Part I The Transnationalisation of Commercial and Financial Law. The Law Concerning Professional Dealings

1.1 Introduction

1.1.1 The Place and Evolution of Modern Commercial and Financial Law in Civil and Common Law. The Concept of Transnationalisation

Commercial law, including financial and trade law, has long had a somewhat different status in civil and common law. This has, first, to do with the different attitudes towards the role of legislation and particularly towards systematic legal thinking, but it is also a matter of coverage and practice and ultimately one of the recognition (or not) of the special place that commercial and financial law may have in either legal system. This discussion has acquired renewed relevance in modern times and is increasingly influenced or matched by the idea or realisation that, at least in international dealings or professional cross-border activities however defined, the relevant commercial and financial law might not emanate from states at all, either in the civil or common law tradition, but rather from *a legal order of its own* and may then be considered *transnationalised.* This goes back to an era when commercial law was indeed not national and did not belong to any particular legal order except its own.

To the extent that commercial and financial law must still be considered national, the evolution of the civil and common law, their origins and their differences, remain very relevant in discussing the nature and application of this law as we shall see. It is of special importance and may create particular problems if these national laws are applied in international cases by courts in other countries or by international arbitrators. Even if commercial and financial law were to become fully transnationalised, consideration should still be given to whether the common law or civil law approach and methodology should be followed or favoured or whether a different approach altogether should prevail. The differences between the two systems will be discussed in greater detail below in sections 1.2 and 1.3.[1] Here it is sufficient to note that in *civil law countries* the codification ethos

[1] As far as civil law is concerned (as will be discussed in greater detail below), its history is largely Roman; its method is largely that of the natural law school of Grotius and his followers; and the nationalistic statutory approach is largely due to nineteenth-century political imperatives and developments. Roman law and the common law are the only truly original Western legal systems of private law. The natural law school may suggest a third development in Western Europe, but it is usually associated with the development of the Roman law into the modern civil law. It is, in any event, highly important for a proper understanding of the civil law as we know it today. For valuable discussions of this development see the classic treatises of Paul Koschaker, *Europa und das römische Recht* (1947, reprinted 1953) and of Franz Wieacker, *Privatrechtsgeschichte der Neuzeit*, 2nd edn (1967, reprinted 1996).

looks primarily for legislation and (often) assumes in that connection that private law, including commercial and financial law, is *one* intellectually coherent *national system* that is essentially statutory or codified. This suggests that private law is imposed from above as an internally consistent system that is complete, explainable from within, and capable of finding solutions for all eventualities, present and future, on the basis of the proper application of its rules or otherwise the principles underlying it.[2]

This attitude is rule-oriented and formal. In essence, it waits for the state to effectuate change through legislation when there is a need to adapt the law, which is thus nationalised as to its formation, and territorial. Since the system and its coherence are here considered of primary importance, in private law codification, states will rely on academic advice to preserve intellectual rigour and consistency—at least that is the idea. The application of this law is subsequently seen mainly as a technique which has logic as its core and automatically correct solutions are expected if this intellectual system of rules is properly applied. Extraneous sources of law are irrelevant. That applies especially to fundamental and general principles but also to custom and party autonomy unless the statutory texts specifically refer to them and allow them to operate. There is no other source of law.

This approach was the result of three nineteenth-century paradigm shifts that changed the private law on the European Continent completely and also fundamentally affected commercial and financial law. The result was the modern civil law differentiating it henceforth from the earlier universal Roman law and also from the approach of the common law. The idea is then that a) all law, including private law, is national; b) it issues from states, hence the dominance of legislative texts; and c) these texts present or should aspire to present an intellectual system which is internally coherent and complete, and reflects per definition the reality of human relationships. As we shall see, in the European Union (EU) projects for private law unification there is an unarticulated combination of these various views, as there is in UNCITRAL and UNIDROIT, the sum total of which is the continuation of a top-down statist approach to private law formation. It claims exclusivity for its texts which control all private law, including, in principle, the contractual content. There are no overriding values and party autonomy operates only by licence of the state.[3] Private law is nationalised. Treaty law is no more than national law adopted by the contracting states.

[2] As we shall see below in s 1.2.9, this was particularly a German intellectual ideal that, combined with the early nineteenth century Romantic emphasis on nationality and creativity and the subsequent notion of the creation of society according to preconceived intellectual or academic models (but always by country), also began to dominate civil law thinking outside Germany during the nineteenth and twentieth centuries. For German orthodoxy in this respect, see K Larenz, *Methodenlehre der Rechtswissenschaft*, 6th edn (1991) 6, 437 and the student version, revised by CW Canaris, 3rd edn (1995) 263.

[3] A dynamic forward-moving force in the law is not denied here, but it is not autonomous and depends on a liberal interpretation within this more static, abstract system. *cf* n 185 below for other (minority) views in Germany. This situation is very different from the one in the US under the Uniform Commercial Code (UCC) which, as we shall see, encourages the common law, equity and custom or the law merchant to operate besides it (Sec 1-103), accepts and favours bottom-up law formation and is in that sense not a European-style codification at all. See also text at n 26 below. It is further imbued by realism as the Americans perceive it, see ss 1.3.4-5 below, that is guided by practical need and a continuous search for operational sufficiency which requires and allows constant adaptation in the practice of the law, here commercial law in particular, and permits its continued expansion 'through custom, usage and the agreement between the parties.' There is true party autonomy and respect for the contract and its content as such, subject only to public order and policy requirements, as indeed there was on the European Continent before the nineteenth century.

