> in one of the two languages in which it was issued by UNIDROIT, is contained in the annex hereto.

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its seventeenth session, *Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 17* (A/39/17), para. 113 (reproduced in this Yearbook, part one, A).

<sup>2</sup>The Explanatory Report is contained in UNIDROIT Document 1983, Study XLIV—Doc. 24, pp. 9-35."

<sup>a</sup>I.U.D.P. 1966—Etude: XLIV—Doc. 1.

3. In accordance with these instructions, the Secretariat commissioned a preliminary report on the warehousing contract from the late Dr. Donald J. Hill of the Queen's University, Belfast.<sup>3</sup> Dr. Hill outlined his report to the Council at its 55th session, held in September 1976, and the Council instructed the Secretariat to transmit the report to Governments and to the organisations concerned with a request for observations on the desirability and feasibility of preparing uniform rules in this connection.

4. The bulk of the observations received<sup>4</sup> favoured continuance of work by UNIDROIT and at its 56th session held in May 1977 the Governing Council decided to set up a Study Group, the composition of which should reflect a balance between States with different economic and legal systems and also between the various modes of transport, to draw up uniform rules on the warehousing contract.

5. The Study Group held three sessions under the chairmanship of Professor Kurt Grönfors (Sweden), member of the Governing Council of UNIDROIT.<sup>5</sup> At the first session,<sup>6</sup> held in Rome from 10 to 12 April 1978, the Group had before it Dr. Hill's preliminary report, as well as the analysis of the replies to the enquiry conducted by the Secretariat. On the basis of this documentation, the Study Group gave lengthy consideration to such questions as the nature of a possible future instrument on the warehousing contract, the scope of the operations to be covered by it, the obligations of the warehouseman and the liability regime to which he should be subject, including rules on limitation of liability, the obligations of the customer, the warehouseman's lien etc. On many points a wide measure of agreement emerged and, in accordance with the instructions of the Group, the Secretariat prepared the text of a preliminary draft Convention on the liability of international terminal operators<sup>7</sup> which was considered by the Study Group at its second session, held in Rome from 23 to 26 January 1979.<sup>7</sup>

6. In the course of this session, the Study Group substantially amended the text elaborated by the Secretariat and instructed the latter to prepare an explanatory report for submission, together with the revised text of the preliminary draft Convention, to the Governing Council.

<sup>1</sup>Study XLIV—Doc. 2. UNIDROIT 1976. This report is also reproduced in the Uniform Law Review 1978, 1, 55.

<sup>2</sup>Analysed in UNIDROIT 1977, Study XLIV—Doc. 3.

<sup>3</sup>For the participants in the three sessions of the Study Group, see the Annex hereto.

<sup>4</sup>For the report, see UNIDROIT 1978, Study XLIV—Doc. 4.

<sup>5</sup>UNIDROIT 1978, Study XLIV—Doc. 5.

<sup>6</sup>The report on this session is contained in UNIDROIT 1979, Study XLIV—Doc. 13.

7. At its 58th session (September 1979) the Council decided to transmit the text of the preliminary draft Convention to Governments and to the interested international organisations with a request for observations. Replies were received from fifteen Governments and from four international organisations, most of which expressed keen interest in the UNIDROIT initiative. A consolidated document setting out these observations<sup>8</sup> was submitted to the Study Group at its third session, held in Rome from 19 to 21 October 1981.<sup>9</sup> In the light of these comments a substantial number of amendments were made to the text of the preliminary draft Convention, the revised version of which (Study XLIV—Doc. 14) was, in accordance with a decision of the Governing Council taken at its 61st session in April 1982, submitted to organisations for a final round of observations.

8. These observations were considered by a restricted group of members of the Council, chaired by Professor Grönfors, which met on 2 and 3 May 1983 in Rome. The text of the preliminary draft Convention on operators of transport terminals as drawn up by this group was approved by the Governing Council on 4 May 1983 in the course of its 62nd session.

## II. General considerations

9. In embarking upon the preparation of uniform rules governing the warehousing contract, the scope of which was subsequently extended to deal with other operations carried out by modern terminal operators, the UNIDROIT Study Group recognised from the outset that its task was one of particular difficulty, the complexity of the problem having already been clearly illustrated in Dr. Hill's preliminary report. Not only was there the distinction between long-term and transit warehousing but in addition customs and practices differed widely among warehousemen and terminal operators, not only as regards the conduct of their operations but also in respect of the liability regime applied. Then again, unlike carriage operations, warehousing was a sphere of activity which had been left almost exclusively within the province of national regulation and it was to be feared that there might be opposition to the introduction of rules designed to bring about uniformity.

10. Notwithstanding these difficulties, a general feeling prevailed that there was a need for the introduction of uniform rules relating to the safekeeping of goods, especially in the context of international carriage. This latter subject had, to a very large extent, been regulated by international Conventions and yet, paradoxically perhaps, the most frequent cases of damage to, or loss of, goods could be proved statistically to occur before and after transport operations. In these circumstances it seemed important to try to fill in the gaps in the liability regime left by the existing international trans-

port law Conventions and to ensure the availability of a recourse action to the carrier or the multimodal transport operator against non-carrying intermediaries such as the warehouseman or terminal operator.

11. Given these premises, the majority of the Group was of the opinion that it would be desirable to limit the application of the future instrument to international operations as it was felt that unification of domestic law, where there are substantial differences in conceptual approach between different legal systems, might be an unrealistic goal at the present time. A consequence of this conclusion was the decision to deal only with the safekeeping of goods linked to international carriage, as it is this dynamic element alone which would permit the delimitation of the scope of the preliminary draft Convention in such a way as to exclude from its application purely domestic operations as well as long-term warehousing *per se*. It was further agreed that the future instrument should be applicable irrespective of the mode, or modes, of transport preceding or following the safekeeping, although in this connection some of the written observations from States and interested organisations indicated that such a Convention might be of less relevance to the safekeeping of goods in connection with carriage by road and rail and one member of the Group suggested that if it were finally decided to adopt a fully mandatory Convention, then it might be wise to consider attempting to delimit its scope of application more strictly, for example by restricting it to operations related to carriage by certain modes of transport only.

12. Although the regulation of international warehousing operations was seen as the main objective of the preliminary draft Convention, the Study Group recognised at the same time that modern terminal operators often undertake a number of services associated with the handling of goods, such as loading, stowage and unloading, and while there was little support for the idea of extending the scope of the future instrument to cover the performance of such operations in all cases, and thus to regulate what might be termed the "contrat de transit", it was nevertheless agreed that to the extent that the operator who undertakes the safekeeping of goods also undertakes to perform or to procure the performance of such operations, he should be liable in the same way and on the same basis as he would be in the performance of his obligation to ensure the safekeeping of the goods.

13. Another question which was the subject of lengthy discussion by the Group was that of the character of the future instrument. While some members argued in favour of a Convention of a traditional nature, the provisions of which would be of a mandatory character, others considered that it might be difficult to overcome the pressure of the professional interests involved on States not to adopt such a Convention and a number of compromise solutions were considered. That enjoying most support was one whereby those States which wished to do so might apply the provisions of the future instrument to all terminals operating in their territory whereas others might make a declaration to the effect

<sup>8</sup>UNIDROIT 1981, Study XLIV—Doc. 10.

<sup>9</sup>The report on this session is contained in UNIDROIT 1981, Study XLIV—Doc. 13.

that they would give effect to the rules relating to the operators of transport terminals contained in the Convention only in respect of those operators who expressly or impliedly undertook to apply the rules. Those pleading in favour of this semi-mandatory solution considered that the voluntary acceptance of the minimum rules by operators might be obtained if the Convention were to contain a number of incentives such as a moderate liability regime based on that of the Hamburg Rules, a limitation on liability which could be broken only in highly exceptional circumstances, the granting of a wide lien over the goods, a short prescription period, and above all the fact that the insertion of those rules in general conditions would be recognised by the courts of Contracting States, whereas they might otherwise be exposed to the risk of being struck down in the face of the growing pressure of consumer and users' lobbies. In the opinion, however, of the restricted group of members of the Governing Council which finalised the text of the preliminary draft Convention, it would be preferable to avoid undue complication at this stage of the elaboration of the uniform rules, the final form of which could not be foreseen at present. The uniform rules are therefore presented as a preliminary draft Convention, as is customary in UNIDROIT, but without prejudice to the ultimate form which the instrument containing them will assume.

14. As to the general structure of the preliminary draft Convention, it may be stated that it is built around the concept of the "operator of a transport terminal (OTT)", who is defined in Article I as "any person acting in a capacity other than of a carrier, who undertakes against remuneration the safekeeping of goods before, during or after carriage, either by agreement or by taking in charge such goods from a shipper, carrier, forwarder or any other person, with a view to their being handed over to any person entitled to take delivery of them".

15. For the uniform rules to apply, however, Article 2 lays down two further requirements, namely that the operations for which the OTT is responsible are performed in the territory of a Contracting State and that they are related to carriage in which the place of departure and the place of destination are situated in two different States, thus providing the international element referred to above in paragraph 11.

16. Article 3 lays down the general statement of the responsibility of the OTT in respect of the performance of his obligations for the safekeeping of the goods and also indicates the period during which he shall be liable. Paragraph 2 of the article extends the responsibility of the OTT to the time before the taking in charge of the goods or after their handing over in respect of operations of discharging, loading or stowage of the goods which the OTT has undertaken to perform or the performance of which he has procured.

17. Two key articles of the preliminary draft are Articles 4 and 5. Article 4 is concerned with the issuance by the OTT of a dated document acknow-

ledging receipt of the goods and stating the date on which they were taken in charge. Such a document, however, need only be issued if requested by the other party to the contract for the safekeeping of the goods. Article 5, which is modelled to a certain extent on corresponding provisions of the UNIDROIT draft Convention on the hotelkeeper's contract, deals with the OTT's rights of retention and sale over goods.

18. Articles 6 to 15 of the preliminary draft Convention are based in very large measure on corresponding provisions of the Hamburg Rules and of the Geneva Convention of 1980 on International Multimodal Transport of Goods (hereafter referred to as "the Geneva Convention") and this is true especially of the basic liability regime (presumed fault with the burden of proof reversed) and the rules governing limitation of liability, availability of defences, loss of the right to limit liability, notice of loss, prescription and nullity of stipulations contrary to the provisions of the Convention. As regards the question of the unit of account the draft contains the text of the model provisions worked out by UNCITRAL (Article 13) while Article 14 provides that the Convention does not modify any rights or duties which may arise under any international Convention relating to the international carriage of goods.

19. During the final revision of the text, the restricted group of members of the Governing Council reached the conclusion that it would be premature at this stage to insert a set of draft final clauses although it considered that it would be desirable to include a provision, Article Y, relating to the revision of the limitation amounts and unit of account and based on the UNCITRAL model.

20. It is necessary to realise that the preliminary draft Convention does not deal with a number of important aspects of contracts concluded by OTTs. In particular, it is silent on the question of the customer's obligation such as those of paying the price for the services and, in the event of his tendering dangerous goods to the OTT for handling or safekeeping, that of giving the necessary instructions. Neither does it deal with the OTT's right to dispose of or to sell dangerous goods nor with the obligations of the person tendering the goods for safekeeping or of the OTT to take them in charge when a contract for their safekeeping has been concluded in advance. It is, in effect, an outline draft concerned essentially with establishing a set of minimum rules governing essentially the liability of OTTs, and many points of detail have been omitted which might be included at a later stage or alternatively regulated by standard conditions which, if a need for them were to be recognised, might be prepared by the interested commercial organisations such as the CMI, the ICC, and International Association of Ports and Harbours (IAPH). Other organisations might wish to co-operate in this task but what was considered essential was to avoid any incompatibility between such conditions and the prospective Convention on operators of transport terminals.

### III. Article by article commentary on the preliminary draft Convention

#### *Article 1*

21. The text adopted by the Governing Council contains only two definitions of terms which recur throughout the preliminary draft Convention, although it should be noted that the first of these definitions, that of the "operator of a transport terminal (OTT)" to some extent determines the scope of application of the future instrument. For the purposes of the Convention the OTT is defined as "any person, acting in a capacity other than that of a carrier, who undertakes against remuneration the safekeeping of goods before, during or after carriage, either by agreement or by taking in charge such goods from a shipper, carrier, forwarder or any other person, with a view to their being handed over to any person entitled to take delivery of them".

22. Now, it will readily be seen that this definition of a legal figure, the OTT, not only contains a description of his primary obligations, that of "the safekeeping of goods . . . with a view to their being handed over to any person entitled to take delivery of them" and of the capacity in which he acts, that is, "other than [in] that of a carrier", but that it also specifies the safekeeping of goods with which the preliminary draft Convention is concerned, namely that which occurs "before, during or after carriage" as well as the manner in which the OTT undertakes such safekeeping, that is to say "either by agreement or by taking [the goods] in charge". In these circumstances it would seem desirable to examine in detail the constituent elements of the definition, which to a large extent reflects the whole philosophy underlying the preliminary draft Convention.

23. In the first place then, why speak of "an operator of a transport terminal" rather than of a warehouseman in English and of an "exploitant de terminal de transport" instead of an "entrepositaire" in French? The reason for the choice of terminology is that, on the one hand, it was felt that the very concept of a "warehouse", with its implication of shelter, was becoming increasingly outmoded as new techniques of storing goods are developed and, on the other, that in view of the decision to hold the operator liable in certain cases in respect of the performance of handling services which would not normally have been entrusted to the traditional warehouseman (see below, paragraph 35 et seq.), it could be positively misleading to use the terms "warehouseman" or "entrepositaire", the latter of which has fairly strict connotations in some legal systems. Moreover, warehousing unconnected with carriage operations was not dealt with by the draft. It was therefore deemed advisable to seek a more neutral term and the growing use of the concept of "terminal" in a number of modes of transport was seen as militating in favour of the expression "operator of a transport terminal".

24. Some criticism was levelled by members of the Group and in governmental observations at the language used in Article 1, paragraph 1, in particular in relation

to the circumscribing of the OTT's obligation of safekeeping under the prospective Convention to the period "before, during or after carriage" and it was in particular suggested that the words "during . . . carriage" might be taken as referring to the carrier's obligations in respect of the goods during actual carriage. It has however been pointed out that such an interpretation cannot stand alongside Article 14 and that the clear intention of the drafters must be to cover cases of safekeeping during transshipment and not the carriage itself. To make the matter absolutely clear however the Study Group decided to introduce at the beginning of paragraph 1 the words "acting in a capacity other than that of a carrier".

25. The view was also expressed by one participant in the work of the Study Group that, as a rule, and in particular in the case of carriage by sea, the cargo would be covered by an insurance policy against all risks from warehouse to warehouse. Provided that such insurance had been taken out, the customer would not be interested in the liability regime applicable to the warehouse where the goods were stored, whether this be a port terminal or a state warehouse such as a customs warehouse. He feared therefore that the end result of the exercise would be to increase costs by duplicating insurance cover of goods. The future instrument should therefore, he argued, deal with warehousing operations *per se* and not concentrate on those occurring between different legs of a transport operation, for otherwise there was a danger of impinging upon the activities of freight forwarders and combined transport operators.

26. To this it was replied that while insurance considerations were most certainly of importance, the fact could not be overlooked that at the UNCITRAL Conference for the adoption of the Hamburg Rules the view had prevailed that the determination of the liability regime should precede the consideration of insurance questions. Moreover, if one were to argue that it is the exclusive function of cargo insurance to cover the gaps left by the international transport Conventions, one might equally well ask why it was thought desirable to lay down mandatory rules governing the carriage operations themselves. Finally, as already mentioned above, statistics seemed to show that most cases of damage to, or loss of, goods arise before, and more especially after, carriage, at least in the maritime sector, and in this connection stress was laid on the need to secure the availability of an effective right of recourse to carriers who have extended their liability beyond the period of actual carriage itself, especially under modern container contracts, and to other persons, including freight forwarders and combined transport operators, against intermediaries handling the goods such as terminal operators.

27. This view was shared by the majority of the Group, who also considered that if the definition of the OTT were to contain a clear statement of his principal obligations, namely the safekeeping of the goods and their handing over to any person entitled to take delivery of them, it would not be necessary to define the contract for the safekeeping of goods. This approach

was reinforced once the Group had agreed that the OTT should, in certain cases, also be responsible, under the terms of Article 3, paragraph 2 of the preliminary draft Convention, for the performance of other services associated with the handling of the goods, as the performance of such services could not be regarded as falling within the traditional scope of warehousing operations.

28. As mentioned above in paragraph 22 of this explanatory report, the definition of the OTT also indicates the manner in which he assumes the obligation of safekeeping of the goods and, although it was recognised that in a great majority of cases the contract would be concluded by his physically taking the goods in charge, it was agreed that logic dictates that reference should first be made to the situation in which an agreement is concluded for the safekeeping of the goods prior to their taking in charge, without prejudice to the theoretical question of whether taking in charge itself constitutes an agreement. In this connection the Group also rejected a proposal the effect of which would have been to clarify the cases in which a person could be deemed to be an OTT for the purposes of the prospective Convention by deleting the words "or by taking in charge such goods" and by introducing a provision to the effect that the operator would only be considered to be an OTT where a special agreement was concluded to that effect. Such a sweeping restriction, it was considered, would deprive the Convention of much of its importance by removing from its scope of application one of the commonest situations arising in practice.

29. Two other points should be mentioned in connection with the definition of the OTT. The first of these is that the words "against remuneration" indicate that the future Convention should only apply to operations conducted by operators acting for reward and hire, the word "remuneration" having been chosen in preference to "payment" to make it clear that consideration does not necessarily consist in the payment of a sum of money. As to a statement of the customer's obligation to pay the price for the services provided by the OTT, the Group felt however that it would be desirable to leave this to be regulated in the context of the operator's general conditions.

30. The last aspect of the definition of an OTT calling for comment is the reference to the persons from whom the OTT takes the goods in charge, namely the "shipper, carrier, forwarder or any other person", a formula which recognises the central position of the OTT in the context of the movement of goods and the variety of factual situations in which he may be called upon to act.

31. The second definition, that of "goods" in paragraph 2 of Article 1, is based on that to be found in Article 1, paragraph 7 of the Geneva Convention, and was chosen in preference to the lengthier formula contained in Article 1, paragraph 5 of the Hamburg Rules.

### *Article 2*

32. This article is concerned with the geographical scope of application of the Convention. Paragraph (a) recognizes the essentially "static" nature of the operations performed by the OTT, as opposed to the dynamic character of transport which involves the movement of goods, and it consequently provides that the connecting factor for the application of the Convention is that the operations for which the OTT is responsible are performed in the territory of a Contracting State. Paragraph (b), on the other hand, defines the international element which is necessary for the future instrument to apply, namely that the operations for which the OTT is responsible must be related to "carriage in which the place of departure and the place of destination are situated in two different States". The reason for the limitation of the sphere of application of the draft to international operations has already been given in paragraph 10 *et seq.* of this report but it should be noted that this view was not shared by all members of the Study Group.

33. In particular, some participants considered that it would be a worthwhile task to unify the law relating to all contracts for the safekeeping of goods throughout the world and that from a practical viewpoint the limitation of the scope of the future instrument to operations connected with international carriage would deprive it of much of its interest. Moreover, hesitations were voiced in this connection as regards the precise circumstances in which the OTT would be responsible under the future Convention and the objection was in particular raised that goods might be stored in a terminal without it being known *ab initio* whether they would be the subject of international carriage. At what time therefore would an operator cease to be a simple warehouseman and instead become an OTT? One member of the Group considered that what was vital was the operator's knowledge of the international character of the carriage preceding or subsequent to the safekeeping for otherwise he would not know whether he had to take out insurance to cover his eventual liability under the Convention. In his view it would be preferable to speak of the OTT's undertaking the safekeeping of goods in connection with international carriage and to define this notion by reference to whether the OTT knew or ought to have known that the safekeeping was to take place before, during or after international carriage. A majority of the Group however was of the opinion that it would be extremely difficult, if not impossible, to prove knowledge in such cases and accordingly it retained the objective criterion to be found in Article 2 (b).

### *Article 3*

34. Paragraph 1 of this article reverts to the primary obligations of the OTT referred to in Article 1, providing as it does that he "shall be responsible for the safekeeping of goods from the time he has taken them in charge until their handing over to the person entitled to take delivery of them". It should be noted that this

pinpointing of the time during which the OTT is liable for the safekeeping of goods excludes his liability under the draft for failure to accept them when he has undertaken to do so by prior agreement, as the Group as a whole considered that this question should not be dealt with in an international instrument seeking to lay down minimum rules governing the rights and duties of OTTs, but rather be left to be regulated by general conditions, as also should a number of other matters connected with non-performance of contractual obligations.

35. As mentioned above in paragraph 16 of this explanatory report, paragraph 2 of the article provides that the OTT shall also be responsible for goods which he has taken in charge for safekeeping when he undertakes to perform in relation to them additional operations of discharging, loading or stowage or when he undertakes to procure the performance of such operations by an independent contractor. This solution, which reflects the view of the majority of the Group, represents a compromise between two more radical proposals. One of these recommended the application of the future instrument to all handling operations performed before, during, or after carriage operations, irrespective of whether the operator had undertaken the primary obligation of the safekeeping of the goods, while the other would have restricted the scope of the preliminary draft to warehousing operations *stricto sensu*, principally on the ground that Article 3, paragraph 2 would introduce differences in the liability regime applicable to those engaged in handling operations according to whether or not such operations were linked to the safekeeping of the goods. It was also suggested that it was not clear whether paragraph 2 would apply when the safekeeping was ancillary to the handling operations, performed for example by stevedores, and that such uncertainty would be even less acceptable if the future Convention were to be fully mandatory in character.

36. A majority of the members of the Group considered however that the future instrument should, as far as possible, fill in the gaps left in the liability regime established by existing international Conventions dealing with the carriage of goods and, given the tendency to reduce the period of safekeeping by means of advanced technology with a view to cutting costs, it was agreed that regard must be had to the fact that more and more comprehensive services are provided by modern terminal operators. Such operators should not, therefore, be permitted to avoid the application of the provisions of the Convention by alleging that the damage occurred to the goods not during the period of safekeeping but in the course of the performance of handling operations. On the other hand, it was felt that there could be strenuous resistance on the part of the interested professional circles to an extension of the Convention to cover all handling operations before, during or after carriage, principally because the liability regime proposed under Article 6 might not prove to be suitable for all such operations.

37. Desirable as it might be, therefore, to establish at international level a uniform liability for handling intermediaries on the model of the French law of 1966, it

was considered unrealistic to seek to achieve this goal at the present time. It was further agreed that the operations contemplated by Article 3 paragraph 2 should not extend to those, such as checking of the goods, which would fall within the French concept of "actes juridiques" as opposed to "actes matériels", and the defective performance of which, although giving rise to financial loss, does not result in actual damage to, or loss of, the goods. Similarly the handling operations covered by the provision are restricted to discharging, stowage and loading, that is to say operations directly linked to the vehicle or craft transporting the goods and do not include such services as distribution of the goods from a terminal at the end of international carriage.

38. Notwithstanding the general feeling within the Group that ancillary handling operations should be dealt with by the future instrument, some participants considered that paragraph 2 was unnecessary as the handling operations mentioned therein were already covered by the wording of paragraph 1, while others were of the opinion that even if this were the case it might still be desirable to add the words "and handling" after "safekeeping" so as to make it clear that the OTT is liable in respect of such handling operations. With respect to this latter suggestion it was however pointed out that the notion of taking in charge, mentioned in paragraph 1, while perfectly compatible with the safekeeping of goods, did not perhaps fully fit in with the performance of handling operations.

39. It should be noted that paragraph 2 establishes a certain parallelism with paragraph 1 in that whereas the former states that the period of responsibility in relation to the safekeeping of goods runs from the time the OTT takes them in charge until their handing over to the person entitled to take delivery of them, the period of responsibility is extended under paragraph 2 to cover the duration of the additional operations performed, even before the taking in charge of the goods or after their handing over. The language of paragraph 2, when read in conjunction with Article 6, paragraph 1, makes it clear that the OTT is liable only for damage to or loss of the goods occurring during the period of safekeeping or during the operations specified in Article 3 and not for the due performance of his obligations as such. Thus, for example, if faulty stowage of goods were to result in damage to goods during the voyage, the OTT would not be liable for such damage under the Convention, irrespective of what his position might be under his general conditions or under the applicable law.

#### Article 4

40. This article was the subject of lengthy discussion by the Group and represents a compromise solution between the various solutions proposed. On the one hand, some participants expressed scepticism as to the need for another document in international transport operations. In particular, it was suggested that it would be unnecessary for the OTT to issue a document acknowledging receipt of the goods when they were already covered by a transport document against which the goods

would have to be handed over and that today, as modern transport techniques increase the speed with which goods are moved, operations might be unduly slowed down if an OTT were always to have to issue a document when taking the goods in charge. In addition, one participant considered that if the OTT were to be obliged to issue a document, the evidentiary value of which would have some bearing on his liability, he ought to be entitled to insure the goods unless he receives contrary instructions indicating that they are already covered.

41. Against this view, one member of the Group argued that there was no value in laying down an elaborate liability regime for OTTs intended to fill in the gaps in Article 4, paragraph 2 of the Hamburg Rules and providing the carrier with a recourse action against the OTT, or the cargo interest with a direct action against him if no document were to be available to prove that the goods had actually been taken in charge. In some countries no confirming documents were issued or, if they were, then many weeks or months after discharge of the goods from the terminal and with no indication whatever regarding the state of the goods on arrival or discharge. This was particularly the case with barge enterprises in typical roadstead ports and with customs warehouses. There should therefore be a duty to confirm the taking over of the goods and a statement of their quantity and quality within a certain limited time in a dated document, for if the issue of the document were to be conditional upon a request by a customer and the OTT were to refuse to issue the document, how could the former prove that he had in fact requested it? Only in those cases where the document was to be of a negotiable character therefore should it be necessary for an express request to be made, while provision should in addition be allowed for sanctions in the event of the OTT failing to observe his duty to issue a document acknowledging receipt of the goods. In such cases, as also in those where the OTT issued the said document in a way which did not conform to the requirements of Article 4, paragraph 2 of the preliminary draft, it should, in the absence of proof to the contrary, be presumed that he had taken delivery of the goods in the circumstances appearing from the documentary evidence provided by the other party to the contract, i.e. the last document in the latter's possession relating to the goods, including his own exit certificate.

42. The prevailing view was however that such a proposal would go too far. In the first place, it was suggested that the need for a confirming document as evidence of the goods having been taken in charge would vary according to the circumstances. In some cases, the parties would prefer to dispense with a document as evidence for the taking in charge as being too expensive or time-consuming and a simple receipt would be sufficient, especially when the goods were not of any great value. Moreover, on the question of refusal by the OTT to issue a document on request, it was suggested that the matter could best be left for determination by national law, and one member of the Group recalled that in his experience he had come across no case of a maritime carrier refusing to issue a bill of lading in accordance with Article 3, paragraph 3 of the 1924 Brussels Convention on Bills of Lading.

43. In these circumstances, it was agreed that Article 4, paragraph 1 of the preliminary draft should provide merely for the issuing on request by the OTT of a document acknowledging receipt of the goods, it being understood that signature by the OTT of a carriage document should be regarded as the issuance of a document for the purposes of the provision. With a view to allaying some of the fears expressed during the discussions, paragraph 1 further stipulates that the document must be dated and that it must also state the date on which the goods were taken in charge. The question of the legal consequences of failure to issue such a document is therefore left to national law.

44. The document to be issued in accordance with paragraph 1 of Article 4 is not however a mere receipt as paragraphs 2 and 3 are concerned respectively with its content and with its evidentiary effect. Here it was considered unnecessary to enter into the detail to be found in the various Conventions concerning the carriage of goods, for example the provisions of Articles 15 to 18 of the Hamburg Rules. As regards the content of the document therefore, paragraph 2 provides that it shall "indicate any inaccuracy or inadequacy of any particular concerning the description of the goods taken in charge as far as this can be ascertained by reasonable means of checking", although one member was of the opinion that the last words of the paragraph were unduly wide and that they might permit the OTT to make general reservations of a sweeping character in cases where it would be impossible to make an adequate check, thereby rendering the whole provision ineffective. In reply to these criticisms, it was however recalled that the preliminary draft was not seeking to regulate all points of detail and that one might perhaps envisage the elaboration by the interested professional organisations of some kind of check list to assist OTTs.

45. With respect to the evidentiary value of the document to be issued by the OTT, paragraph 3 is modelled on Article 18 of the Hamburg Rules in that it provides that the document is "*prima facie* evidence of the contract for the safekeeping of goods and the taking in charge of the goods as therein described".

46. Paragraph 4 of Article 4 seeks to deal with a question which was discussed at considerable length by the Study Group, namely whether the document acknowledging receipt of the goods should be of a negotiable character or not. The principal difficulty encountered in this connection was that the Group did not feel itself to be in a position to judge the extent to which international trade actually experiences the need for a negotiable warehouseman's document, although it was recognised that there might well be some such need at distribution terminals in cases where it is not known to whom the goods will be sold upon their arrival at the terminal. In consequence, it was decided that no final decision should be taken on the question until further information had been obtained but that with a view to stimulating discussion on the question within the interested circles provision be made in paragraph 4, the wording of which is in part inspired by Article 1, paragraph 7 of the Hamburg Rules, for the possibility of the OTT's document being of

a negotiable character, subject however to two conditions, namely that the parties so agree and that the national law, i.e. the law of the State where the safekeeping and, where appropriate, handling operations are performed, so permits.

47. Paragraph 5 was inserted at the request of a number of participants who considered that the future Convention should take account of the ever increasing trend away from a traditional paper documentation in favour of the use of mechanical and electronic means of communication and the provision is based on a simplified form of wording of Article 14, paragraph 3 of the Hamburg Rules (Article 5, paragraph 3 of the Geneva Convention). In this connection it should however be pointed out that, as it stands, paragraph 5 may be taken as referring only to the document referred to in Article 4 itself and that provision might also be made elsewhere, as is the case with Article 1, paragraph 8 of the Hamburg Rules (Article 1, paragraph 10 of the Geneva Convention), to the effect that "writing" includes, *inter alia*, telegram and telex, which could be of relevance in particular in connection with Articles 6, 10 and 11 of the preliminary draft Convention.

#### *Article 5*

48. A number of members of the Group expressed the opinion throughout its meetings that the presence of a provision in the future Convention granting a right of general lien to the OTT might prove to be an incentive to operators to accept the provisions of the Convention as a whole. They considered that such a lien would permit the OTT to grant credit to his customers, thus speeding up the flow of goods, and that it would also be important in those situations where there was a dispute over the price of the agreed services for in such cases there could be a risk of the OTT's delay in delivery of the goods being converted into a liability for physical loss (see below, paragraph 55). It was, admittedly, true that many freight forwarders' and warehousemen's general conditions provided for such a general lien but it was far from clear that such liens were recognised in all countries so that the availability of a right of general lien under an international Convention could be of real benefit to operators in those countries where the exercise of such a lien is not permitted or where it is doubtful whether it would be upheld by the courts.

49. Other members of the Group were however of the opinion that it might not, at the present time, be realistic to attempt to unify the widely differing national laws governing the warehouseman's lien and were opposed to the granting to the OTT of a general lien, partly on the ground that such a lien was not recognised by their legal systems and partly for fear of the confusion which might be caused by the creation of unconnected liens. It was, moreover, suggested that the existence of such a wide right of retention would seriously reduce the value of any negotiable document which might be issued under Article 4, paragraph 4, while possible conflicts were also seen between the OTT's right of retention and his duty to surrender goods on production of a carriage document.

50. The same difference of opinion emerged from the written observations of States and international organisations on the preliminary draft and in these circumstances the Group came to the conclusion that it would not be possible to accord a right of general lien to the OTT under the future Convention. On the other hand it was considered necessary to avoid giving rise to an *a contrario* interpretation that it did not permit a general lien. Paragraph 1 consists therefore of two sentences, the first of which makes provision for the OTT's right of retention over goods taken in charge by him for costs and claims relating to those goods. The second sentence states that "nothing in this Convention shall affect the validity under national law of any contractual arrangements extending the OTT's security in the goods", thereby seeking to uphold, *inter alia*, provisions in the general conditions of OTTs providing for a general lien which are not themselves contrary to the applicable law. Finally, in connection with paragraph 1, it may be questioned whether the words "fees and warehousing rent included" do not suggest that Article 5 applies not only in respect of claims relating to the safekeeping of the goods but also to the other services which may be provided by the OTT and for which he is responsible under Article 3, paragraph 2.

51. Paragraph 2 of the article which, like paragraph 3, is based on Article 10 of the UNIDROIT draft Convention on the hotelkeeper's contract, makes provision for the operator's being obliged to release the goods if the person entitled to them provides, or obtains from another person, a sufficient guarantee for the sum claimed, as he might be willing to do so as to ensure that the goods may be moved out of the terminal and sold, pending the settlement of a dispute between the operator and himself. Similarly, the OTT will not be entitled to retain the goods if a sum equivalent to that claimed by him is deposited with a mutually accepted third party or with an official institution in the State where the operations for which the OTT is responsible under the Convention are performed.

52. Paragraph 3 asserts the principle that the OTT, in addition to his right of retention of the goods, may also "sell or cause to be sold all or part of the goods retained by him so as to obtain the amount necessary to satisfy his claim" after giving adequate and timely notice, a notion to be interpreted according to the applicable law.

#### *Article 6*

53. This article lays down the basic liability regime to which the OTT is subject under the preliminary draft Convention and it will readily be seen that this regime closely follows that established by Article 5 of the Hamburg Rules and Article 16 of the Geneva Convention, namely that referred to in basic principle (d) of the Preamble to the Geneva Convention where it is provided that "the liability of the multimodal transport operator under this Convention should be based on the principle of presumed fault or neglect". Although the Group did not find it possible for technical reasons to follow precisely the language of the above-mentioned

provisions of the Hamburg Rules and the Geneva Convention, its intention was however, subject to the decision not to deal in principle with liability for delay, to lay down the same liability system as that contained in those two Conventions and it is for this reason that the comma before the last three words of paragraph 1 has been inserted so as to make it clear that the verb "avoid" refers not only to the occurrence which caused the loss or damage, but also the consequences of that occurrence.

54. Broadly speaking, the choice of the liability regime established by Article 6 represents the preference of the Group as a whole as no participant spoke in favour of a system under which the customer could be called upon to prove that the loss or damage had been caused by the fault of the OTT or his servants and agents as a pre-condition for recovery. Although some doubts were expressed as to whether a regime based on that of the Hamburg Rules and founded on the presumed fault of the OTT, which was less severe than that imposed upon carriers by air, road and rail, was appropriate, the choice of the "Hamburg" and "Geneva" solution was seen by the majority of the Group, as well as of the States and organisations which commented on the preliminary draft, as being dictated by a number of considerations. In the first place, it was recalled that the present legal position of warehousemen, as Dr. Hill's report had illustrated, is characterised by many restrictions on legal liability and a low level of financial responsibility, irrespective of whether the rules are based on statute, conditions of trading or general conditions, although with the development of containerisation larger consortia have been successful in obtaining higher levels of liability. If, therefore, it was hoped to overcome the opposition of the profession to the imposition of liability in excess of that to which it is accustomed, then a realistic, uniform level of liability would have to be established. It was this concern for laying down a uniform liability for OTTs, an innovation which would certainly be favoured by banks who are opposed to gaps in liability regimes, which also led the Group to reject the idea of increasing the OTT's liability to the level of that of the carrier in those cases where the carrier has himself extended his liability to cover the period after carriage and before delivery to the ultimate consignee, while considerations based on grounds of practicality caused it to dismiss a similar suggestion that the OTT's liability might somehow be related to the mode of transport with which the terminal operations were connected. Such a solution might be workable, although contrary to the interests of uniformity, if only one mode of transport were involved but, if the terminal operations were to be sandwiched between carriage effected by different modes of transport, there would be no objective criterion for determining which liability regime should be applicable.

55. After lengthy discussion, the Group decided, as mentioned above in paragraph 53, in principle not to make provision for the OTT's liability for loss or damage resulting from delay in handing over the goods. On the one hand, some participants saw no reason why an efficient OTT should not in normal circumstances be

able to hand over goods to the consignee on demand and they added that there would usually be evidence, for example the issuing of a receipt for the goods by the OTT to the carrier, which would indicate whether the delay in delivery to the consignee had been caused during the transport operations or by an event occurring while the goods were in the terminal. There did not therefore seem to be valid reasons for not holding the OTT liable for damage resulting from delay in handing over the goods. On the other hand however, a majority of members of the Group, whose view was moreover shared by a number of Governments in their written observations, were opposed to dealing in the preliminary draft with the OTT's possible liability for delay on the ground that the question of delay is one essentially tied up with the movement of goods as opposed to stationary goods, such as those deposited in a terminal. In reply to the observation that to leave liability for delay to be determined in principle by national law would be to expose an OTT who might be responsible for loss or damage resulting from delay to large claims for consequential damage which would not be subject to limitation under the future Convention, it was pointed out that such cases could be settled in the general conditions of the operators who might, for example, limit their liability to the cost of retrieving the goods. Failing this, they would be liable under paragraph 2 of Article 6, which deals essentially with the case where the OTT claims that he intends to hand over the goods and that he will do so as soon as he has found them. Usually, failure to produce the goods could be attributed to the fact that the OTT no longer has them and to avoid his indefinitely claiming that the goods are simply misplaced, the Group decided to impose a time-limit after which the person entitled to the goods may treat them as lost. Although some criticism was made of the period of 60 days laid down in Article 6 paragraph 2 as being too long, the Group decided to retain it on the model of the corresponding provision of the Hamburg Rules. It did not however see any justification in this context for taking over the longer period of 90 days referred to in Article 16, paragraph 3 of the Geneva Convention.

56. In view of the decision not to deal with delay as such in Article 6, the provisions of that article are concerned only with those cases where the goods have been damaged or lost as a result of the defective performance of the OTT's obligations under the preliminary draft Convention. It was not the Group's intention, therefore, that he be liable thereunder for loss caused, for instance, by his failure to take the goods in charge at the agreed time in cases where the contract for the safekeeping of the goods has been concluded prior to their being taken in charge, as it was felt that such question could best be dealt with in standard conditions (see above, paragraph 20). Similarly, the wording of Article 6 is such that the OTT will not be liable thereunder where the customer suffers financial loss as a result, for example, of the OTT's failing to clear out old invoices.

57. To the extent that Article 6 closely follows, where appropriate, the corresponding articles of the Hamburg

Rules and the Geneva Convention, its provisions do not call for any detailed comment, except for one point, relating to the use of the words "servants and agents". A number of participants in the Study Group expressed dissatisfaction with this term, in view of the differences in interpretation to which the concept of an "agent" is open. The suggestion was therefore made that some form of words such as those to be found in Article 3 of the Convention on the Contract for the International Carriage of Goods by Road (CMR), which speaks of the persons of whose services the carrier makes use in the performance of his obligations, might be preferable. Ultimately, however, it was decided to retain the term used in the Hamburg Rules and the Geneva Convention as it represented the most recent expression of the will of States, although here again it was agreed that the matter could be reverted to at a later stage of the elaboration of the preliminary draft Convention when a final decision might be taken as to the precise form of wording to be employed, it being understood that what the Group had in mind were the classes of persons referred to in Article 3 of the CMR.

#### *Article 7*

58. The provisions of this article are to a large extent based on an amalgam of those of Article 6 of the Hamburg Rules and of Article 18 of the Geneva Convention. The principal differences between Article 7 of the preliminary draft and the above-mentioned articles lie in the absence of any provision relating to delay, given the decision in respect of Article 6, and in the fact that a majority of the members of the Study Group was opposed to the application to the liability of OTTs of the alternative between the package limitation and the limitation by kilogramme, an important practical difficulty as regards the former being that goods might arrive in a terminal in the form of a package after carriage, especially by sea, and then be broken up and sent on by other modes of transport to another destination. Furthermore, it was considered unnecessary in connection with the activities of terminal operators to draw the distinction to be found in Article 18, paragraph 3 of the Geneva Convention between international transport which does, and that which does not, include carriage of goods by sea or by inland waterway for the purpose of establishing different limitation figures in the two situations.

59. It will be noted that the Group has taken as the limitation figure in paragraph 1 of Article 7 that of 2.75 units of account per kilogramme of the gross weight of the goods, based on Article 18, paragraph 1 of the Geneva Convention, rather than that of 2.50 units of account which was retained in Article 6, paragraph 1 of the Hamburg Rules as in this respect it was considered preferable to follow the most recent expression of the will of the international community. Finally, with regard to the amount of the limitation, the Group considered it advisable to reserve for a future stage of the elaboration of the future Convention the question of whether a limit of liability per event should be introduced to cover those cases of excessive damage,

caused for example by fire or explosion, where a simple limitation by kilogramme might still result in a limitation figure that it would not be possible to insure.

60. While paragraph 2 of Article 7 calls for no comment, it should be mentioned that some hesitations were expressed in connection with the inclusion of a provision in paragraph 3 similar to Article 6, paragraph 4 of the Hamburg Rules, under which the OTT may, by agreement, increase the limits of liability provided for in paragraph 1 of Article 7. It was, in particular, argued that by making provision for such an alteration of the limit on compensation payable by the OTT, the future instrument might prove less attractive to the operators in question, some of whom are exposed to pressure by large shipping companies, and that it was in principle undesirable to stimulate competition between them on the basis of the most favourable limitation amounts on offer rather than on the ground of price and efficiency. Indeed, it was suggested that the existence of such a provision would go so far as to deny the OTT the benefit of the limitation laid down by paragraph 1. Sympathy was expressed with this view but on the other hand it was recalled that it was only in the CMR among the international instruments dealing with the carriage of goods that a prohibition was put upon altering the limitation figure established by the Convention and that even their ingenious insurance schemes were sometimes used to get round the letter of the Convention. In addition, the fact that the limitation figures contained in Article 7 were to be found in an international Convention, which would hopefully be backed up by standard conditions to be prepared by the interested professional organisations, would strengthen the bargaining position of terminal operators, although of course the latter would not be entirely protected against pressure being exerted on them to raise their limitation figures by strong shipping lines. It has also been pointed out in this connection that some States might have difficulty in accepting a Convention which did not make allowance for an increase in the limitation amounts.

#### *Article 8*

61. This provision, dealing with the applicability of the defences and limits of liability provided under the Convention to non-contractual claims, follows closely Article 7 of the Hamburg Rules, subject only to minor drafting changes.

#### *Article 9*

62. This provision is almost entirely modelled on Article 8 of the Hamburg Rules and on Article 21 of the Geneva Convention. As regards paragraph 1, it differs from those mentioned above in that it contains no reference to liability for delay. Originally the text contained a further amendment to the Hamburg and Geneva texts, namely the addition of the word "per-

sonal" before "act or omission" which sprang from the desire of many members of the Group to make the limitation as "unbreakable" as possible. In the first place this addition was advocated on the ground that as a general rule insurance prefers unbreakable limits, thus permitting the calculation of realistic premiums. Secondly, it was suggested that such a limitation would be attractive to OTTs and an incentive for them to accept the provisions of the future Convention as a whole, and thirdly that the presence of the word "personal" would serve to indicate expressly what was implicit in the corresponding provisions of the Hamburg Rules and Geneva Convention. It would moreover, it was argued, halt the tendency of courts in some countries whenever possible to break the limits applicable under international Conventions. In the view of some members of the Group there would be no purpose in introducing any limitation system if the OTT could be held liable in full for the wilful misconduct of his servants or agents, as would for instance be the case where they stole goods in the safekeeping of the OTT.

63. Other members of the Group however considered that the addition of the word "personal" would bring about a change in the system as conceived by the Hamburg Rules and by the Geneva Convention. It was not in their view by chance that it had not been included in Article 8, paragraph 1 of the Hamburg Rules or in Article 21, paragraph 1 of the Geneva Convention where the intention had precisely been to lay down breakable limits. On the other hand, these members of the Group considered that the case of theft of goods by a servant would not result in the breaking of the limitation, either because the servant would not be regarded as acting within the scope of his employment in such a situation, or because the court would only hold the OTT liable if the fault had been committed by a sufficiently senior executive such as the managing director or possibly a member of the board of directors, or if there were gross negligence in the organisation of the terminal.

64. In these circumstances the Study Group decided by way of compromise to include the word "personal" in square brackets so as to permit full debate on the matter during the next stage of the work, but in view of the strong objections to its presence raised by some members of the restricted group of members of the Governing Council it was deleted.

65. Finally, it should be noted that the same objections to the word "agent" were made in this connection as had been levelled against its use in Article 6 (see above, paragraph 57).

#### *Article 10*

66. The provisions of this article, concerning the giving of notice of loss or damage, are based on those of Article 19 of the Hamburg Rules and Article 24 of the Geneva Convention. The text has however been somewhat simplified to take account on the one hand

of the differences between carriage and safekeeping and on the other of the fact that the preliminary draft Convention is not concerned with liability for delay as such.

67. Paragraph 1 of Article 10 follows very closely the language of the corresponding provisions of the Hamburg Rules and of the Geneva Convention although it should be noted that the wording of the French text has been altered with a view to obtaining greater clarity. It was however decided to retain in paragraph 2 the period of 15 consecutive days, which had been taken over from Article 19 of the Hamburg Rules, as opposed to that of six days, as in Article 24, paragraph 2 of the Geneva Convention, for the reason that the shorter six day period was necessary there for the multimodal transport operator as he might himself have to pass on notice to his sub-contractors.

68. Lengthy consideration was given to the introduction of a provision similar to Article 19, paragraph 8 of the Hamburg Rules and Article 24, paragraph 8 of the Geneva Convention indicating the persons to whom, for the purpose of the article, notice may validly be given. Particular difficulties were however experienced in this connection in determining who would be those persons. Would notice to a lighterman or a docker, for example, be sufficient? The Group considered that if the word "person" were to be read as a "person authorised to receive such notice", then the provision would be acceptable and indeed paragraph 8 of Article 19 of the Hamburg Rules gave some guidance on the matter by speaking of "a person... including the master or the officer in charge of the ship". Even this formulation was not, however, fully satisfactory as the number of persons might be increased considerably by the application of the *eiusdem generis* rule. In these circumstances, the Group decided to include no such provision and to leave the matter to be determined by national law.

#### *Article 11*

69. In view of the fact that a majority of the members of the Group saw their task as the preparation only of minimum rules relating to the operations of OTTs, and given that some had also insisted on its semi-mandatory character, it was not deemed appropriate at this stage to include provisions dealing with such procedural questions as jurisdiction, enforcement of judgments and arbitration which are customarily found in international transport Conventions. The Group also considered the introduction of a provision which would indicate those persons, other than those contractually bound by the OTT, who might institute proceedings against him under the future Convention. It was recognised that this was an important and complex question but it was thought preferable to follow the precedents established by the transport law Conventions, especially the Hamburg Rules and the Geneva Convention, and not to deal specifically with the matter in the preliminary draft Convention.

70. In these circumstances the draft only contains an article dealing with limitation of actions based on provisions contained in Article 20 of the Hamburg Rules and Article 25 of the Geneva Convention. Although some participants considered the two year limitation period provided for in paragraph 1 to be too long, and suggested an alternative of one year, it was considered that even a two-year period would represent a substantial improvement in the position of terminal operators in some countries where a general limitation period of thirty years is at present applicable to actions brought against them.

71. Attention was also drawn to the absence from the article of any provision concerning the interruption or suspension of actions of the kind to be found in the International Convention concerning the Carriage of Goods by Rail (CIM) and CMR Conventions which, it was suggested, would be advantageous to the extent that they permit a reduction in litigation. In this connection it was pointed out that the CIM/CMR system whereby the lodging of a substantiated claim automatically interrupts the period of limitation often gives rise to difficulties of computation in practice and that the solution, which had hitherto been confined to European regional Conventions, had not been taken over in the Hamburg Rules.

72. Even if the CIM/CMR system were not adopted, one member of the Group still considered that the drafting of the article was defective in that it did not state whether the limitation period could in any circumstances be suspended or interrupted, and reference was made in particular to the difficulties which had arisen in the interpretation of Article 29 of the Warsaw Convention in respect of which the highest courts of different States had reached widely divergent decisions. Some rule regarding interruption and suspension of actions should, it was therefore recommended, be included in the article. Another member pointed out that it was the wording of Article 29 of the Warsaw Convention and the difficulties surrounding the concept of a "délai de déchéance" which had given rise to problems of interpretation and, while he therefore saw no serious defect in the text as it stood, he proposed that a provision be inserted to the effect that questions relating to the interruption and suspension of the limitation period be left to be regulated by national law. After further discussion, however, the Group decided to adopt the formulation of the Hamburg Rules without prejudice of course to the matter being taken up again in the final stages of the drafting of the future instrument.

#### *Article 12*

73. This article, concerned as it is with certain contractual stipulations, is inspired by Article 23, paragraphs 1 and 2 of the Hamburg Rules and, more particularly as regards the French text, by Article 28, paragraphs 1 and 2 of the Geneva Convention. Paragraph 1 establishes the general rule that the parties may not derogate from the provisions of the Convention.

Paragraph 2 has been subjected to the same criticism as Article 7, paragraph 3 in that it permits derogation only in the sense that the OTT's responsibilities under the Convention may be increased. It should however be borne in mind that although Article 12, paragraph 2 encompasses Article 7, paragraph 3 in that the latter provision already contemplates the possibility of the OTT's increasing the limitation figures laid down by the preliminary draft, Article 12, paragraph 2 goes further and would, for example, permit the OTT to accept a more onerous liability regime or to extend the time during which notice of loss or damage might be given under paragraphs 1 or 2 or Article 10.

74. Finally in connection with Article 12, it was not considered necessary to introduce a provision along the line of Article 23, paragraph 3 of the Hamburg Rules and Article 28, paragraph 3 of the Geneva Convention under which the OTT would be obliged to make a statement that the safekeeping of the goods is subject to the provisions of the Convention.

#### *Article 13*

75. As mentioned in the general considerations (paragraph 18, above) the text of this article follows the model provision for a universal unit of account approved by UNCITRAL.

#### *Article 14*

76. This article resolves in favour of international Conventions relating to the international carriage of goods any conflict which might arise between the provisions of such Conventions regarding rights and duties arising thereunder and the provisions of the future instrument governing the liability of OTTs.

#### *Article 15*

77. This article reproduces a provision increasingly to be found in international Conventions dealing with private law matters adopted within the United Nations, and corresponds to Article 7 of the 1980 United Nations Convention on Contracts for the International Sale of Goods.

#### *Article Y*

78. As already mentioned above in paragraph 19 of this report, the introduction of this provision, which is of course closely related to Articles 7 and 13 and which follows the new UNCITRAL model, constitutes the one exception to the decision of the Governing Council of UNIDROIT not to include any final provisions in the text of the preliminary draft Convention.

## V. CO-ORDINATION OF WORK

### A. Co-ordination of work in general: report of the Secretary-General (A/CN.9/255)<sup>a</sup>

1. In its resolution 38/134 of 19 December 1983 on the report of the Commission on the work of its sixteenth 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. The main activities undertaken for the purpose of co-ordination since the sixteenth session of the Commission are set forth below.<sup>1</sup>

2. On the occasion of the Second Symposium on Transborder Data Flows organized by the Organisation for Economic Co-operation and Development (OECD) (London, 30 November—2 December 1983), the secretariats of the Economic Commission for Europe (ECE), Customs Co-operation Council (CCC), OECD, Nordic Legal Committee and UNCITRAL discussed means of co-operating in the field of legal problems of automatic data processing. Subsequently, the secretariats of UNCITRAL and CCC jointly prepared questionnaires on the legal value of computer records. The CCC questionnaire, which focused on the legal acceptability of a goods declaration submitted to customs authorities in computer-readable form, was sent to the member States of CCC and was enclosed for information with the questionnaire from the UNCITRAL secretariat. The UNCITRAL questionnaire was sent to all States members of the United Nations and was enclosed for information with the questionnaire sent by CCC. The UNCITRAL secretariat has also established formal liaison status with the Banking Commission (TC 68) of the International Organization for Standardization and the secretariat was represented at meetings of the Sub-committees on Bank Operations and Procedures and on Telecommunication Messages in Banking (Toronto, Canada, 6-9 September 1983). The UNCITRAL secretariat was also represented at the meeting of the ECE/UNCTAD Working Party on Facilitation of International Trade Procedures (Geneva, 26-30 September 1983) at which legal problems arising in the context of trade facilitation and the need for co-ordination of activities of international organizations concerned were discussed.

3. With regard to the UNCITRAL project on electronic funds transfers, the secretariat was represented at the Fifth Meeting of Latin American Lawyers Expert in Banking Laws (Guayaquil and Quito, Ecuador, 3-5 October 1983), and the annual seminar of the Society for World-wide Interbank Financial Telecommunications (S.W.I.F.T.) (Montreux, Switzerland, 26-30 September 1983). The UNCITRAL secretariat was also invited to the Forum on Legal Issues organized by the American Bar Association for the International Telecommunication Union's Telecom '83, (Geneva, 29 October—1 November 1983). The Bank for International Settlements (BIS), the International Monetary Fund (IMF) and the Latin American Banking Federation (FELABAN) are also co-operating with the UNCITRAL secretariat in the work on electronic funds transfers. The International Monetary Law Committee of the International Law Association has been kept informed of the activities of UNCITRAL in the field of international payments, including the preparation of draft chapters of the legal guide on electronic funds transfers, in the context of their undertaking to examine finality of payment questions in international transactions.

4. In the context of construction contracts, the Expert Group on International Contract Practices in Industry of the ECE (Geneva, 12-16 December 1983), considered a draft of a legal guide for drawing up international contracts on services relating to maintenance, repair and management of industrial works. Because of the close relationship to the draft legal guide on drawing up international contracts for the construction of industrial works, being prepared by UNCITRAL, a close liaison has been established with the Group. The United Nations Industrial Development Organization (UNIDO) and the UNCITRAL secretariat have continued the programme of inter-secretariat meetings to co-ordinate activities, begun in 1982. The UNCITRAL secretariat will be represented as an observer at the Fourth General Conference of UNIDO (Vienna, 2-18 August 1984). Besides 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) continue to co-operate actively with the UNCITRAL secretariat in the preparation of draft chapters on the legal guide on international contracts for the construction of industrial works.

<sup>a</sup>For consideration by the Commission see Report, chapter VI, A (part one, A, above).

<sup>1</sup>See also Chapter VII, "Training and assistance" (A/CN.9/256, reproduced in this Yearbook, part two, VII).

5. The UNCITRAL secretariat was represented at a meeting organized by UNIDO and the International Centre for Public Enterprises in Developing Countries (ICPE) (Ljubljana, Yugoslavia, 16-19 April 1984) 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 thirty-three countries. It is planned to collaborate with ICPE in areas of common interest in the legal field, particularly in connection with the preparation of the legal guide on industrial works.

6. The International Chamber of Commerce (ICC), which adopted the 1983 revision of the Uniform Customs and Practice for Documentary Credits on 21 June 1983 with an effective date of 1 October 1984, submitted the text to UNCITRAL for its possible endorsement. The text of the 1983 revision with an explanatory note by the ICC secretariat is reproduced in document A/CN.9/251 (reproduced in this Yearbook, part two, V, B). During the period of preparation of the 1983 revision the UNCITRAL secretariat co-operated with ICC in this task by sending a note verbale on 16 August 1982 to all Governments enclosing the then current draft of the revision with a request for comments. The comments received were forwarded to ICC for its consideration. The UNCITRAL secretariat was represented at the meetings of the ICC Commission on Banking Technique and Practice at which the revision was considered. The ICC Commission on International Contract Practices recommended to the national committees of ICC that they encourage their respective Governments to ratify the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980) (Vienna Sales Convention) and approved a commentary aimed at giving practical advice to parties involved in negotiating and drafting international sales contracts in the context of the Convention once it will have come into force.

7. The second session of the Special Commission of the Hague Conference on Private International Law to consider the revision of the 1955 Convention on the Law Applicable to International Sales of Goods in the light of the adoption of the Vienna Sales Convention was held at The Hague (7-18 November 1983). In addition to the member States of the Conference, the States members of UNCITRAL and previous States members of UNCITRAL who had participated in the 1982 meeting were invited to attend. The Special Commission adopted the draft text of the revision and it is expected that the Hague Conference will convene a diplomatic conference in 1985 to revise the Convention.

8. The secretariat of UNCTAD and the UNCITRAL secretariat have exchanged information on the work

being carried out by UNCTAD on the rights and duties of container terminal operators and users pursuant to paragraph 8 of UNCTAD resolution 144 (VI), and by UNCITRAL on the liability of transport terminal operators. UNCTAD has also been encouraging the ratification of the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg Rules), in particular in paragraph 13 of resolution 144 (VI). The secretariats of the two organizations have also expressed their interest in participating in regional seminars on topics of mutual interest sponsored by the other organization.

9. UNCITRAL has been invited by the Economic Commission for Africa to participate in an inter-institutional co-ordinating committee on the modernization and unification of maritime legislation in Africa. The other members of the committee are the International Maritime Organization, UNCTAD, the International Labour Organisation and the Ministerial Conference of West and Central African States on Maritime Transport. Several other international organizations have also been invited to participate.

10. The UNCITRAL draft model law on international commercial arbitration will be the main theme at the Interim Congress of the International Council for Commercial Arbitration (ICCA) (Lausanne, Switzerland, 10-12 May 1984). The secretariat will participate in that Congress where about 550 experts on arbitration from all over the world will assemble and it is expected that the contribution of ICCA to the UNCITRAL project on a model arbitration law will be as great as it was with regard to the preparation of the UNCITRAL Arbitration Rules. The UNCITRAL secretariat was represented at the Arbitration Congress of ICC (Paris, 11-13 October 1983) on the occasion of the sixtieth anniversary of the ICC Court of Arbitration.

11. In General Assembly resolution 38/128 of 19 December 1983 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 progressive development of the principles and norms of international law relating to the new international economic order. As in the past, information on relevant activities of the Commission was supplied by the UNCITRAL secretariat to UNITAR for use in its study.

12. In addition to those organizations mentioned in the preceding paragraphs, the secretariat maintains close contact with the Asian-African Legal Consultative Committee, the Council of Mutual Economic Assistance and the Organization of American States.

## B. Uniform customs and practice for documentary credits: report of the Secretary-General (A/CN.9/251)<sup>a</sup>

1. The Commission, at its fifteenth session (1982), received a note submitted by the secretariat describing the revision then in progress by the International Chamber of Commerce (ICC) of the 1974 version of the Uniform Customs and Practice for Documentary Credits (UCP) (A/CN.9/229; *Yearbook 1982*, part two, VI, C).
2. The note pointed out that the subject of documentary credits had been on the Commission's priority list of topics since 1968 and that the Commission at its second session in 1969 had recommended to Governments the use of the 1962 version of UCP, while at its eighth session in 1975 it had recommended the use of the 1974 version of UCP. The latter recommendation was adopted in a form suitable for ICC to reprint in its brochure containing the text of UCP.
3. The note further pointed out that developments in documentary credit practice, and especially those brought about by changes in transport technology and documentation and the increased use of stand-by letters of credit, had led to the revision of UCP then in progress. In order to permit interested circles in countries not represented in ICC to make observations on the operation of UCP so that these could be taken into account in the revision, the Secretary-General, in accordance with the past practices on this subject, had addressed to all Governments the same questionnaire as was sent by ICC to its National Committees and had transmitted the replies received to ICC for its consideration. It was expected that the final version of the revised text would be available for the sixteenth session of the Commission, and it was suggested that the Commission might wish to consider at its sixteenth session the possibility of recommending the use of the revised text of UCP, as it had in respect of the 1962 and 1974 versions of UCP.
4. At the fifteenth session of the Commission, a proposal was made that a study should be undertaken by the secretariat on the operation of letters of credit in order to identify legal problems arising from their use, especially in connection with contracts other than those for the sale of goods.<sup>1</sup> The proposal was accepted. However, it was noted that such a study, which would be a long-term project, should not prejudice any future endorsement by the Commission of the new revision of UCP, since the revision had been undertaken largely to reflect recent changes in transport technology and banking practice as they affected the sale of goods.<sup>2</sup>
5. Although it had been initially expected that the revised text of UCP would be ready for the Commission's sixteenth session for endorsement, final approval of the text was delayed beyond that time, and on 21 June 1983 the Council of ICC adopted the 1983 revised version of UCP to be in force as from 1 October 1984. Accordingly, ICC has now submitted the 1983 revised version of UCP to the Commission with a request that the Commission consider recommending its use in international trade, as was done in respect of the 1962 and 1974 revisions. A short explanatory note on the current revision prepared by ICC is contained in annex I. The original text of the 1983 revision of UCP, in English or French, is contained in annex II.

### ANNEX I

**Explanatory note submitted by the International Chamber  
of Commerce to the seventeenth session of the  
United Nations Commission on International Trade Law  
on the 1983 revision of uniform customs and practice  
for documentary credits**

The code applied to documentary credit operations throughout the world—the Uniform Customs and Practice for Documentary Credits—has been revised. The revision was carried out by the Code's "author", the International Chamber of Commerce (ICC), and will come into effect on 1 October 1984.

Documentary credits—also known as letters of credit—are often used to effect payment for goods in international trade. A bank in the buyer's country undertakes to pay the seller against presentation of documents giving shipment and other key details of the goods. Usually the credit is made payable to the seller at a bank in his own country. Payment may be at sight or on deferred terms. Credits frequently stipulate that drafts are to be presented for acceptance or negotiation.

The international rules of practice applied to these operations were first codified by ICC in 1933. The last revision—agreed in 1974—is accepted in nearly every country, and was commended for use by UNCITRAL at its eighth session in 1975.

The principal aim of the 1983 revision has been to update the sections dealing with the transport documents the seller has to produce to show that the goods have been dispatched to the buyer. The old rules emphasized the traditional maritime bill of lading which indicated loading on board a particular ship. The amended version makes it easier for banks to accept new style documents covering containerized shipment and multi-modal transport operations. Such documents normally indicate taking in charge at an inland point rather than loading on board.

<sup>a</sup>For consideration by the Commission see Report, chapter VI, B (part one, A, above).

<sup>1</sup>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. 109-112 (*Yearbook 1982*, part one, A).

<sup>2</sup>The secretariat intends to submit, after consultation with ICC, a preliminary report on this study at the eighteenth session of the Commission (1985).

Other changes include clarification of the different ways of making a credit payable to the seller, and of procedures for amending the credit terms. A new provision stipulates that documents produced by electronic and other copying processes are acceptable as originals, subject to safeguards. Stand-by letters of credit—issued mainly by banks in the United States of America to guarantee the obligations of suppliers in international projects—are now specifically covered by the rules.

The revision was adopted by the Council of ICC on 21 June 1983, and is the result of three and a half years' work of the ICC Banking Commission. The time-lag before it will come into effect is intended to give banks and other interested parties enough time to acquaint themselves with the new provisions and to adapt their procedures accordingly.

The work was carried out by representatives of the users of the rules—banks, commercial parties, insurers and transport operators in particular. Business and financial interests in ICC member countries in both the industrialized and developing worlds were able to comment and influence the revision procedure as it progressed. Other interested international organizations—including the UNCITRAL secretariat—were also kept informed of progress, and the revision work was periodically reviewed in a Special ICC Liaison Committee with Chambers of Commerce from the Socialist Countries of Eastern Europe.

The revised Uniform Customs and Practice will be published initially in English and French. Additional language versions will be made available at a later time.

The work is a private codification applied by voluntary acceptance. National banking associations obtain their members' adherence and notify this to ICC headquarters. Individual credits make reference to the Uniform Customs and Practice.

## ANNEX II

### Text of the uniform customs and practice for documentary credits\* (1983 revision)

#### A. General provisions and definitions

##### Article 1

These articles apply to all documentary credits, including, to the extent to which they may be applicable, standby letters of credit and are binding on all parties thereto unless otherwise expressly agreed. They shall be incorporated into each documentary credit by wording in the credit indicating that such credit is issued subject to Uniform Customs and Practice for Documentary Credits, 1983 revision, ICC Publication No. 400.

##### Article 2

For the purposes of these articles, the expressions "documentary credit(s)" and "standby letter(s) of credit" used herein (hereinafter referred to as "credit(s)"), mean any

\*Copyright 1983, by ICC Publishing S.A., Publication No. 400.

arrangement, however named or described, whereby a bank (the issuing bank), acting at the request and on the instructions of a customer (the applicant for the credit),

- i. is to make a payment to or to the order of a third party (the beneficiary), or is to pay or accept bills of exchange (drafts) drawn by the beneficiary,  
or
- ii. authorizes another bank to effect such payment, or to pay, accept or negotiate such bills of exchange (drafts),

against stipulated documents, provided that the terms and conditions of the credit are complied with.

##### Article 3

Credits, by their nature, are separate transactions from the sales or other contract(s) on which they may be based and banks are in no way concerned with or bound by such contract(s), even if any reference whatsoever to such contract(s) is included in the credit.

##### Article 4

In credit operations all parties concerned deal in documents, and not in goods, services and/or other performances to which the documents may relate.

##### Article 5

Instructions for the issuance of credits, the credits themselves, instructions for any amendments thereto and the amendments themselves must be complete and precise.

In order to guard against confusion and misunderstanding, banks should discourage any attempt to include excessive detail in the credit or in any amendment thereto.

##### Article 6

A beneficiary can in no case avail himself of the contractual relationships existing between the banks or between the applicant for the credit and the issuing bank.

#### B. Form and notification of credits

##### Article 7

- a. Credits may be either
  - i. revocable, or
  - ii. irrevocable.
- b. All credits, therefore, should clearly indicate whether they are revocable or irrevocable.
- c. In the absence of such indication the credit shall be deemed to be revocable.

##### Article 8

A credit may be advised to a beneficiary through another bank (the advising bank) without engagement on the part of the advising bank, but that bank shall take reasonable care to check the apparent authenticity of the credit which it advises.

*Article 9*

a. A revocable credit may be amended or cancelled by the issuing bank at any moment and without prior notice to the beneficiary.

b. However, the issuing bank is bound to:

- i. reimburse a branch or bank with which a revocable credit has been made available for sight payment, acceptance or negotiation, for any payment, acceptance or negotiation made by such branch or bank prior to receipt by it of notice of amendment or cancellation, against documents which appear on their face to be in accordance with the terms and conditions of the credit;
- ii. reimburse a branch or bank with which a revocable credit has been made available for deferred payment, if such branch or bank has, prior to receipt by it of notice of amendment or cancellation, taken up documents which appear on their face to be in accordance with the terms and conditions of the credit.

*Article 10*

a. An irrevocable credit constitutes a definite undertaking of the issuing bank, provided that the stipulated documents are presented and that the terms and conditions of the credit are complied with:

- i. if the credit provides for sight payment—to pay, or that payment will be made;
- ii. if the credit provides for deferred payment—to pay, or that payment will be made, on the date(s) determinable in accordance with the stipulations of the credit;
- iii. if the credit provides for acceptance—to accept drafts drawn by the beneficiary if the credit stipulates that they are to be drawn on the issuing bank, or to be responsible for their acceptance and payment at maturity if the credit stipulates that they are to be drawn on the applicant for the credit or any other drawee stipulated in the credit;
- iv. if the credit provides for negotiation—to pay without recourse to drawers and/or bona fide holders, draft(s) drawn by the beneficiary, at sight or at a tenor, on the applicant for the credit or on any other drawee stipulated in the credit other than the issuing bank itself, or to provide for negotiation by another bank and to pay, as above, if such negotiation is not effected.

b. When an issuing bank authorizes or requests another bank to confirm its irrevocable credit and the latter has added its confirmation, such confirmation constitutes a definite undertaking of such bank (the confirming bank), in addition to that of the issuing bank, provided that the stipulated documents are presented and that the terms and conditions of the credit are complied with:

- i. if the credit provides for sight payment—to pay, or that payment will be made;
- ii. if the credit provides for deferred payment—to pay, or that payment will be made, on the date(s) determinable in accordance with the stipulations of the credit;
- iii. if the credit provides for acceptance—to accept drafts drawn by the beneficiary if the credit stipulates that they are to be drawn on the confirming bank, or to be responsible for their acceptance and payment at maturity if the credit stipulates that they

are to be drawn on the applicant for the credit or any other drawee stipulated in the credit;

iv. if the credit provides for negotiation—to negotiate without recourse to drawers and/or bona fide holders, draft(s) drawn by the beneficiary, at sight or at a tenor, on the issuing bank or on the applicant for the credit or on any other drawee stipulated in the credit other than the confirming bank itself.

c. If a bank is authorized or requested by the issuing bank to add its confirmation to a credit but is not prepared to do so, it must so inform the issuing bank without delay. Unless the issuing bank specifies otherwise in its confirmation authorization or request, the advising bank will advise the credit to the beneficiary without adding its confirmation.

d. Such undertakings can neither be amended nor cancelled without the agreement of the issuing bank, the confirming bank (if any), and the beneficiary. Partial acceptance of amendments contained in one and the same advice of amendment is not effective without the agreement of all the above named parties.

*Article 11*

a. All credits must clearly indicate whether they are available by sight payment, by deferred payment, by acceptance or by negotiation.

b. All credits must nominate the bank (nominated bank) which is authorized to pay (paying bank), or to accept drafts (accepting bank), or to negotiate (negotiating bank), unless the credit allows negotiation by any bank (negotiating bank).

c. Unless the nominated bank is the issuing bank or the confirming bank, its nomination by the issuing bank does not constitute any undertaking by the nominated bank to pay, to accept, or to negotiate.

d. By nominating a bank other than itself, or by allowing for negotiation by any bank, or by authorizing or requesting a bank to add its confirmation, the issuing bank authorizes such bank to pay, accept or negotiate, as the case may be, against documents which appear on their face to be in accordance with the terms and conditions of the credit, and undertakes to reimburse such bank in accordance with the provisions of these articles.

*Article 12*

a. When an issuing bank instructs a bank (advising bank) by any teletransmission to advise a credit or an amendment to a credit, and intends the mail confirmation to be the operative credit instrument, or the operative amendment, the teletransmission must state "full details to follow" (or words of similar effect), or that the mail confirmation will be the operative credit instrument or the operative amendment. The issuing bank must forward the operative credit instrument or the operative amendment to such advising bank without delay.

b. The teletransmission will be deemed to be the operative credit instrument or the operative amendment, and no mail confirmation should be sent, unless the teletransmission states "full details to follow" (or words of similar effect), or states that the mail confirmation is to be the operative credit instrument or the operative amendment.

c. A teletransmission intended by the issuing bank to be the operative credit instrument should clearly indicate that the credit is issued subject to Uniform Customs and Practice for Documentary Credits, 1983 revision, ICC Publication No. 400.

d. If a bank uses the services of another bank or banks (the advising bank) to have the credit advised to the beneficiary, it must also use the services of the same bank(s) for advising any amendments.

e. Banks shall be responsible for any consequences arising from their failure to follow the procedures set out in the preceding paragraphs.

#### *Article 13*

When a bank is instructed to issue, confirm or advise a credit similar in terms to one previously issued, confirmed or advised (similar credit) and the previous credit has been the subject of amendment(s), it shall be understood that the similar credit will not include any such amendment(s) unless the instructions specify clearly the amendment(s) which is/are to apply to the similar credit. Banks should discourage instructions to issue, confirm or advise a credit in this manner.

#### *Article 14*

If incomplete or unclear instructions are received to issue, confirm, advise or amend a credit, the bank requested to act on such instructions may give preliminary notification to the beneficiary for information only and without responsibility. The credit will be issued, confirmed, advised or amended only when the necessary information has been received and if the bank is then prepared to act on the instructions. Banks should provide the necessary information without delay.

#### *C. Liabilities and responsibilities*

##### *Article 15*

Banks must examine all documents with reasonable care to ascertain that they appear on their face to be in accordance with the terms and conditions of the credit. Documents which appear on their face to be inconsistent with one another will be considered as not appearing on their face to be in accordance with the terms and conditions of the credit.

##### *Article 16*

a. If a bank so authorized effects payment, or incurs a deferred payment undertaking, or accepts, or negotiates against documents which appear on their face to be in accordance with the terms and conditions of a credit, the party giving such authority shall be bound to reimburse the bank which has effected payment, or incurred a deferred payment undertaking, or has accepted, or negotiated, and to take up the documents.

b. If, upon receipt of the documents, the issuing bank considers that they appear on their face not be in accordance with the terms and conditions of the credit, it must determine, on the basis of the documents alone, whether to take up such documents, or to refuse them and claim that they appear on their face not to be in accordance with the terms and conditions of the credit.

c. The issuing bank shall have a reasonable time in which to examine the documents and to determine as above whether to take up or to refuse the documents.

d. If the issuing bank decides to refuse the documents, it must give notice to that effect without delay by telecommunication, or, if that is not possible, by other expeditious means,

to the bank from which it received the documents (the remitting bank), or to the beneficiary, if it received the documents directly from him. Such notice must state the discrepancies in respect of which the issuing bank refuses the documents and must also state whether it is holding the documents at the disposal of or is returning them to, the presentor (remitting bank or the beneficiary, as the case may be). The issuing bank shall then be entitled to claim from the remitting bank refund of any reimbursement which may have been made to that bank.

e. If the issuing bank fails to act in accordance with the provisions of paragraphs (c) and (d) of this article and/or fails to hold the documents at the disposal of, or to return them to, the presentor, the issuing bank shall be precluded from claiming that the documents are not in accordance with the terms and conditions of the credit.

f. If the remitting bank draws the attention of the issuing bank to any discrepancies in the documents or advises the issuing bank that it has paid, incurred a deferred payment undertaking, accepted or negotiated under reserve or against an indemnity in respect of such discrepancies, the issuing bank shall not be thereby relieved from any of its obligations under any provision of this article. Such reserve or indemnity concerns only the relations between the remitting bank and the party towards whom the reserve was made, or from whom, or on whose behalf, the indemnity was obtained.

##### *Article 17*

Banks assume no liability or responsibility for the form, sufficiency, accuracy, genuineness, falsification or legal effect of any documents, or for the general and/or particular conditions stipulated in the documents or superimposed thereon; nor do they assume any liability or responsibility for the description, quantity, weight, quality, condition, packing, delivery, value or existence of the goods represented by any documents, or for the good faith or acts and/or omissions, solvency, performance or standing of the consignor, the carriers, or the insurers of the goods, or any other person whomsoever.

##### *Article 18*

Banks assume no liability or responsibility for the consequences arising out of delay and/or loss in transit of any messages, letters or documents, or for delay, mutilation or other errors arising in the transmission of any telecommunication. Banks assume no liability or responsibility for errors in translation or interpretation of technical terms, and reserve the right to transmit credit terms without translating them.

##### *Article 19*

Banks assume no liability or responsibility for consequences arising out of the interruption of their business by Acts of God, riots, civil commotions, insurrections, wars or any other causes beyond their control, or by any strikes or lockouts. Unless specifically authorized, banks will not, upon resumption of their business, incur a deferred payment undertaking, or effect payment, acceptance or negotiation under credits which expired during such interruption of their business.

##### *Article 20*

a. Banks utilising the services of another bank or other banks for the purpose of giving effect to the instructions of

the applicant for the credit do so for the account and at the risk of such applicant.

b. Banks assume no liability or responsibility should the instructions they transmit not be carried out, even if they have themselves taken the initiative in the choice of such other bank(s).

c. The applicant for the credit shall be bound by and liable to indemnify the banks against all obligations and responsibilities imposed by foreign laws and usages.

#### *Article 21*

a. If an issuing bank intends that the reimbursement to which a paying, accepting or negotiating bank is entitled shall be obtained by such bank claiming on another branch or office of the issuing bank or on a third bank (all hereinafter referred to as the reimbursing bank) it shall provide such reimbursing bank in good time with the proper instructions or authorization to honour such reimbursement claims and without making it a condition that the bank entitled to claim reimbursement must certify compliance with the terms and conditions of the credit to the reimbursing bank.

b. An issuing bank will not be relieved from any of its obligations to provide reimbursement itself if and when reimbursement is not effected by the reimbursing bank.

c. The issuing bank will be responsible to the paying, accepting or negotiating bank for any loss of interest if reimbursement is not provided on first demand made to the reimbursing bank, or as otherwise specified in the credit, or mutually agreed, as the case may be.

#### *D. Documents*

##### *Article 22*

a. All instructions for the issuance of credits and the credits themselves and, where applicable, all instructions for amendments thereto and the amendments themselves, must state precisely the document(s) against which payment, acceptance or negotiation is to be made.

b. Terms such as "first class", "well known", "qualified", "independent", "official", and the like shall not be used to describe the issuers of any documents to be presented under a credit. If such terms are incorporated in the credit terms, banks will accept the relative documents as presented, provided that they appear on their face to be in accordance with the other terms and conditions of the credit.

c. Unless otherwise stipulated in the credit, banks will accept as originals documents produced or appearing to have been produced:

- i. by reprographic systems;
- ii. by, or as the result of, automated or computerized systems;
- iii. as carbon copies;

if marked as originals, always provided that, where necessary, such documents appear to have been authenticated.

##### *Article 23*

When documents other than transport documents, insurance documents and commercial invoices are called for, the credit should stipulate by whom such documents are to be issued and their wording or data content. If the credit does

not so stipulate, banks will accept such documents as presented, provided that their data content makes it possible to relate the goods and/or services referred to therein to those referred to in the commercial invoice(s) presented, or to those referred to in the credit if the credit does not stipulate presentation of a commercial invoice.

#### *Article 24*

Unless otherwise stipulated in the credit, banks will accept a document bearing a date of issuance prior to that of the credit, subject to such document being presented within the time limits set out in the credit and in these articles.

#### *D.1 Transport documents (documents indicating loading on board or dispatch or taking in charge)*

##### *Article 25*

Unless a credit calling for a transport document stipulates as such document a marine bill of lading (ocean bill of lading or a bill of lading covering carriage by sea), or a post receipt or certificate of posting:

a. banks will, unless otherwise stipulated in the credit, accept a transport document which:

- i. appears on its face to have been issued by a named carrier, or his agent, and
- ii. indicates dispatch or taking in charge of the goods, or loading on board, as the case may be, and
- iii. consists of the full set of originals issued to the consignor if issued in more than one original, and
- iv. meets all other stipulations of the credit.

b. Subject to the above, and unless otherwise stipulated in the credit, banks will not reject a transport document which:

- i. bears a title such as "Combined transport bill of lading", "Combined transport document", "Combined transport bill of lading or port-to-port bill of lading", or a title or a combination of titles of similar intent and effect, and/or
- ii. indicates some or all of the conditions of carriage by reference to a source or document other than the transport document itself (short form/blank transport document), and/or
- iii. indicates a place of taking in charge different from the port of loading and/or a place of final destination different from the port of discharge, and/or
- iv. relates to cargoes such as those in Containers or on pallets, and the like, and/or
- v. contains the indication "intended", or similar qualification, in relation to the vessel or other means of transport, and/or the port of loading and/or the port of discharge.

c. Unless otherwise stipulated in the credit in the case of carriage by sea or by more than one mode of transport but including carriage by sea, banks will reject a transport document which:

- i. indicates that it is subject to a charter party, and/or
- ii. indicates that the carrying vessel is propelled by sail only.

d. Unless otherwise stipulated in the credit, banks will reject a transport document issued by a freight forwarder unless it is the FIATA Combined Transport Bill of Lading approved by the International Chamber of Commerce or otherwise indicates that it is issued by a freight forwarder acting as a carrier or agent of a named carrier.

**Article 26**

If a credit calling for a transport document stipulates as such document a marine bill of lading:

a. banks will, unless otherwise stipulated in the credit, accept a document which:

- i. appears on its face to have been issued by a named carrier, or his agent, and
- ii. indicates that the goods have been loaded on board or shipped on a named vessel, and
- iii. consists of the full set of originals issued to the consignor if issued in more than one original, and
- iv. meets all other stipulations of the credit.

b. Subject to the above, and unless otherwise stipulated in the credit, banks will not reject a document which:

- i. bears a title such as "Combined transport bill of lading", "Combined transport document", "Combined transport bill of lading or port-to-port bill of lading", or a title or a combination of titles of similar intent and effect, and/or
- ii. indicates some or all of the conditions of carriage by reference to a source or document other than the transport document itself (short form/blank back transport document), and/or
- iii. indicates a place of taking in charge different from the port of loading, and/or a place of final destination different from the port of discharge, and/or
- iv. relates to cargoes such as those in Containers or on pallets, and the like.

c. Unless otherwise stipulated in the credit, banks will reject a document which:

- i. indicates that it is subject to a charter party, and/or
- ii. indicates that the carrying vessel is propelled by sail only, and/or
- iii. contains the indication "intended", or similar qualification in relation to the vessel and/or the port of loading—unless such document bears an on board notation in accordance with article 27 (b) and also indicates the actual port of loading, and/or the port of discharge—unless the place of final destination indicated on the document is other than the port of discharge, and/or
- iv. is issued by a freight forwarder, unless it indicates that it is issued by such freight forwarder acting as a carrier, or as the agent of a named carrier.

**Article 27**

a. Unless a credit specifically calls for an on board transport document, or unless inconsistent with other stipulation(s) in the credit, or with article 26, banks will accept a transport document which indicates that the goods have been taken in charge or received for shipment.

b. Loading on board or shipment on a vessel may be evidenced either by a transport document bearing wording indicating loading on board a named vessel or shipment on a named vessel, or, in the case of a transport document stating "received for shipment", by means of a notation of loading on board on the transport document signed or initialled and dated by the carrier or his agent, and the date of this notation shall be regarded as the date of loading on board the named vessel or shipment on the named vessel.

**Article 28**

a. In the case of carriage by sea or by more than one mode of transport but including carriage by sea, banks will refuse a transport document stating that the goods are or will be loaded on deck, unless specifically authorized in the credit.

b. Banks will not refuse a transport document which contains a provision that the goods may be carried on deck, provided it does not specifically state that they are or will be loaded on deck.

**Article 29**

a. For the purpose of this article transhipment means a transfer and reloading during the course of carriage from the port of loading or place of dispatch or taking in charge to the port of discharge or place of destination either from one conveyance or vessel to another conveyance or vessel within the same mode of transport or from one mode of transport to another mode of transport.

b. Unless transhipment is prohibited by the terms of the credit, banks will accept transport documents which indicate that the goods will be transhipped, provided the entire carriage is covered by one and the same transport document.

c. Even if transhipment is prohibited by the terms of the credit, banks will accept transport documents which:

- i. incorporate printed clauses stating that the carrier has the right to tranship, or
- ii. state or indicate that transhipment will or may take place, when the credit stipulates a combined transport document, or indicates carriage from a place of taking in charge to a place of final destination by different modes of transport including a carriage by sea, provided that the entire carriage is covered by one and the same transport document, or
- iii. state or indicate that the goods are in a Container(s) trailer(s), "LASH" barge(s), and the like will be carried from the place of taking in charge to the place of final destination in the same Container(s), trailer(s), "LASH" barge(s), and the like under one and the same transport document.
- iv. state or indicate the place of receipt and/or of final destination as "C.F.S." (container freight station) or "C.Y." (container yard) at, or associated with, the port of loading and/or the port of destination.

**Article 30**

If the credit stipulates dispatch of goods by post and calls for a post receipt or certificate of posting, banks will accept such post receipt or certificate of posting if it appears to have been stamped or otherwise authenticated and dated in the place from which the credit stipulates the goods are to be dispatched.

**Article 31**

a. Unless otherwise stipulated in the credit, or inconsistent with any of the documents presented under the credit, banks will accept transport documents stating that freight or transportation charges (hereinafter referred to as "freight") have still to be paid.

b. If a credit stipulates that the transport document has to indicate that freight has been paid or prepaid, banks will accept a transport document on which words clearly indicating payment or prepayment of freight appear by stamp or otherwise, or on which payment of freight is indicated by other means.

c. The words "freight prepayable" or "freight to be prepaid" or words of similar effect, if appearing on transport documents, will not be accepted as constituting evidence of the payment of freight.

d. Banks will accept transport documents bearing reference by stamp or otherwise to costs additional to the freight charges, such as costs of, or disbursements incurred in connection with, loading, unloading or similar operations, unless the conditions of the credit specifically prohibit such reference.

#### *Article 32*

Unless otherwise stipulated in the credit, banks will accept transport documents which bear a clause on the face thereof such as "shippers load and count" or "said by shipper to contain" or words of similar effect.

#### *Article 33*

Unless otherwise stipulated in the credit, banks will accept transport documents indicating as the consignor of the goods a party other than the beneficiary of the credit.

#### *Article 34*

a. A clean transport document is one which bears no superimposed clause or notation which expressly declares a defective condition of the goods and/or the packaging.

b. Banks will refuse transport documents bearing such clauses or notations unless the credit expressly stipulates the clauses or notations which may be accepted.

c. Banks will regard a requirement in a credit for a transport document to bear the clause "clean on board" as complied with if such transport document meets the requirements of this article and of article 27 (b).

#### *D.2 Insurance documents*

#### *Article 35*

a. Insurance documents must be as stipulated in the credit, and must be issued and/or signed by insurance companies or underwriters, or their agents.

b. Cover notes issued by brokers will be not accepted, unless specifically authorised by the credit.

#### *Article 36*

Unless otherwise stipulated in the credit, or unless it appears from the insurance document(s) that the cover is effective at the latest from the date of loading on board or dispatch or taking in charge of the goods, banks will refuse insurance documents presented which bear a date later than the date of loading on board or dispatch or taking in charge of the goods as indicated by the transport document(s).

#### *Article 37*

a. Unless otherwise stipulated in the credit, the insurance document must be expressed in the same currency as the credit.

b. Unless otherwise stipulated in the credit, the minimum amount for which the insurance document must indicate the insurance cover to have been effected is the CIF (cost, insurance and freight... "named port of destination") or CIP (freight/carriage and insurance paid to "named point of destination") value of the goods, as the case may be, plus 10%. However, if banks cannot determine the CIF or CIP value, as the case may be, from the documents on their face, they will accept as such minimum amount the amount for which payment, acceptance or negotiation is requested under the credit, or the amount of the commercial invoice, whichever is the greater.

#### *Article 38*

a. Credits should stipulate the type of insurance required and, if any, the additional risks which are to be covered. Imprecise terms such as "usual risks" or "customary risks" should not be used; if they are used, banks will accept insurance documents as presented, without responsibility for any risks not being covered.

b. Failing specific stipulations in the credit, banks will accept insurance documents as presented, without responsibility for any risks not being covered.

#### *Article 39*

Where a credit stipulates "insurance against all risks", banks will accept an insurance document which contains any "all risks" notation or clause, whether or not bearing the heading "all risks", even if indicating that certain risks are excluded, without responsibility for any risk(s) not being covered.

#### *Article 40*

Banks will accept an insurance document which indicates that the cover is subject to a franchise or an excess (deductible), unless it is specifically stipulated in the credit that the insurance must be issued irrespective of percentage.

#### *D.3 Commercial invoice*

#### *Article 41*

a. Unless otherwise stipulated in the credit, commercial invoices must be made out in the name of the applicant for the credit.

b. Unless otherwise stipulated in the credit, banks may refuse commercial invoices issued for amounts in excess of the amount permitted by the credit. Nevertheless, if a bank authorised to pay, incur a deferred payment undertaking, accept, or negotiate under a credit accepts such invoices, its decision will be binding upon all parties, provided such bank has not paid, incurred a deferred payment undertaking, accepted or effected negotiation for an amount in excess of that permitted by the credit.

c. The description of the goods in the commercial invoice must correspond with the description in the credit. In all other documents, the goods may be described in general terms not inconsistent with the description of the goods in the credit.

#### D.4 Other documents

##### Article 42

If a credit calls for an attestation or certification of weight in the case of transport other than by sea, banks will accept a weight stamp or declaration of weight which appears to have been superimposed on the transport document by the carrier or his agent unless the credit specifically stipulates that the attestation or certification of weight must be by means of a separate document.

#### E. Miscellaneous provisions

##### Quantity and amount

##### Article 43

a. The words "about", "circa" or similar expressions used in connection with the amount of the credit or the quantity or the unit price stated in the credit are to be construed as allowing a difference not to exceed 10% more or 10% less than the amount or the quantity or the unit price to which they refer.

b. Unless a credit stipulates that the quantity of the goods specified must not be exceeded or reduced, a tolerance of 5% more or 5% less will be permissible, even if partial shipments are not permitted, always provided that the amount of the drawings does not exceed the amount of the credit. This tolerance does not apply when the credit stipulates the quantity in terms of a stated number of packing units or individual items.

##### Partial drawings and/or shipments

##### Article 44

a. Partial drawings and/or shipments are allowed, unless the credit stipulates otherwise.

b. Shipments by sea, or by more than one mode of transport but including carriage by sea, made on the same vessel and for the same voyage, will not be regarded as partial shipments, even if the transport documents indicating loading on board bear different dates of issuance and/or indicate different ports of loading on board.

c. Shipments made by post will not be regarded as partial shipments if the post receipts or certificates of posting appear to have been stamped or otherwise authenticated in the place from which the credit stipulates the goods are to be dispatched, and on the same date.

d. Shipments made by modes of transport other than those referred to in paragraphs (b) and (c) of this article will not be regarded as partial shipments, provided the transport documents are issued by one and the same carrier or his agent and indicate the same date of issuance, the same place of dispatch or taking in charge of the goods, and the same destination.

##### Drawings and/or shipments by instalments

##### Article 45

If drawings and/or shipments by instalments within given periods are stipulated in the credit and any instalment is not drawn and/or shipped within the period allowed for that instalment, the credit ceases to be available for that and any

subsequent instalments, unless otherwise stipulated in the credit.