This is also reminiscent of the old common-law tradition, although the English may now be somewhere in the middle. See text at n 17 below. They do not require legislative texts and a top-down approach to pervade all law formation although legislation became increasingly important in private law as well. The Law Commission

This remains the basic approach in modern private law unification to which the Draft Common Frame of Reference (DCFR) and its progeny as models for codification at the level of the EU also testify.[4] It follows that there is no real need for empirical research and this law is not questioned, for example, as to its fairness, efficiency or responsiveness to social or economic needs.[5] They are assumed to result from the system itself, and because it is the law, it must as such be accepted as correct, never mind how far from practical realities it may be, and whatever unexpected and undesirable side effects it may have, or indeed how poor the intellectual back-up may prove to be or to have become. This is the civil law expression of legal positivism (and formalism) and still the mainstream of its thinking.[6] In this approach, it is explicit that commercial (and financial) law is an inextricable part of the national codification (whether or not contained in a separate code) and subject to its method and way of application. It is thus equally national and intellectual, and must be made to fit. It is not independent, merely *lex specialis* or refinement. In this approach, even international commercial transactions are covered by and must find a solution for their problems in these national laws, the proper one then being found through conflict rules or rules of private international law.

It follows, *first*, that the further development of the law, even private law, is perceived primarily as an activity of the state and as such is centralised and monopolised at state level. Law, even commercial and financial law, is thus deemed made and imposed, not found, even if it is based on an analysis of prior experiences. In particular, it denies the autonomous law creation impulses that may emanate from other groupings, for example, in commercial and financial practices or custom unless specially admitted by the state system which always has the last word.

Second, this law, even though commercial and financial, is academic and maintains in civil law countries an aura of self-evidence that derives from the pretence of intellectual consistency and completeness of the codified private law system as a whole. Its true legitimacy is not then in the democratic process, which in any event was often wanting when this law was first codified, or even in economic rationality, but in its systemic consistency and conceptual unity which claims by definition to be close enough to reality—even commercial and financial reality—to guide it and, if necessary, to redirect and control it for the greater benefit of all participants and the public at large.

in particular favours texts of this nature. The English courts so far remain pragmatic, have always dealt with fragmented legal sources, and are comfortable with them but some closing of the gap between Continental and English legal thinking has been noticed and at least English academia does not necessarily follow in the American footsteps: see PS Atiyah and RS Summers, *Form and Substance in Anglo-American Law: A Comparative Study of Legal Reasoning, Legal Theory, and Legal Institutions* (Oxford, Clarendon Press, 1987). No doubt there is greater Scottish comfort with civil-law thinking which trickled through in particular into the Draft Common Frame of Reference (DCFR) as a model for EU codification, where Scottish academics have been more active, but, as will be discussed in greater detail below in ss 1.4.1-2, the tolerance for other sources of law and especially the respect for party autonomy, the lack of systemic thinking, and the absence of a belief in the sufficiency of the academic model remain probably the key distinguishing elements between common and civil law (of the German variety in particular).

[4] See s 1.4.19 below.

[5] Although the question of whether morality in particular would be automatically served in this manner remained important in nineteenth-century German philosophical thinking: see Roscoe Pound, vol II *Jurisprudence* (1959) 223; it became much less of an issue in the run up to the German Codification in 1900 and in subsequent philosophical discourse in Germany.

[6] For the modern form of legal positivism in private law formation and application, see s 1.4.15 below.

Third, as in codification countries, the national private law regime is thus perceived as one intellectual statist system that monopolises the field, it follows that commercial and financial law is considered part of, and captured in, that system. It is not perceived to be independent from it but is merely *lex specialis* as just mentioned. These specialised areas have, therefore, no separate place in the law and cannot evolve independently. Commercial and financial law must fit the system and is then confined in its evolution.

Fourth, this monopolisation of the law formation function at the level of the state confirms that there is little room for the operation of other sources of law, such as commercial and financial practice and custom, or for general principles (other than those underlying the codes), whether or not commercial, national or transnational; or for efficiency considerations or considerations of economic growth; or for any cost benefit analysis, unless expressly admitted or tolerated by the codes or their systems themselves. It was already said that in this approach, even party autonomy setting forth the terms of a deal only operates by government licence and is therefore constrained to what the codified system will allow and it is not respected per se.[7] This approach to party autonomy goes far beyond the ordinary constraints derived from public order and public policy requirements which parties must respect. It concerns here the validity of their agreement itself, which thus depends on statist fiat. There is in fact no party autonomy as source of law.

Fifth, the result is that this law is static and without a dynamic forward-moving force except through legislation or case law which raises the question of interpretational powers and freedom in the state courts. It was secondary as the legislative approach supported by system thinking and a policy-oriented nationalistic outlook remained the focus and assumed for its further development foremost governmental insight (through its academies) into what was necessary in terms of updating and adaptation. Commercial and financial law shows, however—as does regulation—that such insight may not be forthcoming and that autonomous law-creating forces therefore remain necessary to keep private law up to date and functional. This fundamental and general principle, custom and practices, and party autonomy may still have to be included, although not openly but rather hidden in a *liberal* interpretation technique of a domestic nature; in contract, in modern times often operating behind the notion of good faith.

Sixth, in case of doubt or when situations were not explicitly covered or were new, and thus where the formal law lagged behind, it is true that even in civil law there had always been some interpretational flexibility largely based on an extrapolation of rules from existing legislation and its system or implementing case law. It could also mean inductive or otherwise analogical reasoning, but, although in this approach in modern times a more liberal teleological interpretation technique was allowed to provide greater flexibility, whilst even pressing ethical, social, and efficiency considerations might be admitted in the interpretation process, this was still mainly done to support and complete the national system, its tenets and especially its credibility. In essence, this method of interpretation continued to be subservient to the system rather than to society or to the community this law served, which system was thus perceived as remaining formal and closed in principle.

[7] Note that in pre-codification times, this autonomy was subject only to public policy constraints which were at first expressed mainly in the notion of a just cause (*iusta causa*), see vol II, ch 1, s 1.2.6. The approach in modern codification is quite different: party autonomy itself is licensed and not merely made subject to public policy and public order requirements.

Seventh, this attitude also fundamentally affected *international* transactions, even those in commerce and finance. Although these transactions were likely to be outside the immediate scope and concern of local codifications which were seldom written for them, they had to fit into *national* laws as there was (in this way of thinking) no other. It thus became necessary to search for the more appropriate but always *national* law in the above sense under applicable *conflicts of law* (or private international law) rules in international cases leading to the application of the domestic law considered the most closely connected with the case in question, even if, as we shall see, it became increasingly difficult and artificial to define or identify.

Eighth, as a more liberal interpretation technique created some flexibility at the edges, this could have led to the extrapolation and expansion of the *lex fori* into international cases, especially taking into account the foreign elements of the case and increasingly also other more transnational sources of law so that a form of transnationalisation would result in the interpretation of domestic laws. It is an approach that gained some ground in the US also (interstate) as we shall see[8] but not so far in Europe. The problem is that each legal system then creates its own form of transnationalisation.

Ninth, quite apart from the problems of identifying the closest connection, particularly in factual situations with many contacts, there naturally arose, in this approach, ever greater problems when considerations (or values) that surpassed national concerns, it being implicit in the codification approach that all moral, social and economic ordering as well as an adequate level of legal certainty, were expected from and had to be provided by a national legislator in international cases as well. This was hardly any longer feasible in an ever more globalised world and economy, nor was it rational to continue to expect it.

Tenth, regulation which remained mostly domestic also became increasingly a problem in international transactions as it had to be established which governmental interests prevailed in this connection and in what aspects if they were conflicting. This raised the issue of the proper jurisdiction to prescribe, as the Americans call it, as well as the question of the operation of international minimum standards.

At a more philosophical level, the civil law approach assumes above all that in matters of private law we live with an account of human behaviour that can be clarified scientifically and is orderly, in essence based on repetition. That is the neo-classical view in macroeconomics which is often believed to have failed us, but we struggle with the same problem in the law, where it is further complicated by nationalistic thinking. Indeed, the codification approach in its purest form does not consider or accept that the future is different from the past and that it cannot be systematically captured nor that international transactions may require their own transnationalised legal regime that might operate quite differently.

It means that in considering better (private) law, the inclination is always to remedy the shortcomings of the past in a national context, the idea being that new or ever evolving patterns, even if transnational, can still be satisfactorily covered in this manner. Proper and ever better analysis of past experiences is here the ultimate guide in law formation, completed by intellectual extrapolation and systematisation. The idea is that 'truth' can be established in this manner and that the reality of human relations can thus be discovered and formulated in an academic model and can hence be correctly guided, for which the

[8] See s 2.2.3 below. Even in the traditional conflicts of law approach, this may well reflect what actually happens in practice.

state with its power of rule imposition is the superior channel. For those who think in this manner, the only alternative to national codification for international dealings is treaty law, which is, in this view—as has been mentioned before—upon ratification still considered the expression of national law; retains its territorial limitations; and always remains a super-imposed statist formal legal facility.[9]

Nevertheless, in the application of codified law or of treaty law of this nature, inconsistencies and inadequacies could not be avoided. The subsequent need for a liberal interpretation technique meant indeed that other sources of law—which in a globalising world were also not necessarily territorial—revived, not least in international dealings. Thus fundamental and general principle, custom or industry practices, as well as expanded notions of party autonomy resumed their traditional roles to sort out contradictions and inadequacies and to make better sense, although in civil law academia this development remains in essence largely ignored even for international dealings.

Domestic statutory texts and their logical coherence thus remain the centre of attention, even if some uniform transnational law may now be considered if expressed in treaty texts whilst liberal interpretation is further admitted to save the system and its credibility, but law, including private law, remains here in essence a pre-existing national system of formal rules. There are no other admissible sources of law. They would only confuse and deviate from the proper state-ordained path.

In the EU, the DCFR, mentioned above, which since 2008/2009 has been presented as a model for European codification, even though it has as yet no official status, except for its sale carve out in the 2011 EU Commission's proposal for a Regulation concerning a Common European Sales Law (CESL), is the latest expression of this attitude. In that sense the DCFR and CESL are concerned mainly with remaking the past in a territorial manner, now at the level of the EU. See section 1.4.19 below and more particularly Volume II, chapter 1, section 1.6 and chapter 2, section 1.11. Thus the approach remains academic, systematic, legislative, and nationalistic, albeit at the expanded EU level but in the traditional civil law, mainly German, codification manner.

To repeat: in civil law orthodoxy, there is little room here for an autonomous commercial and financial law at the national level, let alone transnationally. Newer globalising tendencies and needs thus continue to be ignored, even in commerce and finance. The DCFR and its progeny are in fact, a product not of transnationalisation but of national codification thinking, now at EU level. In particular, there is little understanding of the emergence of a transnational commercial and financial legal order with its own law and its own public order requirements, the result of which is now usually referred to as the new or modern *lex mercatoria* or international law merchant.[10] This new law merchant is not based on,

[9] This attitude is not limited to civil law, as we shall see. Thus Roy Goode, 'Rule, Practice, and Pragmatism in International Commercial Law' (2005) 54 *ICLQ* 539, 549 limits transnational law to treaty law. That seems extreme precisely because of treaty law's territorial aspects.

[10] In the following, the word 'international' will be reserved largely for transborder *public* law and 'transnational' for transborder *private* law. As we shall see, recognition of other sources of law, especially customary law, general principle and party autonomy as original sources of law, was never as problematic in public international law as was expressed in Art 38(1) of the Statute of the International Court of Justice. This reflects the older Grotian approach which, until the nineteenth century, also prevailed in private law and of which there may remain more in the common law approach. The revival of the same approach for transnational private law formation is the preferred one in this book. See also JH Dalhuisen, 'Legal Orders and their Manifestation: The Operation of the International Commercial and Financial Legal Order and its *Lex Mercatoria*' (2006) 24 *Berkeley Journal of International Law* 129.

and does not adhere to, the civil law codification idea but allows various sources of law to operate and establishes a hierarchy between them. As we shall see, this suggests at least in part a bottom up, dynamic process of law formation and application and in method goes back to pre-codification days.