##### Expiry date and presentation

##### Article 46

a. All credits must stipulate an expiry date for presentation of documents for payment, acceptance or negotiation.

b. Except as provided in Article 48 (a), documents must be presented on or before such expiry date.

c. If an issuing bank states that the credit is to be available "for one month", "for six months" or the like, but does not specify the date from which the time is to run, the date of issuance of the credit by the issuing bank will be deemed to be the first day from which such time is to run. Banks should discourage indication of the expiry date of the credit in this manner.

##### Article 47

a. In addition to stipulating an expiry date for presentation of documents, every credit which calls for a transport document(s) should also stipulate a specified period of time after the date of issuance of the transport document(s) during which presentation of documents for payment, acceptance or negotiation must be made. If no such period of time is stipulated, banks will refuse documents presented to them later than 21 days after the date of issuance of the transport document(s). In every case, however, documents must be presented not later than the expiry date of the credit.

b. For the purpose of these articles, the date of issuance of a transport document(s) will be deemed to be:

- i. in the case of a transport document evidencing dispatch, or taking in charge, or receipt of goods for shipment by a mode of transport other than by air—the date of issuance indicated on the transport document or the date of the reception stamp thereon whichever is the later.
- ii. in the case of a transport document evidencing carriage by air—the date of issuance indicated on the transport document or, if the credit stipulates that the transport document shall indicate an actual flight date, the actual flight date as indicated on the transport document.
- iii. in the case of a transport document evidencing loading on board a named vessel—the date of issuance of the transport document or, in the case of an on board notation in accordance with article 27 (b), the date of such notation.
- iv. in cases to which Article 44 (b) applies, the date determined as above of the latest transport document issued.

##### Article 48

a. If the expiry date of the credit and/or the last day of the period of time after the date of issuance of the transport document(s) for presentation of documents stipulated by the credit or applicable by virtue of Article 47 falls on a day on which the bank to which presentation has to be made is closed for reasons other than those referred to in article 19, the stipulated expiry date and/or the last day of the period of time after the date of issuance of the transport document(s) for presentation of documents, as the case may be, shall be extended to the first following business day on which such bank is open.

b. The latest date for loading on board, or dispatch, or taking in charge shall not be extended by reason of the extension of the expiry date and/or the period of time after the date of issuance of the transport document(s) for presentation of document(s) in accordance with this article. If no such latest date for shipment is stipulated in the credit or amendments thereto, banks will reject transport documents indicating a date of issuance later than the expiry date stipulated in the credit or amendments thereto.

c. The bank to which presentation is made on such first following business day must add to the documents its certificate that the documents were presented within the time limits extended in accordance with Article 48 (a) of the Uniform Customs and Practice for Documentary Credits, 1983 revision, ICC Publication No. 400.

#### *Article 49*

Banks are under no obligation to accept presentation of documents outside their banking hours.

#### *Loading on board, dispatch and taking in charge (shipment)*

#### *Article 50*

a. Unless otherwise stipulated in the credit, the expression "shipment" used in stipulating an earliest and/or a latest shipment date will be understood to include the expressions "loading on board", "dispatch" and "taking in charge".

b. The date of issuance of the transport document determined in accordance with article 47 (b) will be taken to be the date of shipment.

c. Expressions such as "prompt", "immediately", "as soon as possible", and the like should not be used. If they are used, banks will interpret them as a stipulation that shipment is to be made within thirty days from the date of issuance of the credit by the issuing bank.

d. If the expression "on or about" and similar expressions are used, banks will interpret them as a stipulation that shipment is to be made during the period from five days before to five days after the specified date, both end days included.

#### *Date terms*

#### *Article 51*

The words "to", "until", "till", "from", and words of similar import applying to any date term in the credit will be understood to include the date mentioned. The word "after" will be understood to exclude the date mentioned.

#### *Article 52*

The terms "first half", "second half" of a month shall be construed respectively as from the 1st to the 15th, and 16th to the last day of each month, inclusive.

#### *Article 53*

The terms "beginning", "middle", or "end" of a month shall be construed respectively as from the 1st to the 10th, the

11th to the 20th, and the 21st to the last day of each month, inclusive.

#### *E. Transfer*

##### *Article 54*

a. A transferable credit is a credit under which the beneficiary has the right to request the bank called upon to effect payment or acceptance or any bank entitled to effect negotiation to make the credit available in whole or in part to one or more other parties (second beneficiaries).

b. A credit can be transferred only if it is expressly designated as "transferable" by the issuing bank. Terms such as "divisible", "fractionable", "assignable", and "transmissible" add nothing to the meaning of the term "transferable" and shall not be used.

c. The bank requested to effect the transfer (transferring bank), whether it has confirmed the credit or not, shall be under no obligation to effect such transfer except to the extent and in the manner expressly consented to by such bank.

d. Bank charges in respect of transfer are payable by the first beneficiary unless otherwise specified. The transferring bank shall be under no obligation to effect the transfer until such charges are paid.

e. A transferable credit can be transferred once only. Fractions of a transferable credit (not exceeding in the aggregate the amount of the credit) can be transferred separately, provided partial shipments are not prohibited, and the aggregate of such transfers will be considered as constituting only one transfer of the credit. The credit can be transferred only on the terms and conditions specified in the original credit, with the exception of the amount of the credit, of any unit prices stated therein, of the period of validity, of the last date for presentation of documents in accordance with Article 47 and the period for shipment, any or all of which may be reduced or curtailed, or the percentage for which insurance cover must be effected, which may be increased in such a way as to provide the amount of cover stipulated in the original credit, or these articles. Additionally, the name of the first beneficiary can be substituted for that of the applicant for the credit, but if the name of the applicant for the credit is specifically required by the original credit to appear in any document other than the invoice, such requirement must be fulfilled.

f. The first beneficiary has the right to substitute his own invoices (and drafts if the credit stipulates that drafts are to be drawn on the applicant for the credit) in exchange for those of the second beneficiary, for amounts not in excess of the original amount stipulated in the credit and for the original unit prices if stipulated in the credit, and upon such substitution of invoices (and drafts) the first beneficiary can draw under the credit for the difference, if any, between his invoices and the second beneficiary's invoices. When a credit has been transferred and the first beneficiary is to supply his own invoices (and drafts) in exchange for the second beneficiary's invoices (and drafts) but fails to do so on first demand, the paying, accepting or negotiating bank has the right to deliver to the issuing bank the documents received under the credit, including the second beneficiary's invoices (and drafts) without further responsibility to the first beneficiary.

g. Unless otherwise stipulated in the credit, the first beneficiary of a transferable credit may request that the credit be transferred to a second beneficiary in the same country, or

in another country. Further, unless otherwise stipulated in the credit, the first beneficiary shall have the right to request that payment or negotiation be effected to the second beneficiary at the place to which the credit has been transferred, up to and including the expiry date of the original credit, and without prejudice to the first beneficiary's right subsequently to substitute his own invoices and drafts (if any) for those of the second beneficiary and to claim any difference due to him.

#### *Assignment of proceeds*

##### *Article 55*

The fact that a credit is not stated to be transferable shall not affect the beneficiary's right to assign any proceeds to which he may be, or may become, entitled under such credit, in accordance with the provisions of the applicable law.

### C. Current activities of international organizations in the field of barter and barter-like transactions: report of the Secretary-General (A/CN.9/253)<sup>a</sup>

#### CONTENTS

	<i>Paragraphs</i>
INTRODUCTION .....	1-2
I. BARTER OR BARTER-LIKE TRANSACTIONS .....	3-6
II. WORK OF INTERNATIONAL ORGANIZATIONS .....	7-19
A. United Nations organizations .....	7-16
1. United Nations Economic Commission for Europe (ECE) .....	7-14
2. United Nations Industrial Development Organization (UNIDO) ...	15-16
B. Work of other organizations .....	17-19
1. Organisation for Economic Co-operation and Development (OECD)	17
2. Work of academic research centres .....	18-19
(a) Centre de Droit des Obligations: Working Group on International Contracts .....	18
(b) Fondation pour l'Etude du Droit et des Usages du Commerce International (FEDUCI) .....	19
III. SOME LEGAL ASPECTS OF BARTER-LIKE TRANSACTIONS .....	20-32
A. Counter-purchase transactions .....	22-27
B. Product buy-back transactions .....	28-32
IV. CONCLUSION .....	33

#### INTRODUCTION

1. At its eleventh session in 1978 the Commission, in its decision on its new programme of work, decided to include as a priority item the subject of international barter and exchange.<sup>1</sup> At its twelfth session the Commission had before it a report of the Secretary-General entitled "Barter or exchange in international trade".<sup>2</sup>

<sup>a</sup>For consideration by the Commission see Report, chapter VI, C (part one, A, above).

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its eleventh session (1978), *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17 (A/33/17)*, paras. 67-69 (Yearbook 1982, part one, II, A).

<sup>2</sup>A/CN.9/159 (Yearbook 1979, part two, I, A).

The Commission decided to request its secretariat to include in the studies then being conducted in respect of contract practices, consideration of clauses of particular importance in barter-like transactions. The Commission also requested the secretariat to approach other organizations within the United Nations engaged in studies on such transactions, and to report to it on the work being undertaken by these organizations.<sup>3</sup>

2. This report is submitted in response to the request of the Commission at its twelfth session. It constitutes a

<sup>3</sup>Report of the United Nations Commission on International Trade Law on the work of its twelfth session (1979), *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17 (A/34/17)*, paras. 21 and 22 (Yearbook 1979, part one, II, A).

part of the series of reports on the work of other organizations in particular areas of international trade law, pursuant to the decision of the Commission at its fourteenth session.<sup>4</sup>

### I. Barter or barter-like transactions

3. The needs of some countries to finance their imports have led importers from these countries to resort to barter or barter-like transactions. Such transactions may assist the importer in developing markets for his own exports in the exporter's country or in third countries, and also help to reduce foreign exchange costs. While barter or barter-like transactions are particularly common in East-West trade, over the last ten years they have also become more common in North-South trade.

4. Barter, in its strict legal sense, is generally defined as a transaction which provides for a direct exchange of goods of approximately equal value between two parties, with no money involved. Such barter transactions, which were employed extensively immediately after the Second World War, are today less often used, because it is difficult to find two parties prepared to make a simultaneous or nearly simultaneous exchange of goods of equivalent value.

5. Barter-like transactions are those transactions which have as a basic characteristic a linkage, legal or otherwise, between exports and imports of goods or services in addition to, or in place of, financial settlement. In contrast to barter, a barter-like transaction is often effected by more than one contract. The terms used in available documents and literature to describe various types of barter-like transactions include counter-trade, contra-trade, and linked transactions. Although there is no generally accepted definition of these terms, the Economic Commission for Europe (ECE) has used the term "counter-trade" as the generic term covering both barter and barter-like transactions, "counter-purchase" to designate short- and medium-term transactions involving an original sales contract and a counter-purchase agreement, and "product buy-back" to designate long-term industrial co-operation agreements where compensation is in whole or in part effected by the purchase of resultant products.<sup>5</sup>

6. *Multilateral barter-like transactions:* In addition to bilateral counter-purchase transactions and buy-back transactions, multilateral forms of barter-like transactions which involve more than two parties also occur. An exporter in State A may conclude an agreement to supply *X* goods to an importer in State B with the coming into force of this agreement made subject to the conclusion or performance of another agreement between an exporter in State B and an importer in State

A for the supply of *Y* goods. Such transactions are sometimes called conjunctive transactions and are concluded in connection with an interstate bilateral clearing agreement with the aim of preventing an undesired surplus in the payment balance of one of the States party to the clearing agreement. Where both the contracts are made interdependent, such transactions are sometimes called reciprocal transactions. Where interdependent agreements are concluded between parties in different States, the value of the goods exchanged between the two States is equal, and no interstate bilateral clearing agreement exists between those States, the monetary obligation may be settled by each of the importers paying the exporter from his State in their local currency, thereby excluding the need for any international payment. Such kinds of transactions are sometimes known as compensation transactions or multilateral barter transactions.

### II. Work of international organizations

#### A. United Nations organizations

##### 1. Economic Commission for Europe (ECE)

7. The subject of counter-trade was first discussed by the ECE at the twenty-seventh session of the Committee on the Development of Trade in 1978, in the context of the Committee's "Review of recent and prospective trends, policies and problems".<sup>6</sup> At the conclusion of its discussion, the Committee invited its secretariat to prepare a report for submission to the twenty-eighth session of the Committee that would define and describe the use of counter-trade practices in the ECE region.<sup>7</sup>

8. Part of the report prepared pursuant to this request, which was entitled "Counter-trade practices in the ECE region",<sup>8</sup> contained a typology of counter-trade arrangements, a description of the main practices encountered in the ECE region and a brief assessment of trends in various sectors. Part two dealt with policies at the national and international levels in the field of counter-trade, and examined the role and the motives of enterprises and organizations engaged in this type of activity. Contractual and financial aspects were also dealt with in the second part of the study. Two addenda to the report, prepared by the joint unit of the ECE secretariat and the United Nations Centre for Transnational Corporations (CTC), dealt with counter-trade practices in specific industries.<sup>9</sup>

<sup>4</sup>ECE/TRADE/130.

<sup>5</sup>Ibid., para. 24 (i).

<sup>6</sup>TRADE/R.385.

<sup>7</sup>"East-west industrial co-operation in the automotive sector and counter-trade arrangements" (TRADE/R.385/Add.1). In view of the close connections between counter-trade and industrial co-operation in the automotive sector, a part of the report was concerned with the terminology, typology and economic significance of various forms of counter-trade. "Institutional arrangements at the national level for counter-trade in selected western countries" (TRADE/R.385/Add.3) examined some of the forms of counter-trade practiced by western chemical producers and plant engineering and contracting firms, including buy-back of resultant or related products and counter-purchase arrangements of non-resultant and often unrelated products.

<sup>8</sup>Report 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).

<sup>9</sup>A useful description of the terminology in use in different countries and for different types of transactions is found in the report of the Economic Commission for Europe, "Counter-trade practices in the ECE region" (TRADE/R.385).

9. Following discussion of this report, the ECE Committee decided to convene an *Ad Hoc* Meeting on Compensation Trade to be held in 1981.<sup>10</sup>

10. In addition to the report previously submitted to the twenty-eighth session of the ECE Committee, four more reports were submitted to the *Ad Hoc* Meeting on Compensation Trade:

(a) "Large-scale and long-term compensation agreements in East-West trade".<sup>11</sup> The purpose of this report was to review the main developments which had taken place since 1968, when the first large-scale and long-term arrangements were signed between Eastern and Western enterprises;

(b) "Reciprocal trading arrangements at the western enterprise level, with special reference to East-West trade".<sup>12</sup> This report examined a representative sample of organizational forms and trading practices currently in use within various industrial and commercial sectors;

(c) "Short- and medium-term linked transactions in East-West trade".<sup>13</sup> This report reviewed the main types of short- and medium-term linked transactions found in East-West trade;

(d) "Counter-trade practices in the chemicals industry: the experience of selected Western chemicals producers and plant contractors in East-West trade".<sup>14</sup>

11. The report of the *Ad Hoc* Meeting on Compensation Trade<sup>15</sup> and a note by the secretariat entitled "Recent developments in compensation trade in the ECE region"<sup>16</sup> containing updated information relevant to compensation trade in the ECE region and a discussion of the problems and perspectives of this type of trade were submitted to the thirty-first session of the ECE Committee held in 1982. The ECE Committee decided to convene a Special Experts' Meeting on Compensation Trade in the summer of 1983 and to return to the subject at its thirty-second session in December 1983.<sup>17</sup>

12. The Special Experts' Meeting had before it a study entitled "Compensation trade in the ECE region: a survey of quantitative estimates".<sup>18</sup> The Meeting also discussed the practical problems encountered in compensation trade by both Eastern and Western operators, in particular small and medium-sized enterprises.

13. At the most recent meeting of the ECE Committee on the Development of Trade, held in December 1983, the subject of compensation agreements was considered

<sup>10</sup>ECE/TRADE/136, annex 1, work area 15.1.1. The preparatory meeting for the *Ad Hoc* Meeting on Compensation Trade was held from 4-7 May, and from 2-4 September 1981, at which the provisional agenda for this meeting was drawn up (see TRADE/AC.18/1).

<sup>11</sup>TRADE/AC.18/R.1.

<sup>12</sup>TRADE/AC.18/R.2.

<sup>13</sup>TRADE/AC.18/R.3.

<sup>14</sup>TRADE/R.410.

<sup>15</sup>TRADE/AC.18/2.

<sup>16</sup>TRADE/R.444.

<sup>17</sup>ECE/TRADE/144, para. 46.

<sup>18</sup>TRADE/AC.19/R.1.

in the context of a "Review of recent and prospective trends, policies and problems in intra-regional trade: a profile of the East-West trade of the USSR".<sup>19</sup>

14. It will be seen that the ECE Committee on the Development of Trade has since 1979 had an active interest in barter-like transactions as they are used in East-West trade. Its studies and reports have described the various forms in which these transactions take place and have served a useful role in clarifying the terminology, typology and economic significance of these transactions.

## 2. United Nations Industrial Development Organization (UNIDO)

15. The subject of compensation and buy-back agreements was considered by the UNIDO Expert Group Meeting on Industrial Financing, in 1978<sup>20</sup> and, subsequently, by the UNIDO Expert Group Meeting on Buy-back Agreements, in 1979.<sup>21</sup> Both meetings dealt with the financing of industrial development in the developing countries.

16. As part of the background material for the study *Industry 2000—New Perspectives*,<sup>22</sup> prepared for the Third General Conference of UNIDO in 1980, UNIDO published a study on barter-like trade and investments.<sup>23</sup>

## B. Work of other organizations

### 1. Organisation for Economic Co-operation and Development (OECD)

17. The OECD secretariat has published various studies on compensation transactions related to major industrial contracts.<sup>24</sup>

### 2. Work of academic research centres

#### (a) Centre de Droit des Obligations: Working Group on International Contracts

18. The Working Group on International Contracts (Louvain) studied the legal aspects of compensation contracts. The results of this study were reflected in a report published in 1981.<sup>25</sup> The report considers the nature of counter-purchase and buy-back transactions and some of the clauses found in such transactions.

<sup>19</sup>TRADE/R.442/Add.5

<sup>20</sup>ID/WG.287/10.

<sup>21</sup>UNIDO/EX.78.

<sup>22</sup>ID/237 (ID/CONF.413).

<sup>23</sup>J. Outters-Jaeger, "Barter-related investment mechanisms" (UNIDO/IOD/324, vol. 1) p. 349.

<sup>24</sup>E.g., OECD, *Counter-trade Practices in East/West Economic Relations* (Paris, 1979); OECD, *East-West Trade in Chemicals* (Paris, 1980); and OECD, *East-West Trade: Recent Developments in Counter-trade* (Paris, 1981).

<sup>25</sup>Marcel Fontaine, "Aspects juridiques des contrats de compensation", *Droit et Pratique du Commerce International—International trade law and practice*, vol. 7, (1981), p. 179.

(b) *Fondation pour L'Etude du Droit et des Usages du Commerce International (FEDUCI)*

19. FEDUCI (Paris) sponsored a colloquium on "Aspects juridiques des contrats de compensation" (Legal aspects of compensation contracts) in 1982. In addition, a number of articles on industrial barter agreements were published under its auspices in *Droit et Pratique du Commerce International—International trade law and practice*.<sup>26</sup>

### III. Some legal aspects of barter-like transactions

20. The dearth of available barter-like contracts in practice makes it difficult to undertake an analysis of the various types of clauses found in such contracts. It has been pointed out in an ECE study that:

"Despite the increasing number of studies which have been devoted in recent years to this phenomenon [compensation trade], the analysis of compensation trade is fraught with considerable difficulties. These difficulties are for the most part attributable to reasons of commercial confidentiality (which limits the scope of available information) and to the different meanings attached to the notion of compensation in various countries (which restrict the comparability of whatever data are available)."<sup>27</sup>

21. While the comment in the ECE study was made to explain the difficulty of analysing the economic effects of barter-like transactions, it applies equally to the legal aspects of these transactions. The following is a review of some of the legal aspects of barter-like transactions as found in documents and literature published on that subject.<sup>28</sup>

#### A. Counter-purchase transactions

22. A counter-purchase transaction often involves two separate agreements, i.e. the original sales contract and an agreement on the part of the primary exporter to

<sup>26</sup>Marcel Fontaine, "Les contrats de contre-achat", *Droit et Pratique du Commerce International—International trade law and practice*, vol. 8 (1982), p. 161; Octavian Capatine, "Considérations sur les opérations de contre-achat dans les relations de commerce extérieur de la Roumanie", *ibid.*, p. 175; Patrick Rothey, "Les contrats de buy-back", *ibid.*, p. 187; Pascal Durand-Bartez, "Le troc dans le commerce international et les opérations de 'switch'", *ibid.*, p. 195; and Albert Previsani, "Coopération industrielle et compensation", *ibid.*, p. 209.

<sup>27</sup>"Compensation trade in the ECE region: a survey of quantitative estimates" (TRADE/AC.19/R.1) para. 3.

<sup>28</sup>Some of the documents published by ECE, UNIDO and OECD which are cited in this study contain some discussion on the legal aspects of barter-like transactions as understood in this study. The work of the Centre de Droit des Obligations and of FEDUCI, is the most thorough source of information on the legal aspects of barter-like transactions. Another significant source of information are the publications by Business International S.A., Geneva, which include the following: *Current Countertrade Policies and Practices in East-West Trade—A Group Research Study* (1976); *Doing Business in Eastern Europe—Operating Techniques* (1977) vols. 1 and 2; *Selling Turnkey Plants and Equipment to Eastern Europe* (1979); and *Payment Practices in Eastern Europe* (1980). See also, Thomas B. McVey, "Countertrade and barter: alternative trade financing by third world nations", *International Trade Law Journal*, vol. 6, (1980-81), p. 197.

counter-purchase an agreed amount of goods. If the counter-purchase goods can be identified with sufficient specificity at the time of the original transaction, a counter-purchase sales agreement for those goods may also be concluded at that time if the parties do not wish to conclude a barter transaction. If not, the parties may agree only that the primary exporter will purchase goods up to a certain value, with the specific goods to be determined in the future. At the time the counter-purchase goods are agreed on, a suppletive counter-purchase sales agreement will be concluded.

23. Even though the economic nature of a counter-purchase transaction may anticipate a minimal net exchange of money, each of the two agreements is usually priced in an agreed currency. This aids in accounting for the transaction, and lays a basis for such matters as customs duties.

24. When the counter-purchase agreement simply specifies that goods up to a certain value are to be purchased in the future, there can be difficulties both in regard to the administration of the contract and in regard to its legal effects. When the goods to be counter-purchased are not specified in detail, there may later be disagreement as to the nature and quality of goods which are to be delivered under the agreement. If the description, quantity and price of the goods are not specified, or a means to determine them is not agreed on in the original contract, some legal systems may even refuse to recognize either that a contract is in existence or that there is an obligation to conclude a contract in the future.

25. The primary exporter may be required to counter-purchase goods for which he has little use and is not equipped to sell. To overcome this difficulty an assignment of the rights and obligations under the counter-purchase agreement is often made to a third party who specializes in such transactions. The anticipated involvement of a third party may call for different terms of the counter-purchase agreement than would be the case if the primary exporter intended to take the counter-purchase goods himself.

26. Most reported counter-purchase agreements contain penalty clauses for the failure to counter-purchase the goods as required. The penalty was usually based on the percentage of the value of the goods to be counter-purchased. A concern often expressed by those obligated to counter-purchase goods was that they might have to pay the penalty even though the reason they have not accepted the goods was their belief that the goods did not meet the necessary standards of quality. A penalty provision may also be included to render the seller under the counter-purchase contract liable for failing to deliver goods of the required quality or for late deliveries.

27. One of the primary legal concerns in connection with counter-purchase transactions is whether the two or more related agreements should be considered legally separate or whether a failure by one party to perform his obligations under one agreement should affect the other party's obligations under another agreement. The

conclusion of two or more agreements may even make it possible to argue that the original sales contract and the counter-purchase agreement are legally separate. In general, the seller under a counter-purchase agreement prefers them to be considered together, since he might have to pressure the primary exporter to accept goods under the counter-purchase agreement. The primary exporter tends to prefer separate treatment so that disputes in regard to the counter-purchase agreement would not affect the original sales contract. On the other hand, however, if the original sales contract is terminated for any reason, he may not wish to continue to be obligated under the counter-purchase agreement. Third parties to whom the rights and obligations under the counter-purchase agreements have been assigned may have an interest that the agreement be treated separately since they may already have made arrangements in anticipation that the counter-purchase agreement would be executed.

#### B. Product buy-back transactions

28. Product buy-backs occur in long-term industrial co-operation agreements for the acquisition of plants, equipment or natural resources. These agreements which usually include licensing or transfer of technology necessary to operate the items purchased, are considerably more complicated than those for the ordinary counter-purchase of goods or services. Furthermore, their long-term nature often makes it difficult to specify in the contract all of the matters which will arise during the course of the contract. Although this is true of all contracts for the acquisition of large industrial works, particular difficulties arise in connection with the buy-back aspect of the transaction.

29. In a buy-back agreement the goods to be purchased by the primary exporter are usually the resultant product from the plant to be supplied by him. To this extent the buy-back agreement tends to be more specific than is a counter-purchase agreement.

30. However, since the buy-back obligation does not commence until the plant or equipment is installed and operating and it usually extends over a long period of time, there are particular difficulties in establishing the

price. According to an ECE study,<sup>29</sup> there does not appear to be any accepted formula for calculating the price of counter-deliveries under buy-back agreements as the pricing formula may depend on the types of buy-back products.

31. The UNIDO Expert Group Meeting on Buy-back Agreements, held in 1979, suggested some methods of pricing and made the following main observations: "(i) Products should be supplied at best market prices plus appropriate commissions; (ii) Each shipment needs a separate agreement on pricing through negotiation; (iii) Fix prices on the basis of the calculated price with an escalation clause which would go into force through renegotiations if the deviation would exceed, for instance, +10%; (iv) Competitive bidding (offers); . . . and (vi) Periodic price fixing (every 3, 6 or 12 months) could be agreed upon."<sup>30</sup>

32. Since the goods to be purchased under the buy-back agreement are usually the product of the plant or equipment installed under the primary contract, the obligations under the buy-back agreement would usually be legally linked to the obligations under the primary contract.

#### IV. Conclusion

33. There have been attempts to overcome various obstacles existing in the field of international payments which interfere with the development of trade, by resorting to barter or barter-like transactions. However, most of the studies on the subject indicate that problems encountered in such transactions are far more economic and financial than legal. Moreover, even if an international uniform regulation were desired, the complexity of these transactions and their variety may militate against such a possibility. At the same time, any general conclusion may be somewhat hazardous in the absence of a sufficient volume of contracts that are easily available for analysis. The Commission may wish to take note of the intention of the secretariat to continue to monitor developments in this field.

<sup>29</sup>"Counter-trade practices in the chemicals industry: The experience of selected western chemicals producers and plant contractors in East-West trade" (TRADE/R.410) para. 34.

<sup>30</sup>UNIDO/EX.78, para. 4.

#### D. Legal aspects of automatic data processing: report of the Secretary-General (A/CN.9/254)<sup>a</sup>

#### CONTENTS

	<i>Paragraphs</i>
INTRODUCTION .....	1-3
SOME LEGAL ISSUES .....	4-17
A. Legal value of computer records .....	4-6
B. Requirement of a writing .....	7

<sup>a</sup>For consideration by the Commission see Report, chapter VI, D (part one, A, above).

	Paragraphs
C. Authentication .....	8-9
D. General conditions .....	10-11
E. Liability .....	12-13
F. Bills of lading .....	14-17
<b>CONCLUSION .....</b>	<b>18</b>

---

## INTRODUCTION

1. The Commission, at its sixteenth session, had before it a note by the secretariat which conveyed in an annex a report on the legal aspects of automatic data processing (ADP) of the ECE/UNCTAD Working Party on Facilitation of International Trade Procedures (A/CN.9/238; *Yearbook 1983*, part two, V, D). 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 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. The Commission took note of the intention of the secretariat to submit to the seventeenth session a report on this subject.<sup>1</sup>

2. The use of various ADP techniques is already firmly established throughout the world and is to be found in most phases of both domestic and international trade. As the cost of ADP equipment has reduced, the cost advantages arising out of its use have extended to an increasing number of activities and users in all countries, and this trend is continuing. One consequence has been that legal rules based upon pre-ADP paper-based means of documenting international trade transactions are leading to legal insecurity in some cases and in other cases are impeding the efficient use of ADP where its use is otherwise economically justified.

3. The legal issues in respect of which the Commission might best serve as the central forum are those in which adaptations in the existing law governing international trade transactions may be necessary in order to accommodate the use of ADP for the facilitation of trade. Although no complete listing of such legal issues can be made at this time, since developments in ADP are certain to give rise to new problems not presently foreseen, some important legal issues have already been identified.

## Some legal issues

- A. *Legal value of computer records*
- 4. In many countries rules of general application require that commercial as well as other types of transactions must be in writing, or provide that those transactions can be proven in case of dispute only by a writing. In these countries the record of a transaction stored in a computer or in a magnetic tape or other computer memory device is of doubtful legal value. Furthermore, paper-based records produced by the computer may also be of questionable legal value, since there may be the same doubts as to the accuracy of the data.
- 5. As a result of the need to accommodate the widespread use of computers for commercial and administrative purposes, a number of countries have changed the relevant legislation to permit the use of computers in these circumstances and to accept as evidence records stored in computers or in computer memory devices when certain criteria are met. Because of the discrepancy in the criteria used to decide on the legal value of these records, as well as the existence of other States which continue not to accord any legal value to computer records, there are serious problems for the use of such records which have been stored in one State as evidence in a dispute arising in another State. Furthermore, many of the laws enacted to facilitate the legal acceptability of computer records did not anticipate the problems which might be created when the computer record was created in the computer of one firm or agency, transmitted to the computer of another firm or agency by teletransmission or by the physical delivery of a computer memory device and stored in the second computer.
- 6. The Commission at its fifteenth session requested the secretariat to submit to a future session of the Commission a report on the legal value of computer records.<sup>2</sup> A report on this subject will be submitted to the eighteenth session of the Commission. As part of its preparation for the report, the secretariat has sent a note verbale to all Governments enclosing a questionnaire requesting information on this subject.

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its sixteenth session, *Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17 (A/38/17)*, para. 118 (*Yearbook 1983*, part one, A).

<sup>2</sup>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)*, para. 73 (*Yearbook 1982*, part one, A).

### B. Requirement of a writing

7. Many legal rules which require that a transaction be made in or evidenced by a writing, accept a telegramme or a telex as a writing. Presumably, these legal rules would also accept a paper print-out from a computer as a writing. In many cases one party enters data into a computer and for technical or legal reasons produces a print-out of that data for transmission to the other party, who then re-enters the data into its own computer. The Customs Co-operation Council is conducting a study which, *inter alia*, enquires into the extent to which customs authorities accept goods declarations in computer-readable form, either by the teletransmission of the data or by the physical transmission of a computer memory device.

### C. Authentication

8. Paper-based documents are often authenticated by the signature of an authorized person. Although usually handwritten, in many countries a signature may also be made by a stamp or other mechanical or electronic means, and a number of international conventions recognize this practice.<sup>3</sup>

9. Techniques are available to verify the terminal from which a teletransmitted message was sent as well as to verify the identity of the sender of such a message or the source of a magnetic tape or other computer memory device. These techniques seem to offer an assurance of genuineness that is at least equivalent to that of a signature. Nevertheless, authentication of an electronic message by electronic means may not be accepted in all countries. The question has been raised whether an electronic authentication on a paper-based print-out would serve as a "signature" for purposes of a statutory requirement that the particular type of transaction be evidenced by a signed writing.

### D. General conditions

10. Many commercial documents used in international trade contain the general conditions applicable to the transaction. When traditional paper-based documents are eliminated in favour of the teletransmission of the essential data, there is no location available in the teletransmitted message for the economical reproduction of the general conditions applicable to the transaction.

11. In some countries incorporation of general conditions by reference in a contract or in a document is widely practiced. The ECE/UNCTAD Working Party on Facilitation of International Trade Procedures has recommended an incorporation clause for use in

<sup>3</sup>The Commission itself has accepted such forms of authentication for use on paper-based bills of lading (United Nations Convention on the Carriage of Goods by Sea, 1978, art. 14 (3); *Yearbook 1978*, part three, I, B) and a similar provision is before the Commission at this session in the draft Convention on International Bills of Exchange and International Promissory Notes and the draft Convention on International Cheques (A/CN.9/211, art. 4 (10); A/CN.9/212, art. 6 (8); *Yearbook 1982*, part two, II, A, 3 and 5).

shipper-supplied or blank-back transport documents.<sup>4</sup> The recommended clause could easily be adapted to other forms of contract or document. However, in other countries general conditions incorporated into a contract or document by reference are not enforced in respect of some or all types of contracts and documents used in international trade. The general concern is that the party receiving the contract or document, or others who might rely on it, would not have adequate access to the current version of the general conditions and would not, therefore, be in a position to know the intended contractual terms. Furthermore, there is a concern that general conditions whose terms are unknown to one of the parties at the time of contracting may be unfair.

### E. Liability

12. It is expected that the advent of wide-spread inter-firm computer-to-computer teletransmission of data will raise questions of liability which cannot easily be solved by application of traditional rules. Some of the sources of error and delay in the transmission and reception of messages are distinctly different from those where other modes of telecommunication are involved. Although it would appear that the rules in respect of liability might also be different, the outlines of the problem are not clear and there has as yet been little research on the subject. In explanation of this state of affairs the secretariat for the Organisation for Economic Co-operation and Development, which commissioned several studies by consultants attempting to establish a conceptual framework for further analysis of liability in transborder data flows, has observed: "The main problems encountered in determining liability are due to: (1) the number of transactors involved in data flows and thus the wide range of potentially harmful behaviour; (2) the newness of the technology and the consequent lack of precision as regards liability arising from its use, the difficulty of deciding who is liable and the resulting problems of what evidence is required."<sup>5</sup>

13. The impact of the new technology on liability for errors and delay in the context of electronic funds transfers is discussed in the draft chapter of the legal guide on electronic funds transfers which is before the Commission at this session for general comments.<sup>6</sup> The consideration of the problems within that specific factual setting may also help to clarify the issues within the broader setting of data flow in general.

### F. Bills of lading

14. The difficulties arising out of the arrival of goods at the port of destination prior to arrival of the bill of

<sup>4</sup>Recommendation No. 12, para. 16, TRADE/WP.4/INF.61, TD/B/FAL/INF.61, quoted in A/CN.9/225, para. 61 (*Yearbook 1982*, part two, VI, B).

<sup>5</sup>Organisation for Economic Co-operation and Development, "Programme of work on the legal aspects of transborder data flows" (DSTI/ICCP 82.5) p. 2.

<sup>6</sup>A/CN.9/250/Add.4 (reproduced in this *Yearbook*, part two, I, B, 6).

lading are well-known. A number of different solutions have been proposed. When the goods are not to be sold while in transit and are not financed under a letter of credit, in certain trades a sea waybill is often used permitting the carrier to deliver to the consignee without presentation of a transport document.

15. Other proposed solutions rely upon the tele-transmission of data in various forms. When a bill of lading is required at the port of discharge to satisfy administrative requirements, to allow for sale of the goods while afloat or to secure financing under a letter of credit from a bank at the port of discharge, the essential data could be teletransmitted to that port and the bill of lading be issued by the carrier at that place.<sup>7</sup>

16. Under another proposed solution, the bill of lading issued at the port of loading would be deposited in a central registry and subsequent sales or financing of the goods would be notified to the registry by teletransmission. When the goods arrived at the port of discharge, the registry would notify the carrier that it had the bill of lading in its possession and would inform the carrier of the proper recipient of the goods.<sup>8</sup> Yet other proposals envisage the complete substitution of paper-based maritime transport documents by the tele-transmission of the essential data. Such a proposal is most easily implemented where a sea waybill would otherwise be acceptable. Where a bill of lading would be needed to satisfy administrative requirements, to facilitate sale of the goods afloat or to finance the sale through a letter of credit, special techniques have been envisaged which are intended to give the same security of control over the goods as is currently offered by the bill of lading.

<sup>7</sup>A/CN.9/225, para. 33 (Yearbook 1982, part two, VI, B).

<sup>8</sup>The UNCTAD *Ad hoc* Intergovernmental Group to consider Means of Combating all Aspects of Maritime Fraud, including Piracy, at its meeting held at Geneva from 6 to 17 February 1984, requested the Trade and Development Board to invite the relevant specialized international and commercial organizations to study, *inter alia*, this proposal as a means of combatting documentary fraud (TD/B/L.684).

17. The proposals to reduce delays at the port of discharge and to reduce the cost of documentation for ocean shipment of goods by substitution of other acceptable forms of transport documentation, and particularly by the eventual use of data transmission as an optional form of documentation, face many legal and commercial obstacles before they can be realized. Among the legal obstacles are the need to find a means to incorporate general conditions of transport into the contract in an acceptable way, as mentioned in paragraphs 10 to 11 above, and the refinement of the techniques referred to above for assuring adequate control over the goods while afloat.

#### Conclusion

18. The need for co-ordination by the Commission to find appropriate and harmonized solutions to the legal problems which are arising out of ADP has been stressed at various fora as being of particular importance because, with the exception of the Commission, the international organizations competent in respect of aspects of these problems are either regional in nature or have a specialized substantive competence. The Commission at its fifteenth session has already recognized the increasing importance to international trade law of the legal problems arising out of ADP by its request to the secretariat to commence the preparation of a draft legal guide on electronic funds transfers and to submit to a future session of the Commission a report on the legal value of computer records. The Commission may now wish to decide that the subject of legal implications of ADP to the flow of international trade should be added as a priority item. A session of one of the working groups may be held to identify the concrete areas where solutions or the establishment of international understandings are desirable. Other international organizations concerned might be invited with the view in mind to co-ordinate activities in this field as well as to identify concrete projects on which it might be suitable for the Commission to commence work on its own. The holding of such a session may be appropriate after the Commission's eighteenth session.

## VI. STATUS OF CONVENTIONS

### Note by the secretariat (A/CN.9/257)<sup>a</sup>

1. At its thirteenth session, in 1980, 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.\*

2. The present note is submitted pursuant to that decision. The annex hereto sets forth the state of signatures, ratifications and accessions as at 25 May 1984 to the following conventions: Convention on the Limitation Period in the International Sale of Goods (New York, 1974) (*Yearbook 1974*, part three, I, B); Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980) (*Yearbook 1980*, part three, I, C); United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg) (*Yearbook 1978*, part three, I, B); and United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980) (*Yearbook 1980*, part three, I, B).

### ANNEX

#### *1. Convention on the Limitation Period in the International Sale of Goods (New York, 1974)*

<i>State</i>	<i>Signature</i>	<i>Ratification</i>	<i>Accession</i>
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**

<sup>a</sup>For consideration by the Commission see Report, chapter VIII, (part one, A, above).

\*Report 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).

\*\*By virtue of accession to Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980) (article VIII (2) of the Protocol).

<i>State</i>	<i>Signature</i>	<i>Ratification</i>	<i>Accession</i>
German Democratic Republic	14 June 1974		
Ghana	5 December 1974	7 October 1975	
Hungary	14 June 1974	16 June 1983	
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: 10; ratifications and accessions: 8

#### *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).

#### *2. Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980)*

<i>State</i>	<i>Accession</i>
Argentina	19 July 1983
Egypt	6 December 1982
Hungary	16 June 1983

#### *3. United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg)*

<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		

<i>State</i>	<i>Signature</i>	<i>Ratification</i>	<i>Accession</i>	<i>State</i>	<i>Signature</i>	<i>Ratification</i>	<i>Accession</i>
Ecuador	31 March 1978			Chile	11 April 1980		
Egypt	31 March 1978	23 April 1979		China	30 September 1981		
Finland	18 April 1979			Czechoslovakia	1 September 1981		
France	18 April 1979			Denmark	26 May 1981		
Germany, Federal Republic of	31 March 1978			Egypt			6 December 1982
Ghana	31 March 1978			Finland	26 May 1981		
Holy See	31 March 1978			France	27 August 1981	6 August 1982	
Hungary	23 April 1979			German Democratic Republic			
Lebanon			4 April 1983		13 August 1981		
Madagascar	31 March 1978			Germany, Federal Republic of	26 May 1981		
Mexico	31 March 1978			Ghana	11 April 1980		
Morocco			12 June 1981	Hungary	11 April 1980	16 June 1983	
Norway	18 April 1979			Italy	30 September 1981		
Pakistan	8 March 1979			Lesotho	18 June 1981	18 June 1981	
Panama	31 March 1978			Netherlands	29 May 1981		
Philippines	14 June 1978			Norway	26 May 1981		
Portugal	31 March 1978			Poland	28 September 1981		
Romania			7 January 1982	Singapore	11 April 1980		
Senegal	31 March 1978			Sweden	26 May 1981		
Sierra Leone	15 August 1978			Syrian Arab Republic			19 October 1982
Singapore	31 March 1978			United States of America	31 August 1981		
Sweden	18 April 1979			Venezuela	28 September 1981		
Tunisia			15 September 1980	Yugoslavia	11 April 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: 9

#### *Declarations and reservations*

Upon signing the Convention the Czechoslovak Socialist Republic declared in accordance with article 26 a formula for converting the amounts 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.

#### *4. United Nations Convention on Contracts for the International Sale of Goods, Vienna (1980)*

<i>State</i>	<i>Signature</i>	<i>Ratification</i>	<i>Accession</i>
Argentina			19 July 1983
Austria	11 April 1980		

#### *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).

Upon ratifying the Convention the Government of Hungary declared that it considered the General Conditions of Delivery of Goods between Organizations of the Member Countries of the Council for Mutual Economic Assistance (GCD CMEA, 1968/1975, version of 1979) to be subject to the provisions of article 90 of the Convention.

Upon ratifying the Convention the Governments of Argentina and Hungary stated, in accordance with articles 12 and 96 of the Convention, that any provision of article 11, article 29 or Part II of the Convention that allows a contract of sale or its modification or termination by agreement or any offer, acceptance or other indication of intention to be made in any form other than in writing, does not apply where any party has his place of business in their respective States.

## VII. TRAINING AND ASSISTANCE

### Report of the Secretary-General (A/CN.9/256)<sup>a</sup>

1. At its sixteenth session in 1983, the Commission decided that it would be desirable to continue the sponsorship of symposia and seminars on international trade law in collaboration with other organizations.<sup>1</sup> It also affirmed the importance of regional symposia and seminars, both for the purpose of promoting the work of the Commission, and for the purpose of making participants, particularly from developing countries, aware of current legal problems of international trade. The Commission approved the approach taken by the secretariat in organizing symposia and seminars.

2. By its resolution 38/134 of 19 December 1983 on the report of the Commission on the work of its sixteenth session, the General Assembly reaffirmed the importance, in particular for developing countries, of the work of the Commission concerned with training and assistance in the field of international trade law. It also reaffirmed the desirability for the Commission to sponsor symposia and seminars, in particular those organized on a regional basis, to promote training and assistance in the field of international trade law. The General Assembly also expressed its appreciation to Governments and institutions for arranging symposia and seminars, and invited Governments, relevant United Nations organs, organizations, institutions and individuals to assist the secretariat in financing and organizing symposia and seminars. The main activities undertaken in this field by the UNCITRAL secretariat since the sixteenth session of the Commission are set forth below.<sup>2</sup>

3. The UNCITRAL secretariat for the second time co-operated with the Organization of American States (OAS) in its annual international law seminar (Rio de Janeiro, Brazil, 18-19 August 1983). The subjects discussed at this seminar included, *inter alia*, the activities of the Commission, the United Nations Convention on the Carriage of Goods by Sea, 1978 (hereinafter referred to as the Hamburg Rules), and the draft legal guide on drawing up international contracts for the construction of industrial works. The seminar was attended by lawyers from several Latin American countries.

<sup>a</sup>For consideration by the Commission see Report, chapter VII (part one, A, above).

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its sixteenth session, *Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17* (A/38/17), para. 130 (Yearbook 1983, part one, A).

<sup>2</sup>See also, "Co-ordination of work in general" (A/CN.9/255; reproduced in this Yearbook, part two, V, A).

4. An international conference on the techniques of international commerce (Abidjan, Ivory Coast, 21-23 November 1983) was organized by the International Chamber of Commerce and the Chamber of Industry of the Ivory Coast, with the collaboration of the UNCITRAL Secretariat and the Economic Community of West Africa. The subjects considered included, *inter alia*, the work of the Commission, the unification of international trade law and international commercial arbitration. The Conference was attended by lawyers, businessmen and government officials from several countries of West Africa.

5. A regional symposium on arbitration (New Delhi, India, 12-14 March 1984) was organized by the Asian-African Legal Consultative Committee (AALCC) and the UNCITRAL secretariat, and was hosted by the Indian Council of Arbitration. The symposium was attended by government officials and practising lawyers from many countries in the Asian-African region. The focus of the symposium was the work of UNCITRAL in the field of international commercial arbitration. The symposium also considered the activities of the regional arbitration centres at Kuala Lumpur and Cairo organized under the auspices of the AALCC, and problems currently encountered in the practice of arbitration. These regional arbitration centres use the UNCITRAL Arbitration Rules as their own.

6. A regional symposium on the activities of UNCITRAL is planned to be held in June 1984 in Bogota, Colombia. The symposium will be organized by the Chamber of Commerce of Bogota, in collaboration with the UNCITRAL secretariat. The symposium has the support of the OAS secretariat, and lawyers, businessmen and government officials from the Andean region will be invited to participate. The symposium will discuss, in particular, the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980) (hereinafter referred to as the Vienna Sales Convention), the model law on international commercial arbitration, the Hamburg Rules, the draft legal guide on drawing up international contracts for the construction of industrial works, and the relevance of the work of UNCITRAL for the countries of the Andean region.

7. An Asian Pacific Regional Trade Law Seminar (Canberra, Australia, 22-27 November 1984) will be conducted by the Attorney-General's Department of Australia, in association with the UNCITRAL secre-

tariat and the Asian-African Legal Consultative Committee (AALCC). The International Institute for the Unification of Private Law (UNIDROIT) and the Hague Conference on Private International Law will also participate. The UNCITRAL secretariat has cooperated in mobilizing the expertise of these organizations as well as of the AALCC. The Seminar has as its theme the unification and harmonization of international trade law and practices with particular reference to the work and role of the Commission as the core international legal body in the field. The Seminar is specially designed to contribute to the Commission's programme in training and assistance, and the Government of Australia will provide fellowships for participants from the region.

8. A workshop on the Vienna Sales Convention was held at the biennial LAWASIA Conference (Manila, Philippines, 9-13 September 1983). The Conference was very widely attended by lawyers from the Asian and Pacific region. The UNCITRAL secretariat presented the Vienna Sales Convention to the workshop, and interest was created in adhering to the Convention by States of the Asian and Pacific region. A resolution was adopted urging Governments in the Asian-Pacific region to disseminate appropriate information about the Convention with the end in view of ensuring its ratification within the shortest possible time.

9. A workshop on the legal aspects of foreign trade (Geneva, 21-25 November 1983) was organized by the UNCTAD/GATT International Trade Centre, with the collaboration of the UNCITRAL secretariat and of the International Chamber of Commerce. The purpose of the workshop was to produce a guide on the legal aspects of foreign trade to assist chambers of commerce and governmental trade promotion agencies. The guide is being prepared by consultants under the auspices of the UNCTAD/GATT International Trade Centre. The workshop was attended by lawyers and officials representing chambers of commerce and trade promotion agencies in Africa, Asia and Latin America.

10. The UNCITRAL secretariat was invited to a symposium organized by the American Bar Association (Atlanta, United States of America, 1-2 August 1983) on the Vienna Sales Convention. The symposium considered the value of the Vienna Sales Convention as an instrument for harmonizing the law of international sales. The general conclusion of the symposium was that the Vienna Sales Convention was an acceptable compromise between the different approaches of national law towards international sales contracts. An international conference was also organized (New York, 21-22 October 1983) by the Parker School of Foreign and Comparative Law, Columbia University, New

York, on the Vienna Sales Convention. The Conference examined the solutions adopted in the Convention to certain key problems in international sales contracts in relation to solutions adopted in various national systems. The UNCITRAL secretariat was invited to the Conference and explained the approaches adopted in the Vienna Sales Convention to those problems. An international trade law seminar (Ottawa, Canada, 20 October 1983), at which the UNCITRAL secretariat was also invited to participate, was organized by the Department of Justice of Canada. The secretariat described the recent achievements of UNCITRAL, and discussed with participants at the seminar the on-going work programme of UNCITRAL. Interest in the activities of UNCITRAL was exhibited by active participation from all provinces of Canada.

11. The UNCITRAL secretariat was invited to take part in an international conference of experts (Bielefeld, Federal Republic of Germany, 20-22 June 1983) on the theme of the adaptation and renegotiation of international commercial contracts. The secretariat made a presentation on the UNCITRAL Conciliation Rules, and the conference discussed the Rules in the context of the adaptation and renegotiation of contracts. The UNCITRAL secretariat also participated in an international arbitration symposium (London, 5-6 July 1983) organized by the Chartered Institute of Arbitrators. The symposium extensively discussed the UNCITRAL model law project on international commercial arbitration. The secretariat explained the main features of the UNCITRAL model law, in particular with reference to the common law rules on arbitration.

12. The UNCITRAL secretariat participated in a conference of scholars of international private law and international trade law (Ludwigsburg, Federal Republic of Germany, 25-30 September 1983). A presentation was made of explaining some significant features of the Hamburg Rules, and also the work of the Commission on a universal unit of account for international conventions.

13. On several occasions other than those mentioned in the preceding paragraphs, the UNCITRAL secretariat has addressed gatherings of lawyers and government officials in order to promote the work of the Commission. The secretariat intends to keep in touch with organizations and Governments with a view to collaborating with them in organizing symposia and seminars.

14. During the past year, three interns received training with the UNCITRAL secretariat, and were associated with on-going projects of the Commission.

# I. SUMMARY RECORDS OF THE UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW FOR SESSIONS DEVOTED TO THE PREPARATION OF DRAFT LEGAL TEXTS<sup>a</sup>

Draft Convention on International Bills of Exchange and International Promissory Notes and  
draft Convention on International Cheques<sup>b</sup>

*Summary records of the 286th to 299th and 301st meetings  
25 June-6 July 1984*

---

## Summary record of the 286th meeting Monday, 25 June 1984, 3 p.m.

[A/CN.9/SR.286]

Chairman: Mr. SZASZ

The meeting was called to order at 3.10 p.m.

1. Mr. SONO (Secretary of the Commission) said that the two draft Conventions before the Commission were the product of long efforts by the Working Group on International Negotiable Instruments and represented a corner-stone of the Commission's work in the field of international payments. The Commission also had before it an analytical compilation of the comments of Governments and international organizations (A/CN.9/248) and a note by the secretariat which identified major controversial and other issues in the light of comments received (A/CN.9/249 and Add.1).

2. The CHAIRMAN suggested that the Commission should begin with a general discussion and then identify particular points for special debate. He trusted that those points would be along the lines of the key features and major controversial issues identified by the secretariat. He wished to emphasize that the Commission should not function as a drafting or working group; the objective was to take a final decision on the future course of action.

3. Mr. CHAFIK (Egypt) said that efforts in the field of negotiable instruments should be directed towards the revision of 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 with a view to making them more acceptable to countries following the Anglo-American system and more in accord with the present needs of international trade. The Uniform Laws had contributed to unifying banking practice and

resolving legal difficulties. Nevertheless, the draft Conventions under consideration represented a workable compromise between the two current legal systems for negotiable instruments, and were therefore most likely to be adopted by the majority of States. Egypt was ready to accept them, subject to certain formal and substantive amendments.

4. For the provisions to be fully effective and in order to prevent the use of different types of international exchange instruments, the Conventions should be multilateral and binding. The alternative—a uniform law—would not bring about the necessary standardization, and an optional system would lead to a diversity of negotiable instruments in international operations, possibly resulting in a conflict of laws. Two separate Conventions had been recommended to the Commission, and that was a preferable solution since it would leave any State free to adopt the position it deemed most appropriate to its interests with regard to each Convention.

5. Both draft Conventions were purely international in their scope of application. Unfortunately, contracting parties would therefore have two parallel systems in operation, one for national instruments and the other for international instruments. Such parallelism was a complication that could be avoided, and there was nothing in the draft Conventions to prevent a State from extending the scope of the Conventions to both categories of instruments. That was a possibility which some parties might accept but others would reject.

6. Mr. MAEDA (Japan) said that it would be of great benefit to unify the Anglo-American and Geneva systems. His Government believed that the draft Convention on International Bills of Exchange and International Promissory Notes provided an excellent basis for achieving a compromise between the two systems. Japanese banking and trading circles likewise considered the fundamental principles on which the draft was based to be quite acceptable, although it was felt that some provisions could be improved to make the text more comprehensive.

7. With regard to the draft Convention on International Cheques, it was undeniable that electronic funds transfers,

<sup>a</sup>The summary records contained in this volume include the corrections requested by the delegations and such editorial changes as were considered necessary.

<sup>b</sup>For all documents referred to in the discussion, see this Yearbook, part two, I, A.

*inter alia*, were replacing cheques as a tool of international payment. However, cheques still played a significant role in international settlements, and his Government supported the idea of creating an international cheque for the same reason that it supported the idea of a new international bill of exchange or promissory note. Nevertheless, in order to leave States free to adopt either or both of the Conventions, Japan felt it was appropriate to consider the two separately.

8. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics) said that the draft Convention on International Bills of Exchange and International Promissory Notes was the result of a great deal of fruitful work aimed at the further unification of the rules governing such negotiable instruments. To achieve uniformity in international trade law, it was necessary to resolve the problems arising from the differences between the civil-law and common-law systems and to revise existing norms which were not consonant with the needs of present-day practice governing international payments.

9. While the proposed Convention largely met those requirements, the draft nevertheless had certain drawbacks. Some of the provisions were formulated imprecisely or required the reader to refer to other articles for clarification. That applied, for instance, to articles 16 and 17 and also to chapter 5, which did not give a unified picture of the conditions for presentation and recourse. Other provisions were made unduly complicated or were too theoretical. Article 46 was totally impractical in the way it was formulated; a much simpler procedure was already provided under article 34, paragraph (2). His delegation also had misgivings about article 52 and others on delays in presentation. Finally, in some cases the draft diverged from the principle that the rights and obligations of contracting parties should be determined only by the content of the bills of exchange themselves.

10. However, the drawbacks did not detract from the merits of the draft Convention, which on the whole was acceptable and could serve as a basis for further work in producing a final text. His delegation favoured the adoption of a separate convention on negotiable instruments for optional use.

11. Mr. ANKELE (Federal Republic of Germany) said that while his Government welcomed efforts to unify legislation on negotiable instruments so as to facilitate international trade and payments, it seriously doubted that the draft Convention on International Bills of Exchange and International Promissory Notes would serve that purpose. The new legal system proposed in the draft might have an adverse effect on the broad harmonization of legislation already achieved by the Geneva system and could well result in a conflict of laws.

12. Despite its shortcomings, the draft Convention would be acceptable if it met an important practical need. However, that was not the case since the Geneva system had so far not given rise to serious difficulties in the handling of financial operations. The draft was of necessity a compromise, with all the disadvantages that entailed. The new system was unlikely to gain wide use in international practice because, compared with the Geneva system, it was very complex and unclear and offered only limited protection for the circulation of bills of exchange.

13. His Government felt that the Commission's efforts to unify legislation on international negotiable instruments should be aimed at revising the Geneva Uniform Laws so as to make them acceptable to a larger number of States and at developing that system, as necessary, to meet the requirements of modern international payments operations. The Working Group had, of course, a useful role in that process.

14. His Government also had reservations about the practical need for a convention on international cheques. Instruments other than cheques were available for carrying out international transactions. Moreover, given the differences in banking systems, a solution acceptable to the majority could not realistically be expected.

15. Mr. MAGNUSSON (Sweden) said that the texts under consideration represented a workable compromise between the two legal systems. Swedish banking exports, however, had some doubts as to whether the Conventions were necessary. Since the coexistence of the Geneva and common-law systems had as yet presented no problem, there was no clear need for a compromise system. His Government had suggested that it might be time to revise and update the Geneva Uniform Laws, and it had submitted a document on the matter to the Council of Europe. Although the process of revision would involve many practical problems, it would make the Uniform Laws more acceptable to the countries of the common-law system. However, Sweden would not insist on such a revision until it saw the outcome of deliberations on the UNCITRAL draft.

16. Although the draft Convention was commendable in many ways, the text should be clarified and the articles rearranged in order to make it more understandable. The Uniform Laws would also have to be changed to enable States parties to opt out and choose the new system. There was also the question whether the Conventions should be binding.

17. His delegation was optimistic and would not oppose future attempts to create a new compromise system. While it had greater misgivings about the draft Convention on International Cheques, it believed that it would not make sense to have a convention on international bills of exchange without some provision being made for international cheques. Although cheques were becoming less important in international trade, they still played an important role in relations between certain countries.

18. Mr. DUCHEK (Austria) said that his Government viewed the principle of the draft Convention on International Bills of Exchange and International Promissory Notes as an acceptable compromise, but had strong reservations about the over-complicated language and structure. The Working Group should revise and simplify the text. He agreed with the representative of Sweden that States parties to the Geneva Uniform Laws would be unable to ratify the Convention on International Bills of Exchange unless the Uniform Laws were changed.

19. With regard to the draft Convention on International Cheques, he suggested that the work should be concentrated on bills of exchange rather than cheques, since the use of cheques was being replaced by electronic funds transfers.

20. Mr. WAGNER (German Democratic Republic) reaffirmed that both draft Conventions offered an acceptable, fair and practicable compromise in order to facilitate the use of a uniform international legal basis for bills of exchange, promissory notes and cheques. National provisions for domestic transactions would continue to be of importance. In his delegation's view, the two Conventions would not create a third system governing negotiable instruments, but would provide international, uniform rules having their own object, namely, relations of an exclusively international character connected with bills of exchange, promissory notes and cheques. Those relations were characterized not only by their international nature, but by the fact that they resulted mainly from foreign-trade operations and generally involved firms having excellent experience in international dealings.

21. The existing national laws on bills of exchange, promissory notes and cheques were not always adequate to meet the requirements. Moreover, in addition to the differences between the common-law system and the civil-law system, there were considerable differences between national laws within each system. He emphasized that the Geneva Uniform Laws of 1930 and 1931 contained quite a number of reservations, on the basis of which several States had later acted. His delegation believed that the Commission's future activities concerning the two draft Conventions should be directed towards elaborating less complicated and more feasible provisions, with a view to the desired international unification.

22. Mr. ANGELICI (Italy) said that Italy would have preferred to see the activities concerning the draft Conventions directed towards the general unification of domestic laws. It fully appreciated, however, the political necessities that had brought about the present draft Convention on International Bills of Exchange, which was a fair compromise between the Geneva system and the common-law system. Unfortunately, the draft excluded some of the more interesting aspects of the common-law system and had rather complicated formulations.

23. His delegation found Austria's proposals particularly interesting and well balanced, but felt that a discussion of the future of the draft should be postponed until the major outstanding issues were discussed.

24. *The meeting was suspended at 4.20 p.m. and resumed at 4.45 p.m.*

25. Mr. GUEST (United Kingdom) pointed out that despite the considerable investment in time and money in the draft, there remained some serious problems. His delegation agreed with the statement in paragraph 6 (a) of document A/CN.9/249 that the draft Convention represented an acceptable and workable compromise between the civil-law and common-law systems. There was no evidence, however, to support the statement in subparagraph (b) that the draft Convention generally simplified the issue, negotiation and payment of the proposed instruments. The comments contained in subparagraph (c), to the effect that the draft Convention provided certainty in the rules applicable to international commercial transactions and obviated the application of conflict of laws rules, might become true at some time in the future if the Convention gained universal acceptance, but was not true for the time being. On the other hand, the comment contained in subparagraph (d) was on the whole justified.

26. In response to delegations which felt that the text needed to be simplified, he pointed out that a simple text was not necessarily the best text, and that clarity was more important than simplicity. There were three major problems concerning the draft Conventions. First, it was doubtful whether traders and bankers would voluntarily embark upon the use of a new system of bills of exchange and promissory notes. Second, with regard to the question of internationality, it would not be sensible for Governments to adopt one set of rules for international transactions and another for domestic transactions. Third, there was a distinct lack of enthusiasm for the draft Convention on International Cheques. Such cheques, which were little used at present, would be used even less in the future. It would therefore be better to forget about such a convention. That would not make it easy, however, to solve the problem of the regulation of international cheques.

27. Several courses were open to the Commission: (a) the topic could be dropped entirely; (b) work could continue on the drafts, which could then become model laws or be included in

the proposed compilation of international trade law; (c) the draft Conventions could be revised and an international conference held, either to revise the Geneva Uniform Laws or to adopt separate UNCITRAL Conventions. The question was whether the Conventions were worth such additional expenditure. His delegation believed that the Commission should proceed with caution and perhaps pursue more modest goals.

28. Mr. SEVON (observer for Finland) said that he wondered whether there was a need for the two Conventions. So far, banks that dealt in international exchange had not felt such a need, and States would be in no hurry to ratify the Conventions. His delegation did not believe that some States were against the texts because of their complexity. One reason that the Geneva system was being advocated was that all were familiar with it. It was not worth while to spend two more years discussing the draft Conventions. UNCITRAL could put its time to better use.

29. Mr. OLIVENCIA (Spain) said that the unification of international trade law had always been difficult. UNCITRAL should therefore take a realistic approach to its work and acknowledge the existence of two major systems, namely, the Geneva system and the common-law system. While Spain was a party to the Geneva Uniform Laws, it had not incorporated them in its domestic legislation.

30. One way to achieve harmonization of the two systems might be to convene a diplomatic conference to decide on an international text, whatever the obstacles. His delegation believed that UNCITRAL should continue on its slow but sure path towards the unification of international trade law.

31. Mr. OU Zhi Min (China) said that bills of exchange and promissory notes had been used increasingly as means of payment in international transactions. It was therefore imperative to have a universally accepted law on negotiable instruments. His delegation hoped that the current session would be used to obtain the views of all. A serious discussion would help to make both drafts clearer with a view to unifying them and making them fair, reasonable and easy to apply.

32. Mr. DIXIT (India) said that the developing countries had not participated in the development of past laws on international bills of exchange. They believed that there should be a unified system, not a diversity of laws.

33. It had been stated that the two draft Conventions would in effect create a third system. Similar cases occurred even in public international law. His delegation agreed that there might be conflicts among the various laws and that the situation would have to be corrected.

34. Some delegations had criticized the call for simplification. He wished to point out that 90 per cent of the time, simplification meant clarity. Other delegations had suggested that UNCITRAL should not attempt to deal with the larger question of a convention or a protocol. Without a convention, there could be no uniformity. Even when conventions were not ratified, they provided a basis for other international drafts.

35. Mr. ROEHRICH (France) said he wished to correct the impression that his delegation was pessimistic about the future of UNCITRAL. However, it was not at all clear that the two texts adopted by the Working Group on International Negotiable Instruments would lead to widely accepted international conventions.

36. The draft Convention on International Bills of Exchange and International Promissory Notes was extremely complex

and gave rise to considerable substantive problems. There were a number of lacunae in the draft Convention, the most important of which concerned the issue of the liability of the drawee (article 23, paragraph (2), of the draft articles). If the Convention took effect, there would also be problems concerning its compatibility with the domestic legal provisions already in existence, particularly those of countries of the Geneva system. He therefore wondered whether the text could be revised in order to accommodate the needs of those countries. His delegation was prepared to continue work on the draft articles, but believed that it would take at least two or three more years to eliminate most of the difficulties.

37. He was not convinced that there was sufficient interest among delegations in the concept of unifying trade law, since the legal instruments under the Geneva system and the common-law system were coexisting satisfactorily. Although his delegation was willing to endeavour to simplify the draft articles, the entire question must be viewed in the light of the whole programme of work of UNCITRAL. His delegation would not object if other topics were considered more urgent and given priority.

38. His delegation believed that since international cheques did not offer any advantage, consideration of the draft Convention on International Cheques should be discontinued for the time being.

39. Mr. GOH Phai Cheng (Singapore) said that his delegation accepted the draft Convention on International Bills of Exchange and International Promissory Notes as a compromise between the two legal systems. However, it doubted that the draft Convention would serve the needs of the international banking system and was of the view that UNCITRAL should not consider that aspect of the question any further.

40. Mr. CUKER (Czechoslovakia) said that the two draft Conventions provided a good basis for further work. UNCITRAL should endeavour to make the texts clearer and thus more suitable for practical use. His delegation endorsed the views concerning the range of questions to be considered by UNCITRAL, as set forth in document A/CN.9/249.

*The meeting rose at 5.55 p.m.*

### Summary record of the 287th meeting Tuesday, 26 June 1984, 10 a.m.

[A/CN.9/SR.287]

*Chairman: Mr. SZASZ*

*The meeting was called to order at 10.10 a.m.*

1. Mr. VIS (observer for the Netherlands) said that bills of exchange and promissory notes were the preferred instruments for export financing, and their use had increased enormously of late, especially in Europe. They facilitated the conversion of credit sales into cash transactions and enabled the seller to protect himself against any recourse on the part of the purchaser. Clearly, therefore, they fulfilled certain functions in international payment transactions that cheques did not. That was why his delegation wanted the Commission to focus its attention on the draft Convention on International Bills of Exchange and International Promissory Notes. In so doing, it should examine not only the problems which stemmed from the existence of divergent legal rules but also whether the Convention would promote the efficient use of bills and notes in export financing. Although many delegations contended that the absence of litigation proved that the differences among legal systems did not cause serious problems, one of the Commission's questionnaires had shown that the problems were rarely taken to the Courts, because bankers preferred to settle matters among themselves. It was impossible to say to what extent the customer bore the burden of solutions reached in that manner.

2. Although it would be preferable for the draft Convention not to introduce a new legal system governing international negotiable instruments, the Commission had long been working to separate international trade law from domestic law, and the banking community could easily adapt to a new system.

3. As to whether the Convention should be of a mandatory nature or be subject to ratification, he said that his delegation preferred the latter approach. The success of the Geneva

Uniform Laws stemmed not from the fact that 20 countries had ratified them, but from their use as models for the domestic legislation of nearly 60 countries. Regarding the charge that the draft Convention was too complicated he said it was no more so than any other legislation on negotiable instruments which, by its nature, should be detailed. He did not believe that the entire draft Convention should be revised: it was a sound text which had emerged after extensive negotiations in which the Working Group had been assisted by a study group composed of bankers from various parts of the world.

4. Ms. VILUS (Yugoslavia) said that Yugoslav financial experts had found a number of shortcomings in the draft Convention. It would transform the bill of exchange from an abstract legal act into an instrument connected with the main transaction, which could lead to practical difficulties. There were many common-law institutions—the protected holder, for example—which could not be easily incorporated into the current system. Especially in articles 6, 11, 14 and 23, the draft Convention favoured creditors over debtors, which was acceptable in domestic transactions but could cause problems in international payments. Many provisions, for example, those in article 31 (2), needed to be revised because, as currently drafted, they militated against the speedy circulation of bills of exchange.

5. The fact that only 26 Governments had furnished their comments on the draft Conventions made it impossible to determine how the Conventions would actually be received; furthermore, many of the comments were overly diplomatic and skirted the real difficulties. The document on major controversial and other issues (A/CN.9/249) was too general and did not point out the consequences of the concepts incorporated in the drafts. Her country regretted the close resemblance between the two drafts, and believed that the different roles of the different instruments should have been more clearly reflected.

6. Yugoslavia did not advocate abandoning the drafts, but was unsure how best to approach the task of improving them; at any event, an international conference should not be convened before they had been carefully studied in the light of comments received by the Secretary-General and those made at the Commission's current session.

7. Mr. VOLKEN (observer for Switzerland) said that, in view of the time taken for the Geneva Conventions of 1930 and 1931 to be finalized, the 10 years which the Commission had devoted to elaborating the draft Conventions did not seem excessive. The Geneva Conventions had essentially merged the German and French systems, although uniformity had not been achieved in many cases and domestic legislation had had to fill the gaps. Universal uniformity was still a goal to be pursued: that was why Switzerland did not favour creating a third system for bills of exchange. If Governments possessed the will to create a truly uniform system, solutions to the remaining problems, which were primarily technical, could be found. In future, the Commission's work should be focused on the draft Convention on International Bills of Exchange and International Promissory Notes.

8. Mr. GRIFFITH (Australia) said that his delegation supported the establishment of a uniform legislation on international negotiable bills and believed that the draft Convention represented a workable compromise between the two existing systems. The Australian banking community viewed the draft Convention as a distinct improvement on the present situation, and the civil law system was not seen as posing a serious obstacle to adapting the new system to Australian commercial and legal practice. The Conventions did not significantly weaken the existing rights and obligations of parties to international negotiable instruments and should simplify the issuance, negotiation and payment of such instruments. His delegation endorsed the arguments in favour of continuing the work on the draft Conventions set out in document A/CN.9/249, paragraph 6, and believed that to abandon it would undermine the Commission's credibility as a force for the harmonization of international trade law. Although it had been contended that it was impractical to revise the Geneva Conventions of 1930 and 1931 in a way that would be acceptable to the common-law countries, his delegation believed that the Commission could resolve the major outstanding difficulties, and that it should concentrate its work on the draft Convention on International Bills of Exchange and International Promissory Notes.

9. Mr. CRAWFORD (observer for Canada) said that banking and governmental circles in his country favoured the draft Conventions, which were seen as a good basis for compromise among the competing systems now governing international financial instruments. The civil-law countries had mentioned many respects in which their current rules would be modified; the common-law countries were in exactly the same position, but the parties which would be affected by the changes were prepared to accept them. Many technical points should be further discussed and some revisions made to clarify a number of ideas. When the discussion turned to substantive issues, countries might find that they agreed on many points concerning which changes could be made in the wording of the draft Conventions. He hoped, however, that the basic compromise represented by the drafts would not be lost.

10. Mr. ROGNLIEN (observer for Norway) said that the draft Conventions represented a workable compromise between different legal systems. While the need for a new instrument in that field had been questioned, he believed that, if the texts were made optional, the international commercial community could subject them to a trial application. In any

event, it would be unfortunate if work on the draft Conventions was suspended.

11. The drafts created a problem for the countries which had ratified the Geneva Conventions of 1930 and 1931, since the uniform laws contained in those instruments were binding; consequently, those countries could not state in a court that they had derogated from the uniform laws in the matter of a contract. Changes would have to be made in the Geneva Conventions if the countries which had ratified them were to be able to ratify even an optional new convention. Most countries having a civil law system would probably prefer to continue to abide by the Geneva Conventions rather than denounce them. However, since the Geneva Conventions required revision on additional points as well, it was to be hoped that the Commission would be able to carry out such revisions.

12. Mr. SAMI (Iraq) said that there were a number of characteristics which distinguished bills of exchange from other forms of payment, the most important of which was confidence in the instrument generated by assigning a special quality to the note. It was for that reason that important provisions had been included in the Geneva Uniform Law on Bills of Exchange and Promissory Notes which conferred power on the instrument by virtue of its legal definition and not by virtue of the contracts or transactions which had preceded it. The two draft Conventions before the Commission had followed the opposite path; thus, if a challenge was issued to the contract that had preceded the instrument in question, the instrument itself could be revoked. That was a major error in both Conventions which would impede their acceptance in international commercial circles.

13. Another problem was the provision concerning the "protected holder". The many details provided in connection with that subject merely complicated it, since the Geneva Conventions had already ruled on the matter by stating that a holder in good faith would be protected upon receipt of an instrument. Likewise, the question which laws of conflicting legal systems were to be applied to bills of exchange had also been settled in the Geneva Conventions.

14. Nevertheless, his delegation believed that the two draft Conventions covered matters of legal and practical importance in the field of international trade, and he therefore supported the proposals to study the drafts further in order to make them more acceptable to States. Any body established for that purpose must consider whether the Commission wished its draft Conventions eventually to replace the Geneva Conventions or whether the new Conventions would apply only to international bills of exchange.

15. Mr. GLATZ (Hungary) welcomed the Commission's desire to unify international trade law. In that connection, the draft Conventions before the Commission were generally acceptable, despite the need for a few drafting refinements. His delegation supported the optional method of settlement provided for in the draft Convention and felt confident that banking circles would be able to work with a third system intended specifically for international trade.

16. Mr. FARNSWORTH (United States of America) said that his delegation did not support the draft Convention on International Cheques; consequently his remarks would apply only to the draft Convention on International Bills of Exchange and Promissory Notes, which it found generally acceptable.

17. Since there appeared to be a divergence of systems for international payments even within groups of countries having

similar legal systems, the establishment of an optional system under the draft Convention that would unify existing systems had merit. Some delegations had expressed the view that the compromise reached in the draft Convention to countries having a particular legal system was unfavourable. However, he interpreted criticisms of the draft as being directed more at the differences in treatment accorded to borrowers and lenders. Nevertheless, his delegation believed that the compromise fairly accommodated the interests of both groups.

18. Finally, some members had criticized the draft Convention for being unclear. However, any legal instrument in the field of international trade tended to appear complex on first reading. The complexity of the text should not be used as a pretext for claiming that the unification of international trade law was impossible. UNCITRAL should find a means for clarifying the most problematic areas of the text.

19. Mr. MAEDA (Japan) said that, as a country which subscribed to the Geneva system, Japan was interested in the issues raised by other delegations concerning the complexity of the provisions of the draft Conventions and the inadvisability of establishing a third system of international payments. The "protected holder" concept had frequently been cited as an example of the complexity of the provisions of the two draft Conventions; however, it did not appear excessively complex to his delegation. Moreover, that concept appeared to be directly related to article 16, paragraph 2, and article 17 of the Geneva Uniform Law on Bills of Exchange and Promissory Notes, which contained different requirements that must be met in order to protect the holder of an instrument against claims from previous holders. Since the new draft Convention did not make any such distinctions in defining the "protected holder", it could be considered to constitute a simplification, rather than a complication, of the Geneva Uniform Law.

20. With regard to the establishment of a third system, it was true that negotiating instruments currently fell into one of two categories of legal system. However, as previous speakers had pointed out, considerable variety of legislation existed even within similar systems. Under the circumstances, Japan felt that the establishment of a new multilateral instrument was necessary to harmonize the various existing systems.

21. Mr. CHAFIK (Egypt) said that his delegation had originally been in favour of modifying the existing Geneva Conventions so that they might become acceptable to more countries and more compatible with modern commerce. However, since the Commission had decided to draft new instruments and had devoted 10 years to that effort, he did not believe that it could abandon that task at present.

22. The Commission was agreed that the basic problem with the draft Conventions lay in the compromise which they represented between the Geneva and Anglo-American systems. However, the objections raised pertained to details in the instrument, all of which could be revised. The elaboration of the Geneva Conventions had taken a great deal of time; consequently the Commission should not concern itself with deadlines but should seek instead to complete its task.

23. The CHAIRMAN said it appeared that most delegations continued to support the idea of unifying international trade law and felt that the draft Conventions constituted a suitable means to that end. Concern had been expressed at the development of a system of international payments that would parallel existing domestic systems; however, the Commission had on previous occasions formulated a policy involving the development of such international systems.

24. Most delegations appeared to favour the adoption of optional rules and were concerned about the way in which the Geneva Uniform Laws would then be implemented within commercial circles. In the future, the Commission might wish to see how the draft Conventions could be co-ordinated with the existing Geneva system so that countries which had ratified the Geneva Conventions might also make use of the new systems. He suggested that the Commission should examine the texts of the draft Conventions in greater detail in order to determine what further steps would be required for their adoption and implementation.

*The meeting was suspended at 11.35 a.m. and resumed at 12.05 p.m.*

25. The CHAIRMAN invited members to comment on part II of document A/CN.9/249 (paragraphs 12-20), which contained the major controversial issues in respect of the draft Convention on International Bills of Exchange and International Promissory Notes, as well as the draft Convention on International Cheques. With regard to forged endorsements, he drew attention to the note by the Secretariat, contained in paragraph 14, which indicated that only the first of the controversial issues materially affected the compromise proposed in the draft Convention. It was his impression that the structure of the proposed compromise was acceptable and that the Commission should proceed to discuss ways of improving it.

26. Mr. ROEHRICH (France) said that his delegation supported the comments submitted by the Governments of Mexico and Spain in connection with the liability of the transferee from the forger (paragraph 3 (a)). The provisions of article 23 constituted a compromise between the concepts of Anglo-American law and those of the Geneva Convention. The latter placed the greatest risk on the owner of the bill from whom it was stolen, who was in a better position to protect himself against theft. However, there was a contradiction between the provisions of article 23 and those of article 14 (1) (b), which specified that signature by an agent without authority did not interrupt the series of endorsements. In his opinion, the first endorsee should be exempt from any liability. Because the two texts were incompatible and because rigorous formalism was lacking in connection with the effectiveness an instrument could have, his delegation hesitated to support the compromise reached in article 23.

27. Mr. CHAFIK (Egypt) said that the provisions of article 23 (1), even if amended to include receipt of a forged instrument in good faith, were Draconian and should be changed.

28. Mr. ANGELICI (Italy) said that, in his opinion, the question of forged endorsements was not particularly relevant in a field dominated by banks, especially since national courts usually reached different conclusions on similar cases.

29. In general, the articles could perhaps be accepted as a compromise, except for the provisions on endorsement by an agent without authority which made it much more difficult for the endorsee to ascertain the true situation. It was therefore unfair to impose liability on the transferee in every case.

30. Mr. WAGNER (German Democratic Republic) said that he considered the prohibition against forged endorsements to be a fair and workable compromise between the two existing systems. The third system, which placed the burden of liability on the forger, helped to minimize the disadvantages of existing national provisions. In addition, he welcomed the clear and convincing commentary on page 50 of document A/CN.9/213.

31. Although forged endorsements rarely occurred in transactions involving international bills of exchange, provisions governing such situations would favour the circulation of international bills and promissory notes and would reinforce the liability of recipients of forged endorsements. It was important to adhere to the principle that an endorsee must know his endorser, and the inclusion of provisions to that effect in international regulations governing foreign trade was therefore justified. Accordingly, his delegation fully supported the compromise provisions contained in article 23.

32. Mr. GUEST (United Kingdom) supported the compromise reached in connection with article 23 and drew attention to document A/CN.9/213, which described the two existing approaches and gave examples of the application of the new system. The new system did not seem materially to affect the proper negotiation of bills of exchange or promissory notes and appeared to be a satisfactory compromise which could, in his opinion, be accepted by both existing legal systems.

33. Mr. MAGNUSSON (Sweden) said that he preferred the Geneva system whereby the recipient of a forged instrument was protected if he had acted in good faith. He pointed out that banks were generally very careful about accepting instruments. Accordingly, his delegation could accept the proposed provisions, which would probably be acceptable to banking circles as well.

34. Mr. ANKELE (Federal Republic of Germany) said that his delegation did not consider the compromise solution to be satisfactory and found the Geneva system—whereby liability was borne by the person who committed the negligence and not by the payee, if he had received the instrument in good faith—to be much fairer. He also supported the comments made by the representative of France and those submitted by the Governments of Mexico and Spain to the effect that the proposed solution was not likely to produce satisfactory results.

35. Mr. SAMI (Iraq) agreed that the compromise would not solve the problem under consideration. The first paragraph of article 23 would give rise to questions as to whether the endorsement of a bill of exchange was forged, and it was important to provide protection for persons who accepted such instruments without knowing they were forged. His delegation therefore considered the solution provided under the Geneva system to be appropriate and fair.

36. Mr. VIS (observer for the Netherlands) said that, in general, he supported the compromise solution but suggested that article 23 (2) should be given further consideration. The commentary contained in the second paragraph under example D on page 50 of document A/CN.9/213 did not seem to follow from the text of article 23, and he observed that the Geneva Uniform Law contained provisions to indicate when an instrument was properly payable.

37. Mr. OLIVENCIA (Spain) confirmed his delegation's previous comments as contained in document A/CN.9/249 (paragraph 13 (a)). The imbalance between articles 14 and 23 might produce unfair results. Moreover, the non-liability of the endorsee for collection, as in article 23 (2), was unjustified, and his delegation was also opposed to the equating of a forger with a person acting without authority, as in article 23 (3).

38. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics) said that he agreed with the principle behind article 23 (1) but objected to its automatic extension to any payment where a note was endorsed in good faith. Such an extension of the principle could not be supported because,

unlike the endorser and the endorsee who were linked by a bilateral deal involving forgery, the drawee who paid had only a unilateral obligation to the holder, which he fulfilled by paying. Also, in a case where a person facing risk of loss due to forgery sought to prevent payment of a note by so informing the drawee in good time, the drawee would, under the terms of article 68 (3), not be discharged of liability if the note were paid to the forger.

39. In drafting article 23 (2), the Working Group had been unable to decide on the liability of either the drawee or the endorser, but a generally acceptable solution had to be found. The Union of Soviet Socialist Republics supported the rule by which the drawee, having paid the forger of the endorsement or the endorser cashing the note, would be liable under article 23 (1) only if he was aware of the forgery.

40. Mr. ROGNLIEN (observer for Norway) said that he thought article 23 was an acceptable compromise and would support it. The ruling of the Geneva Conventions on the good faith requirement was not embodied in any other convention, and its application in practice differed. Good faith meant that the parties in question should exercise care. However, since it was hard to prove good faith or determine how much care should be exercised, he felt it advisable to dispense with that requirement in connection with article 23.

41. Mr. DUCHEK (Austria) said that the compromise formulation in article 23 (1) was acceptable, particularly in view of existing bank practice. There was, however, a contradiction between that text—according to which the risk of loss because of a forged signature was borne only by the person to whom a note was directly transferred (and not by the drawer or drawee or any other person to whom it might be later transferred)—and the unclear formulation and consequences of article 23 (2), where the important question of the liability of the drawee who paid a note bearing a forged signature was not regulated by the Convention but left to applicable national law. Under common law, however, a drawee who paid on an instrument bearing a forged endorsement was not discharged of liability; he bore the risk of loss until he could transfer the risk to the person to whom he had transferred the instrument. Were, then, such common law provisions to apply as well as those provisions of the Convention which they contradicted? For the compromise in paragraph (1) of article 23 to be acceptable, further consideration should be given to whether paragraph (2) of that article was necessary at all; and article 68 of the Convention should provide expressly that a drawee paying in good faith was discharged of all liability.

42. Mr. FARNSWORTH (United States of America) observed that the compromise provisions of article 23 (1) called for major changes in the mechanical handling of notes by common-law countries. Parties who had believed themselves protected because they had not yet endorsed in blank would now find that they must keep such order notes under lock and key.

43. A number of representatives had suggested that the transferee should be discharged of liability if he accepted a note in good faith. The purpose behind the compromise in article 23 (1), however, had not been to induce honesty but rather to induce a habit of care which was already incorporated in the common-law approach; to induce transferees to take proper care to identify the transferor or, failing that, to take a note at their own risk.

44. Mr. OU Zhi Min (China) said that article 23 (2) which left the liability of a payee of a note bearing a forged endorsement

unregulated in the Convention and subject to national law, would in practice lead to confusion. Some regulation was, therefore, needed. China believed that the payee who paid in good faith should not be liable. The endorsee who accepted in good faith should not bear any responsibility. However, the forger should be liable.

45. Mr. SEVON (observer for Finland) said that Finland could accept article 23 even though it did not correspond to its own legal system. Paragraph 1 of the article was a workable solution, if not perhaps the best. As for paragraph (2), he was in much greater agreement with the commentary on the text than with the draft itself, particularly with the assumptions in examples C and D on page 50 of document A/CN.9/213. He agreed with the representative of Austria, that the solution should be incorporated in the draft Convention and not left to be decided under applicable national law.

46. Mr. CRAWFORD (observer for Canada) said that Canada had supported the compromise text but was concerned about leaving such an important point unregulated in article 23 (2), for solution by national courts. The concern was perhaps groundless, depending on the extent to which the national courts accepted the principle of article 23 (1) and applied it to achieve a uniform application of a uniform law of liability.

47. He himself had difficulty understanding what liability was left to be determined by national law. According to a strict interpretation of article 23 (1), the first endorsee was liable in the case of a forged endorsement of a note. If a drawee had paid such a note before discovery of the forgery on a claim by a drawer, he would be obliged to reimburse the drawer's account and would have a claim against the first endorsee, which would automatically come under article 23 (1) and not under national law. Yet it might be possible under the Geneva system for a

court to allow such a drawee to invoke article 23 (2) and thus escape liability for reimbursement to the drawer's account. The drawer would supposedly then be the one to seek to impose liability under article 23 (1).

48. Given such uncertainties, the Commission should try to resolve the rights of reimbursement in the Convention itself rather than leaving the question to national law.

49. Mr. MACCARONE (observer, European Banking Federation) observed that the compromise solution in article 23 (1) and (2) departed from common law, particularly the American system, more than from the Geneva system. Reading article 23 (1) in conjunction with article 68, the conclusion was that the Geneva Convention diverged only in the case where a note was presented for payment by the forger himself, which was very unlikely. Conversely, if a note was presented for payment by a person who acquired it from the forger, that person was not liable, under the terms of article 68 (3), if he had done so in good faith.

50. A number of speakers had argued for regulating the liability of a drawee more explicitly in article 23 (2), but in his view such a liability was one arising outside the instrument, on grounds other than the bill itself. The general approach had been to leave out of the draft whenever possible any such liability. There were only two exceptions and one was in article 23 itself. To regulate such a liability under article 23 (2) would demand a complete reworking of the basic principles adopted by the Working Group. Therefore, the best approach would be to leave the text as it stood and let national law provide for such liability.

*The meeting rose at 1 p.m.*

### Summary record of the 288th meeting Tuesday, 26 June 1984, 3 p.m.

[A/CN.9/SR.288]

*Chairman: Mr. SZASZ*

*The meeting was called to order at 3.10 p.m.*

1. The CHAIRMAN invited the members of UNCITRAL to express their views on article 23 of the draft Convention of International Bills of Exchange and International Promissory Notes (A/CN.9/211).

2. Mr. PAVLIK (Czechoslovakia) said that his delegation supported the compromise set forth in article 23. Paragraph (2) should contain a reference to the rule of liability, in accordance with the principle that the payee or endorsee should be considered liable in cases where they had been aware of the forgery.

3. Mr. SEVON (observer for Finland) said that the wording of paragraph (2) needed to be made clearer. His delegation could accept the substance of the compromise, as proposed in the draft as a whole.

4. Mr. VOLKEN (observer for Switzerland) said that the implications of paragraph (2) were unclear. Furthermore,

paragraph (1) should be redrafted in order to guarantee the negotiability of instruments.

5. The CHAIRMAN, referring to a question by the representative of Canada about the status of the commentary on the draft Convention (A/CN.9/213), said that for the time being the only authentic text was the draft Convention itself, which must therefore be self-explanatory.

6. Mr. DUCHEK (Austria) said that his delegation could not support a compromise that would permit countries acting in accordance with one legal system to claim that the drawee had to pay a second time, while allowing countries that operated in accordance with the other system to claim that he had discharged his liability. It must be stated clearly in article 23 that a drawee paying an instrument in good faith had no further liability whatsoever. The issue in question should be reconsidered by the Working Group on International Negotiable Instruments.

7. Mr. GUEST (United Kingdom), responding to the statement by the Observer for Switzerland concerning article 23 (1), said that while the system derived from the Bills of Exchange Act (BEA) and the Uniform Commercial Code (UCC) might impose a more extreme liability risk on the person taking the instrument than article 23 did, there was no

evidence that that in any way inhibited the negotiability of bills of exchange within the BEA or UCC systems.

8. Where paragraph (2) was concerned, the intention had been to deal with the question of arrangements which might impose some liability on a party who paid. It had certainly not been the intention to enable, for example, a common-law court to impose a rule that would be at variance with article 68. He recalled, in connection with the words "or of an endorsee for collection who collects, an instrument on which there is a forged endorsement", that a question had arisen concerning liability, in certain common-law systems, for conversion of an instrument by a collecting bank. It had been decided that the question should be regulated by national law, owing to its tricky nature. If the scope of liability dealt with in article 23 was not clear, then it must be made clear.

9. Mr. MACCARONE (observer, European Banking Federation) suggested that paragraph (2) should be deleted.

10. Mr. MAEDA (Japan) said that it would be helpful if there could be a compromise between the BEA and UCC systems.

11. Mr. VIS (observer for the Netherlands) said that his delegation was still having difficulty with article 23, but did not wish to stand in the way of a compromise. In particular, he wished to point out that article 68 did not concern payment by the drawee. A similar problem arose in article 23 (1). His delegation did not wish to introduce the notion of good faith into paragraph (2), which was unclear, and would prefer the notion of payment with or without knowledge of the forgery.

12. The CHAIRMAN said it seemed that the majority supported the compromise reached in article 23, particularly as reflected in paragraph (1). However, it was clear that something must be done about paragraph (2). He believed that there were two drafting possibilities: a substantive rule could be drafted and incorporated in the compromise solution; or a deletion could be made and the substance of the wording that had been deleted could be incorporated in the compromise solution.

13. Mr. MAEDA (Japan), referring to paragraph 13 (c) of the note by the Secretariat (A/CN.9/249), pointed out that the draft Convention on International Bills of Exchange set no limit for compensation recoverable under article 23 (1), whereas a limit was set for the amounts recoverable under articles 41 (2), 64 and 75 (3). His Government felt that the amount recoverable under article 23 (1) should be limited to the amount specified in articles 66 or 67. The amount recoverable from the forger did not need to be limited. He emphasized that his comments were solely directed at improving the draft Convention, not at undermining the compromise.