As just mentioned, the lack of newer thinking is also reflected in the CESL (see for a critique Volume II, section 1.6.13) and covers a subject (sale of goods) that in common law traditionally belongs to the area of commercial law. Indeed, there is no whiff of a transnational approach. Worse, the methodology was never properly considered; the civil law codification approach was assumed to be natural and uncontentious. Although limited to cross-border dealings within the EU, the operation of the modern *lex mercatoria* is ignored; as an opt-in instrument, the only alternative remains here national law. There are still no other sources of law admissible in international professional dealings, at least that is the approach, although it may be questioned whether there is sufficient authority to exclude them. As a minimum, this should have been part of the discussion. The idea that there might be a separate legal order for professional dealings altogether, which develops a law that is not primarily state controlled, is dynamic and also applies within the EU, remains here inconceivable, but it is the real issue.

Quite apart from its other defects and pretentions, nationalistic system thinking of this nature around pre-existing hard and fast local rules has a tendency to stultify the law whatever the reach of more liberal interpretation techniques may be. In fact, this more static statist civil law approach to law formation has a problem with all innovation, even domestic, thus not only in international commercial and financial dealings. In more modern terms, it has particular difficulty with the legal response to a globalising world and cannot cope with its dynamism. See also section 1.1.4 below. This is not without consequence and it may be posited that nationalistic system thinking in the above manner is the reason why modern civil law has been particularly wanting in international commerce and finance, has increased legal risk in these areas, and may well be driving vital markets away. One may think here particularly of international finance and the operation of the financial markets, which are increasingly globalised and for which civil law thinking can give little support.[11] This will be demonstrated throughout this book. As just mentioned, a more liberal interpretation might be used to save the system but the techniques mostly remain national-system-bound and are in any event, contentious in property law. This will be further explained in Volume II. For the reason why, at least in commerce and finance, this civil law approach as a national model or system must now be more fundamentally revisited, see more particularly the discussion in section 1.4 below.

It was not always thus, and may no longer be the way of the future, but it is the nineteenth-century inheritance of the civil law, often closely associated with the emergence of the modern state in Continental Europe. On the European Continent it superseded the received Roman law that had been customary and was supported by the secular natural

[11] We shall see, however, that there is significant acceptance of a more transnational approach, particularly in France where it is demonstrated in particular in the attitude to international arbitration, recently perhaps best represented before the Hague Academy by Emanuel Gaillard, 'Aspects Philosophiques du Droit de l'Arbitrage International' (2008) 329 *Receuil des Cours* 49; see further *Cour de Cass Civ* 1, 29 June 2007 in *Ste PT Putrabali Adyamulia v Societe Rena Holding et Societe Mnugotia Est Epices,* Arret n 1021, 207 *Revue de l'Arbitrage*, 507. As we shall also see in the text at n 29 below, it may be less strong in other codification countries.

law of those days. It was not statist or territorial and had been more universal,[12] although particularly in commerce and finance it was supplemented by a myriad of local laws and practices.[13] In fact, there were multiple sources of law that could compete.

It is also relevant, especially in commerce, that there was at the time a variety of judges,[14] the judicial function often being private, and they would use their own knowledge of custom and practices, as specialised arbitrators may still do today.[15] Enforcement was also mostly private and therefore conducted within the commercial communities themselves. Law formation was not then the natural province of states, most certainly not in commerce, unless public order was engaged, as was often considered the case in bankruptcy but was otherwise exceptional. Where statutes were produced, they were even then normally regional or city compilations of existing customs gathered mainly to provide greater transparency and to promote trade more generally (in which local government often had a taxation interest, which also explains the eagerness to provide order in market places and to protect trade routes as far as possible). Thus the purpose was not to preempt or prevent

[12] This earlier law had never been officially promulgated but was basically found, not imposed. Long considered the best expression of rationality, this Roman law was given a high customary status, see ss 1.2.4–1.2.5 below, and was considered universal, although subject to competing local laws. Fundamental and general principles, custom and industry practices supplemented it and, especially since Grotius, guided the natural law schools, see s 1.2.7 below. Moreover, parties could freely legislate amongst themselves (subject to the requirement of a valid cause or similar public policy constraints which were then minor) and there was true party autonomy in the legal sense. For the history and remnants in France and present day revival see s 1.4.9 below.

Civil law codification wiped them out as independent sources of law. See B Cremades and S Plehn, 'The New Lex Mercatoria and the Harmonisation of the Laws of International Commercial Transactions' (1984) 2 *Boston University International Law Journal*, 324. At first for obvious efficiency and transparency reasons—therefore as a product of enlightenment or rationalism, which also entailed the centralisation and nationalisation of the judicial function. It is substantially the background of the French *Code Civil*, as we shall see in s 1.2.8. below, but the codification drive was later joined and became dominated by forces of pure nationalism in the Romantic Rousseauian and German (Hegelian) variant of the codification theme, in which the state became the expression of the general will or even the true embodiment of the human condition—the individual and its law being considered nothing by themselves. See also section 1.2.9 below.

Ultimately states of this nature took charge of what they then believed to be a society in which they saw themselves as the originator and enforcer of all rules per country. Commerce and finance were not excluded and their international reach was feared. Legal orders different from states were denied existence. There is no place here for international law either, except as some ultimate, unreachable ideal (in terms of world nationality).

Whether these state absolutist notions in law formation helped or distracted from modern capitalism, is less clear. The initial idea was in any event not to redirect and censure trade and commerce, but the commercial law was henceforth *lex specialis* to the national, state-created, system of private law as there was no longer anything else. Whatever international legal unity there still was depended on the old traditions being recognised to some extent in the new laws (although transformed to fit the general private law system per country) and otherwise on treaty law.

[13] This is often referred to as the older *lex mercatoria*. However, it should be understood that its rules were not the same everywhere but developed in answer to practical needs. Only to the extent that these needs were felt everywhere, did the rules show some innate uniformity but there were significant differences. See FR Sanborn, *Origins of the Early English and Maritime and Commercial Laws* 126. The laws of admiralty, for example, were not the same in the English Channel/French coast and offshore Italy (The Amalfian Table). The bankruptcy laws also varied widely. See JH Dalhuisen, *Dalhuisen on International Insolvency and Bankruptcy* (1986) 1–25ff.

[14] See WC Jones, 'An Inquiry into the History of the Adjudication of Mercantile Disputes in Great Britain and the United States' (1958) 25 *University of Chicago Law Review*, 445.

[15] It is well understood that modern arbitrators find on the basis of laws and facts pleaded by the parties and are not free to use or rely on their own knowledge without a proper hearing and argument, unless they may state as *amiable compositeurs* or the arbitration is specialised and depends on peer knowledge in arbitrators, not unusual in quality issues, which are largely factual. This is a different type of arbitration, however, based not on law but on expertise in arbitrators and presents an older type of dispute resolution which left decisions to senior experts trusted in the particular trade and often not requiring any reasoning.

further development by the commercial communities themselves (which were not united except by the needs of their various trades which could be very local).

In the *common law*, the situation was and still is different from the one we find in modern civil law. In its formation and further evolution, common law was often helped, but never monopolised, by legislation. System thinking and the search for and application of one coherent system of private law are here not major issues either, at least not traditionally. By its very nature, the common law moves from case to case, is factual and result-oriented, and in principle leaves room for other sources of law, in trade, commerce and finance especially for industry practices or customs, supported by party autonomy, and therefore by the order that participants create amongst themselves.

This should not be idealised but it is clear that the common law has, at least in principle, the tools and willingness to be more responsive to practical needs. It has avoided the grip of the academic model. As a consequence, commercial law was also able to retain a more independent status and role in common law countries, although especially in England, nationalism and the tightening grip of the common law itself also impacted on a more decentralised approach to commercial law and on the reach of party autonomy, custom and commercial practices, as we shall see.[16] This also affected the commercial law's international status in England. It became there also substantially territorial.

In fact, in England by the eighteenth century the commercial law had already been incorporated into the common law and had lost its independence,[17] although it was not

[16] As to the other source of law: general principle, the common law had always been wary of it, as on the whole it dislikes generalisation, see s 1.4.6 below. Worse perhaps, was that custom became subject to the law of precedent, depending as such on court recognition, see text at n 21 below.

[17] In England, there was already some statutory law and a Statute of Merchants (Acton Burnell) of 1283, in an effort to attract foreign traders to England, promoted the speedy settlement of disputes between all merchants, while an Act of 1303 (*Carta Mercatoria*) had recognised the law merchant as an independent source of law amongst all traders, exempted foreign traders from local taxes, and gave them freedom to trade throughout England.

The old commercial courts did the rest and their laws were originally more particularly connected with fairs and the maritime activities in the Channel ports, where participants were peripatetic merchants or maritime transporters, including foreigners, which required prompt justice to be enforced either against the person of the debtor, if still present at the fair or, particularly in his absence, against his goods before they left the court's jurisdiction. See F Pollock, "The Early History of the Law Merchant in England' (1901) 67(3) *Law Quarterly Review*.

The courts in the staple markets, which also attracted foreigners, were the Staple Courts which were statutory from 1354 onwards. The Staple Courts often consisted of the mayor and two constables or merchants, who could be foreign if a foreign merchant was involved. At more local fairs, on the other hand, there often operated Borough- or Pie Powder Courts, used especially for civil and criminal litigation between the participants in these markets, who were mostly locals. These courts often only operated during the fairs with a process 'from hour to hour and day to day'.

In all these courts, judges and juries of merchants were used to discover the applicable customs, although there were some written sources of the applicable commercial law also, such as the Red Book in Bristol and the Black Book of Admiralty in London. There were others in maritime law, notably the laws of Visby and the laws of Oleron, a small island off the French coast of Aquitaine, which were highly regarded and often consulted elsewhere.

Special maritime courts began to operate after 1360, at first competent mainly in criminal cases (piracy), later also in civil cases with the emphasis on charters, ship mortgages, maritime insurance, early forms of bills of lading and the earlier forms of negotiable instruments such as bills of exchange and cheques. To appear before these courts, the plaintiff had to prove that the defendant was a merchant and establish the applicability of commercial law or custom, but the presence of the defendant was not strictly necessary as long as some of his goods were in the jurisdiction. It should be emphasised that the law merchant of those early days was *not* as a consequence a uniform law in any sense and that its content varied with the markets and products covered—and it could be very local—but the common outstanding feature was that both this law and the courts that administered it were

completely subsumed and retained some special place in particular through the endeavours of Lord Mansfield.[18] But as its courts were similarly overtaken by the common law jurisdiction, this restricted the further independent development of commercial law.[19] Moreover, in the nineteenth century, the notion gained ground, in England too, that all law issued from a sovereign, although it did *not* depend on legislation. That is the school of Bentham and Austin, which became dominant as we shall see in section 1.3.3 below. Nationalism thus entered and further eroded the support for other sources of private law, especially customary law, all the more so when international, although the common law itself was often still considered of 'immemorial usage', but that was then deemed a kind of overriding higher custom[20] and in any event always national.