14. Mr. OLIVENCIA (Spain) said that he agreed with the remarks made by the Chairman in his last statement. Most participants in the general discussion had been in favour of the compromise solution contained in article 23 (1), but the Mexican and Spanish position referred to in paragraph 13 (a) of document A/CN.9/249 had also received considerable support. Spain would agree to any compromise formula that would help to achieve progress in the Commission's work. However, concern had been expressed that the provisions of article 23 might lead to an injustice, and that important issue could not be completely ignored. While it was perhaps

inadvisable to introduce the notion of good faith under article 23, the text could usefully include a provision concerning knowledge or lack of knowledge of the forgery. The conditions under which a person was considered to have knowledge were clearly stated in article 5.

15. Mr. FARNSWORTH (United States of America) said that, if the Commission wished to consider the adoption of the draft Convention on International Bills of Exchange and International Promissory Notes in conjunction with the draft Convention on International Cheques, his delegation would recommend the suggestion referred to in paragraph 13 (e) of document A/CN.9/249. However, if—as appeared to be the case—the Commission wished to concentrate solely on a convention dealing with bills of exchange and promissory notes, his delegation would not press that suggestion further. The problem dealt with in paragraph 13 (e) related to common-law systems and did not arise with respect to bills of exchange to an extent sufficient to warrant a special provision under article 23.

16. Mr. SAMI (Iraq) wondered whether further consideration might be given to the article in a working group.

17. There were discrepancies between the language versions of the draft Convention on International Bills of Exchange. In articles 23 (1) and 41, for example, "party" was rendered in French by "signataire". The meaning of the two terms was not the same. With regard to article 41, a contradiction arose because the article was based on the Geneva Uniform Laws while article 23 (1) was based on the common-law system.

18. Mr. ROEHRICH (France) welcomed the Iraqi representative's remarks about the discrepancies between the language versions. He trusted that the inconsistencies in the presentation and even the substance of certain articles of the draft would be eliminated.

19. The CHAIRMAN said that there would be ample opportunity to reconcile any differences in the texts. Concerning the statement by the representative of Spain, he said that while a certain level of compromise had been achieved on article 23 (1) and while there had been quite significant support for the position referred to in paragraph 13 (a) of document A/CN.9/249, it did not appear that the Commission had expressed the general desire to achieve a higher level of compromise.

20. *The meeting was suspended at 4.15 p.m. and resumed at 4.45 p.m.*

21. The CHAIRMAN suggested that the Commission should next consider paragraphs 15 and 16 of document A/CN.9/249, concerning the concept of holder and protected holder.

22. Mr. DUCHEK (Austria) said that articles 4 (7), 25 and 26 of the draft Convention on International Bills of Exchange were unclear and should be revised. With regard to the substance, he said that the approach of the draft Convention was very similar to that of the Geneva Uniform Laws, with one major exception. Whereas the Uniform Laws stressed the circumstances under which defences could be raised or claims could be brought, the draft Convention described a person's status as either a protected or unprotected holder. Referring to article 4 (7) (a), in particular, concerning a holder's knowledge of a claim to or defence upon the instrument referred to in article 25, he said that there was a danger of a holder's being unfairly deprived of his protection under certain circumstances. A case might occur in which a claim could be brought by a drawer against a holder who had

acquired the status of unprotected holder by virtue of his knowledge about a claim to or defence upon the instrument on the basis of a defective underlying transaction between two previous holders, yet who had no knowledge of an original fraudulent acquisition of the instrument by an entirely different, third party. In such a case, his knowledge of the claim of one holder against another would unjustly affect his status as a protected holder. It was therefore necessary to simplify, or even change, the structure of the articles. Instead of merely describing the status of the holder, the articles should describe the circumstances in which claims could be brought or defences raised.

23. Mr. MAEDA (Japan) offered an additional example of a case where a person might be defined as an unprotected holder although he had no knowledge of a prior fraudulent transaction or a claim to or defence upon the instrument.

24. Mr. GUEST (United Kingdom) said that under the common-law system, bills of exchange must be beyond suspicion; at the time of acquisition of the instrument, the person acquiring it was expected to have no suspicion about any possible defects in the instrument. The draft Convention was correct in establishing the concept of the protected holder. There were legitimate grounds for discussing, however, whether the protected holder could be deprived of his status by virtue of knowledge of any claim to or defence upon an instrument, or of only certain types of claims and defences. That question might be discussed in the appropriate working group.

25. Mr. OLIVENCIA (Spain) said that the focal point of the entire draft Convention was the concept of the protected holder. His delegation felt that the draft was not clear on that point, but that the question was one rather of form than of substance. Spain was opposed in principle to the system of definitions, and felt that the definition of a "holder" in article 4 (6) was incomplete because it referred to another article rather than being self-contained. The definition of a "protected holder" in article 4 (7) was also incomplete and confusing. A person might unjustifiably lose his status as a protected holder merely by virtue of having received an incomplete instrument. The draft articles needed to state clearly what criteria would be used to define a "complete" instrument.

26. Subparagraphs (a) and (b) of article 4 (7) contained subjective concepts and negative formulations which made them difficult to interpret, a problem which was compounded by the lack of co-ordination between that article and the presumptions involved in articles 5 and 28. His delegation continued, therefore, to share the doubts expressed by the representative of Austria, despite the clarifications offered by other representatives.

27. With respect to articles 25 and 26, it did not seem illogical to state that a defence could not be set up against a protected holder. Instead of stating exceptions, those two articles should merely set forth general rules. The substantive problems could be solved through a concerted effort to simplify the draft while respecting the complexity of the subject.

28. Mr. ANGELICI (Italy) said that he agreed with the representatives of Austria and Spain. Efforts should be concentrated on practical problems rather than on theoretical ones. The issue of general definitions could be deferred until

a later date. At present, there was no need for a general definition of the term "protected holder".

29. Mr. MAGNUSSON (Sweden) said that the text was complicated because of the many cross-references between articles. He wondered whether there was any real need for the concept of the protected holder. The text should refer only to the holder and the action which could be brought against that person. He agreed that the deletion of the term "protected holder" would mean substantive changes. However, that could be left to the Working Group.

30. With respect to substance, he supported the idea that the holder should be regarded as protected even if the instrument was incomplete at the time that he became a holder. Accordingly, the term "complete" should be deleted from the definition of "protected holder".

31. Mr. FARNSWORTH (United States of America) said that the definition of "protected holder" could be redrafted. In common law, as the representative of the United Kingdom had pointed out, the holder should be above reproach. However, it was difficult to justify the requirement that the instrument should be complete, even though it was accepted in common law.

32. Mr. ROGNLIEN (observer for Norway) said that knowledge of a particular defence or claim should not preclude protection against other claims of which the holder had no knowledge. The text would be less complicated if a distinction were made between defences which should and those which should not be excluded. The representative of Austria had suggested a good way of making the draft less complicated.

33. Mr. SEVON (observer for Finland) said that while he was not conversant with all the legal niceties which the representatives of the common-law countries were trying to persuade others to accept, in time even he might be able to understand the concept of protected holder. In other words, he was not sure that it should be deleted from the text. He appreciated the contention that everyone should refrain from accepting an instrument that was suspicious. What he was concerned about was the notion that a holder could not be a protected holder if the instrument was incomplete at the time he became a holder, even if the instrument was subsequently completed by that holder in accordance with the authority given. If that concept was removed, then he could accept the definition of "protected holder".

34. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics) said that in principle his delegation endorsed the concepts of holder and protected holder and the conditions under which the definitions applied. It also agreed with the possible defences set forth in articles 25 and 26. However, articles 4 (7), 25 and 26 should be clarified in order to eliminate the possibility of different interpretations of the definitions.

35. Mr. MACCARONE (observer, European Banking Federation) said that he shared the views expressed by the representative of the United States. The concept of protected holder was important in theory, but in practice, if it was retained, the results would be similar to what had occurred with respect to the Geneva Uniform Law. He did not agree that a holder should lose his status as a protected holder even when he had been given the authority to complete an instrument.

**Summary record of the 289th meeting**  
**Wednesday, 27 June 1984, 10 a.m.**

[A/CN.9/SR.289]

*Chairman: Mr. SZASZ*

*The meeting was called to order at 10.20 a.m.*

1. The CHAIRMAN invited the Commission to resume discussion of the concept of holder and protected holder, one of the major controversial issues in the draft Convention on International Bills of Exchange and International Promissory Notes and the draft Convention on International Cheques. The concept was discussed in part II B, paragraphs 15 and 16, of the secretariat commentary in document A/CN.9/249. He informed the Commission that the suggestion contained in subparagraph (iii) of paragraph 16 (a) had been withdrawn.

2. Mr. CHAFIK (Egypt) said that banking circles in his own and other countries had found the concept of holder and protected holder ambiguous and imprecise, as developed in the Convention, all the more so because of the many defences that could be set up against both types of holder under various provisions of the text; thus there was a tendency to prefer the Geneva Convention notion of "holder in good faith".

3. A close look at the draft text, however, revealed that the differences between the two systems were actually minimal in so far as the protection of holders was concerned. Egypt therefore had no objection to the concept of protected holder as such, although the Working Group should simplify it in particular by drawing up a list of defences that could be set up against the two types of holder. The definition of a protected holder in article 28 of the Convention called for a clear further definition of what constituted a non-protected holder.

4. A better term than "protected holder" should be found, however, both because the term was foreign to accepted legal usage and because it seemed to detract from the legitimacy of the non-protected holder. He himself would prefer the term, "holder in due course", taken from English law.

5. Mr. WAGNER (German Democratic Republic) said that, in the interests of clarity and wide circulation of instruments, it would be best not to introduce the distinction between the two types of holder into the Convention. The concept of holder in the Geneva Convention was more comprehensive. Since fewer parties were generally involved in international dealings than in national dealings, there was no need to make the distinction in respect of international dealings.

6. The various articles on the matter gave rise to a number of questions which were insufficiently dealt with in the Convention. The German Democratic Republic joined other Governments in requesting reconsideration of the whole concept.

7. Mr. PAVLIK (Czechoslovakia) agreed that legal regulation of the concept of holder and protected holder must incorporate equal protection of the interests of the holder, on the one hand, and the debtor, on the other. The definition of a holder in the Geneva Uniform Law on Bills of Exchange and Promissory Notes should be adopted in the Convention, since it better covered equal protection of creditor and debtor interests and eliminated the difficult problem of regulating differences between the two types of holder.

8. Mr. ANKELE (Federal Republic of Germany) said that the distinction in the Convention between the two types of holder was one reason why the draft was thought to be too complicated and impractical. He agreed that the draft regulations in that area needed to be reorganized, in line with the more acceptable Geneva provisions. That could be done without undermining the system followed in drafting the text.

9. He agreed with others who had observed that the non-protected holder was in a very weak position, particularly in view of the many defences that could be set up against him under article 25. The question of protection therefore became all-important. Article 4 (7) required that, to be protected, a holder must have had no prior knowledge of a claim to or defence upon an instrument. The representative of Austria had shown convincingly the untoward consequences such a requirement could have. A holder who through negligence did not know of one particular defence upon an instrument should not be denied protection against other claims or defences of which he had no knowledge. As a compromise, denial of protection could be limited to holders who had actual knowledge of a claim or defence. In addition, it did not seem justified to deny protection, under the terms of article 4 (7), to the holder of an instrument endorsed in blank on the ground that the instrument on the face of it was not complete. He agreed with other delegations that article 4 (7) needed revision.

10. Mr. MAEDA (Japan) said that he supported the concept of protected holder. However, the definition in article 4 (7) of the regularity of an instrument which affected the status of a protected holder did not seem sufficiently comprehensive, as indicated by the example given in paragraph 13 of the secretariat commentary (A/CN.9/213, page 21) on that article. There had been disagreement among the Anglo-American members of the Working Group as to whether, for instance, a bearer cheque was regular on the face of it when an endorsement appeared on the back. The whole question of the regularity of an instrument needed further study and, in that connection, the Commission would probably find section 3-304 of the Uniform Commercial Code of the United States very helpful.

11. Ms. VILUS (Yugoslavia) said that she was dissatisfied with the concept of protected holder, which had been introduced into the draft text as a major concession to the common-law system. Although she understood the difficulties of introducing the good faith principle, she also understood that there was a good faith requirement in Anglo-American law and wondered why the Working Group had not included that requirement.

12. The concept of protected holder as formulated could lead to serious problems, particularly in the case of incomplete instruments which were regulated in article 38. Articles 25 and 26, closely connected to article 4 (7), were also the natural result of the compromise on the concept of protected holder. It was difficult to see, however, how that concept could serve the principle of wide circulation of a bill of exchange and why wide circulation should be linked to an underlying transaction. She was particularly unhappy with the term "any defence" in article 25 (1) (b), for it was too broad and could even be dangerous. It would be better to draw up a list of defences, perhaps with cross-references to other articles regulating defences.

13. Mr. DIXIT (India) said that it was difficult to understand from the draft text exactly what the distinction was

between the two types of holder. Since so many intermediate parties, not all of them bankers, were involved in the use of bills of exchange, it was important to make the text more comprehensible. The text lacked clarity partly because there were too many cross-references between articles.

14. In principle, he supported the concept of protected holder. He did not agree with the criticism that the requirements which must be met by a holder in order to obtain protected status were too strict and went beyond those that should be required for a person to be a holder in good faith; such conditions had to be spelled out in detail. Nor did he agree that it was difficult on the basis of the instrument alone to determine the rights of a person in possession of an instrument. It was true that what constitutes a valid claim to the instrument was not regulated but left to applicable national law; but in such situations there had to be a reference to local law.

15. Mr. ROEHRICH (France) said that he had very serious difficulties with the legal consequences of the concept of protected holder, and agreed with the comments in paragraph 15 of document A/CN.9/249, especially subparagraphs (a) and (c). He believed that a protected holder under the draft Convention had less security than a holder under the Geneva Convention. The draft extended the notion of bad faith in a manner prejudicial to the wide circulation of instruments.

16. Under article 4 (7), a protected holder lost that status if he knew of one particular claim to or defence upon an instrument. Elsewhere, in article 5, a person was considered to have knowledge of a fact if he could not have been unaware of its existence. The combined effect of those two articles gave far greater scope to claims or defences.

17. Given such reservations, he could only suggest a return to the concept of holder embodied in the Geneva Convention system.

18. Mr. GRIFFITH (Australia) agreed with the comments made by the representatives of Egypt and Yugoslavia about the fact that article 4 (7) did not refer to a "holder in good faith". The difficulty might be resolved by deleting from article 4 (7) (a) the reference to knowledge of a claim or defence and introducing the concept, recognized in common law, that a protected holder was required to take an instrument in good faith and without knowledge of any defect in the title of the individual who transferred it to him. The wording of article 5 reflected the doctrine of constructive knowledge, which had not been incorporated in the common-law system and had apparently not been widely applied in the civil-law system. He therefore suggested that article 5 should be deleted.

19. Mr. GUEST (United Kingdom) said that bankers and academicians in various countries had apparently praised the draft Convention if it mirrored their own legislation, and criticized it if it did not. The Working Group had made a conscious effort to depart from existing legal systems, however, the draft Convention was intended to be not an amalgam or composite of those systems, but a truly new approach to international commercial legislation.

20. "Good faith" meant different things under the two systems, and even among the civil-law countries the concept varied widely. In developing the protected holder concept, the Working Group has sought, not to reproduce the common-law notion of "holder in due course" or the civil-law idea of "holder in good faith", but to create a new concept which all judges would recognize as not being covered by the juris-

prudence they were accustomed to apply. In no system of law were the rights of the holder absolute and, if the Working Group had failed to make clear the scope of defence against the protected holder and the conditions in which the holder's rights were not absolute, more work could be done on those issues. Delegations should refrain, however, from seeking to insert in the text familiar concepts derived from their own legal systems.

21. Mr. GLATZ (Hungary) said that his delegation agreed that the protected holder system should be simplified. The new system should impose as few conditions as possible on the transfer of international negotiable instruments.

22. Mr. VIS (observer for the Netherlands) said that the example given at the 288th meeting by the representative of Austria illustrated a fundamental difference between the Geneva Conventions of 1930 and 1931 and the draft Conventions. Such differences were mainly policy ones: the Geneva Conventions reflected the majority view that the holder should be protected at all costs in the interest of the free circulation of international negotiable instruments—although they had not necessarily had that effect.

23. The draft Convention represented a fair balance between the competing systems and, wherever possible, rules common to both systems had been incorporated. He agreed that the wording of articles 25 and 26 could be improved, but defended the draft Convention's single approach to both claims and defences, in line with the common-law system and in contrast to the civil-law system.

24. His delegation had no objection to further discussion of the idea of the protected holder, although it disagreed with the representative of Egypt about replacing it with the notion of the "holder in due course".

25. Mr. SAMI (Iraq) said that the legal rules of both commercial systems had been poorly co-ordinated in the draft: the text was much too complicated and left the door open to different interpretations of a single rule. The new concept of protected holder, which illustrated that obscurity, should be abandoned, and the Commission should concentrate instead on the idea of the holder in good faith, which was accepted world-wide, often used in international business transactions, and indirectly reflected in articles 5, 30 and 41 (3) of the draft Convention. In response to the explanation from the representative of the United Kingdom that the draft was intended to establish a new and original system, he said that, in devising rules of trade law, it was essential to take into account notions that were widely and currently accepted and were frequently used by businessmen.

26. Mr. CRAWFORD (observer for Canada) noted that many delegations were unable to accept the provision that "protected holder" status could not be conferred upon the holder of an instrument if the instrument in question was incomplete at the time the holder received it. His delegation supported the draft text as it stood, but could support a proposal to the effect that the provision should deal specifically with an incomplete instrument which was subsequently completed in strict accordance with instructions. The requirement concerning completion would be retained in all other cases. To delete the word "complete" from the definition of protected holder in the Conventions would be unacceptable, however, since it might promote traffic in incomplete instruments. The circumstances covered by that provision demonstrated that the draft Conventions were of necessity complex since they had to provide satisfactory solutions for a wide variety of situations.

27. He was puzzled as to why so many delegations felt that the text would make the face of a bill of exchange less reliable, since dealings involving any commercial instrument necessarily involved more than the face. For example, the Geneva Uniform Law on Bills of Exchange and Promissory Notes contained a provision regarding action to the detriment of the debtor, which could be ascertained only by an examination of facts off the face of the instrument. Further consideration might be given to the modification which the representative of Australia had proposed to article 5 of the draft Convention on International Bills of Exchange and International Promissory Notes; that might allay the concern of those delegations which objected to the extent to which the article permitted inquiries to be made from off the face of an instrument. In his view, article 5 did not incorporate the concept of constructive knowledge, but represented an attempt to legislate a rule of credibility. Constructive knowledge implied that an individual has an intimate knowledge of all the provisions of the legal statutes involved, whereas actual knowledge, the concept embodied in article 5, was limited to knowledge of whether or not an instrument had been correctly completed.

28. It had been suggested that good faith should be added as a qualification for acquiring the status of protected holder. He disagreed with the inclusion of that qualification for the reasons cited by the representative of the United Kingdom. However, his delegation could accept the inclusion of a similar concept if it could be worded in a way that differed significantly from the wording of concepts that appeared frequently in the legislation of the countries whose courts would be required to interpret the provisions of the Convention.

29. The terms "holder" and "protected holder" had been chosen in an effort to protect the person receiving the instrument in due course. In that connection, the proposal made by the representative of Egypt might dispel the confusion with regard to those terms. Thus, the "protected holder" of the draft Convention would be called the "due-course holder", while the current "holder" would become the "unprotected holder". That would serve the purposes of the draft Convention by denying the benefit of negotiation to a person who, in accepting an instrument, was aware of something amiss in the transaction. Such wording would not discourage the negotiation of bills of exchange in transactions where they were desirable, but would promote negotiability in favour of due-course holders.

30. Mr. SPANOGLE (United States of America) said that the deletion of the requirement that an instrument should be complete was acceptable to his delegation as long as the draft Convention included a provision that completion should be authorized. With regard to article 5, the wording could not be construed to mean constructive knowledge as that concept was interpreted in the United States. Finally, the fact that the concept of good faith had been mentioned by so many delegations led him to believe that it should be taken into consideration in any redrafting of the definition of protected holder. The reasons for the Working Group's avoidance of a good faith requirement had been adequately explained by the representative of the United Kingdom; however, he shared the view that a comparable concept should be included that would be worded as precisely as possible so that it would not be confused with the various interpretations of the concept of good faith in different countries.

31. Mr. GOH (Singapore) said that his delegation supported the inclusion of concepts of holder and protected holder in the draft Convention, but appreciated the fact that various

articles in which those concepts appeared were unclear and inconsistent. The drafts should be improved, if possible, in order to satisfy the countries with civil-law systems. However, those countries must also accept the idea that the draft instruments were intended to develop a new system founded on compromise; if the concept of protected holder was deleted, the draft text would not be acceptable to delegations familiar with the common-law system.

32. Mr. MACCARONE (observer, European Banking Federation) agreed that the criticisms of the draft Conventions were largely political in nature, and were based more on a concern as to whether debtors or creditors were to be protected by the instruments. In elaborating the Conventions, the Working Group had had to consider whether to draw on the provisions of the Geneva system or the common-law system; it had evidently steered a middle course, opting to include provisions from both systems. Such a course was obviously necessary, since adhesion to only one legal system would have prevented countries subscribing to the other system from accepting the instrument. If States felt that the Conventions had been poorly drafted or were inconsistent, then those defects must be remedied. However, the Commission could not delete provisions from them simply on the ground that they did not conform to the practices of a particular legal system.

33. The anxiety of countries which followed the Geneva Uniform Laws might be lessened if it was borne in mind that the draft Conventions were ultimately intended for almost exclusive circulation within banking circles. He disagreed with the Australian proposal to delete the provision relating to constructive knowledge so that only actual knowledge of a fact might be taken into consideration. If the burden of proof in an incorrect transaction was to be placed on the liable party and knowledge of the irregularity was considered to be a state of mind, it would be impossible for a court to prove that a person had knowledge of the fact in question. The courts would therefore be compelled to turn to the concept of constructive knowledge even if that concept was not included in the draft Conventions. For that reason, he favoured the inclusion of a constructive knowledge provision in the draft texts.

34. Mr. DUCHEK (Austria) said that the system presented in the draft Conventions was an all-or-nothing system: once a holder was protected, he was fully protected; otherwise, he was subject to claims and defences. That provision came directly from the common-law system. However, if the Commission wished to create an intermediate system, it should try to understand the concerns of the civil-law countries, an approach which had been followed in the Working Group.

35. Some delegations maintained that the proposal which he had made at the 288th meeting to simplify certain articles, particularly by specifying the circumstances under which a holder could make a claim or a defence could be brought, would favour the interests of holders excessively. Attention had been drawn to article 28 of the draft Convention on International Bills of Exchange and International Promissory Notes to illustrate that the burden of proof in cases of irregular transactions lay with the initial holder, even though it would be difficult for him to establish any defect in subsequent transactions or to have constructive knowledge of the relationships between subsequent holders. He wished to know what some speakers meant when they said that an instrument must be above suspicion and a holder above reproach. The concept of protected holder contained in the

present draft would be difficult to abandon, given the complications of the provisions in question.

36. He was not defending the Geneva system *per se*, but rather a system which had been proved effective over time. That was why he maintained that the proposed Conventions should not distinguish between holders and protected holders, but should specify the conditions under which a claim could be brought.

37. Mr. JUMA (United Republic of Tanzania) said he thought that confusion had arisen because the drafting of the text of the draft Conventions was complex. His delegation believed that holders of complete instruments should be afforded greater protection than holders in general, and that the two categories of holder should therefore be defined clearly and simply.

*The meeting rose at noon.*

### Summary record of the 290th meeting Wednesday, 27 June 1984, 3 p.m.

[A/CN.9/SR.290]

*Chairman: Mr. SZASZ*

*The meeting was called to order at 3.25 p.m.*

1. Mr. MAEDA (Japan), referring to the concept of holder and protected holder in the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/211), said that article 4 (7) had no provision regarding bad faith and negligence, unlike the Geneva Uniform Law. However, article 5 of the draft corresponded to the bad faith provision in the Uniform Law. His delegation therefore supported the concept of protected holder in article 4 and supported article 5 as it stood.

2. Mr. VIS (observer for the Netherlands) said that he had held a discussion with the representative of Austria and the observer for Switzerland concerning the example given at the 288th meeting by the representative of Austria; an instrument issued to A was transferred to B in a situation involving fraud; B then transferred it to C in a transaction that was irregular; C then transferred it to D and D had knowledge of what had taken place between B and C, but no knowledge of what had occurred between A and B. The question which the Working Group should consider was whether D would be protected or would be subject to A's claim.

3. The CHAIRMAN said that all delegations had difficulties with the drafting of the text, which they felt needed considerable improvement. Several delegations had supported the concept of holder and protected holder, while others had expressed preference for a structure that was closer to the Geneva Uniform Law. While both approaches had considerable support, he was under the impression that most members would go along with the concept of two categories of holder if the concept of protected holder were broadened to make it easier for a person to become a protected holder. He understood that to be an expression of a policy that would strengthen the position of the creditor. Concern had been expressed that if a careful balance was not established between holder and protected holder, then that would discourage drawers.

4. According to some delegations, the fact that the instrument had been incomplete at the time a person became a holder should not preclude that person from being a protected holder. It had been stated that knowledge of a particular claim or defence should not preclude protection against other claims or defences of which the holder had no knowledge. It had also been stated that article 5 of the draft Convention needed further consideration and that the element

of good faith or bad faith should be included in the definition of "protected holder". There was still the possibility of further clarifying some points before the matter was referred to the Working Group.

5. Mr. ROGNLIEN (observer for Norway) said that if the idea was to retain the concept of protected holder in the text merely for drafting purposes, then the Working Group should be requested to prepare an alternative text with a view to expressing the concept more simply. He hoped that article 5 of the draft could be retained as it stood and that the concept of bad faith, which was unclear in practice, could be avoided.

6. Mr. VIS (observer for the Netherlands), referring to articles 25 and 26, said that the question of defences against a protected holder had given rise to many problems with regard to the Geneva Uniform Law, which had only two references to that matter. He therefore wondered whether defences based on incapacity and forged signatures, referred to in article 26 (1), should not be more clearly defined in an international system.

7. Mr. MACCARONE (observer, European Banking Federation) said that those defences could give rise to problems since a person who signed an instrument as a witness could later state that he had no knowledge of incapacity or forged signature. Inasmuch as there were several provisions governing those matters in national law, no such provision was needed in international law.

8. Mr. VOLKEN (observer for Switzerland) said he agreed with the Observer for Norway that the Working Group should be requested to prepare an alternative text on the question of protected holder. With respect to the point made by the Observer for the European Banking Federation, a concrete solution had to be found lest the international community should find itself always falling back on national law.

#### *Liability of a transferor by mere delivery*

9. The CHAIRMAN invited the members of UNCITRAL to express their views on paragraphs 17 and 18 of the note by the secretariat on major controversial and other issues concerning the draft Conventions (A/CN.9/249).

10. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics) said that the provision in article 41 of the draft Convention on International Bills of Exchange regarding the liability, off the instrument, of the person who was not a party to the instrument because he had not signed it constituted an exception to the basic principle laid down in the draft. The principle in question was that the rights and

duties of the parties to and the holder of the instrument were determined only by the content of the instrument itself and that the uniform norms should govern only the legal consequences of the transfer of the instrument by endorsement and the liability of the parties based on the signing of the instrument.

11. The Working Group had been of the view that all relations not resulting from the signature on the instrument should be governed by the applicable national law. An exception had been made only in the case of article 23, with a view to reaching a compromise between the two legal systems on the question of the risk of damages resulting from forged endorsement.

12. Although article 41 was based on the British and United States legal systems, it in fact went much further in that it gave the holder what, in his delegation's view, were unjustifiably extensive rights. Furthermore, when article 41 was compared with other articles of the draft Convention relating to the liability of the endorser, it could be seen that the liability of the person who had not signed the instrument was in some respects greater than that of the endorser. It would be advisable to consider the question of the endorser's liability more closely. Both the Geneva Uniform Law and the draft Convention regulated only the special function of the endorsement, and it would therefore be desirable to delete article 41 from the draft altogether.

13. Mr. VIS (observer for the Netherlands) said that his delegation was also experiencing difficulties with the part of the draft under consideration, for reasons similar to those stated by the representative of the Soviet Union. He was not sure whether it would be preferable to delete article 41 or to review the whole question of warranties. In any event, the provision in question required further consideration.

14. Mr. MACCARONE (observer, European Banking Federation), supported by Mr. MAGNUSSON (Sweden), said that article 41 should be deleted.

15. *The meeting was suspended at 4.20 p.m. and resumed at 4.50 p.m.*

16. Mr. GUEST (United Kingdom) said that the mere deletion of article 41 would not solve the problem, because there would still be the question, in the individual legal systems, of what warranty was provided by the person who transferred an instrument by mere delivery to the holder. The deletion of article 41 would result in a divergence between the individual legal systems.

17. The scope of the article was relatively narrow in that, in the majority of cases, the holder would not be liable for any claim because he was a protected holder. The question of recourse against the transferor would not arise in most cases. Account must also be taken of the limitation that was set forth in paragraph (3).

18. Admittedly, article 41 raised a number of issues. For example, any person who transferred an instrument by mere delivery was liable *vis-à-vis* any subsequent holder and not merely the immediate transferee. There was also the difficulty of adjusting liability under article 41 to the liability of a person who had actually signed the instrument. However, the fact that those issues were legitimate matters for discussion would not justify the deletion of the article.

19. Mr. OLIVENCIA (Spain) said that his delegation was having difficulties with article 41, particularly paragraphs (1) (d) and (3), and was therefore in favour of deleting it.

20. Mr. GRIFFITH (Australia) said that the question of the potential liability of a person who transferred an instrument by mere delivery would remain even if article 41 were deleted. There was perhaps room for compromise by including a provision under which transfers by mere delivery would incur liability only *vis-à-vis* the immediate transferee. Given the obvious difficulty of ascertaining the identity of subsequent holders, such a provision would be more practical, if less all-embracing, than the one in the draft and might well go some way towards meeting the criticisms expressed by previous speakers.

21. Mr. SPANOGLE (United States of America) welcomed the statement by the representative of the United Kingdom, who had put many of the problems in their proper perspective. It could not be said that article 41 created greater liability for the person who transferred by mere delivery than for an endorser, since the liability of the latter off the instrument was not specified in the draft and would have to be determined by local law.

22. As he saw it, there were two options to choose from. The first was to delete article 41 and leave to local law the question of determining liability for both endorsers and transferors by mere delivery. That option was hardly a model approach for achieving uniformity because of the differences in national laws. He therefore recommended a second option which was to make article 41 applicable to both endorsers and transferors by mere delivery and to cover liability off the instrument within the Convention. That approach was more likely to produce a uniform result. He supported the proposal to limit liability to the immediate transferee, although that was a secondary issue.

23. Mr. OU Zhi Min (China) pointed out that transfers by mere delivery did occur in the negotiation of instruments. In his view, that practice should be regulated. Article 41, which established an important principle concerning liability, should be preserved in some form. One solution might be to provide for the transfer of instruments by endorsement elsewhere in the Convention, thereby making it possible to delete article 41 as such.

24. Mr. BARRERA GRAF (Mexico) said that the article should be deleted because it related to a liability that did not need to be regulated by a convention or law on negotiable instruments. Transfers of such instruments were by endorsement, and the liability of the endorser and any subsequent party was specified under article 40, while article 29 established the general liability of the parties. Article 41 admitted an exception to the general rule of transfer by endorsement. That hypothesis, in his view, should not be envisaged by the draft, and liability in cases of transfer by mere delivery should be determined instead by national law.

25. Mr. ROGNLIEN (observer for Norway) indicated that his country's position had been wrongly stated in document A/CN.9/249. Norway was not in favour of deleting article 41. The text should be applicable to both transferors by mere delivery and endorsers. Furthermore, he would prefer to limit the grounds for liability under the article. The application of paragraph 1 should be restricted to the forged signature of, or the unauthorized signature on behalf of, the drawer. Subparagraphs (b) and (c) should be deleted.

26. Mr. CRAWFORD (observer for Canada) said that it was extremely undesirable to leave the question of liability unregulated. Liability should be established on an equal basis for all transferors and the latter should be liable only *vis-à-vis* the immediate transferee.

27. Mr. VOLKEN (observer for Switzerland) called for the deletion of article 41. The hypothetical situation with which it dealt could be covered in another context.

28. Mr. CHAFIK (Egypt) agreed that article 41 should be deleted. If it were retained, he wondered whether a liability claim would be subject to the rules of the proposed Convention and what scope it could have.

29. Mr. PAVLIK (Czechoslovakia) also called for the deletion of the article. There was little need in international trade for a provision such as the one contemplated in the draft for regulating transfers by mere delivery.

30. Mr. SEVON (observer for Finland) said that he favoured the proposal to include a provision applicable to both transferors by mere delivery and endorsers. However, extending the scope of article 41 to establish equal liability would mean that the principle of article 23 (1) would apply as a general rule, and he had some misgivings about that implication. He would favour some provision in the Convention based on article 41, as well as a combination of the proposals made by the Observers for Norway and Canada. Deleting subparagraphs (b) and (c) and limiting subparagraph (a) to the signature of the drawer would probably eliminate most of the negative effects pointed out by previous speakers.

31. Mr. WAGNER (German Democratic Republic) said that article 41 should be deleted because it imposed liability, off the instrument, on a transferor by mere delivery. Such a provision was not necessary because the international transfer of instruments by mere delivery was extremely rare.

32. Mr. ROEHRICH (France) said that his delegation was in favour of deleting article 41 for the reasons developed by the representative of Mexico and the observer for Switzerland.

33. Mr. CRAWFORD (observer for Canada) said it was not safe to assume that the international transfer of instruments by mere delivery was extremely rare. Loans to Canadian corporations by European banks could be made payable to the bearer and could be transferred many times and in various places. Such instruments should not be left unregulated.

34. Mr. ANKELE (Federal Republic of Germany) said that article 41 should be deleted because it provided for liability on the part of the transferor, even if there was no knowledge of any irregularity. Such a liability would be unacceptable because it would be contrary to the general principle of good faith. He agreed that the transfer of an instrument by mere delivery was extremely rare in international transactions.

35. Mr. VIS (observer for the Netherlands) said that his delegation would be in favour of the deletion of article 41 if it were certain that such a deletion would not impair the use of the international instrument. If no warranty was provided in the Convention for liability due to a fraudulent change in the face amount of an instrument, there would be uncertainty with regard to the right of action under the various local laws.

36. Mr. SAMI (Iraq) said that the deletion of article 41 would open the way for anyone who was aware of defects in an instrument to transfer it by mere delivery and therefore not incur liability. The article should be reconsidered by the relevant working group.

37. Mr. DUCHEK (Austria) asked whether it was worth taking the risk of leaving the matter to national law and thereby contradicting the goal of unification. Forgeries and alterations in international transactions had so far been rare, but if such problems began to arise more often, they would have to be solved. Perhaps there was no need for a strict liability rule but instead for a rule to cover cases where the party involved knew or ought to have known of the defect.

38. Mr. VIS (observer for the Netherlands) asked whether cheques were being included in the discussion, since the blank endorsement of cheques was standard practice. A rule in the draft Convention which provided a penalty for forging or altering an instrument might have an influence on practice.

39. Mr. DIXIT (India) said that article 41 was needed but should be modified so as not to impose an unnecessary burden on transferors by mere delivery.

40. The CHAIRMAN said it appeared that the majority favoured the deletion of article 41 of the draft Convention. Such a decision would be premature, however, because the drafting was not yet in the final stage and the composition of the majority and the minority was based on the different legal traditions of the various countries. Many of those in the minority had said that liability should be regulated so that transfers by mere delivery and transfers by endorsement and delivery would receive equal treatment. The Commission's final report should reflect both the majority view and the arguments in favour of retaining article 41, especially the reasons given by Canada. It should also reflect proposals, such as those of Australia, Canada and Norway, in favour of retaining the article with a narrower sphere of application.

*The meeting rose at 6 p.m.*

### Summary record of the 291st meeting Thursday, 28 June 1984, 10 a.m.

[A/CN.9/SR.291]

*Chairman:* Mr. SZASZ

*The meeting was called to order at 10.20 a.m.*

1. The CHAIRMAN reminded members that a small majority had favoured the deletion of article 41 of the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/211), while other members had been divided into groups advocating several other approaches. Accordingly, he felt that a final decision on that issue should be postponed.

2. *It was so decided.*

3. Mr. CHAFIK (Egypt), supported by Mr. SAMI (Iraq), pointed out that, because of ambiguous wording, article 41, paragraph 3, in the Arabic version of the draft on bills of exchange actually meant the opposite of what was intended. At the request of the secretariat he personally had prepared an Arabic translation of the draft in order to correct that and other ambiguities and, accordingly, he asked why the erroneous version was still in circulation.

4. The CHAIRMAN invited members to consider section D of document A/CN.9/249, which concerned crossed cheques and cheques payable in account, and, in particular, to decide

whether in the long term the commission should discuss the two draft Conventions in a parallel manner or should make a distinction between them.

5. Mr. DIXIT (India), supported by Mr. SAMI (Iraq), said that, although the work on international cheques was important, the draft on bills of exchange and promissory notes should be given priority. Simultaneous discussion of the two drafts would give rise to ambiguity and would complicate the Commission's work. Therefore, the discussion of the draft on bills of exchange, as a separate document having wider practical application, should be completed first and the draft Convention on International Cheques (A/CN.9/212) should be dealt with at a later date in the light of the former discussion.

6. Mr. SEVON (observer for Finland) agreed that the Commission's work should focus on the draft on bills of exchange; it seemed less likely that anything could be achieved in connection with international cheques, even at a later date. However, he suggested that the decision on whether to abandon that issue should not be taken until the draft on bills of exchange had been finalized.

7. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics) said that international cheques played an important role in international trade, and unification in that connection was of particular interest. Since a great deal of work had already been done in preparing the draft Convention on International Cheques, the Law Commission should proceed to consider that useful and appropriate question in more detail. However, his delegation would support the majority decision on whether or not the two drafts should be dealt with in a parallel manner.

8. Mr. CHAFIK (Egypt) said that he supported the regulation of international cheques, which played an important role in some areas of international trade, and felt that the subject should receive the priority granted to it originally in the Commission's programme of work. That undertaking would be greatly facilitated by the work on electronic funds transfers.

9. However, he did not object to postponing consideration of the draft on international cheques until the consideration of that on bills of exchange had been completed.

10. Mr. MAGNUSSON (Sweden) said that he was not opposed to the future consideration of international cheques, since they played an important role in international trade and since it might seem strange for there to be up-to-date provisions on bills of exchange and not on international cheques. However, the Commission's work should focus first on the draft Convention on Bills of Exchange. He agreed with the observer for Finland that the final decision on the draft on international cheques could be taken at a later date.

11. Mr. BARRERA GRAF (Mexico) supported the comments made by the representative of Sweden and the observer for Finland. His delegation felt that the regulation of international cheques was necessary but that it was premature to consider the draft prepared to that effect because of the similarity between many of its provisions and those of the draft on bills of exchange. Accordingly, consideration of the former should be postponed until a final decision was taken on the latter.

12. Mr. DUCHEK (Austria) said that it was not necessary to unify the different systems of law governing international cheques and that the current draft could not serve as a

suitable basis for fruitful discussion. Therefore, his delegation felt that the work on international cheques should not be continued. If the decision on that issue was postponed, his delegation's position in the discussion of the draft bills of exchange would be based on the assumption that there would be no convention on international cheques. The discussion on bills of exchange should be entirely separate from any consideration of international cheques.

13. Mr. FARNSWORTH (United States of America) supported the comments made by the representative of Austria. His delegation did not believe that the draft on international cheques offered any hope of unification and felt that the Commission should decide to abandon, not postpone, consideration of it. Eliminating consideration of international cheques, which were not a frequent occurrence, would facilitate consideration of the draft on bills of exchange. In the United States and, if he was not mistaken, in other common-law countries as well, international cheques constituted a particular kind of bill of exchange and, for those countries, it would be necessary merely to include in the convention on bills of exchange a very general provision to the effect that certain regulations did not apply to international cheques.

14. The CHAIRMAN suggested that, in the light of the views expressed, the Commission should focus on completing the draft Convention on Bills of Exchange but should not take any decision on the draft on international cheques until work on the former convention had been concluded. Accordingly, the Commission would not discuss part D of document A/CN.9/249 at the current stage.

15. *It was so decided.*

16. The CHAIRMAN invited the Commission to consider the additional issues outlined in part III of document A/CN.9/249.

17. Mr. MAEDA (Japan) referred to the issue dealt with in paragraph 22: whether the criteria established in article 1 (2) (e) of the draft Convention on International Bills of Exchange and International Promissory Notes were sufficient to make a bill of exchange qualify as an international instrument. Japan, as indicated in paragraph 22, felt that the places specified in article 1 (2) (e) should be divided into two groups: one including those specified in subparagraphs (i) and (ii), and one including those specified in subparagraphs (iii), (iv) and (v). An instrument would qualify as an international instrument only when at least one of the places in one group and one of the places in the other group were situated in different States.

18. Furthermore, Japan proposed that, of the places specified in article 1 (2) (e) and (3) (e), the place where the instrument was drawn or made and the place of payment should be designated as indispensable requisites for purposes of the application of the Convention, just as they were regarded as essential factors determining the law applicable to issues not covered by the draft Convention.

19. Mr. GUEST (United Kingdom) explained that the Working Group had thought that the most important element for determining the internationality of an instrument was the inclusion of the words "international bill of exchange (Convention of . . .)" or "international promissory note (Convention of . . .)", as required in article 1 (2) (a) and 1 (3) (a) respectively. It had been felt that, in view of the presence of those words in the text of the instrument itself, the bill or note could safely be given the largest possible scope. Thus, if

at least some international element was present, coupled with the presence of those words, the Convention should apply. Otherwise, there was some risk that an instrument bearing the words in question might fail to meet the internationality requirements and so be made subject to national law.

20. Regarding the second point raised by Japan, the bills or notes would probably be pre-printed, so that at least the place of drawing was likely to appear. However, the indication of the place of payment depended on whether the address of the payee appeared on the bill or note.

*The meeting was suspended at 11.15 a.m. and resumed at 11.55 a.m.*

21. Mr. PISEK (Czechoslovakia) said that he favoured the text of article 1 (2) (e) as drafted. If the drawer of an instrument was of the opinion that in a particular case two alone of the elements listed in subparagraph (e) were not sufficient, he could exclude the applicability of the Convention by omitting from the text of the instrument the words "international bill of exchange" or "international promissory note".

22. The basic question in article 1—the elements that must be present in order for an instrument to be an international instrument—was perfectly clear in paragraph (2) (a) through (d). With regard to paragraph (2) (e), it was not certain whether all five of the elements listed had to be indicated or only two of them. He himself felt that perhaps all five elements must be indicated in a bill or note and that, of the five places specified, two must be situated in different States.

23. Mr. MAGNUSSON (Sweden) agreed with the representative of the United Kingdom that the scope of an instrument should be as wide as possible. If the instrument included "international bill of exchange" or "international promissory note", the details of the wording of paragraph (2) (e) became less crucial. Indeed, one could then ask why paragraph (2) (e) should not be deleted together and why the inclusion of those words was not sufficient. The parties would then have perfect freedom to choose when they wanted to use the set of rules embodied in paragraph (2) (e), even for an instrument of purely domestic character.

24. Mr. ROGNLIEN (observer for Norway) said that he agreed with the representative of Sweden and wished to go further and propose the deletion of paragraph (2) (e) and its detailed criteria, since the really important element was the inclusion of the heading "international bill of exchange" on a bill. Indeed, the detailed criteria in paragraph (2) (e) could be a trap for the parties, not all of whom would necessarily scrutinize all the elements and ensure that all were present.

25. Mr. OLIVENCIA (Spain) said that his delegation could not support either the draft text or the amendment suggested by Japan. The problem raised by Japan was related to other general issues with which Spain had difficulty, such as the international character of an instrument, the optional character of the draft Convention, the specific elements to be taken into account for an instrument to qualify as international and the essential requisites for internationality.

26. Given the optional nature of the draft Convention, there would be some international instruments which the drawers opted not to make subject to the Convention under the terms of article 1 (2). The distinction therefore had to be made between international instruments and international instruments subject to the Convention and article 1 (1) should therefore refer explicitly to the optional nature of the Convention and its necessarily limited sphere of application.

27. The chief difficulty stemmed from the fact that paragraph (2) (e)—and indeed the whole of article 1—confused two issues that should be separated: the question of the essential requirements to be met in order for a bill or note to be a valid international instrument, and the question of the elements of internationality arising from the instrument itself. Not all the elements of internationality listed in paragraph (2) (e), for example, were essential to an international bill or note; some, like those in subparagraphs (ii) and (iv), were optional. Yet, according to the related article 11, instruments which lacked any element whatsoever of the requirements listed in article 1 (2) or (3) were considered to be incomplete instruments. For the purpose of article 11 as well, a clearer distinction had to be made between essential requirements for internationality and elements of internationality.