In the meantime, in common law countries, the emerging rule of precedent confined the role of custom or market practices further (see section 1.3.3 below,) and to a large extent

autonomous. Others have noted as other common features the customary nature of these courts, their summary jurisdiction, and spirit of equity and common sense that was not concerned with technicalities. See, eg W Mitchell, *An Essay on the Early History of the Law Merchant* (Cambridge University Press, 1904). Jealousy eventually manifested itself in the common law courts, especially in the Court of Admiralty in London. The common law judges eventually took the view that the older commercial and admiralty courts only operated by franchise and could, therefore, be controlled by the common law courts. Consequently, these older courts started to disappear, although they were never formally abolished; after the middle of the eighteenth century only the Court of Tolzey in Bristol survived. The overriding influence of Chief Justice Sir Edward Coke is often mentioned in this connection. Eventually the requirements that the defendant had to be a merchant and that commercial law or custom was applicable disappeared. After 1765, the common law courts considered that 'the law of merchants and the law of the land are the same: a witness cannot be admitted to prove the law of merchants'. See *Pillans v Van Mierop* [1765] 97 ER 1035 [1765] 3 Burr 1663, 1669. That appears to have concluded the trend.

[18] Although this integration of commercial law into the common law is generally considered to have been completed under Chief Justice Coke, Lord Mansfield in particular subsequently tried to develop commercial law alongside commercial practice but always within the confines of the common law and its courts. As we shall see, this left at least some room for commercial custom and practices as independent sources of law but it did not re-establish independence. In *Pillans v Van Mierop*, see n 17 above, Lord Mansfield accepted that the rules of the law merchant had become part of the common law and were no longer autonomous custom. He accepted the jurisdiction of the common law courts but added that the common law and its courts had to recognise the *dynamics of international business* so that commercial law was to evolve alongside commercial practice. Yet the law merchant as an independent legal order governing the legal relationship between merchants had ceased to be recognised and the national common law sustained the international character of commerce to only a limited extent, more in the nature of courtesy or *comitas*. *cf* C Schmitthoff, 'International Business Law: A New Law Merchant' (1961) *Current Law and Social Problems* 129, 138. This nevertheless proved particularly important for negotiable instruments (although the first time the promissory note was declared a negotiable instrument in England was earlier in 1680, in the case of *Sheldon v Hently* [1681] 2 Show 160 involving bills of lading, and (later) documentary sales, such as the FOB and CIF sales, ship mortgages, the stoppage of goods in transit and in the concept of bailment, therefore the protection of the physical possession of goods, in agency, partnership and joint ownership where commercial principle continued to be closely followed.

However, once having lost the autonomy of its courts, the commercial law never recovered a truly independent role in common law countries, and the same may now also be said of its modern branch of financial law. Nevertheless, it is not incidental or mere *lex specialis*, and it clearly covers whole areas of the common law in full.

[19] However, commercial law was poorly administered by the common law courts, and this is an important reason why in common law the law of chattels long remained, and probably still remains, underdeveloped. The greater speed and flexibility of the older proceedings, not bogged down by procedural and evidential formalities, had fostered trade and proved especially important for foreigners and their protection. These benefits were lost when the common law judges became the commercial judges, most with experience only in land law and some in tort. Even today this is reflected in high costs and inefficiencies.

The further result was that much commercial expertise and flexibility were lost in this part of the law. By the end of the nineteenth century, the international connection had also been neglected, so that commercial law became a domestic affair in England, a situation further promoted by the preponderant impact of British colonial trade.

[20] Not, therefore, very different from the Roman law on the European Continent, see s 1.2.5 below.

they lost their status as a dynamic source of law.[21] As we shall see, this also affected equity that until then had functioned as another more flexible corrective or supplement of the law, particularly important in commerce and now also in finance, a facility in the meantime often taken over by legislation, although the equitable jurisdiction is not completely exhausted as we shall also see.

More recently, especially in England, academia has become more active in the law and has subsequently started to look for a more coherent system of rules distilled from disparate case law and statutory texts. Although the English courts have remained pragmatic, there thus also entered a measure of *nationalistic system thinking*, at least at academic level in England,[22] more so than in the US where this struggle is now often cast in terms of legal realism versus legal formalism as we shall see.[23] This may also affect the commercial and financial law and integrate it further into the common law.

The consequence of the integration of commercial law into the common law is, however, that the distinction between commercial and other private law is no longer fundamental in common law either, except that no systemic unity is assumed. As already mentioned, the distinction between *law* and *equity*, discussed in section 1.3.1 below, at first each with their own courts, may remain here more important, and also cuts through what may still be considered commercial and modern financial law, equity notions having become a particularly important support for commercial and financial law (despite the confining nature of the rule of precedent). Here we find company and bankruptcy law, the law of trusts, including related structures—now mostly statutory—and floating charges and conditional or finance sales, assignments and set-off, indirect agency and fiduciary duties.

Indeed, in all common law countries, there is now also substantial legislation in the field of private law, which may also extend into commercial and financial law. To a large extent it superseded the corrective power of the equity judges. Whilst the equity judges had often looked for inspiration abroad, especially in the Roman law, statutory law is by definition nationalistic or at least territorial. Even so in common law countries statutory intervention is generally still different from the civil law approach in that it tends to be corrective or remedial and therefore incidental, except perhaps in typical equity areas such as company and bankruptcy law, where legislation is more comprehensive. However, even then it does not aspire to systematic thinking or overarching intellectual conceptualisation that seeks automaticity in its application and eliminates in the process other more spontaneous sources of law.

[21] It set customary law in concrete and it thus lost much of its dynamic character; it was thought that this prevented courts from becoming confused, a somewhat strange argument. See JH Baker, *An Introduction to English Legal History*, 3rd edn 1990) 418; see also RW Aske, *The Law Relating to Custom and the Usages of Trade* (1909) 23; and HJ Berman and C Kaufman,'The Law of International Transactions (Lex Mercatoria)' (1978) 19 *Harvard International Law Journal* 221, 227.

[22] Especially in the 20th century, when the academic study of law became more established and valued in England. See ss 1.3.2 and 1.3.3.below for the role of the Law Commission in this process and for early codification ideas in England. A more formalistic approach is adopted here but it is not the traditional common law attitude that was fact-, rather than rule-oriented, and moved from case to case.

[23] See more particularly s 1.3.4 .below and for the UCC approach, also n 3 above.

Legal formalism is the opposite of legal realism and rests on the idea of the self-sufficiency of the legal system as a set of pre-existing, often hard and fast, black-letter rules that can be more or less mechanically applied and that are considered to produce acceptable results in a more objective manner. In doing so, legal formalism is inclined to disregard the original purposes which a particular norm was meant to serve and does not test its practical effects.

In the US, the Uniform Commercial Code (UCC) in section 1-103 clearly expresses the view that the statutory texts are to be interpreted so as to leave as much room as possible for the common law, equity, custom, the law merchant and party autonomy.[24] Even though it calls itself a 'code', it is therefore not a code in the civil law sense because it does not seek to monopolise the field and eliminate other sources of law,[25] and, although undoubtedly looking for structure, it is also not systemic in the civil law manner.[26]

This represents the more traditional common law approach, which still finds an equivalent in England in the mostly literal and therefore restrictive interpretation of statutory private law texts,[27] again to leave as much room as possible for the more traditional sources of law, especially the common law and equity (although, as we have already seen this may now be less true for the custom), even if increasingly construed and perceived academically as one national coherent system.

On the other hand, the predominantly nationalistic approach to private law formation and operation, although still different from the civil law approach, has also led in common law countries to the extension of *domestic* law to *international* transactions and consequently to an embrace of Continental European conflicts of law or private international law notions pointing to the proper connection, therefore to the idea that *only* domestic laws could apply to international transactions, even in international commerce and finance. This is not, therefore, transnational law. Although private international law as a system of hard-and-fast conflict rules has long been reconsidered in the US, as we shall see in sections 2.2.2 to 2.2.3 below, this has not been the case in England.

In fact, as we shall also see, the more robust resistance against the alternative of transnationalisation of private law, including the rejection of other autonomous transnational sources of law in the modern *lex mercatoria*, often comes from England, even though it would benefit English practitioners most and appears to fit the common law tradition much better than the civil law.[28] It is more welcome in France where greater transnationalism is now accepted in these matters.[29]

[24] In s 1-103 UCC it is further stated that the principles of law and equity, including the law merchant and the law relative to the capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, or other validating or invalidating cause, shall supplement the UCC, unless displaced by particular (mandatory) provisions of it.

[25] It is also practical and misses the typical nationalistic element. See RM Buxbaum, 'Is the Uniform Commercial Code a Code?' in U Drobnig and M Rehbinder, *Rechtsreaklismus, multikulturelle Gesellschaft und Handelsrecht* (Berlin, 1994) 197; and J Gordley, 'European Codes and American Restatements: Some Difficulties' (1981) 81 *Columbia Law Review* 140; see further s 1.3.3 below for earlier American attempts at codification.

[26] The UCC does not, for example, maintain a uniform concept of property law for all the chapters or Articles. In Art 2 on the sale of goods it maintains a more general notion of ownership and its transfer that also exists between non-professionals, but in Art 2A on equipment leases and Art 8 on the trading and holding of modern investment securities entitlements, proprietary rights are only defined incidentally, that is for each specific structure without resorting to general proprietary principles or a unitary system of proprietary rights. That is also true in Art 9 on secured transactions.

[27] See s 1.3.3 below.

[28] This has been pointed out by others, see notably AF Lowenfeld, 'Lex Mercatoria: an Arbitrator's View' (1990) 6 *Arbitration International* 133 in reply to English nationalism and positivism represented by Lord Mustill 'Contemporary Problems in International Commercial Arbitration' (1989) 17 *International Business Lawyer* 161ff, who even considered as absolutely void a contract in which transnational law is chosen as the controlling law. This has now officially been denied in the EU Regulation, (EC) No 593/2008, on the Law Applicable to Contractual Obligations (Rome I, Preamble 13).

[29] See n 11 above.

1.1.2 The Transnationalisation of Commercial and Financial Law. Common or Civil Law Approach? Methodology

Whatever the aims of nineteenth-century nationalism in private law may have been, both in civil and common law, commercial law formation through an autonomous process of transnationalisation, mainly through the force of principles and practices, was never entirely eradicated in international dealings even in civil law countries. One may think of the law concerning bills of lading; negotiable instruments especially eurobonds and euromarket practices including clearing and settlement; the law of assignment, of set-off and netting in international finance, and of letters of credit (UCP) and trade terms (Incoterms). It may also concern the important and connected issue of finality of title transfers and payments. For more detailed references see section 1.4.4 below.

It is clear that it concerns here the key *legal infrastructure of the international markets*, which can no longer be suitably covered by domestic laws. Where a generation ago the international markets might still have been peripheral to domestic markets and domestic legal systems, they have now moved to the centre, their size being far greater than that of the largest domestic markets.

If we think of the form this new transnational law takes, or should take, and how it compares to the more traditional common or civil law concepts of private law, it should be repeated that it is ultimately system thinking and the technical or mechanical approach to law and its application that truly distinguishes civil law from common law. That also affects our perception of commercial and financial law in common and civil law, more so than the statist or nationalistic and legislative approach per se, which to some extent both now share.

It is indeed this issue of domestic system thinking that may particularly affect our views of the place of commercial and financial law. If we mean to go forward with globalisation in a more coordinated manner, from a legal point of view, this presents a fundamental *methodological issue*, which needs to be resolved and also affects the appropriateness of codification in the civil law manner (through treaty law or, in the EU, possibly through regulation) of private law at the transnational level, especially in its elimination of all other sources of law.