28. Similarly, there should also be some clarification in paragraph (2) (e) as to how the information listed was to be indicated. For the purposes of internationality, the simple indication of geographical place could be sufficient; but for the purpose of satisfying essential requirements, a simple geographic indication would have to be complemented by more specific indications of address.

29. Another concern was the fact that, if the sphere of application of the Convention were extended too far, its optional character could serve as an excuse allowing drawers to elude national laws by opting for the regulations of the Convention in order to give bills or notes a false appearance of internationality. The Convention might thereby come into conflict with national laws.

30. Mr. SAMI (Iraq) said that the two requirements for a bill of exchange to be international, namely that the word "international" should appear on it and that the places specified in paragraph (2) (e) should be situated in two different States, were insufficiently stringent to prevent individuals from negotiating under the Convention instruments which were not truly international. The Japanese proposal was not sufficiently far-reaching to represent a solution to the problem, and he recalled that the United Nations Convention on Contracts for the International Sale of Goods provided that, in order for a sale to be considered international, the two parties had to be domiciled in two different States. The Commission should reconsider article 1 and develop more specific criteria for the internationality of an instrument in order to prevent individuals from evading coverage of their transactions by domestic legislation.

31. Mr. BARRERA GRAF (Mexico) said that he endorsed the text of article 1, but that a distinction had to be drawn between the requirements of internationality that applied to an instrument from the outset and those that applied at the time it was drawn. The relationship between article 1 (2) (e) and article 1 (4) was not clear: because of the latter provision, the requirements set out in article 1 (2) (e) might not apply; in that case, in order to fall within the scope of the Convention, an instrument would only have to be labelled "international". The Convention's sphere of application would thus be expanded to include instruments normally covered by domestic legislation. The two paragraphs he had just mentioned must be borne in mind when considering the Canadian proposal that a readily reproducible symbol or abbreviation be adopted to aid the process of recognition of the instruments requiring special treatment under the Convention.

32. Mr. CRAWFORD (observer for Canada) said that the concern expressed about article 1 (2) (e) corroborated the validity of his delegation's suggestion about symbols or abbreviation. Canada could support the idea of differentiating between those elements which conferred internationality upon

an instrument, as described in article 1, and those which made it complete for the purposes of due negotiation, as set out in article 11, and did not fear that makers of international instruments would be encouraged to evade domestic jurisdiction by the ease of invoking article 1 (4). His delegation supported the draft as a whole.

33. Mr. ROEHRICH (France) said that his delegation endorsed the sphere of application of the Convention as set out in article 1, including the list of places given in paragraph (2) (e), and could not accept the Swedish proposal to delete that paragraph. He did not understand why the Japanese delegation wished to regroup the places mentioned in paragraph (2) (e); as the representative of the United Kingdom had stated, the list should be as comprehensive as possible. His delegation understood that article 1 did not list elements which were all absolutely essential in order for a bill of exchange to be valid, but that article 11 did.

34. Mr. DIXIT (India) agreed with the representative of Iraq that the genuinely international nature of a negotiable instrument should be the factor determining the applicability of the Convention.

35. Mr. VIS (observer for the Netherlands) said that his delegation endorsed the text of article 1 as it stood.

36. Mr. GRIFFITH (Australia) said that his delegation had no difficulty with article 1 and agreed with the representative of the United Kingdom that the inclusion of the words "international bill of exchange" was sufficient to establish the internationality of an instrument.

37. Mr. VOLKEN (observer for Switzerland) said that his delegation endorsed the proposal that article 1 should draw a distinction between the material validity and the internationality of a bill of exchange. He opposed the deletion of article 1 (2) (e).

38. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics) expressed support for the draft article but agreed with the

Japanese delegation that indication of the place where the bill was drawn should be an essential requisite for the application of the Convention.

39. Mr. DUCHEK (Austria) endorsed the underlying concept of article 1. Paragraph (2) (e) should not be deleted, but it was necessary to clarify whether all the places specified therein had to be indicated in the instrument or whether they were merely criteria for the application of the Convention and only two of them had to be indicated. An indication on the bill of the place where it was drawn should definitely be a mandatory requirement for the application of the Convention, while reference to the place of payment should perhaps also be made mandatory.

40. Mr. VINCENT (Sierra Leone) said that his delegation favoured the retention of paragraph (2) (e); without it, the Convention's sphere of application was unclear.

41. Mr. AKINLEYE (Nigeria) said that those elements which made a bill of exchange international were clearly set out in paragraphs (2) (a) to (d), but that paragraph (2) (e) did not specify that only two of the elements listed in it would suffice in order for the Convention to apply. The Working Group might have to improve the wording to make that clear. He agreed that article 1 should be read in conjunction with article 11 and that further consideration should be given to the relationship between the two articles.

42. Mr. CHAFIK (Egypt) said that his delegation endorsed the text of article 1 but believed that further consideration should be given to expanding the criteria for internationality to cover cases in which the place where the bill was drawn and paid were situated in the same State but the instrument was endorsed in another State. His delegation understood paragraph (2) (e) to mean that only two of the places listed had to be indicated on the instrument and had to be in different States.

*The meeting rose at 12.55 p.m.*

### Summary record of the 292nd meeting Thursday, 28 June 1984, 3 p.m.

[A/CN.9/SR.292]

*Chairman:* Mr. SZASZ

*The meeting was called to order at 3.15 p.m.*

1. Mr. ANKELE (Federal Republic of Germany) said that his delegation supported the principle of article 1 of the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/211) as an appropriate basis for achieving the goals accepted by most delegations. In particular, he did not feel that it was possible to eliminate the criteria mentioned in article 1 (2) (e), because of the practical difficulties that would arise from the coexistence of the different judicial systems.

2. The CHAIRMAN said that while some delegations wished to narrow the scope of article 1, others wished to broaden it. Most delegations, however, seemed in favour of the existing structure of the article, even though the drafting left room for improvement.

3. He suggested that the Commission should next take up the question of definition of signature dealt with in articles 4 (10) and (X) of the draft Convention on International Bills of Exchange and in paragraph 23 of document A/CN.9/249.

4. Mr. MAGNUSSON (Sweden) said that in Swedish banking circles it had been regarded as a considerable disadvantage that bills of exchange and cheques had to be signed by hand. His delegation was therefore strongly in favour of a rule allowing the issue of cheques or promissory notes signed by mechanical means. He pointed out that the use of promissory notes was becoming more frequent in international transactions and that bonds and debentures were normally signed by mechanical means.

5. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics) noted that the concept of signature contained in article 4 (10) could cause problems for countries whose legislation required handwritten signatures on instruments. His delegation felt that a contracting State should have the right, as indicated in article (X) to make a declaration to the effect that a signature placed on an instrument in its territory must be

handwritten. It would also be desirable to include in the Convention an article along the lines of article 12 of the United Nations Convention on Contracts for the International Sale of Goods.

6. Mr. CRAWFORD (observer for Canada) said his delegation understood that many national laws relating to forgery might affect the issue and was sympathetic to delegations which had difficulties in that area. Many means were available, however, to ensure security in the use of mechanical devices. The number of practical uses of mechanical signatures in international commerce was increasing. A change in national laws regarding forgery should therefore be encouraged by the Commission in order to permit mechanical signatures to be used. That would simplify modern business practice and enhance the Convention by eliminating one more point on which national law might intrude and produce different results in different countries.

7. Mr. VOLKEN (observer for Switzerland) said that paragraph 12 (b) of document A/CN.9/249/Add.1 did not accurately reflect his Government's position. If Switzerland felt that facsimile and other technical means should not be used in international exchanges, it was not because there would be problems with national legislation, but rather because it would be more appropriate to apply the provision to cheques, on which the use of mechanical means might be quite justifiable.

8. Mr. WAGNER (German Democratic Republic) and Mr. PAVLIK (Czechoslovakia) expressed strong support for the retention of article (X) of the draft Convention and for the inclusion of an article along the lines of article 12 of the United Nations Convention on Contracts for the International Sale of Goods.

9. Mr. CHAFIK (Egypt) suggested that article 4 (10) of the draft Convention should be reworded so that the term "signature" would cover all kinds of signatures, even handwritten ones. Article (X) was useful and should be incorporated in article 4 (10).

10. Mr. SAMI (Iraq) proposed that, if article 4 (10) were to be retained, the following phrase should be added at the beginning of the paragraph: "Taking into consideration the provisions of national laws". Article (X) was not an adequate provision because it covered only written signatures and omitted signature by thumb-print, and means of signature used in many developing countries.

11. Mr. SEVON (observer for Finland) said that his delegation supported article 4 (10). It had already been recognized in the Commission that handwritten signatures were not the only feasible means of signature. It was important to solve the problem within the Convention and not leave it to national law. The existing provision would mean that non-handwritten signatures would be recognized by all States parties to the Convention, even if they did not allow mechanical signatures in their own territory.

12. His delegation could not see how that would make forgery easier. A handwritten signature was easier to forge than a printed one. The draft offered a sound solution in so far as it recognized that there were States whose legislation required that a signature on an instrument must be handwritten and allowed such States to make a declaration to that effect.

13. Mr. OLIVENCIA (Spain) said that paragraph 23 (c) of document A/CN.9/249 did not accurately reflect his Government's position. Spain did not oppose the use of mechanical

signatures when necessary, in the case of mass-produced documents such as cheques, for example. They were not necessary on bills of exchange, which were not mass-produced, and the requirement of handwritten signature could be retained. Spain had not proposed the deletion of article 4 (10), but had merely expressed a reservation on it.

14. His delegation had also expressed concern about the disconnected manner in which the text dealt with forgery. All the references to that subject in the draft should be brought together and dealt with as a whole. In short, articles 4 (10), 23 (3), 30 and 32 should all be revised together. His Government had expressed reservations about article 23 (3) because it did not believe that a forger should be placed on the same footing as a person exceeding his authority.

15. Mr. VIS (observer for the Netherlands) said that the declaration provided for in article (X) was an acceptable compromise. However, he would like some clarification about its legal implications. He wondered whether a mechanical signature by, for example, a Soviet citizen in the Soviet Union would be valid in Canada. If he could get such clarification, he would agree that articles 4 (10) and (X) should be retained.

16. Mr. ANKELE (Federal Republic of Germany) said that article 4 (10) raised certain problems. His country's banks were happy with the legal requirement that a signature on an instrument must be handwritten. While he would be inclined to agree that a handwritten signature could be replaced by a facsimile, he believed that article 4 (10) went too far in permitting all kinds of mechanical means, which would increase considerably the risks of forgery. Since a bill of exchange was not a mass-produced document, he wondered whether there was any practical need to include all kinds of mechanical means. He therefore believed that article (X), which should be more clearly defined, should be included if article 4 (10) was to be retained.

17. Mr. ROGNLIEN (observer for Norway) said that, for reasons of social justice, he supported the retention of article 4 (10) as a means of enabling those who could not write to issue bills of exchange.

18. Mr. SPANOGLE (United States of America) said that his delegation's proposal in paragraph 23 (d) of document A/CN.9/249 was intended only as a drafting change, not a policy change. The definition of "forged signature" should be comprehensive.

19. Mr. GUEST (United Kingdom) said that the Working Group had considered at length the various forms of signature, including everything from thumb-prints to modern means of coded magnetic symbols. It should be borne in mind that the users of international bills of exchange were sophisticated people and hardly illiterates. His delegation could support article 4 (10) and had no objection to article (X). He interpreted the latter to mean that if a signature by mechanical means was used outside of the Soviet Union, for example, then that country would recognize it.

20. Mr. ROEHRICH (France) said that he understood the point just made by the representative of the United Kingdom and believed that members should attempt to move away from national concerns when drafting an international uniform law. While he was prepared to accept the inclusion of article (X), he believed that the real issue was what would be the effects of the declaration. He interpreted the wording of article 4 (10) to mean that a Contracting State would recognize all forms of signature referred to therein, even if it had made the reservation provided for in article (X). In other words, the requirement of handwritten signature would apply

only to documents signed in the country making the declaration. The draft Convention should provide for modern processes which might eventually replace handwritten signatures. The arguments about forgery were not conclusive because it was as easy to forge a handwritten signature as a mechanical signature.

21. Mr. ANGELICI (Italy) said his delegation believed that article 23 (3) should be deleted because a forged endorsement was quite different from an endorsement by a person exceeding his authority. He agreed in substance with article 30 as it stood and therefore could not support the United States proposal. He supported the text of the draft Convention, including article (X).

22. Mr. GRIFFITH (Australia) said that one difficulty with article 4 (10) was that it could be interpreted in such a way as to allow a person to place a symbol on a document without identifying himself. One should be able to ascertain the identity of the person signing. Article (X) should be more specific because it too was open to abuse.

23. Mr. GOH (Singapore) said that while his delegation generally supported article 4 (10), it had difficulty with the suggestion that the term "forged signature" should cover a signature by the wrongful or unauthorized use of mechanical means. The wrongful use of mechanical means should not be placed on the same footing as the forgery of a handwritten signature.

24. With respect to article (X), he sympathized with those delegations whose national laws required that signatures be handwritten. Accordingly, he could accept the inclusion of that article, but believed that it should be redrafted. An instrument signed by mechanical means in a given country and presented for payment in another country would be accepted if both recognized mechanical means. He wondered, however, what would be the situation if an instrument signed by mechanical means in one country was then presented for payment in a country that required handwritten signatures. Article (X) should be more specific in that respect.

*The meeting was suspended at 4.20 p.m. and resumed at 4.50 p.m.*

25. Mr. PERSSON (Sweden) said that promissory notes were widely used on international financial markets and there might be mass production of documents in that field. It would therefore be desirable to include article 4 (10) in the draft Convention.

26. He agreed that signature by mechanical means could lead to an increased number of cases of forgery; even though handwriting could also be forged.

27. Mr. VIS (observer for the Netherlands) said that the issues relating to the legal effects of articles 4 (10) and (X) should be dealt with in the Working Group.

28. Mr. MACCARONE (observer, European Banking Federation) said that the latest revision of the Uniform Customs and Practice for Documentary Credits, which was about to enter into force, contained a provision allowing for the production of documents by computer and other mechanical means.

29. Although bills of exchange were not usually mass produced, bank acceptances were. He could cite the example of a large company in which bills were drawn and endorsed by computer. Virtually all the negotiable instruments in question were circulated through bank channels on the basis of mechanical endorsement.

30. Mr. SEVON (observer for Finland) said that he wished to know the purpose of including in the draft Convention a provision along the lines of article 12 of the Sales Convention.

31. Mr. DUCHEK (Austria) said that the Working Group should reconsider the issue of forged signatures and signatures by unauthorized persons. The question of what was understood by "authority" and what obligation the transferee had when taking an instrument from a person purporting to have authority must be clarified at least to the extent that it affected article 23 of the draft Convention. If a new provision on forgery was drafted, as he hoped, the question of the precise meaning of authority should be reconsidered.

32. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics) said that when the inclusion of article (X) had been proposed and reference had been made to article 12 of the Sales Convention, the intention had been to indicate that, in cases where the legislation of an individual country required a handwritten signature, a corresponding provision should be included in agreements, including the draft Convention. Since there were many secondary issues that called for further discussion, it would be desirable for the Working Group to consider the entire question in detail.

33. The CHAIRMAN said that there appeared to be agreement on policy matters, including the retention of article (X), although it was clear that further work was required in order to solve drafting problems. Since UNCITRAL had reached a clear decision on policy, it would not be necessary for the Working Group to reconsider the issues concerned.

34. Mr. EFFROS (observer, International Monetary Fund) said that article 4 (11) of the draft Convention on International Bills of Exchange and International Promissory Notes would introduce a definition of "money" or "currency". In recent years, monetary units had been established by a number of intergovernmental institutions. Under the law governing traditional negotiable instruments, the effect of an instrument drawn in relation to such a monetary unit was not clear. There was now an opportunity, in the draft Convention, to make the status of instruments clear. There were two reasons for clarifying the matter. Firstly, it would be desirable to make it clear that, under the Convention, States Members of intergovernmental institutions, and other holders authorized by them, might make or draw instruments denominated and payable in a particular monetary unit. Secondly, it would be desirable to enable a private party to denominate a negotiable instrument under the Convention in terms of a monetary unit, even though such an instrument was payable in a currency rather than in the unit itself.

35. If a working group considered the matter subsequently, it might be desirable to examine whether a distinction should be made between the terms "money" and "currency". It might also be appropriate to consider whether a distinction should be made between the concepts of credit and physical currency.

36. Mr. FARNSWORTH (United States of America) said his delegation agreed that the definition of the terms "money" and "currency" could be improved; that was largely a drafting problem. It supported the proposals put forward by the observer for the International Monetary Fund and considered that the Working Group should look into the question of currency and credit, particularly in the light of the United States proposal set forth in paragraph 24 (b) of the note by the secretariat (A/CN.9/249).

37. Mr. PAVLIK (Czechoslovakia), supported by Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics), endorsed the idea of introducing the substance of article 4 (11) into the draft Convention. The definition of the terms "money" and "currency" should be expanded to include units of account established by intergovernmental treaties, conventions and agreements.

38. Mr. VIS (observer for the Netherlands) pointed out that if article 4 (11) was accepted, certain modifications would probably have to be made in the draft, for example, in article 6.

39. The CHAIRMAN said that, if he heard no objection, he would take it that the Commission decided that the square brackets enclosing article 4 (11) should be deleted, that the definition should be based upon the proposal of the International Monetary Fund as contained in paragraph 24 (c) of document A/CN.9/249, with certain modifications, and that the definition should clearly differentiate between physical currency and immediately available credit.

40. *It was so decided.*

41. The CHAIRMAN invited comments on paragraphs 25 and 26 of document A/CN.9/249.

42. Mr. PAVLIK (Czechoslovakia) said that the Czechoslovak proposal referred to in paragraph 25 (a) of the document should be considered in connection with article 7 (4) of the draft Convention with a view to elaborating a single provision covering the rate of interest stipulated.

43. Mr. ANKELE (Federal Republic of Germany) observed that the draft had frequently been criticized for its complexity. It could be simplified by the deletion of subparagraphs (b) and (c) of article 6 since they dealt with a problem of little importance in banking practice. That deletion would facilitate the implementation of subparagraphs (c) and (d) of article 8 (3).

44. Mr. SPANOGLE (United States of America) said that his delegation did not wish to pursue the proposal in paragraph 25 (a) of document A/CN.9/249. The point made in paragraph 25 (b), however, involved a major policy decision that he wished to recommend. Floating rate notes were not negotiable under most statutory systems, yet the majority of notes in circulation today were floating rate notes. He would like the Commission to consider whether the proposed Convention should apply to promissory notes that were outstanding in international trade.

45. Mr. SAMI (Iraq) said that the Geneva Uniform Law contained a clearer provision than the draft with regard to the rate of interest stipulated. He agreed with the representative of the Federal Republic of Germany that it was unnecessary to retain subparagraphs (b) and (c) of article 6.

46. Mr. PERSSON (Sweden) expressed strong support for article 6 (a). One of the main defects in the present text of the Geneva Uniform Law was that interest could not be stipulated on all kinds of bills of exchange. He supported the United States proposal concerning floating rate notes.

47. Mr. CRAWFORD (observer for Canada) also supported that proposal. A provision on floating rate notes would be a powerful incentive to use the Convention. It was customary in many markets to use a 360-day year, rather than the calendar year, for such notes. That was contrary to some national laws and it might also increase the effective rate of interest. The matter required some consideration in the adoption of what was otherwise a very valuable suggestion.

48. Mr. GUEST (United Kingdom), referring to the observation made by the representative of the Federal Republic of Germany, indicated that promissory notes in the United Kingdom almost invariably stipulated the rate of interest, and a reasonable proportion of such notes were in the form envisaged by subparagraphs (b) and (c) of article 6. Clearly, practice varied from country to country.

49. The adoption of the United States proposal in paragraph 25 (b) of document A/CN.9/249 would have a beneficial effect on the use of the Convention and the proposed instruments. Some difficulties might arise, at the drafting stage, in defining a floating rate, but he was confident that those difficulties could be overcome.

50. Mr. VIS (observer for the Netherlands) said that he was in favour of article 6 as it stood and agreed with the proposal concerning floating rate notes.

51. Mr. BARRERA GRAF (Mexico) said that he supported the provision in article 6 (a) as long as it was interpreted in accordance with article 7 (4). With regard to the United States proposal, negotiable floating rate notes might impose a greater burden on the payer of the instrument. Also, a rate that was not fixed might be considered as contrary to the very concept of a bill of exchange as expressed in article 1 (2) (b), which referred to "a definite sum of money". Although he was reluctant to accept a floating rate of interest, the Working Group might be able to arrive at a formulation that would clearly indicate how such rates should operate so as not to be detrimental to the payer of the instrument.

52. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics) said that his delegation was in favour of article 6 as it stood. It did not support the proposal to delete subparagraphs (b) and (c) because the kinds of instruments for which they provided were often placed in circulation. With regard to the proposal on floating rate notes, he agreed with the views of the representative of Mexico. The question was an interesting one and merited further consideration in the Working Group.

53. Mr. VOLKEN (observer for Switzerland) said that Swiss bankers had a number of reservations about the rate of interest on bills of exchange. Difficulties might arise if a particular bank wished to apply a different rate from the one stipulated on the instrument.

54. Ms. VILUS (Yugoslavia) said that her delegation had reservations about floating rate notes and agreed with the comments made by the representative of Mexico.

55. Mr. CHAFIK (Egypt) said that he was in favour of interest being stipulated on the instrument. He was opposed, however, to instalments at successive dates as proposed in subparagraphs (b) and (c) of article 6, since that would create difficulties when the instrument was presented for payment. He felt that the proposal concerning floating rate notes was a useful one. With regard to article 7 (4), he felt that the condition imposed by that provision was excessive.

56. Mr. OLIVENCIA (Spain) said that he agreed with the representative of Egypt concerning the stipulation of interest and, like him, was hesitant to accept the idea of payment by instalments at successive dates. His delegation had reservations about permitting floating rate notes to be negotiable: there was no objection to considering the proposal in the Working Group, but specific guarantees or limits were necessary.

**Summary record of the 293rd meeting  
Friday, 29 June 1984, 10 a.m.**

[A/CN.9/SR.293]

*Chairman: Mr. SZASZ*

*The meeting was called to order at 10.20 a.m.*

1. Mr. PERSSON (Sweden) said that most medium- and long-term loan contracts in the international financial market contained clauses stipulating that, in cases where tax was withheld by debtor States on the interest to be paid on a loan, the interest rate would be correspondingly increased to offset the loss represented by the tax withheld. He proposed that article 6 of the draft Convention on International Bills of Exchange and International Promissory Notes should contain such a provision.

2. Mr. BARRERA GRAF (Mexico) reiterated his delegation's reservations to the proposed provision for variable or floating interest rates in the light of the remarks just made by the representative of Sweden. The problem of a withholding tax on the interest payable under an instrument of credit was not specifically related to the instruments covered by the draft Conventions; nevertheless, contract practices of that nature, which were so unfair to debtors should not be sanctioned in an international legal text. Consequently, Mexico remained opposed to the inclusion in article 6 of a provision for floating interest rates.

3. Mr. VOLKEN (observer for Switzerland) associated himself with the reservations which had been expressed concerning the inclusion of a provision for payment by instalments at successive dates. Other procedures currently existed that would yield the same results. For example, individual bills of exchange could be drawn up for each payment, a system which simplified the procedure for protesting the non-payment of an instalment. The drafting of individual documents for each instalment meant that each could be treated as a separate transaction, thereby eliminating the need for paying stamp duty on cheques for partial payments. If article 6 was to be examined further, his delegation wished to have those considerations taken into account.

4. Mr. CRAWFORD (observer for Canada) said that delegations that viewed the introduction of a floating rate of interest as a new source of uncertainty should understand that it was actually a common method for controlling uncertainty, since the risks to both parties inherent in the setting of a fixed rate were removed. By including a reference to a rate set in an established financial centre, both parties would be assured that in their transaction no hidden costs would result from a change in interest rates.

5. The proposal of the representative of Sweden, on the other hand, appeared to inject an undesirable element of uncertainty into the draft Convention. While a clause requiring debtors to pay an additional amount to compensate for withholding tax was common in commercial agreements, pertinent facts regarding the debtor, such as his identity, were generally known when the instrument was drawn up, which meant that the creditor could determine whether such an additional payment would be necessary and could even calculate the exact amount required. In the case of a negotiable instrument such as a promissory note, however, the liability of the borrower was variable and depended on the

identity or even location of the debtor at the time the financial instrument matured.

6. Mr. de PAIVA (Brazil) said that his delegation shared the reservations expressed by the representative of Mexico.

7. Mr. SAMI (Iraq) said that his delegation rejected the inclusion of a requirement for variable interest rates, since such a provision was harmful to the interests of debtor States, particularly developing countries. The most important consideration in negotiating an instrument for a commercial transaction was the precise amount that was to be owed. The acceptance of a provision for floating interest rates would prevent States from having such information at hand when they negotiated an instrument.

8. Mr. DIXIT (India) said that, as the representative of a developing country, he could not accept the concept of a floating interest rate. Negotiable instruments were acceptable in general precisely because of the clear way in which they laid down obligations. Utilization of a floating rate meant that the parties to an instrument would not know the exact amount of their obligation when the instrument was negotiated. Furthermore, the utilization of a floating rate ran counter to the foreign-exchange regulations in effect in many developing countries.

9. His delegation also opposed the payment of negotiable instruments by instalments at successive dates, as stipulated in article 6 (b), preferring instead the issuing of separate negotiable instruments for each instalment.

10. Mr. GUEST (United Kingdom) said that the draft Convention had attempted to accommodate practices followed by countries in different parts of the world, even if such practices were not universal. The Working Group had taken that approach with a view to giving the largest possible scope, within the limits of reasonableness, to the use of existing institutions. For example, the use of payment by instalments, with an acceleration clause in the event that one instalment was not paid, was a common practice in the United Kingdom in so far as promissory notes were concerned. Unlike bills of exchange, promissory notes were generally negotiated only once, with the financial institution advancing the money against the debt represented by the note. The rationale for the inclusion of a provision allowing variable rates of interest was similar, in that it would allow countries which already followed that practice to continue to do so. Those provisions were not intended to make such practices mandatory, but rather to allow countries that already used them to continue to do so.

11. He urged that, as the draft text was examined further, subsequent references to practices that might appear foreign to some delegations should not be eliminated on that basis alone. However, the proposal made by the representative of Sweden should be investigated with great caution.

12. Mr. FARNSWORTH (United States of America), supported by Mr. GRIFFITH (Australia) and Mr. GOH (Singapore), endorsed the remarks made by the representative of the United Kingdom. He added that promissory notes payable in instalments were commonly used in his country; consequently, there might be some consternation if an international convention dealing with that instrument did not provide for that practice.

13. Mr. BARRERA GRAF (Mexico) said that he could agree to the regulation of payment by instalments at successive dates, even though that possibility did not exist in Mexico in connection with bills of exchange or promissory notes. Moreover, the Convention should regulate both payment by instalments at successive dates as stipulated in a single instrument and the acceleration of payments if several instruments were issued upon default in payment on one or several of the instruments. It was important also for the Working Group to bear those possibilities in mind in its work in that regard.

14. Mr. VOLKEN (observer for Switzerland) said that he agreed with the representative of the United Kingdom that the draft should make provision for arrangements which were used only in certain countries or regions. However, there were fears that, if the arrangements used in the common-law countries were included in the draft, they might be applied to bills of exchange as well as promissory notes. He therefore suggested that a clear distinction should be made between the two types of instrument.

15. Mr. SEVON (observer for Finland) said that, although Scandinavian law did not contain any provisions on payment by instalments, the proposal to that effect might constitute an improvement. Similarly, it seemed unrealistic to avoid the issue of the currently unstable interest rates. If floating rates were prohibited, interest rates might be used to cover currency fluctuations, and that might result in even higher interest rates. Therefore, he also supported the proposal on floating rate notes.

16. Mr. OLIVENCIA (Spain) said that it was necessary to be precise in regulating bills of exchange and promissory notes and that existing international practices did not meet that need adequately. His delegation did not object either to the frequency or to the possible effects that floating rates and payment by instalments might have on the economies of States. Its main concern was to ensure that clear regulations were established to govern bills of exchange. The scope of the draft provisions should not be expanded to the point of distorting the nature of bills of exchange and complicating such fundamental matters as circulation and liability. If the provisions of subparagraphs (b) and (c) were to apply to bills of exchange, all the related problems must be foreseen and fully regulated.

17. His delegation also had reservations about the legal regulation of floating rate notes, which would continue to circulate even if unregulated. In that connection, he asked whether the concept of the liability of successive endorsers would be compatible with the concept of floating interest rates, since the elimination of that type of liability would affect the amount of interest established and therefore the circulation of that type of note.

18. In conclusion, while reiterating his delegation's opposition to subparagraphs (b) and (c), he suggested as a compromise that they could perhaps be retained only for promissory notes. He stressed that, if extended to include bills of exchange, the provisions must be completely clear and precise.

19. Mr. DIXIT (India) said that, while floating interest rates might continue to be used even if unregulated, States must be able to know in advance what financial obligations were entailed by the instruments they signed. Moreover, the foreign exchange acts in force in many countries should not be disregarded. Accordingly, his country could not agree to permit floating interest rates. Although a distinction could be

made between bills of exchange and promissory notes in that regard, that might undermine the coherence of the Convention.

20. Mr. CRAWFORD (observer for Canada) supported the suggestion that the provisions on instalments should apply only to promissory notes. He drew attention to the fact that the objections expressed in connection with those provisions were similar to his delegation's objections to article 39, paragraph 3, which divided a bill of exchange into a good half and a bad half and thus would create uncertainty.

*The meeting was suspended at 11.20 a.m., and the part of the meeting covered by the summary record was resumed at 12.05 p.m.*

21. Mr. SHU Xianli (China) noted that, owing to the constant change in international interest rates, the creditors in international financial transactions often required interest on international instruments to be paid at the international market rate prevailing on the date of the payment. He therefore proposed that a phrase should be added to the draft allowing interest to be paid at the international market rate at a definite time and place. Such a stipulation should be written on the time bill itself in specific and unambiguous terms. In such a case, of course, the holder of the instrument would not know its precise value in advance, which could be a problem. China would not press its proposal if the Commission believed it would be too difficult to implement.

22. Mr. DUCHEK (Austria) said that payment on instruments by instalments and with floating interest rates was a common practice in the common-law countries. That fact should be reflected in the Convention. His first preference, therefore, would be to include subparagraphs (b) and (c) but restrict their provisions to promissory notes, according to the compromise solution put forward.

23. The sphere of application of the Convention should also be broadened to make floating interest rates possible, but also only for promissory notes. For the moment he wished to reserve his delegation's position on the specific suggestion made by the representative of China with regard to floating interest rates, since he did not know what was meant by "international market rate" or to what legal set of rules it referred. The matter should be studied, and, if such a worldwide rate existed, Austria would accept it.

24. Mr. ANGELICI (Italy) said that the various provisions of article 6 needed improvement. He was, however, reserving his position on the article until his and other Governments had had an opportunity to review all the specific points involved.

25. Mr. MAEDA (Japan) said that he supported the United States proposal regarding floating interest rates because it would broaden the scope of international negotiable instruments under the Convention, and, in practice, such instruments were needed in some financial markets. It seemed to him that the Commission had already permitted a kind of floating rate for interest after maturity, in article 66 (2).

26. Regarding subparagraphs (b) and (c) of article 6, Japan felt they should be retained.

27. Mr. PISEK (Czechoslovakia) said that, even though Czechoslovak law and banking practice did not permit instruments to be paid by instalments at successive dates, the practice did exist in other countries and that subparagraphs (b) and (c) should, therefore, be included in article 6 to broaden the sphere of application of the Convention.

28. Regarding floating interest rates, a bill of exchange should, in principle, state a specific rate of interest. However, the floating rate was a reality, and the scope of the Convention would therefore be broadened if it regulated instruments bearing such rates. That should be done, however, without prejudice to the certainty of the instrument: the clauses on floating interest rates must be very clear, and both payer and holder must know how to calculate, without any controversy or ambiguity, from the face of the instrument itself, the exact amount of interest.

29. Mr. CHAFIK (Egypt), supported by Mr. ANKELE (Federal Republic of Germany) and Ms. VILUS (Yugoslavia), said that, although his delegation had been in favour of deleting subparagraphs (b) and (c) of article 6, it would now accept, as a second choice, the compromise proposal to make them applicable only to promissory notes and not to bills of exchange.

30. Mr. ANKELE (Federal Republic of Germany) said that he still had reservations regarding floating interest rates but would accept the compromise suggestion made by Spain to limit such rates to promissory notes.

31. Ms. VILUS (Yugoslavia) said that she maintained the reservations expressed earlier regarding floating rates of interest.

32. Mr. CHAFIK (Egypt) said that Egypt was in favour of regulating floating interest rates in the Convention, because they were a widespread practice in all banking operations. Since, however, the practice worked against the developing countries, Egypt would follow the wishes of the majority as to whether a provision on floating interest rates should be included or excluded.

33. Mr. MATHANJUKI (Kenya) said that his delegation had reservations about including a provision on floating interest rates in article 6, because it felt it would create uncertainty over the negotiability of the bills themselves. If, however, a definite mechanism could be developed for

calculating such rates and the amount due could be indicated with certainty on the bills themselves, his delegation would not object to such a provision.

34. The CHAIRMAN, summarizing the results of the discussions on article 6, said that the problem of how to relate article 6 (a) to article 7 (4) was felt to be essentially a drafting problem.

35. Regarding article 6 (b) and (c), the impression was that many of those who opposed those two subparagraphs might accept a compromise that restricted their application to promissory notes. He suggested, therefore, that the Commission should instruct the Working Group to draft texts along those lines.

36. *It was so decided.*

37. The CHAIRMAN, referring to the discussion on floating interest rates, observed that, while some delegations still had strong reservations, the majority seemed to be in favour of including a provision on floating interest rates in the Convention, although in many cases their approval was conditional upon the degree of certainty that could be guaranteed to the parties to an instrument. A suggested intermediary solution of restricting floating interest rates to promissory notes had not received strong support.

38. The main issues were how the practice of floating interest rates could be reconciled with the Convention's approach to international instruments and how an international instrument could fulfil its function as a legal document, with adequate guarantees, under such a system. He therefore suggested that the Working Group should prepare an appropriate draft on the matter for further consideration, taking account of the reservations and conditional approvals that had been expressed.

39. *It was so decided.*

*The meeting rose at 12.50 p.m.*

### Summary record of the 294th meeting Friday, 29 June 1984, 3 p.m.

[A/CN.9/SR.294]

*Chairman: Mr. SZASZ*

*The meeting was called to order at 3.15 p.m.*

1. The CHAIRMAN invited comments on article 9 of the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/211) and on paragraph 16 of document A/CN.9/249/Add.1.

2. Mr. VOLKEN (observer for Switzerland) said that since the plurality of drawers or payees was almost never encountered in practice, the usefulness of the procedure envisaged in article 9 (1) was doubtful. The deletion of subparagraphs (b) and (c) of that article would simplify the text. Another solution was to amend paragraph (3) so as to provide that payment would be made to only one of the payees unless expressly stated otherwise in the bill.

3. Mr. ANKELE (Federal Republic of Germany) agreed with what the Observer for Switzerland had said about article

9 (1). However, he took note of the United Kingdom representative's earlier observation that the procedures envisaged in that article was followed in some countries, and he therefore favoured the proposal to amend paragraph (3).

4. Mr. OLIVENCIA (Spain) said that the presumption of article 9 (3) should be reversed. Joint and several liability should be indicated when, for example, there were two or more drawers. Although the other provisions of article 9 covered cases which rarely occurred, he would prefer their retention.

5. Mr. CHAFIK (Egypt) said that he favoured the retention of article 9 as it stood. He saw no particular merits, nor indeed any real drawbacks, in paragraphs (1) and (2). The presumption made in paragraph (3) was logical, and there was no good reason to change it.

6. Mr. PISEK (Czechoslovakia) reiterated his Government's view that payment to all holders at the same time would be difficult from the technical point of view unless divisible payment was split in equal portions among all holders (A/CN.9/248, page 42).

7. Mr. VIS (observer for the Netherlands) said that he was in favour of the present text of article 9.
8. Mr. DUCHEK (Austria) said that he too favoured the retention of article 9. With regard to paragraph (3), he supported the proposal made by the Observer for Switzerland.
9. Mr. ANGELICI (Italy) said that he also supported that proposal.
10. The CHAIRMAN invited comments on article 10 of the draft Convention and on paragraph 27 of document A/CN.9/249.
11. Mr. SHU Xianli (China) referred to his Government's proposal that article 10 (a) should be supplemented with the words "and regarded by the holder as an international promissory note;" (A/CN.9/249, para. 27). That was simply a drafting matter, not a question of policy or principle; a bill drawn by the drawer on himself was by nature a promissory note.
12. Mr. MACCARONE (observer, European Banking Federation) said that was not simply a drafting matter. If a bill was drawn by the drawer on himself, it would have to be established whether the bill was to be presented for acceptance, whether the drawer became primarily liable by accepting the bill or drawing it on himself, and whether there was any difference between the case where the bill was accepted by the drawer and the case where it was dishonoured.
13. It was insufficient to say that the bill could be regarded by the holder as a promissory note. If the Commission wished to accept the Chinese proposal, the text of the Convention would have to state explicitly that the instrument was indeed a promissory note.
14. Mr. OLIVENCIA (Spain) said that he fully endorsed the comments just made. The issue was all the more important because of the differences between national legal systems.
15. Mr. GRIFFITH (Australia) said that he also agreed with the observer for the European Banking Federation.
16. Mr. VIS (observer for the Netherlands) said that if the provision in article 10 were to be retained he would prefer the wording proposed by China, which was in line with section 5 of the British Bills of Exchange Act. The proposal was therefore not without precedent and merited further consideration.
17. The CHAIRMAN drew attention to the Chinese proposal on page 44 of document A/CN.9/248 concerning article 11 of the draft Convention.
18. Mr. SHU Xianli (China) said that his Government favoured the delegation of the article for the reasons stated on page 44 of document A/CN.9/248.
19. Mr. PISEK (Czechoslovakia) and Mr. WAGNER (German Democratic Republic) strongly supported the retention of article 11, because incomplete instruments were frequently used in international trade.
20. Mr. OLIVENCIA (Spain) proposed that article 11 should be retained and revised, with a view to eliminating the differences in the interpretation of article 1 (2) (e). The essential requirements and the deadline for completing the instrument must be spelt out. A promissory note lacking in some of those requirements would be defective, and *in rem* defences could be set up against it.
21. Mr. VOLKEN (observer for Switzerland) pointed out that under article 11 (2), especially subparagraph (b), a party who signed a promissory note completed otherwise than in accordance with the agreement could no longer make any defence against the holder, even though the latter had acted in bad faith. The holder who acted in bad faith should not be protected by the Convention, and the article should therefore be revised.
22. Mr. DUCHEK (Austria) said that article 11 should be retained. He fully supported the approach in paragraph (2) (a). The same concept should be expanded to include the defences provided for under article 25 (1) (b) and the claims provided for under article 25 (2).
23. Mr. BARRERA GRAF (Mexico) said that article 11 should be retained. However, the question of the simultaneity of the completion of the requirements and the concept of "incomplete instrument" should be clarified.
24. The CHAIRMAN said he took it that the Commission was generally in favour of retaining the substance of article 11. The proposals aimed at clarifying the article and bringing it into harmony with article 1 would need to be discussed in the appropriate working group.
25. *The meeting was suspended at 4.15 p.m. and resumed at 4.45 p.m.*
26. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics), referring to articles 30, 52, 58 and 63, said that the concept of implied act or omission was not clearly defined. The concept of implied dishonour could in practice lead to disputes among parties. It was impractical and inappropriate and should be deleted from the text.
27. Mr. GLATZ (Hungary) agreed with the representative of the Soviet Union. The concept of implied act or omission should be deleted.
28. Mr. WAGNER (German Democratic Republic) said that his delegation supported the position of the Soviet Union for the reasons set forth in document A/CN.9/248.
29. Mr. PISEK (Czechoslovakia) said that he shared the views of the three previous speakers. The concept of implied act or omission could lead to problems of interpretation.
30. Mr. GUEST (United Kingdom) said that a look at the pattern of articles 52, 58 and 63 would show that they took into account situations where presentation, protest and notice of dishonour were dispensed with. The articles followed the same pattern.
31. Mr. ROEHRICH (France) said that the difficulty arose because there were two different schools of thought. His delegation associated itself with the position taken by the representative of the Soviet Union on articles 30, 52, 58 and 63. Provisions such as those could give rise to uncertainty and artificial disputes.
32. Mr. ANGELICI (Italy) said that the concept of implied act would be interpreted differently by courts in different countries and should therefore not be retained in the Convention.
33. Mr. VOLKEN (observer for Switzerland) said that he associated himself with the views expressed by the representative of the Soviet Union.

34. Mr. MACCARONE (observer, European Banking Federation) said that the concept of implied act or omission was confusing and could be deleted.

35. Mr. SAMI (Iraq) said that the obligations under the instrument must be clear and accepted by all parties. There could be no legal effects with respect to matters that had nothing to do with the instrument. Transactions or events outside of the instrument could cause confusion and problems. His delegation therefore opposed the concept of implied act or omission.

36. Mr. ANKELE (Federal Republic of Germany) said that his delegation too opposed the concept of implied act.

37. Mr. GUEST (United Kingdom), supported by Mr. GOH (Singapore), proposed that the words "expressly or implied by" should be deleted from article 30.

38. Mr. OLIVENCIA (Spain) said that the deletion would not solve the problem completely. What was needed was greater clarity.

39. Article 30 must be considered in conjunction with article 23, and it must be recognized that articles 52, 58 and 63 gave rise to problems of a different nature. All the articles in question must be reconsidered.

40. Mr. CHAFIK (Egypt) said that the word "expressly" did not need to be deleted.

41. Mr. MAGNUSSON (Sweden) said that while his delegation had no strong views on the matter, it doubted the wisdom of deleting article 30 altogether.

42. Mr. SPANOGLE (United States of America) said that his delegation did not have a strong opinion on the question of implied waivers as it affected articles 52, 58 and 63, although it favoured the current wording of those articles. However, it was extremely unfortunate that the discussion of the concepts affected by the deletion of the words "or impliedly" from article 30 should be enveloped in a debate on a number of relatively unimportant points. His delegation objected to the attempt being made, through the elimination

of a particular word from the draft Convention, to dispense with the concepts of implied authorization and apparent authorization.

43. Mr. BARRERA GRAF (Mexico) said that the current discussion was yet another manifestation of the differences between the two legal systems. The United Kingdom proposal could be regarded as acceptable. In any event, it might be desirable to clarify the implications of the articles in question.

44. Mr. GRIFFITH (Australia) said that while his delegation could go along with the United Kingdom proposal, it would prefer to retain the current text of articles 30, 52, 58 and 63.

45. Mr. VIS (observer for the Netherlands) said that the Working Group should be requested to produce an appropriate solution.

46. Mr. JUMA (United Republic of Tanzania) said that his delegation was somewhat surprised at the United Kingdom proposal and was in favour of deleting the words "or impliedly" and "or by implication" from articles 30, 52, 58 and 63.

47. Mr. MACCARONE (observer, European Banking Federation) said that the United States representative had introduced the issue of the position of a principal who recognized the authority of an agent who signed an instrument without authority. Although that was an important issue, article 30 was not the right place in which to deal with it. The question of lack of authority could be dealt with in other articles of the draft Convention. There was no reason to equate forged endorsements with unauthorized signatures.

48. Mr. DIXIT (India) said that his delegation was in favour of deleting the words "or impliedly" and "or by implication".

49. The CHAIRMAN said it was clear from the discussion that the United Kingdom proposal would not solve the problem. The Working Group should consider the various implications of deleting the terms "or impliedly" and "or by implication" from articles 30, 52, 58 and 63.

*The meeting rose at 6 p.m.*

### Summary record of the 295th meeting Monday, 2 July 1984, 10 a.m.

[A/CN.9/SR.295]

Chairman: Mr. SZASZ

*The meeting was called to order at 10.15 a.m.*

1. The CHAIRMAN drew attention to paragraph 30 of document A/CN.9/249, concerning the provision for exclusion of liability by a drawer contained in article 34 (2) of the draft Convention on International Bills of Exchange and International Promissory Notes and invited delegations to submit their views on it.

2. Mr. OLIVENCIA (Spain) said that a crucial feature of a bill of exchange was that the drawer not only issued the order of payment but assumed liability until the bill was accepted, thus becoming the principal debtor. Article 40 (2) stipulated that an endorser could exclude or limit his own liability by an express stipulation on the instrument, a notion to which no objections had been raised. However, under article 35 (2) of

the draft Convention, the liability of the maker of a promissory note could not be limited or excluded, since the maker was the principal debtor in the transaction.

3. Following that reasoning, Spain could not accept the inclusion of such a provision in the draft Convention in the case of bills of exchange that had not been accepted, since, under those circumstances, the principal debtor was not the drawee. His delegation preferred article 9 of the Geneva Uniform Law on Bills of Exchange and Promissory Notes, since it authorized the drawer to release himself from liability for acceptance but not for payment of the instrument.

4. Mr. ROGNLIEN (observer for Norway) said that he, too, opposed the provision contained in article 34 (2). If a drawer wished to exclude his liability, he might do so by drawing up an instrument of a type other than those covered by the draft Convention. It would be disconcerting, however, to discover that the drawer of a bill of exchange had excluded his liability even before the bill had been accepted.

5. The draft Convention should not require persons utilizing bills of exchange to scrutinize the instrument in order to identify all the minute provisions it might contain. Under the circumstances, the Commission would do better to retain the provisions contained in the Geneva Uniform Law.

6. Mr. CHAFIK (Egypt) said that the role attributed to the drawer under the draft Convention merited serious consideration. The draft Convention treated the drawer as a simple guarantor, and not as a principal debtor, even before the instrument was accepted by the drawee. For instance, article 34 of the draft Convention enabled the drawer to exclude or limit his liability without making any distinction between guarantee of acceptance and guarantee of payment. However, while one might allow a drawer to exempt himself because he was unsure of the drawee's attitude towards the order of payment, it was unacceptable to allow him to exempt himself also from the guarantee of payment of a bill which he had drawn up against a value which he had obtained at the time of issue.

7. Other examples of the weakness of the drawer's obligation could be found in articles 49, 53 and 59 of the draft Convention, which gave to the drawer, even in cases of non-acceptance of the instrument by the drawee, the right to take advantage of the holder's negligence when a bill was not duly presented for acceptance or payment or when it was not duly protested for non-payment. In general, the concept of the drawer's obligation was too weak in the draft Convention and did not promote the negotiability of bills of exchange. The whole system should therefore be reconsidered when the text was reviewed.

8. Ms. VILUS (Yugoslavia) expressed surprise that no reference had been made to her delegation's observations in document A/CN.9/249, even though they had been included in document A/CN.9/248. She agreed with the views expressed by previous speakers but wished to emphasize her delegation's view that article 34 (2) should refer only to bills of exchange and not to promissory notes. If the provision applied to both instruments, it contradicted article 1 (3), which defined a promissory note as containing an unconditional promise. An unconditional promise could not involve exemptions and remain unconditional. Consequently, she proposed that paragraph (2) of article 34 should be either deleted or reworded so that it applied only to bills of exchange.

9. The CHAIRMAN drew the attention of the representative of Yugoslavia to article 35 (2) of the draft Convention.

10. Mr. ROEHRICH (France) said that, although the exclusion in question was not permitted under the Geneva Uniform Law, to which France subscribed, his delegation favoured it, since it enabled the drawer to exercise a number of options, including outright discounting, invoicing and confirmation of orders. However, those operations presupposed the drawer's guarantee of the existence of the claim and thus of the drawee's acceptance. Consequently, he proposed that article 34 (2) should be reworded to begin: "When a bill of exchange has been accepted, the drawer may exclude or limit . . .".

11. Mr. VIS (observer for the Netherlands) pointed out that the existing text of article 34 accommodated a practice utilized only in common-law countries. His delegation therefore favoured a compromise solution along the lines suggested by France. The Geneva Uniform Law already provided for the exclusion of liability for the sum of a non-acceptance, and that provision should therefore be retained. He also agreed

that the drawer should be allowed to exclude his liability if the bill had been accepted.

12. In addition, since article 43 made provision for an *aval* to a drawee, the drawee should then also be allowed to excuse his liability for dishonour by non-payment.

13. Mr. CHAFIK (Egypt) said that it should be specified that the representative of the Netherlands was concerned not with a guarantee of acceptance but only with a guarantee of payment.

14. Regarding the French compromise proposal, it should be pointed out that the normal practice was for a drawer to insert a stipulation disclaiming liability for payment at the time a bill was drawn or issued and for the acceptance to come only after the bill was drawn or issued. The compromise proposed by France, however, covered only the very unusual case in which the drawer inserted a clause disclaiming liability after the acceptance of the bill.

15. Mr. WAGNER (German Democratic Republic) said his delegation accepted article 34 (2) as it stood. In his understanding, the drawer was a secondary debtor and should therefore be in the same position as an endorser to exclude liability.

16. Mr. ANKELE (Federal Republic of Germany) said there was no justification for allowing a drawer to exclude his obligation; a bill of exchange that was drafted with such a clause appeared to him obscure, and he questioned the significance of such an instrument in international practice. However, since the remarks made by other delegations seemed to indicate that such practices were followed in other States, he could accept the French proposal limiting the application of the provision to a drawee who had accepted a bill of exchange.

17. Mr. SAMI (Iraq) said that, as the drawer's signature was the only signature to appear on a bill of exchange when it was issued, he was the principal liable party. The Geneva Uniform Law did not allow the drawer to exclude his liability, since, if he could, the bill of exchange would become meaningless and the holder would have no guarantee. Consequently, his delegation fully supported the French proposal.

18. Mr. PERSSON (Sweden) said he favoured the draft text as it stood but could accept the French proposal. An exporter-drawer holding a bill of exchange often wanted to discount the bill without recourse because he wanted the bill off the books as a guarantee. Banks would often allow that practice so as not to exercise the drawer's liability. Thus, while he could understand why, in theory, a drawer should not be allowed to claim exclusion—so that someone would bear responsibility for the bill—he nevertheless believed that the practical reasons which he had cited should take precedence.

19. Mr. JOKO-SMART (Sierra Leone) said that the provisions contained in article 34 (2) were entirely acceptable. Presumably, the drafters of that article had been thinking of the "accommodation bill" which existed in the common-law system. In such a bill, the drawee lent his name to the drawer, who might not be in a position to make payment if the bill was dishonoured. That practice was entirely legitimate in his country, and he saw no reason why it could not be extended to apply to the case of an endorser who accommodated a drawer. The holder of such a bill was well protected, since he was free to accept or refuse to accept it.

20. Mr. DIXIT (India) opposed the clause in question for the reasons stated by the representatives of the Federal Republic of Germany, Iraq and Spain. While such exclusions were utilized in some countries, it should be borne in mind that the Commission was trying to promote trade in which bills of exchange which conformed to the Convention would be used. Article 34 (2) went against the spirit of the draft Convention.

21. He proposed that the word "engages" in article 34 (1) should be replaced with the word "undertakes".

22. Mr. SPANOGLE (United States of America) agreed with the representative of India that the Commission ought to promote the use of instruments covered by the draft Conventions. Various delegations had shown that instruments containing the provision under discussion were in use under the common law system. If the UNCITRAL system was to preclude their use by the deletion of article 34 (2), such instruments would be used outside that system regardless. Therefore, in order to ensure that the draft Convention were widely followed, the clause in question should be retained.

23. Mr. BARRERA GRAF (Mexico) said he thought that the French proposal could be broadened to provide for another obligation or liability in accordance with the provisions of article 42, which stated that the drawer could have certain guarantees from the guarantor. He proposed that, when the drawer limited or excluded his liability, the bill should specify that another person could be made liable. Acceptance must also cover cases in which the drawer was sending a bill at his own charge. When a bill was delivered on the account of the drawer, then the signature of the drawer must be interpreted as signifying acceptance when it was transferred on his behalf. He agreed to the provisions contained in article 34 (2) on condition that the bill was accepted. At the same time, however, such a condition appeared to contradict article 42 (4) (b), which stated that the signature alone of the drawee on the front of the instrument was an acceptance. If that was true, then the drawer would also be the acceptor of the bill. However, by limiting the provisions of article 34 (2) to apply to cases in which another party was made liable for payment as well as in cases of acceptance, the inconsistency might be corrected.

24. Mr. GUEST (United Kingdom) said he supported the text as it stood for the practical reasons stated by the representative of Sweden.

25. Mr. DUCHEK (Austria) said he could support the exclusion of liability by the drawer only when the bill had been accepted; he also favoured allowing exclusion if there was a guarantor.

26. Mr. GRIFFITH (Australia) said that his delegation supported the draft text as it stood.

27. Mr. GOH (Singapore) said that his delegation also supported the present text, but could agree to the compromise proposed by the representative of France.

28. Mr. ANGELICI (Italy) expressed support for the proposal made by the representative of Mexico.

29. Mr. PAVLIK (Czechoslovakia) said that it would be hard to imagine how a bill of exchange bearing only the signature of a drawer who had excluded his liability for acceptance and for payment could be circulated. If, however, such a bill was backed by a banking instrument, as often happened in practice, that would enable the drawer, who had

been authorized under that banking instrument to draw without liability, to shift the entire burden on the bank. In such cases, article 34 (2) as drafted might be useful.

30. Mr. CRAWFORD (observer for Canada) said that he supported the text as drafted but could accept the compromises proposed by the representatives of France and the Netherlands.

31. He felt, however, that an undesirable circumvention of the Convention would be fostered by the fact that its provisions discouraged established practices such as forfeiting, where there was complete negotiation of documentation without recourse, thus encouraging the parties to use some other body of law and make side agreements allowing the drawer to be indemnified against the liability that the Convention prevented him from negating.

32. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics) said that the Soviet Union was satisfied with the draft for reasons already stated by other members of the Commission.

33. Mr. ROGNLIEN (observer for Norway) said that he would like to have a survey of how many exclusion clauses were allowed on a bill of exchange according to the Convention rules. If there were too many such clauses, it would be hard for the parties to use the instrument because they would have to read it very closely. Another question was how legible such clauses should be—should they be printed in block capitals on the face of the bill or in small print?

34. The CHAIRMAN said that, although opinions were still very divided on the question, it was his feeling that the Commission was ready at least to decide on a policy to be followed with regard to article 34 (2), namely, that the drawer should be permitted to exclude or limit his liability in those cases where some other liable person could be found. The appropriate working group would then proceed, in the light of that policy, to study not only the compromise proposed by France and the exceptions mentioned by other delegations but also any other cases that might be covered by that policy, and to draft appropriate provisions.

35. Mr. VIS (observer for the Netherlands) said that his delegation could accept the policy proposed by the Chairman only if the drawer was allowed to disclaim liability for dishonour by non-payment. Moreover, it could accept the exceptional cases mentioned by the various delegations only if, indeed, the drawer issued an accepted bill or issued a bill containing a guarantee for the drawee at the time of issuance and not at a later stage.

36. The CHAIRMAN said that he would take it that the Commission wished the appropriate working group to pursue the policy he had just suggested with regard to article 34, on the understanding that the implications of the policy should be made as broad as possible.

37. *It was so decided.*

*The meeting was suspended at 11.15 a.m. and resumed at 11.50 a.m.*

38. The CHAIRMAN invited the Committee to consider paragraph 31 of document A/CN.9/249 regarding the concept of guarantee in article 42 of the draft Convention.

39. Mr. WAGNER (Federal Republic of Germany) said that his delegation objected to the irrefragable presumption in

article 42 (5) that, if a guarantor had not specified the person for whom he had become guarantor that person was the acceptor or the drawee in the case of a bill and the maker in the case of a note, on the ground that the intention of the guarantor was usually expressed by the fact that his signature was placed next to that of the person for whom the guarantee was given. The Convention should provide only for a simple presumption of the real intention of the guarantor. That would make it easier for his delegation to accept the principle that an *aval*, or guarantee, should be given for a drawee—a questionable principle because it provided a security for a non-existent obligation.

40. The CHAIRMAN drew the Commission's attention to the fact that Switzerland had made the same proposal.

41. Mr. MAEDA (Japan) said that article 42 as drafted did not make it clear whether or not an incomplete instrument could be guaranteed, while article 38 (1) did clearly state that an incomplete instrument which satisfied the requirements set out in article 1 (2) (a) might be accepted by the drawee under certain conditions. It was difficult to see why a guarantee should be treated differently from an acceptance. Therefore, Japan proposed that a provision should be added to article 42 to the effect that an incomplete instrument might be guaranteed before it had been signed by the drawer or the maker or while otherwise incomplete.

42. Mr. OLIVENCIA (Spain) said that Spain questioned the provision in article 42 (1) allowing a guarantee to be given for a drawee who was not an acceptor and therefore not liable on an instrument. The provision did, of course, have the advantage of strengthening liability under the instrument and giving effect to a signature appearing on the instrument. The problem was to understand how, legally, article 42 (1) could allow a guarantee—which was normally given for another liable party—to be given for the drawee, in whose case there was no liability to be guaranteed. In that connection, it should be noted that the provision in article 43 (1)—that a guarantor was liable to the same extent as the party for whom he had become guarantor—had not been made to apply in article 43 (2) to a guarantor for the drawee, since the former undertook to pay the bill at maturity.

43. The practical question that then arose was whether the guarantee for a drawee was really a true *aval* and a true exchange intervention, or whether it was not rather an acceptance in the sense of article 36 (2). If the latter was the case and such a guarantee was, for instance, subject to qualification, the provisions of article 39 (2) would have to apply. Spain believed that the legal consequences of the guarantee for the drawee should be clearly and fully specified in the text of article 42 by the Working Group.

44. The CHAIRMAN observed that the proposal of Japan was relevant in terms of the policy decision just taken with respect to article 34.

45. The Spanish objections to the text of article 42 seemed to be a question not of changing the policy but rather of improving the clarity of the draft.

46. Mr. ROEHRICH (France) said that, on the whole, his delegation favoured article 42 as drafted, including paragraph (5). His delegation did feel, however, that the Convention should allow the useful option—which existed in several national legislations—of giving a guarantee in a separate document. Article 42 (2), as drafted, apparently covered only a guarantee written on the instrument itself or on an *allonge*.

47. Mr. PISEK (Czechoslovakia) said that his delegation supported article 42 as drafted, in view of prevailing inter-

national business practice. From that same point of view, it could not support the proposal by the Federal Republic of Germany, which would be prejudicial to the principle of legal certainty and sound interpretation. He did support the proposal of Japan, in view both of established international business practice and of the fact that civil law allowed the possibility of giving guarantees for future business operations.

48. Mr. VIS (observer for the Netherlands) said that articles 42 and 43 as drafted had incorporated the Geneva system legislation of the *aval* but had gone beyond it to add the rule, which his delegation favoured, that permitted a person to become a guarantor for the drawee. The Working Group had made that addition on the basis of replies by Governments to the questionnaire of the UNCITRAL Study Group on International Payments, which had indicated that such stipulations as payment guarantees were found in practice in both the civil law and the common law systems.

49. The Convention contained other rules where the guarantor had guaranteed payment and was therefore the guarantor for the drawee, as in article 50 and article 53 (3); and his delegation therefore preferred that the rule should be maintained in article 42.

50. Mr. WAGNER (Federal Republic of Germany) said that it was customary in international transactions for a guarantee to be issued for the principal debtor, namely, the acceptor of the draft or the maker of the note. On the basis of that international practice, his delegation deemed it appropriate to specify for whom a guarantee was given by express wording on the instrument in all cases where a guarantee had to be given for a party who was secondarily liable. It therefore favoured maintaining the draft text as it stood.

51. Mr. AKINLEYE (Nigeria) said that his delegation found article 42 entirely acceptable as drafted. However the Working Group could improve on the wording of paragraph (5) in order to allay the fears expressed by the Federal Republic of Germany, since it was not clear in the draft text whether the presumption involved was rebuttable or not.

52. Mr. SAMI (Iraq) said that his delegation favoured adding a clarification to the text of article 42 (5) along the lines suggested by the Federal Republic of Germany, to the effect that a guarantee did not always favour the guarantor but sometimes also another party who was not an acceptor. The obligation of the guarantor was an obligation of principle which could not be disclaimed, a fact demonstrated by article 50 (2) (b), which permitted an immediate right of recourse against the guarantor of the drawee.

53. Mr. PERSSON (Sweden) said that, under the Geneva system, *aval* was almost always applied to the acceptor. Problems had arisen because many people were unaware of that. With regard to international bills of exchange, his country favoured the current text because of the presumption that *aval* was meant to be security for the acceptor's liability.

54. Mr. DUCHEK (Austria) said that his delegation favoured the current draft of articles 42 and 43. It was true that the presumption in article 42 (5) was prejudicial to cases where the signature of the guarantor was next to the signature of a party on the instrument. In such cases, however, it was clear that the guarantor did not wish to guarantee for the person to whom the presumption would apply, but rather for the person besides whose signature he had placed his own signature. Nevertheless, the first sentence of article 42 (5) did not stipulate that specification must be explicit. Under the Geneva system implied specification must be considered in the cases referred to by the representative of the Federal Republic of Germany. Therefore, even if article 42 (5) was not redrafted,

that practice could continue under the Convention. Such a presumption would not apply to the cases referred to by the representative of the Federal Republic of Germany. There would, however, be specification in favour of the person whose signature was next to the signature of the guarantor.

55. The CHAIRMAN said that it was clear that the majority of the members of the Commission supported the wording of article 42 and wished to retain the presumption contained in paragraph (5). The various drafting proposals would be taken into consideration. The Commission did not seem to support the proposal made by Japan. Nevertheless, in accordance with the policy decision taken with regard to article 34, the working group to which the text was referred might decide that the Japanese proposal should be incorporated into the text of article 42.

56. Mr. VIS (observer for the Netherlands), Mr. GRIFFITH (Australia), Mr. SPANOGLÉ (United States of America), and Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics) said that they supported the proposal made by Japan.

57. The CHAIRMAN said that the proposal made by Japan could be incorporated in the text of article 42 if the Commission carried out the policy decision made with regard to article 34 (2).

58. Mr. WAGNER (German Democratic Republic) reaffirmed the comments made by his Government with regard to articles 48 and 52 of the draft Convention and contained in document A/CN.9/248. The current version should be revised in order to provide also those possibilities for exercising the right of recourse before maturity which were based on the Geneva Convention and had proved their practical effectiveness in many countries.

59. Mr. PISEK (Czechoslovakia) said that, in accordance with the comments by his Government concerning article 55 of the draft Convention, his delegation supported the view expressed by the representative of the German Democratic Republic.

60. Mr. GLATZ (Hungary) reaffirmed the position of his Government as set forth in paragraph 32 of document A/CN.9/249.

61. Mr. KOZHEVNIKOV (Union of Soviet Socialist Republics) reaffirmed the position of his Government with regard to the articles under consideration and expressed support for the position of the German Democratic Republic.

62. Mr. OLIVENCIA (Spain) reaffirmed his Government's position with regard to articles 48 and 52. The current text should be further clarified with regard to cases of insolvency of the drawee. The text should also include the other major legal consequences arising out of insolvency and bankruptcy. Under article 50 (2), if a bill was dishonoured by non-acceptance, the holder could exercise an immediate right of recourse against the drawer, the endorsers and their guarantors.

63. Mr. VIS (observer for the Netherlands) said that he thought that the proposal made by the German Democratic

Republic was covered by article 48 of the draft Convention. The Working Group had intended that there should be an immediate right of recourse for non-acceptance and non-payment in cases involving bankruptcy.

64. Mr. GUEST (United Kingdom) said that the Working Group had intended that the words "has no longer the power freely to deal with assets by reason of his insolvency" in article 48 should cover cases involving bankruptcy and other types of insolvency. There were so many types of insolvency under domestic legislation that a general phrase of that sort was required. Under the legislation of certain countries of the Geneva system there was an acceleration of liability if the drawee or acceptor became bankrupt before the date of maturity. That acceleration of liability was not provided for in the draft Convention. In the case of dishonour by non-payment it would be necessary to wait until the date of maturity. If at that time the acceptor was bankrupt, then the liability to present the bill for payment would be waived and there would be a case of dishonour and liability.

65. Mr. ROEHRICH (France) said that article 48 gave rise to a number of difficulties for his delegation both with regard to form and substance. It was clear that the formulation in paragraph 48 (a) covered cases of bankruptcy. Nevertheless, his delegation felt that the draft text contained too many cases of anticipated recourse without acceptance. Under the Geneva system such types of recourse were considered exceptional. The number of cases in which presentment for acceptance was dispensed with under article 48 (a) seemed excessive.

66. Mr. ROGNLIEN (observer for Norway) said that the phrase "a necessary or optional presentment for acceptance" was not clear. With regard to article 48 (a), he pointed out that, if a deceased drawee had an estate, it might be in the interest of the estate to accept the bill. For that reason, the draft should be made more flexible by stating that, if the deceased drawee had an estate which under the law of the place of business was able to succeed in respect of the rights and obligations of the deceased person, then presentment for acceptance should not be dispensed with, if presentment was possible under the national law.

67. With regard to cases of insolvency, a bankrupt estate might be in a position to accept and it might be in the interest of the parties to arrange acceptance. If a bill was not presented, it would be dishonoured even if the estate was unable to act.

68. Mr. VIS (observer for the Netherlands), referring to the view expressed by the representative of the United Kingdom, said that acceleration of liability arising out of dishonour by non-acceptance was provided for under the draft Convention. If the drawee was bankrupt, there was an immediate right of recourse by the holder against prior parties. The holder would, therefore, be paid. The word "necessary" was required in article 48 because article 45 (a) gave the drawer the possibility of stipulating that the bill must be presented for acceptance. Under article 48 the necessary presentment for acceptance was dispensed with if the drawee was bankrupt or insolvent.

*The meeting rose at 1.05 p.m.*

### Summary record of the 296th meeting Monday, 2 July 1984, 3 p.m.

[A/CN.9/SR.296]

*Chairman: Mr. SZASZ*

*The meeting was called to order at 3.10 p.m.*

1. The CHAIRMAN invited the members of UNCITRAL to clarify further their views on articles 48 and 52 of the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/211).

2. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) drew attention to the relevant differences between the two basic legal systems regarding the immediate right of recourse for the holder of the instrument against the acceptor whose bankruptcy took place prior to maturity.

3. With respect to immediate recourse, she referred first of all to the question of non-acceptance. Articles 48 (a) and 52 (2) (a) envisaged situations where the drawee no longer had the power to deal freely with assets by reason of his insolvency, in other words, his bankruptcy. In such instances, it was not necessary to make a protest either. Under article 50 (2) (a), if a bill was dishonoured by non-acceptance, the holder could exercise an immediate right of recourse against the drawer, the endorsers and their guarantors. That was the way in which the draft Convention dealt with the problem of the right of recourse prior to maturity in cases of non-acceptance.

4. There was, however, the question whether it was possible to have immediate recourse in cases where, although the instrument was accepted, the acceptor went bankrupt after a protest had been made but prior to maturity. In that connection, she referred to articles 52 (2) (d), 58 (2) (d) and 54 (1) (b). Article 54 did not allow the holder to exercise an immediate right of recourse in cases of non-payment owing to bankruptcy prior to maturity. That approach was inappropriate for practical reasons, particularly where international instruments were concerned. The holder's interests must be safeguarded properly, through provision of an immediate right of recourse in the case of bankruptcy of the acceptor prior to maturity.

5. Mr. ROGNLIEN (observer for Norway) said that the *chapeau* to article 48 should be brought into line with the French text.

6. With regard to the substance of that article, he noted that in many cases business continued as usual after the drawee's death and should not be disrupted. He therefore suggested two possible approaches, the first being the deletion of the words "is dead or" from subparagraph (a). If that alternative was chosen, it must be made clear that the provisions in question also applied in the case of the death of the drawee. The other possibility was to insert a separate subparagraph into article 48 to deal with cases where the drawee was dead. Such a subparagraph could be drafted along the following lines: "If the drawee is dead and is not succeeded by an organized estate which under the law of his place of business is entitled to accept the bill".

7. Mr. VIS (observer for the Netherlands), referring to his response to the United Kingdom representative at the previous meeting, said that he had since ascertained that that representative's interpretation of the draft Convention was in fact correct.

8. Mr. OLIVENCIA (Spain) said that his delegation supported the recent drafting suggestion regarding the first line of article 48. The scope of subparagraph (a) of that article was too broad, and the wording of the subparagraph was too vague. His delegation supported the general thrust of the comments made by the observer for Norway on situations where the drawee was dead. However, it believed that the legal implications in such cases were not very clear.

9. The immediate right of recourse laid down in article 50 gave rise to considerable problems of interpretation. It would be necessary to clarify whether the holder had an immediate right of recourse in the case of the drawee's death, as in cases of non-payment.

10. Mr. ANGELICI (Italy) said that he was substantially in agreement with the suggestion made at the previous meeting by the representative of France. An effort was needed to simplify the rules in question, especially by reducing the large number of cross-references in the text. It was also desirable to limit the situations in which presentment for acceptance was dispensed with because such cases were exceptional and broader provisions were bound to lead to practical difficulties. For example, it was not always easy to establish when a corporation had ceased to exist or whether a person did not have the capacity to incur liability on the instrument as an acceptor. In the case of a fictitious person, there was the additional problem of the burden of proving the non-existence of the person indicated on the instrument.

11. Mr. JOKO-SMART (Sierra Leone) pointed out that some legal systems made a distinction between a fictitious person and a non-existent person; the draft could be clearer on that point. In other respects, he was in favour of the present text.

12. Mr. SPANOGLI (United States of America) said that he was grateful for the Soviet Union representative's explanation of the reasons for the suggested amendment to articles 48 and 52. If he understood correctly, it related to those rare cases where a bill of exchange had been acceptable and then held out for an extensive period, creating concern about the delay. It was also necessary, however, to consider the case of an accepted bill that was payable at sight or upon demand. Any modification of the text would involve inserting a very condition-laden amendment. Thus, while he took note of the argument advanced by the representative of the Soviet Union, he nevertheless supported the present draft. In the case of a bill of exchange which was used as a financing document and would be outstanding for a significant period, the proper means of obtaining the result desired by the representative of the Soviet Union was, in his view, a clause providing for accelerated payment.

13. Mr. GUEST (United Kingdom) said that he had no strong feelings on the question of accelerated payment where the acceptor of the bill became bankrupt. The case could be regarded as a kind of anticipatory breach of the obligation of the acceptor, with the result that an immediate right of recourse would come into effect against the parties which were secondarily liable. On the other hand, it could be said the guarantors and endorsers had placed their names on the bill in the expectation that their liability would accrue, if at all, at a much later date.

14. With regard to article 48 (a), the representative of Italy had not made it clear what would happen if the drawee was a fictitious person or if a corporation had ceased to exist. Where, when and to whom could the bill be presented for acceptance? That problem, in his view, had been solved by the draft; an alternative might be possible, but some solution was definitely required.

15. The representative of Spain had drawn attention to the difference between article 48 (a), which referred specifically to the death of the drawee, and article 52 (2) (d), which did not. The Working Group had made a firm distinction between the two cases, feeling that, if the drawee died, there was no need to present the bill to his heirs for acceptance. In the case of presentment for payment, however, it was felt necessary and indeed proper to present the bill to those persons who succeeded to the estate. Views might differ on the two cases, but the distinction was deliberate and not accidental.

16. The CHAIRMAN said that, as he saw it, the various proposals to amend articles 48 and 52 concerned only certain

marginal aspects of the two articles and could be dealt with at a later drafting stage. The majority view was in favour of the present text.

17. He invited comments on article 58 (2) (d) of the draft Convention.

18. Mr. OLIVENCIA (Spain) said that his delegation had misgivings about the provision on dispensation of protest for dishonour in article 58. Specifically, it objected to paragraph 2 (d), which dispensed with protest for dishonour by non-acceptance or non-payment if presentment for acceptance or for payment was dispensed with. The scope of the provision was too broad and the reasons for the dispensation in so many cases were not clear. The mechanism for protest was supposed to provide security; however, the wide range of cases in which protest was dispensed with would increase the insecurity of liable persons. Thus, a question of principle was clearly involved. His delegation felt that there was no logical or necessary symmetry between the basis for waiver of presentment on the one hand and the dispensation of protest on the other. The question of protest should be subject to greater restriction in the draft.

19. Mr. ANGELICI (Italy) said that he fully endorsed the statement by the representative of Spain.

20. The CHAIRMAN noted that the majority of members were in favour of the present text of article 58.

21. *The meeting was suspended at 4.15 p.m. and resumed at 4.55 p.m.*

22. The CHAIRMAN drew the Commission's attention to paragraph 34 of document A/CN.9/249, which dealt with the concept of "ius tertii" as it applied to article 68 (3).

23. Mr. ROGNLIEN (observer for Norway) reiterated his Government's contention that the position of a party liable on the instrument might be rather delicate if a third party asserted a claim to it (A/CN.9/248, p. 112). The problem was in several countries dealt with by specific rules on discharge by paying the amount due into court or by other similar procedures. Norway suggested that article 68 (3) should refer to the national law of the place of payment regarding such arrangements.

24. Mr. SPANOGLE (United States of America) reiterated his Government's proposal that article 68 should be amended

to make an exception to discharge of the payor where the third party claimant both notified the payor of his claim and provided security deemed adequate by the payor before the instrument had been paid by the payor (A/CN.9/248, p. 113). That would protect a third party claimant and permit him to delay payment long enough to seek court resolution of competing claims.

25. Mr. PELICHET (observer, Hague Conference on Private International Law), referring to Norway's proposal, requested an exact definition of "place of payment".

26. Mr. CRAWFORD (observer for Canada) said that a person making payment ought not to be at risk if he had only partial information. He therefore supported the United States proposal. If court proceedings were not available under domestic law, a person could then show willingness to perform and have time to clarify any allegations against him.

27. Mr. OLIVENCIA (Spain) said that his delegation was not in favour of the existing text of article 68 (3) because it established a régime of insecurity for the payor. Purely subjective criteria might be used to determine whether the payor had knowledge at the time of payment that a third person had asserted a valid claim to the instrument. He therefore felt that either the Norwegian proposal or the United States proposal would improve the draft Convention.

28. Mr. VIS (observer for the Netherlands) said that his delegation supported the United States proposal but wished to have further clarification of its precise legal effects.

29. Mr. PAVLIK (Czechoslovakia) said that the United States proposal would solve a very difficult problem. However, he believed that it should be broadened to provide for settlement by a court in cases where the parties failed to reach agreement.

30. Mr. GUEST (United Kingdom) said that the United States proposal rested on the supposition that there would be a court that was prepared to take a decision on the matter and that that court would be in a country that was a party to the Convention. The question of conflict of laws again arose.

31. The CHAIRMAN said that while the Norwegian and the United States proposals had both received support, neither had been supported by a majority of members.

*The discussion covered in the summary record ended at 5.35 p.m.*

### Summary record of the 297th meeting Tuesday, 3 July 1984, 10 a.m.

[A/CN.9/SR.297]

*Chairman: Mr. SZASZ*

*The meeting was called to order at 10.20 a.m.*

1. The CHAIRMAN said that, in accordance with the decision taken at the previous meeting, the Commission would discuss the substantive aspects of articles 1 (2), 16, 46, 51 (h), 68 (4) and 69 (1). Proposed drafting changes would be considered by an appropriate working group to be set up for that purpose.

2. Mr. PISEK (Czechoslovakia) said that under article 1 (2) the drawer of a bill or the maker of a note enjoyed a

privileged position in making the initial choice to use an instrument subject to the Convention. There should be an express provision regulating the initial choice, particularly with regard to the consequences of that choice.

3. Mr. ROGNLIEN (observer for Norway) inquired whether the statement made by the representative of Czechoslovakia was a drafting point.

4. Mr. PELICHET (observer for the Hague Conference on Private International Law) said that under the current system, a drawer could determine the legal system governing bills of exchange and could draw a bill on a country which would not be a contracting party to the future Convention. It was very unlikely that such a bill would be accepted by businessmen or

bankers in international trade. That fact gave rise to serious doubts about the viability of the future Convention. He, therefore, proposed that the scope of article 1 should be limited by stipulating that bills of exchange could be drawn only on countries which were contracting parties.

5. Furthermore difficulties would also arise due to conflict of laws. For the countries of the Geneva system, autonomy of the parties was not possible. The draft Convention should be amended in order to take that into account. Granting autonomy to the parties was a double-edged sword. Both the drawer and subsequent parties could exercise autonomy. Under that system parties could choose a non-State legal régime, which could give rise to great difficulties in a number of areas such as arbitration. Under article 1 as currently worded, it was possible to draw a bill of exchange on a country which was not a contracting party. That could authorize the choice of a legal régime in a State which was not party to the future Convention. Stipulating that bills of exchange could be drawn only on countries which were contracting parties would not solve all problems but would limit the number of difficulties which would arise. In general it would be the country of the drawee or the place of payment where legal problems would occur. In view of the linkage between common law and the Geneva Convention, the legal régime of the country of the drawee or the place of payment would be the most suitable one for regulating the system under which a bill of exchange would be issued. The current text of article 1 would, in his opinion, doom the entire Convention to failure.

6. Mr. DUCHEK (Austria) said it was not clear whether the representative of Czechoslovakia was proposing a drafting change or a substantive amendment to article 1. He requested the representative of Czechoslovakia to clarify the intent of his proposal.

7. He did not support the view expressed by the observer for the Hague Conference that the scope of article 1 of the draft Convention should be limited in such a manner. The reasons put forward were not convincing. Restricting the application of the draft Convention would not promote the use of international bills of exchange and would seriously hamper the effectiveness of the future Convention. It was not clear how a new set of rules governing conflict of laws could be drafted on the basis of party autonomy. He did, however, support the view that something should be done to enable States parties to the Geneva Convention, which did not provide for autonomy of choice of the legal régime, to function under the draft Convention. A subsidiary instrument would have to be drawn up so that the two Conventions could coexist. He agreed with the view that changes would have to be made in the Geneva system in that regard. Lastly, it was doubtful whether it would be necessary to draw up rules governing conflict of laws on the basis of party autonomy. Further consideration should be given to that matter.

8. The CHAIRMAN said that on the basis of the comment made by the Government of Czechoslovakia on article 1 (2) (a) in document A/CN.9/248 it seemed that the proposal made by the representative of Czechoslovakia was primarily a drafting proposal.

9. Mr. ROGNLIEN (observer for Norway) said that, if the scope of the future Convention was not limited with regard to conflict of laws, the application of the Convention would vary according to different States and legal systems. If a dispute arose in a State which was not a party to the Convention, the application of the Convention would depend on the conflict

of laws rules in force in that country. The problem could not be solved by limiting the scope of the Convention to contracting parties. Autonomy of parties was of great importance in the field of bills of exchange. His delegation did not support the proposal to impose such an arbitrary limitation on the scope of the draft Convention.

10. Mr. PISEK (Czechoslovakia) proposed that the following sentence should be incorporated into the text of article 1: "Person other than the drawer or the maker are bound by the provisions of the Convention by virtue of their signature on the international instrument or by taking it up". That sentence was contained in paragraph 1 of the commentary on article 1 of the draft Convention in document A/CN.9/213. That was essentially a question of policy.

11. The CHAIRMAN said that he felt that the proposal made by the representative of Czechoslovakia was basically a drafting proposal, since that point was already covered in the current draft text.

12. Mr. SEVON (observer for Finland) said that his delegation did not disagree with the provision in the draft Convention which would allow the drawer to determine what legal system would govern his transaction. However, he cautioned that the drawer's action could have different effects, depending on the country in which his instrument was evaluated. The draft Convention dealt only with the interpretation that a court or other body in a contracting State might give to an instrument which fulfilled the requirement of article 1 (2). In a State which was not party to the Convention, however, the interpretation might be quite different. Nevertheless, the Commission should be prepared to accept that situation, since, if it was to limit the scope of the draft Convention, it would change the area in which difficulties arose but would not eliminate them.

13. He agreed with the representative of Austria that the Geneva system did not grant autonomy to the extent proposed in the draft Convention. The Geneva Convention itself must be amended to enable States parties to it to accede to the UNCITRAL Convention.

14. He did not think that the draft Convention could be reworded to solve the difficult problems relating to conflict of laws. Moreover, he did not think that the problems raised by the observer for the Hague Conference were serious enough to warrant amending articles 1 and 2.

15. Mr. SAMI (Iraq) agreed with the observer for the Hague Conference that the Convention must specify the legal régime to be used to settle cases of conflict of laws with regard to negotiable instruments. Since a drawer could not issue a negotiable instrument if he was not located in a State party to the Convention, he wondered how the Convention might be implemented when a bill was made payable to a State not a party to the Convention. To have an international bill of exchange, an international convention, established by the International Law Commission, was necessary. Thus, in cases of conflict, a judge could turn to domestic law to resolve a conflict of laws if necessary. It was also important to determine how States not parties to the Convention could accept a negotiable instrument issued in accordance with the Convention.

16. Mr. BRANDT (German Democratic Republic) said he agreed with the comments made by the representative of Czechoslovakia. His delegation also wished to be assured that the provision in question was intended to make the Convention applicable to all parties and that all relationships in a

transaction would be clearly identified in the original bill or note. That appeared to have been the intention of the Working Group, as indicated in document A/CN.9/213. However, the question of the application of the Convention might be solved by a rewording along the lines proposed by the representative of Czechoslovakia.

17. The question of conflict between conventions in force must, of course, be settled properly; however, the Commission should complete its drafting of the text of the Convention and take up the question of conflict at a later stage.

18. Mr. VIS (observer for the Netherlands) said that the observer for the Hague Conference had raised a number of important questions whose answers merited consideration. However, he did not believe that the Commission was the appropriate forum for dealing with those questions, which might be more appropriately discussed by The Hague Conference itself.

19. Mr. ROEHRICH (France) agreed with previous speakers that the draft Convention's scope of application should not be limited. He conceded that the problem might arise in which the courts in a non-contracting State were faced with a complaint in respect of a supposedly "international" bill of exchange which met the conditions of article 1 of the draft Convention; nevertheless, that was not sufficient reason for preventing the Convention from having as broad a scope of application as possible.

20. He agreed with the observer for the Netherlands that the question of possible problems for non-contracting States which the Convention's broad scope of application posed were not problems which should be addressed by the Commission. If problems relating to conflict of laws should arise, the Hague Conference should perhaps devise a new system for dealing with such problems and review the Geneva Convention.

21. Mr. SHU Xianli (China) said that his delegation thought it preferable to limit the application of the Convention to States parties. Thus, the places specified in article 1 (2) (e) should all be located within contracting States. If the holder of an instrument was to decide which legal régime would govern the transaction, problems might arise if the drawer did not come from a State party and refused to accept liability. On the other hand, if the drawer was from a Contracting State, he would be bound by the rules of the Convention in the event of a conflict of laws.

22. Mr. OLIVENCIA (Spain) said his delegation approved of the optional nature of the Convention. Nevertheless, he agreed with the representative of Czechoslovakia that the text of article 1 should be further clarified with regard to the optional nature of the Convention. While that point might be considered to be a drafting question, he felt that it was related to an important substantive issue.

23. He drew attention to the reference to article 1 contained in article 11 and noted that it would be desirable for article 1 to refer specifically to international bills of exchange which contained the words "international bill of exchange" at the time of issue. In that way, article 1 would state the essential prerequisites for the existence of an international bill of exchange. The issue of the international nature of a bill of exchange should not be confused with the prerequisites of that instrument's existence.

24. Once the optional nature of the Convention was clearly established, the Convention should make it possible for the bill of exchange to have the broadest possible scope of

application. However, it should be borne in mind that problems of international law, and particularly conflict of law, might arise. Commercial circles in his own country had pointed out that the consequences of the provisions of article 2 should be studied more thoroughly. He tended to agree with the remarks made by the observer for the Hague Conference on that subject, but agreed also with the observer for the Netherlands regarding the appropriate forum for such discussions. There was still ample time for a working group of the Commission to study problems intrinsically related to the text of the draft Convention in greater detail. At the same time, the Hague Conference might prepare a paper for consideration by the Commission, setting forth the legal problems which would arise if the current text was adopted. While he did not advocate a restriction of the régime contained in the draft Convention, he welcomed an opportunity for further consideration of the text, since more authoritative opinions were required in the matter.

25. The CHAIRMAN suggested that the Commission might accept the notion of a wide sphere of application of the Convention and be prepared to confront the problems of conflict of laws that were inherent in that approach. The Commission clearly could not investigate those problems in detail at present; perhaps, as several delegations had proposed, it should be dealt with in a more appropriate forum. However, one remaining problem was posed by the fact that the proposed UNCITRAL system, which was optional in nature, could not be used by States parties to the Geneva Convention, and that it would consequently be necessary to amend that Convention so that those States might participate in the newly established system.

*The meeting was suspended at 11.40 a.m. and resumed at 12.10 p.m.*

26. The CHAIRMAN invited the Commission to resume its considerations of article 1 of the draft Convention and to turn to the problems related to the inclusion in the text of an instrument of words invoking the Convention, namely, "international bill of exchange (Convention of . . .)" (article 1 (2) (a)), and "international promissory note (Convention of . . .)" (article 1 (3) (a)).

27. Mr. HERRMANN (International Trade Law Branch) said that, as could be seen from the written comments of Governments contained in document A/CN.9/248 regarding that point, certain members of the Commission had urged the use of a standard form for bills and notes under the Convention and others had argued that the words invoking the Convention should be made in some manner conspicuous on the instrument itself.

28. Mr. MAEDA (Japan) said that an international bill of exchange or promissory note governed by the Convention should be clearly distinguishable from other existing international instruments. Persons choosing to issue an instrument subject to the Convention should be required to use a universally standard form which could be attached to the Convention as an annex. Limiting the languages which might be used in the text of the bill or note might be another useful solution. If those ideas were judged to be impractical, it would be worth considering the requirement that the words invoking the Convention should be written in certain specified languages, such as English or the United Nations official languages, in addition to the original language.

29. Mr. SPANOGLE (United States of America) said that his delegation felt that a dual requirement would be useful: to have the words invoking the Convention written into the text to prevent falsification, but also to have those words appear in a conspicuous manner. Despite the complication involved,

other provisions of article 1—such as (2) (e) and (3) (e)—had also established more than a single requirement. Part of the problem in the point under discussion stemmed from the different conceptions under different legal systems of what constituted the body of the instrument, and that issue could be considered in a drafting group.

30. Mr. CHAFIK (Egypt) said that he felt all the proposals just made were good, and his delegation would add that the instrument should be drawn up on a special form fulfilling all those conditions but on paper of a particular colour.

31. Mr. VIS (observer for the Netherlands) said that he favoured requirements of conspicuousness and identification by colour but cautioned that such requirements might conceivably impede the circulation of instruments.

32. Mr. ROGNLIEN (observer for Norway) said that an authoritative standard form, such as one issued by the United Nations, should be used by the public. The question remained, however, whether that standard form should be made a requisite for the application of the Convention.

33. The CHAIRMAN suggested that the problem should be referred to an appropriate working group which would devise ways of making it clear, when appropriate, that the drawer's intention was to draw a bill under the régime of the Convention, without at the same time overly restricting the use of the words invoking the Convention.

34. *It was so decided.*

35. The CHAIRMAN observed that another outstanding problem in connection with article 1 (2) was the meaning of the term "written instrument".

36. Mr. SPANOGLE (United States of America) said that the suggestion contained in the comments by his Government in document A/CN.9/248 had been intended merely as a drafting suggestion regarding qualification of an instrument and not as a statement of a policy issue. An appropriate drafting group should consider the question and formulate the precise language.

37. *It was so decided.*

38. The CHAIRMAN invited the Commission to consider article 16 of the draft Convention and the relevant comments by Governments in document A/CN.9/248.

39. Mr. SPANOGLE (United States of America) said that there were two problems with article 16 as drafted. First, the article referred to two different transactions—restrictions put on an instrument by the drawer, and restrictions put on an instrument by the endorser—and then proceeded to treat them in the same manner. The two should instead be separated, and the second type of restriction belonged more properly, in the view of his delegation, in article 20 of the Convention. Secondly, as the Government of Denmark had also noted, there was the policy issue of whether provisions should be made for the issuance of a non-negotiable instrument under a convention on international negotiable instruments.

40. Mr. PAVLIK (Czechoslovakia) said that he agreed that two different kinds of endorsement were involved, one prohibiting further transfer of the instrument and the other making it an instrument for collection. He also agreed with the United States representative that there was a second policy issue involved, although in international trade, of course, the instruments in question were very rare.

41. Mr. CHAFIK (Egypt) said, with reference to the legal nature of the presumptions in article 16, that it should be specified that *vis-à-vis* the holder there was a *juris de jure* presumption, and *vis-à-vis* the relations between endorser and endorsee there was a *juris tantum* presumption.

42. Mr. OLIVENCIA (Spain) said that he agreed that article 16 treated two different questions, each with different legal consequences, in the same manner. The article should have made a distinction between the insertion of a non-negotiability clause by the drawer and its insertion by the endorser; but instead it stipulated only a single legal consequence—that the transferee did not become a holder except for purposes of collection—which was in itself not clearly expressed.

43. The "transferee" in question was presumably a subsequent transferee by virtue of a transfer transaction of the kind prohibited; but the term could be taken to mean the acceptor of the bill from the drawer, or the endorsee receiving it from the endorser.

44. The phrase "does not become a holder" was also equivocal and could be understood as contradicting the definition of holder in articles 6 and 14. His delegation took it to mean that if the drawer inserted one of the non-negotiability clauses mentioned, he would not be liable in respect of any subsequent transferee but would be liable in respect of the acceptor. If, on the other hand, an endorser inserted such a clause, he would not be liable in respect of a subsequent transferee, but that transferee would retain full rights against the drawer and any previous endorsers. The latter instance could just as easily be dealt with under article 20.

45. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that she agreed with the comments of previous speakers and especially with those of Spain regarding the ambiguity of article 16.

46. The sole purpose of article 16, an unusual one in relation to both the common-law and the civil-law systems, was to give the drawer (or maker), as well as the endorser, an opportunity to prohibit transfer of an instrument to any person other than the person to whom the instrument was made out. Thus, regardless of how often the instrument was circulated, the first transferee after the insertion of a non-transferability clause in the instrument was legally a genuine holder whose rights, however, were limited with regard to further transfers. Any subsequent transferee would be only a holder for collection.

47. The Working Group had decided to adopt such an unusual rule in article 16 because, under both the civil-law and the common-law systems, only the original signature of the drawer (or maker) could make an instrument non-negotiable. That was the effect, for instance, of articles 11 and 16 of the Geneva Uniform Law on Bills of Exchange and Promissory Notes, and the principle was incorporated as well into all national legislations. The Working Group had decided to depart from the established principle for practical purposes. In current banking practice, even when a creditor issued an instrument bearing a non-negotiability clause, a condition which was intended by the parties to restrict the instrument to one transfer, the instrument was under existing laws still freely negotiable. The Working Group was seeking, therefore, to extend the legal sphere of application in the draft Convention and to allow the parties to an instrument to

express their intentions. The Soviet Union agreed with the principle in article 16, although the article itself should be redrafted.

48. If no general agreement on article 16 was reached in the Commission, then there would be no point in dividing the article as suggested and switching the part regarding endorsements to article 20, because the restrictive endorsements under articles 16 and 20 differed. Under article 20, all transferees without exception were mere holders for collection and never genuine holders as could be the case under article 16.

49. The CHAIRMAN observed that all speakers had agreed that article 16 was unclear and that its treatment, in particular, of the legal consequences of its provisions was ambiguous. He suggested, therefore, that the text should be assigned for further drafting to a working group which would study the various options which the Commission had proposed.

50. *It was so decided.*

*The meeting rose at 12.50 p.m.*

### Summary record of the 298th meeting Tuesday, 3 July 1984, 3 p.m.

[A/CN.9/SR.298]

*Chairman: Mr. SZASZ*

*The meeting was called to order at 3.15 p.m.*

1. The CHAIRMAN invited the members of UNCITRAL to take up article 46 of the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/211) and drew attention to the comments reproduced in document A/CN.9/248.

2. Mr. SPANOGLE (United States of America) said that some of the comments raised problems with respect to the application of article 46, especially in situations where the holder wished to know the worth of the instrument before the due date. It might be better to delete the article altogether. If it was retained, then at least its scope should be restricted.

3. Mr. OLIVENCIA (Spain) said that while his delegation was inclined to endorse the provisions of article 46, it believed that their legal effects should be clarified. If a bill was presented for acceptance notwithstanding a stipulation permitted under article 46 (1) and acceptance was refused, then neither the drawer nor the holder should be liable for that non-acceptance. The text should be redrafted to provide clearly for all potentially liable persons to be freed from any liability that might result from dishonour by non-acceptance in such circumstances.

4. His delegation believed that while the drawer should be able to stipulate the date on which the instrument could be presented, he should not be able to state that it must not be presented before a specified event. The provision to that effect should be deleted.

5. Mr. CHAFIK (Egypt) said that he fully agreed with the representative of Spain. The solution might be to begin the article with the words "Notwithstanding the provisions of article 45 (1) . . .".

6. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) reaffirmed her Government's comments set forth on page 92 of document A/CN.9/248 and agreed with the statements made by the representatives of Spain and Egypt. The article should not be deleted altogether since its provisions were in keeping with current business practices. However, the provisions of paragraph (1) should be narrowed down to conform to article 45 (1).

7. Mr. SAMI (Iraq) said that he agreed with the representative of Spain and supported the Egyptian proposal.

8. Mr. GLATZ (Hungary) reaffirmed his Government's comments reproduced on page 91 of document A/CN.9/248.

9. The CHAIRMAN said that the matter had not been thoroughly discussed because only a few delegations had spoken. The general feeling seemed to be that the scope of article 46 should be restricted and that the legal effects of its application should be brought out.

10. He invited the Commission to turn its attention to article 51 (h) of the draft Convention.

11. Mr. GUEST (United Kingdom) said that his Government supported the inclusion of article 51 (h); its comments reproduced on page 101 of document A/CN.9/248 related only to the drafting of the article.

12. Mr. CRAWFORD (observer for Canada) said that his Government too supported the inclusion of article 51 (h), subject to the reservation that the instruments in question should be presented only in accordance with the rules of local clearing-houses because international instruments should be on the same footing as local instruments.

13. Mr. ROEHRICH (France) said that he was somewhat puzzled by what the observer for Canada had just stated, which would mean that the provision in the article would be void if a local clearing-house ruled that international bills could not be presented for payment. He wondered whether the provision in article 51 (h) was really necessary. Even if it were not in the Convention, the international community could take the position that bills could be presented at local clearing-houses for payment. Negative provisions or restrictive clauses should not be in the Convention because that would only cause problems.

14. Mr. CRAWFORD (observer for Canada) said that without the provision he had suggested, he rather doubted that international instruments could be presented at clearing-houses, certainly not in Canada. He would welcome the provision set forth in article 51 (h) provided that the affairs of the clearing-house were not disrupted. International bills presented at a clearing-house not organized to deal with them could disrupt local practices and result in disappointment for the holder.

15. Mr. SPANOGLE (United States of America) said that Canada's proposal on conditions under which clearing-houses should be used was acceptable to his delegation, which strongly supported the retention of article 51 (h). However, the word "may" in the paragraph would in United States courts be interpreted to mean that there were restrictions on the use of clearing-houses.

16. Mr. VIS (observer for the Netherlands) said that he supported the inclusion of article 51 (h) because it was a familiar provision that was included in the Geneva Uniform Law. He could accept the point made by the Observer for Canada on the understanding that if payment was refused at a clearing-house, then a protest should be made elsewhere, not at the clearing-house.

17. Mr. BARRERA GRAF (Mexico) said that he supported the Canadian proposal. In Mexico, which followed the Geneva system, a clearing-house was used only for cheques, not promissory notes and international bills of exchange. He therefore believed that paragraph (h) should be supplemented by a provision that bills of exchange and promissory notes should not be presented at local clearing-houses when those establishments did not permit presentation of such instruments.

18. The CHAIRMAN said it appeared that drafting changes were needed to clarify the provisions of article 51 (h) that could be left to an appropriate working group.

19. He invited the members of UNCITRAL to consider article 68 (4).

20. Mr. PISEK (Czechoslovakia) said that his Government had made the suggestion set forth on page 113 of document A/CN.9/248 with a view to simplifying the wording of article 68 (4) (a).

21. Mr. SAMI (Iraq), supported by Mr. SHU Xianli (China), said that there was no need to provide for the delivery of the protest to the drawee.

22. Mr. OLIVENCIA (Spain) said that his delegation was in favour of the current wording of paragraph (4) (a). The only doubts it had were related to its reservations concerning article 6 (b). It should be indicated in article 68 (4) that payment at maturity must be recorded on the instrument.

23. Mr. BARRERA GRAF (Mexico) said that his delegation was in favour of the current wording of paragraph (4). With reference to the statement made by the representative of Spain, Mexico believed that the draft Convention should indicate that instalment payments must be recorded on the instrument.

24. The CHAIRMAN said that most delegations appeared to be in favour of the current text of paragraph (4). It was clear that the relevant working group should consider the matter in the light of articles 6 (b) and 69 (1).

*The meeting was suspended at 4.15 p.m. and resumed at 4.50 p.m.*

25. The CHAIRMAN invited the members of UNCITRAL to consider article 69 (1) in the light of the comments reproduced in document A/CN.9/248.

26. Mr. CHAFIK (Egypt), supported by Mr. ANKELE (Federal Republic of Germany), Mr. SEVON (observer for Finland) and Mr. SAMI (Iraq), said that the right accorded to

the holder in article 69 (1) was unwarranted. Paragraph (1) should state that it was obligatory for the holder to accept partial payment, and the remainder of article 69 should be redrafted accordingly. If that proposal was not adopted, then it should be stated in the article that, in cases where partial payment was refused, the party who had signed the instrument should be freed from the obligation to pay the sum offered.

27. Mr. SHU Xianli (China) said that his delegation was in favour of the current wording of paragraph (1).

28. Mr. GUEST (United Kingdom) said that he had no strong views on the matter. However, since partial payment was seldom offered unconditionally, he had a slight preference for the current formulation.

29. The CHAIRMAN suggested that it would be preferable to defer a decision on article 69 (1) pending consideration of how the matter might be dealt with by a working group.

*Future course of action with regard to the draft Convention on International Bills of Exchange and International Promissory Notes*

30. Mr. SONO (Secretary of the Commission) said that the Commission might wish to consider establishing a working group composed of all its members to review the draft Convention as a whole, including points which had not been discussed by the Commission at its seventeenth session. In order to expedite its work, the Commission might also wish to consider dispensing with a full-scale re-examination of the revised draft.

31. After a procedural discussion in which a number of delegations took part, the CHAIRMAN said that the Commission would resume its deliberations at the following meeting with a view to deciding what further consideration should be given to the draft Convention, in what kind of body the text should be considered, and what should be the size and composition of the body in question. One suggestion was that the Working Group on International Negotiable Instruments should remain in existence, should be expanded to include non-members of the Commission wishing to participate in its deliberations, and should be entrusted with consideration of the draft, together with the Commission's proposals and comments from Governments. On the other hand, it had been argued that the next course of action should be to convene a conference of plenipotentiaries. However, the majority view appeared to be that it would be premature to take a decision on the future of the draft when completed, before a revised text had been prepared and submitted to Governments for consideration. It had been suggested that the revision could be done, if not by the aforementioned Working Group, then by a committee of the whole.

32. He understood the feeling of the Commission to be that the draft Convention should be referred to a working group composed of all members of the Commission, with the instruction that it should be guided by the decisions of the Commission. The working hypothesis should be that the working group would supply the Commission with a text which would not necessitate a detailed re-examination.

*The meeting rose at 6.10 p.m.*

**Summary record of the 299th meeting  
Thursday, 5 July 1984, 10 a.m.**

[A/CN.9/SR.299]

*Chairman: Mr. SZASZ*

*The meeting was called to order at 10.20 a.m.*

*Future course of action with regard to the draft Convention on  
International Bills of Exchange and International Promissory  
Notes (continued)*

1. The CHAIRMAN said that most delegations appeared to favour the establishment of a working group composed of all members of UNCITRAL to review the draft Convention, since that would obviate the need to repeat a paragraph-by-paragraph discussion at future UNCITRAL sessions. The terms of reference of such a working group would be to work at a reasonably fast pace to finalize the text in the light of the Commission's discussions and policy decisions. The working group would hold a session in 1985 and make a progress report to UNCITRAL at its eighteenth session.

2. After a procedural discussion in which a number of delegations took part, he said it seemed that many delegations would be unable to participate in the work of a working group of the whole. Most members of the Commission believed that the Working Group on International Negotiable Instruments should be expanded with the addition of four or five members to ensure a proper geographical balance and the representation of all legal systems. It was his intention to suspend the meeting and consult with all interested delegations concerning the expansion of the Working Group.

*The meeting was suspended at 11.40 a.m. and resumed at 12.15 p.m.*

3. The CHAIRMAN said that the consultations were still in progress. The Commission would return to the question at a later date and conclude its consideration of agenda item 4.

*The discussion covered in the summary record ended at 12.20 p.m.*

**Summary record of the 301st meeting  
Friday, 6 July 1984, at 10 a.m.**

[A/CN.9/SR.301]

*Chairman: Mr. SZASZ*

*The meeting was called to order at 10.20 a.m.*

...  
4. The CHAIRMAN reported on his consultations with the members of the Commission regarding the composition of an expanded Working Group on International Negotiable Instruments, which was to revise the text of the draft Convention on International Bills of Exchange and International Promissory

Notes in the light of the discussions and decisions of the Commission.

5. Mexico would be replacing Chile on the Working Group, which would be expanded by six members. He would take it, if he heard no objection, that the Commission wished to appoint Australia, Cuba, Czechoslovakia, Japan, Sierra Leone and Spain as the six additional members.

6. *It was so decided.*

*The discussion covered in the summary record ended at 10.30 a.m.*

## II. BIBLIOGRAPHY OF RECENT WRITINGS RELATED TO THE WORK OF UNCITRAL

### 1. General

Berman, H. The law of international commercial transactions (Lex Mercatoria). A lawyer's guide to international business transactions, part III. W. Surrey and D. Wallace, eds. Philadelphia, American Law Institute, 1983, p. 42-49.

Die XVI. Tagung der UNCITRAL. *Recht im Aussenhandel* (Berlin) 66:I-IV, 1983. (Supplement of *DDR-Aussenwirtschaft*, 37, 7 September 1983)

Die XVII. Tagung der UNCITRAL. *Recht im Aussenhandel* (Berlin) 72:I-V, 1984. (Supplement of *DDR-Aussenwirtschaft*, 36, 5 September 1984)

Kikuchi, Y. The 17th session of UNCITRAL. *Kokusai shoji homu* (Tokyo) 12:10:715-720, 1984.  
In Japanese.

Schmitthoff, C.M. The codification of the law of international trade. *Journal of business law* (London) 34-44, January 1985.

Sono, K. The work programme of UNCITRAL. In Proceedings of the First International Trade Law Seminar—1983. Ottawa, Department of Justice, 1983, p. 5-12.

### 2. International sale of goods

Bainbridge, S. Trade usages in international sales of goods: an analysis of the 1964 and 1980 sales conventions. *Virginia journal of international law* (Charlottesville) 24:3:619-665, spring 1984.

Barbić, J. Uniform law on the international sale of goods, uniform law on the formation of contracts for the international sale of goods (1964) and United Nations Convention on Contracts for the International Sale of Goods (1980). In Hague-Zagreb essays 4 on the law of international trade. C.C.A. Voskuil and J.A. Wade, eds. The Hague, Nijhoff, 1983, p. 3-21.

Barrera Graf, J. Convención de las Naciones Unidas sobre los contratos de compraventa internacional de mercaderías. *Boletín Mexicano de derecho comparado* (México, D.F.) 16:48:889-925, septiembre-diciembre 1983.  
Spanish text of Convention, p. 893-925.

— The Vienna Convention on International Sales Contracts and Mexican law: a comparative study. *Arizona journal of international and comparative law*, 1:1:122-156, 1982.

Birenbaum, D. F. and M. T. Marley. Drafting contracts after the UN Convention. The UN Convention on international sales of goods presents problems for common law jurisdictions, which can be avoided by proper drafting. *International financial law review* (London) 3:5:17-19, May 1984.

Cain, G. H. The Vienna Convention: posing a new international law of sales. *Connecticut bar journal* (Hartford) 57:4:327-340, August 1983.

Coelho Bento Soáres, M. A. B. and R. M. Moura Ramos. Les moyens dont dispose l'acheteur en cas de contravention au contrat (autre que le défaut de conformité) d'après la convention de Vienne de 1980 sur la vente internationale de marchandises. *Documentação e direito comparado* (Coimbra) 11:243-261, 1982.

— Os meios à disposição do comprador, no caso de violação do contrato pelo vendedor, na convenção de Viena de 1980 sobre os contratos de compra e venda internacional de mercadorias. *Revista de direito e economia* (Coimbra) 8:83-109, 1982.

Doratt, P. (comp.) Das UNCITRAL-Kaufrecht im Vergleich zum österreichischen Recht. Wien, Manz, 1985, 198 p. (Schriftenreihe: Recht—Wirtschaft—Aussenhandel, v. 1). “Übereinkommen der Vereinten Nationen über Verträge über den internationalen Warenkauf”, pocket inside back cover.

Enderlein, F., D. Maskow and M. Stargardt. Kommentar. Konvention der Vereinten Nationen über Verträge über den internationalen Warenkauf. Konvention über die Verjährung beim internationalen Warenkauf. Protokoll zur Änderung der Konvention über die Verjährung beim internationalen Warenkauf. Berlin, Staatsverlag der DDR, 1985.

Enderlein, F. and M. Stargardt. Zur Anwendung des UN-Kaufrechts auf Aussenhandelskauf- und -lieferverträge und sein Verhältnis zum GIW. *Recht im Aussenhandel* (Berlin) 75:VI-XII, 1985. (Supplement of *DDR-Aussenwirtschaft*, 7, 13 February 1985).

Farnsworth, E. A. Unification of sales law: usage and course of dealing. In Unification and comparative law in theory and practice. Contributions in honour of J. G. Sauveplane. Deventer, Kluwer, 1984, p. 81-89.

Galston, N. and H. Smit (eds.). International sales: The United Nations Convention on Contracts for the International Sale of Goods. Proceedings from the 1983 conference held by the Parker School of Foreign and Comparative Law, Columbia University. New York, Bender, 1984

González, O. M. Remedies under the U.N. Convention for the International Sale of Goods. *International tax and business lawyer* (Berkeley) 2:1:79-100, winter 1984.

Goodfriend, D. E. After the damage is done: risk of loss under the United Nations Convention on Contracts for the International Sale of Goods. *Columbia journal of trans-national law* (New York) 22:3:575-606, 1984.

Hellner, J. Consequential loss and exemption clauses. *Oxford journal of legal studies* (Oxford) 1:13-49, 1981.

— UN-konventionen om internationella köp och den nordiska köprätten. *Tidsskrift för rättsvitenskap* (Oslo) 96:5:449-468, 1983.

- Herber, R. Die Abweichungen des UNCITRAL-Kaufrechts gegenüber dem geltenden Recht. *Rechtsinformation* (Köln) 179:4-20, Mai 1984.
- Honnold, J. O. On the road to unification of the law of sales. Deventer, Kluwer law and taxation publications, 1983. 31 p. (Forum international, No. 2). Text of Vienna Sales Convention in English, p. 15-31.
- \_\_\_\_\_. The state of the law of contracts for the international sale of goods. In Proceedings of the First International Trade Law Seminar—1983. Ottawa, Department of Justice, 1983. p. 13-26.
- \_\_\_\_\_. Uniform law for international sales under the 1980 United Nations Convention. Deventer, Kluwer, 1982. 586 p. (Reviewed by I. I. Kavass. *Vanderbilt journal of transnational law* (Nashville) 17:2:549-556, spring 1984.)
- Loewe, R. Das Wiener Welt-Kaufrecht ist im Kommen. *Österreichisches Recht der Wirtschaft* (Wien) 5:130-137, 1984.
- Memmo, D. La "sede di affari" secondo la disciplina uniforme sulla vendita internazionale nella più recente giurisprudenza della Corte federale tedesca. *Rivista trimestrale di diritto e procedura civile* (Milano) 37:755-761, 1983.
- Moecke, H.-J. Das UNCITRAL-Übereinkommen über Warenkauf und die Allgemeinen Geschäftsbedingungen—doch etwas mehr als nichts? *Recht der Internationalen Wirtschaft/Aussenwirtschaftsdienst des Betriebs-Beraters* (Heidelberg) 30:9:678-679, 1984.
- Neumann, G. W. Zur Anpassung der Vertragsbedingungen an das neue Recht; Anwendung oder Abbedingung des UNCITRAL-Kaufrechts. *Rechtsinformation* (Köln) 38:53, Mai 1984.
- Olivencia, M. Derechos y obligaciones del vendedor y transmisión de riesgos en la convención. Ponencia al coloquio internacional de derecho mercantil: la Convención de las Naciones Unidas sobre la Compraventa Internacional de mercaderías. Instituto de Investigaciones Jurídicas, Universidad Nacional Autónoma de México, julio 1981. Anuario jurídico (México, D.F.) 10:73-95, 1983.
- Richards, B. J. Contracts for the international sale of goods: applicability of the United Nations convention. *Iowa law review* (Iowa City) 69:209-240, 1983.
- Rohwer, C. D. and J. J. Coe, Jr. The 1980 Vienna Convention on the International Sale of Goods and the UCC—Peaceful coexistence? In Legal aspects of international business transactions. Amsterdam, North-Holland, 1984.
- Rosett, A. Critical reflections on the United Nations Convention on Contracts for the International Sale of Goods. *Ohio State law journal* (Columbus) 45:2:265-305, 1984.
- \_\_\_\_\_. The International Sales Convention: a dissenting view. *International lawyer* (Chicago) 18:2:445-449, 1984.
- Samson, C. The Vienna Convention from the point of view of the civil law of Quebec. In Proceedings of the First International Trade Law Seminar—1983. Ottawa, Department of Justice, 1983. p. 32-44.
- Schlechtriem, P. Recent developments in international sales law. *Israel law review* (Jerusalem) 18:3-4:309-326, 1983.
- Schlieffen, A. v. Besondere Fragen: Verspätungshaftung, Gefahrübergang, Vertragsstrafe, höhere Gewalt. *Rechtsinformation* (Köln) 179:21-37, Mai 1984.
- Stumpf, H. Das UNCITRAL Übereinkommen über den Warenkauf und Allgemeine Geschäftsbedingungen — viel Lärm um nichts? *Recht der Internationalen Wirtschaft/Aussenwirtschaftsdienst des Betriebs-Beraters* (Heidelberg) 30:5:352-353, 1984.
- Unification and certainty: the United Nations Convention on Contracts for the International Sale of Goods. *Harvard law review* (Cambridge) 97:8:1984-2000, 1984.
- U.S.A. Hearing before the Committee on Foreign Relations, United States Senate, ninety-eighth congress, second session on treaty document 98-9: Proposed United Nations Convention on Contracts for the International Sale of Goods. Washington, Government Printing Office, 1984. 82 p.
- Van der Velden, F. J. A. The law of international sales: The Hague Conventions 1964 and the UNCITRAL Uniform Sales Code 1980—some main items compared. In *Hague-Zagreb essays 4* on the law of international trade. C.C.A. Voskuil and J.A. Wade (eds.). The Hague, Nijhoff, 1983. p. 46-106.
- \_\_\_\_\_. Uniform international sales law and the battle of forms. In *Unification and comparative law in theory and practice. Contributions in honour of J. G. Sauveplane*. Deventer, Kluwer, 1984, p. 233-249.
- Völter, J. and H. Wagner. Einheitliches Recht für internationale Kaufverträge. *Wirtschaftsrecht* (Berlin) 3:141-144, 1980.
- Wey, M. Der Vertragsschluss beim internationalen Warenkauf nach UNCITRAL- und schweizerischem Recht. Mit Einschluss der Anwendungs- und allgemeinen Bestimmungen des Übereinkommens der Vereinten Nationen über Verträge über den internationalen Warenkauf. 562 p. 2v. Inaugural dissertation. Hohe Juristische Fakultät der Universität Basel, 1984.
- Winship, P. International sales contracts under the 1980 Vienna Convention. *Uniform commercial code law journal* (Boston) 17:1:55-71, 1984.
- Ziegel, J. S. A Canadian viewpoint on the Vienna International Sales Convention. In Proceedings of the First International Trade Law Seminar—1983. Ottawa, Department of Justice, 1983. p. 26-32.
- \_\_\_\_\_. Should Canada adopt the International Sales Convention? New developments in the law of export sales/Les tendances actuelles dans le droit des ventes à l'exportation. Don Mills, Ontario, R. De Boo, 1983. p. 67-85. (Meredith memorial lectures, Faculty of Law, McGill University, 1982)
- Ziontz, M. L. The new uniform law for the international sale of goods: is it compatible with American interests? *Northwestern journal of international law and business* (Chicago) 2:1:129-178, spring 1980.
- Zur Vertragsgestaltung im Auslandsgeschäft nach UNCITRAL-Kaufrecht. *Rechtsinformation* (Köln) 179:1-53, Mai 1984.

### 3. International commercial arbitration and conciliation

- Aksen, G. The need to utilize international arbitration. *Vanderbilt journal of transnational law* (Nashville) 17:1:11-17, 1984.
- Aoyama, Y. On UNCITRAL model arbitration law. *JCA Journal* (Tokyo) 12-20, May 1984; 12-20, June 1984. In Japanese.

- Böckstiegel, K.-H. The relevance of national arbitration law for arbitrations under the UNCITRAL Rules. *Journal of international arbitration* (Geneva) 1:3:223-236, 1984.
- Das UNCITRAL-Modell-Gesetz für die internationale Wirtschafts-Schiedsgerichtsbarkeit. *Recht der Internationalen Wirtschaft/Aussenwirtschaftsdienst des Betriebs-Beraters* (Heidelberg) 30:9:670-678, 1984.
- Branson, D. J. and W. M. Tupman. Selecting an arbitral forum: a guide to cost-effective international arbitration. *Virginia journal of international law* (Charlottesville) 24:4:917-938, 1984.
- Broches, A. A model law on international commercial arbitration? A progress report on the work undertaken within the U.N. Commission on International Trade Law (UNCITRAL). *George Washington journal of international law and economics* (Washington, D.C.) 18:1:79-95, 1984.
- Congrès ICCA de Lausanne. *Bulletin* (Bâle, Association suisse de l'arbitrage) 2:3:137-146, 1984.
- Convegno dell'ICCA sul progetto di legge modello dell'UNCITRAL sull'arbitrato commerciale internazionale, Losanna, 9-12 maggio 1984. *Rassegna dell'arbitrato* (Roma) 24:1-2:1-57, 1984.
- Dahl, E. and A. M. Garro. Cuba's system of international commercial arbitration: a convergence of Soviet and Latin American trends. *Lawyer of the Americas* (Coral Gables) 15:3:441-466, winter 1984.
- De Vries, H. P. International commercial arbitration: a contractual substitute for national courts. *Tulane law review* (New Orleans) 57:42-79, 1982.
- International commercial arbitration: a transnational view. *Journal of international arbitration* (Geneva) 1:1:7-20, April 1984.
- Facilities for international commercial arbitration. *ICA arbitration quarterly* (New Delhi) 18:4:12-15, January-March 1984.
- Fleischhauer, C. A. UNCITRAL and international commercial dispute settlement. *Arbitration journal* (New York) 38:4:9-13, 1983.
- Glossner, O. Genèse d'une loi-modèle. *Revue de l'arbitrage* (Paris) 2:248-250, 1983.
- Das UNCITRAL-Modellgesetz als Gesetzesmodell für die internationale Schiedsgerichtsbarkeit. *Recht der Internationalen Wirtschaft/Aussenwirtschaftsdienst des Betriebs-Beraters* (Heidelberg) 29:2:120, 1983.
- Healy, N. J. Arbitration (Il seminario di Buenos Aires sulle Regole di Amburgo). *Diritto marittimo* (Genova) 85:742, 1983.
- Hermann, A. H. The International Arbitration Congress in Lausanne: doubts over the UNCITRAL model law. *Business law brief*, 3-4 May 1984. (Supplement of Financial Times)
- Herrmann, G. Die UNCITRAL-Vergleichsordnung. *Zeitschrift für Zivilprozess* (Köln) 97:4:445-470, 1984.
- The UNCITRAL Conciliation Rules: an aid also in contract adaptation (and performance facilitation). In *Adaptation and renegotiation of contracts in international trade and finance*. Norbert Horn ed. Deventer, Kluwer, 1985. p. 217-234.
- UNCITRAL's work towards a model law on international commercial arbitration. *Pace law review* (New York) 4:3:537-580, spring 1984.
- UNCITRAL's work towards a model law on international commercial arbitration. In Report and other documents of the Regional Seminar on International Commercial Arbitration, New Delhi-1984. New Delhi, Secretariat of AALCC, 1984. p. 75-104.
- Hoellering, M. F. UNCITRAL model law: commercial arbitration. *New York law journal* (Middletown) 12 January 1984.
- Hoffman, J. E., Jr. The Iranian asset negotiations. *Vanderbilt journal of transnational law* (Nashville) 17:1:47-57, 1984.
- Hunter, J. M. H. International commercial arbitration: the UNCITRAL model law. *International business lawyer* (London) 189-192, April 1984.
- Proposed model law on international commercial arbitration. *Arbitration* (London) 49:13:247-251 and 263, February 1984.
- Ingriselli, F. C. International dispute resolution and the People's Republic of China. *International business lawyer* (London) 376-380, October 1984.
- Jarvin, S. Beilegung internationaler Handelsstreitigkeiten. *Recht der Internationalen Wirtschaft/Aussenwirtschaftsdienst des Betriebs-Beraters* (Heidelberg) 30:7:512-516, July 1984.
- Kerr, M. Arbitration and the courts — The UNCITRAL model law (The Alexander lecture). *Arbitration* (London) 50:1:3-16, August 1984. (Slightly revised version published in *International and comparative law quarterly* (London) 34:1:1-24, January 1985.)  
Text of draft model law, p. 19-24.
- Lew, J. D. M. The unification of the law on international commercial arbitration. *Business law review* (Morgantown) 5:6:145-147, June 1984.
- McDonell, N. E. The availability of provisional relief in international commercial arbitration. *Columbia journal of transnational law* (New York) 22:2:273-302, 1984.
- Rhodes, J. M. and L. Sloan. The pitfalls of international commercial arbitration. *Vanderbilt journal of transnational law* (Nashville) 17:1:19-45, 1984.
- Rubino-Sammartano, M. A civil law approach to the UNCITRAL model law and to arbitral rules of evidence. *Arbitration* (London) 51:1:278-282, February 1985.
- Sanders, P. Harmonization of arbitration laws — a model law? In *Festschrift für Arthur Bülow zum 80. Geburtstag*. Köln, Heymanns, 1981. p. 185-187.
- Sanders, P. (ed.) UNCITRAL Arbitration Rules. Survey of model clauses as recommended by arbitral institutions for services under these rules. In *Yearbook of commercial arbitrations*, v. IX. Deventer, Kluwer, 1984. p. 174-177.
- UNCITRAL's project for a model law on international commercial arbitration. Proceedings of the International Council for Commercial Arbitration interim meeting, May 9-12, 1984 in Lausanne, Switzerland. Deventer, Kluwer, 1984. 267 p.
- Schneider, M. E. The ICCA Interim Meeting in Lausanne on the UNCITRAL model law, 9-12 May 1984. *Arbitration* (London) 51:1:248-251, February 1985.
- Secretariat of the Japan Commercial Arbitration Association. The UNCITRAL draft model arbitration. *JCA journal* (Tokyo) 2-11, November 1984.  
In Japanese.

- Selby, J. M. and D. P. Stewart. Practical aspects of arbitration claims before the Iran-United States claims tribunal. *International lawyer* (Chicago) 18:2:211-244, spring 1984.
- Shilston, A. International Symposium on UNCITRAL model law for international commercial arbitration. *Arbitration* (London) 49:3:240-246, February 1984.
- \_\_\_\_\_. Revolution or evolution? *Arbitration* (London) 49:1:1-2, August 1983.
- \_\_\_\_\_. Report on the two-day Symposium of London International Commercial Arbitration. *Arbitration* (London) 49:1:3-8, August 1983.
- \_\_\_\_\_. UNCITRAL model law—the challenge ahead. Report on symposium. *Arbitration* (London) 51:1:252-259, February 1985.
- Sono, K. UNCITRAL and international commercial dispute settlement with particular emphasis on UNCITRAL Arbitration Rules. In Report and other documents of the Regional Seminar on International Commercial Arbitration—1984. New Delhi, Secretariat of AALCC, 1984. p. 55-63.
- Strohbach, H. Force majeure and hardship clauses in international commercial contracts and arbitration. The East-German approach. *Journal of international arbitration* (Geneva) 1:1:39-51, April 1984.
- Taki, H. International transaction and amicable arbitration. *JCA journal* (Tokyo) 22-28, January 1984. In Japanese.
- The Chartered Institute Annual Conference 1984, Guernsey, Channel Islands, 10-14 October 1984. Chairman's report and papers. *Arbitration* (London) 51:1:260-277, February 1985.
- UNCITRAL's model law on international commercial arbitration. In Asian-African Legal Consultative Committee. Working papers for the Trade Law Sub-Committee, v.1. New Delhi, Secretariat of AALCC, 1984. Text of draft model law, p. 15-30.
- UNCITRAL-Vergleichsordnung 1980. *Recht im Aussenhandel* (Berlin) 60:1-5, 1982. (Supplement of *DDR-Aussenwirtschaft*, 33, 11 August 1982)
- #### 4. International legislation on shipping
- Astle, W.E. The Hamburg Rules. London, Fairplay, 1981. 163 p.
- Birch-Reynardson, W. R. A. et al. The maritime carrier's liability under the Hamburg Rules. In *Recht über See: Festschrift Rolf Stöder zum 70. Geburtstag am 22. April 1979*. Hamburg, Decker, 1979. p. 3-26.
- Birch-Reynardson, W. R. A. Notice of loss or damage or delay (Il seminario di Buenos Aires sulle Regole di Amburgo). *Diritto marittimo* (Genova) 85:735-738, 1983.
- Canada. Marine Administration. International rules for the carriage of goods by sea. Discussion paper. Ottawa, Transport Canada, December 1984. 24 p. Published also in French.
- Chandler, G. F., III. A comparison of "COGSA", the Hague/Visby Rules, and the Hamburg Rules. *Journal of maritime law and commerce* (Cincinnati, Ohio) 15:2:233-291, April 1984.
- Hague-Visby-Hamburg Rules. Units. *Gerichtsentscheidung*, Bundesgerichtshof, 19. September 1983. *European transport law* (Antwerp) 19:1:27-34, 1984.
- Herber, R. Gedanken zur internationalen Vereinheitlichung des Seehandelsrechts. In *Recht über See: Festschrift Rolf Stöder zum 70. Geburtstag am 22. April 1979*. Hamburg, Decker, 1979. p. 55-77.
- Kindred, H. M. From Hague to Hamburg: international regulation of the carriage of goods by sea. *Dalhousie law journal* (Halifax) 7:3:585-619, October 1983.
- Maher, J. A. and J. D. Maher. Marine transport, cargo risks, and the Hamburg Rules—rationalization or imagery? *Dickinson law review* (Carlisle) 84:2:183-220, 1980.
- Necker, K.-H. Zur Statutenkollision im Seefrachtrecht. Von den Haager zu den Hamburger Regeln. In *Recht über See: Festschrift Rolf Stöder zum 70. Geburtstag am 22. April 1979*. Hamburg, Decker, 1979. p. 89-100.
- O'Hare, C. W. Cargo dispute resolution and the Hamburg Rules. *International and comparative law quarterly* (London) 29:219-237, 1980.
- Okuda, Y. Zur Anwendungsnorm der Haager, Visby und Hamburg Regeln. Vortrag gehalten vor dem Deutschen Verein für internationales Seerecht am 16. September 1982. Hamburg, Deutscher Verein für internationales Seerecht, 1983. 23 p.
- Ray, J. D. La Conferencia y las Reglas de Hamburgo de 1978. *La ley* (Buenos Aires) 1979-A:667-677.
- Richter-Hannes, D. Die Hamburger Regeln 1978—Neuregelung über die Güterbeförderung zur See. Berlin, Transpress VEB Verlag für Verkehrswesen, 1982. 160 p. Text of Hamburg Rules in German p.142-160.
- \_\_\_\_\_. UNO-Konventionen zum internationalen Transport und die Mitgliedschaft der DDR. *DDR Verkehr* (Berlin) 16:344-347, 1983.
- Yancey, B. W. The carriage of goods: Hague, COGSA, Visby and Hamburg. *Tulane law review* (New Orleans) 57:1238-1259, 1982/83.
- #### 5. International payments
- Crawford, B. The draft Conventions on International Bills of Exchange and Promissory Notes and on International Cheques. In *Proceedings of the First International Trade Law Seminar—1983*. Ottawa, Department of Justice, 1983. p. 55-62.
- \_\_\_\_\_. The UNCITRAL draft guide on electronic funds transfer systems. In *Proceedings of the First International Trade Law Seminar—1983*. Ottawa, Department of Justice, 1983. p. 62-69.
- Draft Convention on International Bills of Exchange and International Promissory Notes. In Asian-African Legal Consultative Committee. Working papers for the Trade Law Sub-Committee, v. 1. New Delhi, Secretariat of AALCC, 1984. p. 31-89. Text of draft convention p. 55-89.
- Hafke, H. C. UNCITRAL-Wechsel und UNCITRAL-Scheck. *Zeitschrift für das gesamte Kreditwesen* (Frankfurt am Main): 298, 300-301, 1984.
- Kikuchi, Y. International negotiable instrument project and UNCITRAL 17th session. *Kinyu homu jijyo* (Tokyo) 1070, October 1984. In Japanese.

Sono, K. UNCITRAL project on electronic funds transfer. *Ginko jitsumu* (Tokyo) 14:7:44-47, 1984.  
In Japanese.

#### 6. New international economic order

Basnayake, S. The work of UNCITRAL in the field of industrial contracts. *International construction law review* (London) 1:3:273-276, April 1984.

Böckstiegel, K.-H. (ed.). *Vertragsgestaltung und Streit-erledigung in der Bauindustrie und im Anlagenbau. Contracts and dispute settlement in civil engineering and construction of plants.* Köln, Heymans, 1984. 348 p.

Hunter, J. M. H. UNCITRAL and construction industry arbitration. *International construction law review* (London) 2:2:165-176, January 1985.

Internationale Verträge über Consulting Engineering. *Recht im Aussenhandel* (Berlin) 70:I-XI, 1984. (Supplement of *DDR-Aussenwirtschaft*, 18, 2 May 1984).

Regional co-operation in the context of the new international economic order. In Asian-African Legal Consultative Committee. Report of the 20th, 21st and 22nd sessions. New Delhi, Secretariat of AALCC, 1984. p. 124-190.

Sawada, T. UNCITRAL legal guide on international contracts for the construction of industrial works: exemption and

hardship clauses. *Kokusai shoji homu* (Tokyo) 12:5:295-305, 1984 and 12:6:397-402, 1984.  
In Japanese.

Westring, G. Balance of power in the F.I.D.I.C. contract with special emphasis on the powers of the engineer. *International construction law review* (London) 1:2:117-125, January 1984.

Zum Stand der Ausarbeitung eines Leitfadens über die Gestaltung von Verträgen über die Lieferung und Errichtung grosser Industrieanlagen im Rahmen der UNCITRAL. *Recht im Aussenhandel* (Berlin) 62:1-5, 1982. (Supplement of *DDR-Aussenwirtschaft*, 51, 15 December 1982).

#### 7. Other topics

Coelho Bento Soáres, M. A. B. and R. M. Moura Ramos. Cláusulas penais em contratos internacionais. Análise das Regras Uniformes da CNUDCI de 1983. *Documentação e direito comparado* (Coimbra) 271-321. (Supplement of *Boletim do Ministério da Justiça*, 15, 1983).

Text of Uniform Rules on Contract Clauses for an Agreed Sum due upon Failure of Performance in English, French and Portuguese, p. 313-321.

Larsen, P. B. New work in UNCITRAL on stable, inflation-proof liability limits. *Journal of air law and commerce* (Dallas) 48:4:665-692, summer 1983.

### III. CHECK-LIST OF UNCITRAL DOCUMENTS

#### List of documents before the Commission at its seventeenth session

<i>Title or description</i>	<i>Document symbol</i>	<i>Location in present volume</i>
<b>A. General series</b>		
Provisional agenda, annotations thereto and tentative schedule of meetings	A/CN.9/244 and Corr.1 (English only)	Not reproduced
Report of the Working Group on International Contract Practices on the Work of its sixth session (Vienna, 29 August-9 September 1983)	A/CN.9/245	Part two, II, A, 1
Report of the Working Group on International Contract Practices on the Work of its seventh session (New York, 6-17 February 1984)	A/CN.9/246	Part two, II, B, 1
Report of the Working Group on the New International Economic Order on the Work of its fifth session (New York, 23 January-3 February 1984)	A/CN.9/247	Part two, III, A
Draft Convention on International Bills of Exchange and International Promissory Notes and Draft Convention on International Cheques: analytical compilation of comments by Governments and international organizations	A/CN.9/248	Part two, I, A, 1
Draft Convention on International Bills of Exchange and International Promissory Notes and Draft Convention on International Cheques: major controversial and other issues	A/CN.9/249 and Add. 1	Part two, I, A, 2
Draft legal guide on electronic funds transfers	A/CN.9/250 and Add. 1-4	Part two, I, B
Uniform customs and practice for documentary credits	A/CN.9/251	Part two, V, B
Liability of operators of transport terminals	A/CN.9/252	Part two, IV, A
Current activities of international organizations in the field of barter and barter-like transactions	A/CN.9/253	Part two, V, C
Co-ordination of work: legal aspects of automatic data processing	A/CN.9/254	Part two, V, D
Co-ordination of work in general	A/CN.9/255	Part two, V, A
Training and assistance	A/CN.9/256	Part two, VII
Status of Conventions	A/CN.9/257	Part two, VI

<i>Title or description</i>	<i>Document symbol</i>	<i>Location in present volume</i>
<b>B. Restricted series</b>		
Draft report of the United Nations Commission on International Trade Law on the work of its seventeenth session (New York, 25 June-11 July 1984)	A/CN.9/XVII/CRP.1 and Add.1-13	Not reproduced, but see part one, A
<b>C. Information series</b>		
List of participants	A/CN.9/XVII/INF.1	Not reproduced

**Working Group on International Contract Practices, sixth session**

<b>A. Working papers</b>		
Provisional agenda	A/CN.9/WG.II/WP.43	Not reproduced
Model law on international commercial arbitration: revised draft articles A to G on adaptation and supplementation of contracts, commencement of arbitral proceedings, minimum contents of statements of claim and defence, language in arbitral proceedings, court assistance in taking evidence, termination of arbitral proceedings, and period for enforcement of arbitral award: note by the secretariat	A/CN.9/WG.II/WP.44	Part two, II, A, 2, a
Model law on international commercial arbitration: redrafted articles I to XII on scope of application, general provisions, arbitration agreement and the courts, and composition of arbitral tribunal: note by the secretariat	A/CN.9/WG.II/WP.45	Part two, II, A, 2, b
Model law on international commercial arbitration: revised draft articles XXV to XXX on recognition and enforcement of arbitral award, and recourse against award: note by the secretariat	A/CN.9/WG.II/WP.46	Part two, II, A, 2, c

**B. Restricted series**

Draft report of the Working Group on International Contract Practices on the work of its sixth session (Vienna, 29 August-9 September 1983)	A/CN.9/WG.II/VI/CRP.1 and Add. 1 to 9	Not reproduced but see part two, II, A, 1
---	---------------------------------------	--

**C. Information series**

List of participants	A/CN.9/WG.II/VI/INF.1	Not reproduced
----------------------	-----------------------	----------------

**Working Group on International Contract Practices, seventh session****A. Working papers**

Provisional agenda	A/CN.9/WG.II/WP.47	Not reproduced
--------------------	--------------------	----------------

<i>Title or description</i>	<i>Document symbol</i>	<i>Location in present volume</i>
Composite draft text of a model law on international commercial arbitration: note by the secretariat	A/CN.9/WG.II/ WP.48	Part two, II, B, 3, a
Model law on international commercial arbitration: territorial scope of application and related issues: note by the secretariat	A/CN.9/WG.II/ WP.49	Part two, II, B, 3, b
Composite draft text of a model law on international commercial arbitration: some comments and suggestions for consideration: note by the secretariat	A/CN.9/WG.II/ WP.50	Part two, II, B, 3, c

**B. Restricted series**

Draft text of a model law on international commercial arbitration as revised by the drafting group during its seventh session	A/CN.9/WG.II/VII/ CRP.1	Not reproduced but see part two, II, B, 2
Draft report of the Working Group on International Contract Practices on the work of its seventh session (New York, 6-17 February 1984)	A/CN.9/WG.II/VII/ CRP.2 and Add. 1-10	Not reproduced but see part two, II, B, 1

**C. Information series**

List of participants	A/CN.9/WG.II/VII/ INF.1	Not reproduced
----------------------	----------------------------	----------------

**Working Group on the New International Economic Order, fifth session****A. Working papers**

Provisional agenda	A/CN.9/WG.V/ WP.10	Not reproduced
Draft legal guide on drawing up international contracts for construction of industrial works: draft chapters	A/CN.9/WG.V/ WP.11 and Add. 1 to 9	Part two, III, B

**B. Restricted series**

Draft report of the Working Group on the New International Economic Order on the work of its fifth session (New York, 23 January-3 February 1984)	A/CN.9/WG.5/5/ CRP.1 and Add. 1 to 8	Not reproduced but see part two, III, A
---	---	--

**C. Information series**

List of participants	A/CN.9/WG.5/5/ INF/2	Not reproduced
----------------------	-------------------------	----------------