It may be repeated in this connection that the informal formation of transnational law with reference to a number of autonomous sources of law is traditionally more suited to a common law rather than civil law environment; common law being 'bottom up' and going from case to case. If a more formal approach is taken, notably through treaty law, we may on the other hand come closer to the civil law technique, top-down, through an intellectual, government-endorsed framework or system. It has been said before that this appears to be the approach of UNCITRAL and UNIDROIT. Such a system may not easily admit other competing independent sources of law, especially of overarching fundamental principle, custom and general principle, or party autonomy, even if the good faith notion may *indirectly* reintroduce them at least in contract. A more liberal interpretation technique may generally do so in other areas as well, such as, for example, in the structures of movable property, as we shall see in section 1.4.3, although a liberal interpretation technique is traditionally much less common in this area of civil law.

This may all be considered to have a special relevance in the EU where attempts are now being made towards a kind of codification at the transnational level in Europe, in

which connection the 2008–2009 DCFR and the 2011 draft Regulation on a Common European Sales Law (CESL) have already been mentioned. They also cover, by way of their unitary approach, professional dealings (although limited in the CESL to transactions that involve at least one SME), and thus also the areas of international commerce and finance and the operation of the international market place to the extent operating in the EU. The fuller implementation of the DCFR (and CESL) would then also affect its centre in London, and may result in a version of commercial and financial law which is very different from the one that currently obtains there. In the EU, this approach through legislation (treaty law or regulation) would at the same time fundamentally affect and curtail the more informal transnationalisation drive in the modern *lex mercatoria* with its spontaneous revival of the different autonomous transnational sources of law as we shall see.

In the view presented in this book, the new, immanent *lex mercatoria* is preferred for professional dealings and is indeed considered to be substantially based on fundamental and general principles, industry practices or custom, and party autonomy as independent sources of law: see section 1.4 below for a more detailed description of these sources of law. Treaty law (assuming it is widely adopted), although in principle still territorial and limited to activities in contracting states, may also figure, but is then only one of the sources of this law, not the dominant source, and must find its place amongst the others and even if mandatory may yield to a higher mandatory international fundamental principle or public order requirements and mandatory international custom.

This *lex mercatoria* or new transnational law merchant is as a consequence not, or not necessarily, systemic, intellectual and abstract in the traditional civil law codification sense, but may be closer to traditional common law in its development and operation, and not altogether different from public international law and its sources, as they function in the law between states, recognised as such in Article 38(1) of the Statute of the International Court of Justice (ICJ). In recent times, the best operation of this multiple source type of law can be seen in foreign investment arbitral awards, which may represent the most vivid expression of this approach.

As we shall see in section 1.4.13,[30] rather than the formation of one coherent, comprehensive system, the result is a *hierarchy* in these various sources of law that become potentially applicable. Domestic law may still remain the residual rule (although itself then also transnationalised).[31] As we shall also see, this transnational private law is *deferential* to public policy, normally of a domestic regulatory nature including domestic tax and environmental laws, assuming that there is sufficient conduct or effect of the transaction on the territory of the state which wants its policies enforced in this respect in the international transaction in question. This may also be the case for fundamental domestic values and may then be encapsulated in public order requirements.

[30] See also JH Dalhuisen, 'Legal Orders and their Manifestation: The Operation of the International Commercial and Financial Legal Order and its *Lex Mercatoria*' (2006) 24 *Berkeley Journal of International Law* 129 and JH Dalhuisen, 'The Operation of the International Commercial and Financial legal order: The Lex Mercatoria and Its Application' (2008) 19 *European Business Law Review* 985.

[31] See ss 1.4.12–1.4.13ff below. For the residual rule of domestic law in particular, see JH Dalhuisen, 'What could the Selection by Parties of English Law in a Civil Law Contract in Commerce and Finance Truly Mean?' in M Andenas and D Fairgrieve (eds) *Tom Bingham and the Transformation of the Law* (2009) 619.

As the new transnational law itself is private law, as such it does not mean to circumvent relevant domestic public policy of this nature (although between the parties it may still seek to rearrange the risks and financial consequences), and also respects domestic public order requirements as overarching if a sufficiently similar contact can be shown, but it is subject at the same time to the very *transnational* public-order considerations obtaining in the transnational commercial and financial legal order itself from which the modern *lex mercatoria* issues and in which it fundamentally operates.[32] In international transactions, domestic concepts of public order may then increasingly be tested against the concept of transnational public order in terms of internationally accepted *minimum* standards. This is an important development and is then outside the new *lex mercatoria* proper.

In the area of professional dealings, the formation and operation of this transnational private law—a de-nationalised law, shedding its statist and territorial nature—may be considered the natural and unavoidable consequence of globalisation and the internationalisation of the flows of persons, goods, services, knowledge, capital and payments. This is the perspective of this book. It introduces legal structures particularly made for and suited to these international dealings, which need not then be borrowed from local laws.

This transnationalising law between professionals should be *distinguished* in particular from *consumer law*, which remains by its very nature more domestic and protection-oriented, as well as more subject to special domestic (regulatory or policy) concerns. This may have immediate repercussions, for example, in the way concepts of reliance or good faith are applied in contract law. The protection they bring may be less proper and necessary, or may play out very differently for professionals in their international dealings. Relationship thinking thus takes over. As we shall see in section 1.1.4 below and later in Volume II, chapter 2 and Volume III, chapter 1, this may also be relevant for financial structures involving movable assets of professional parties seeking funding in more creative ways internationally, which structures may be much less suitable for consumers domestically.

The distinction between professional and consumer dealings becomes here fundamental (see further section 1.1.8 below): the former being legally increasingly transnationalised, the latter remaining domestic in a legal sense; the former being subject to immanent law creation forces, the latter being essentially regulated and therefore increasingly statutory, based on repeat transactions and need for public protection of weaker participants under national laws.[33] The result is, at least conceptually, an ever-increasing fracturing of the traditional systemic approach of the civil law even domestically according to the *nature of the relationship* of participants. This is a crucial departure in civil law thinking and is more familiar to common law.

[32] In American terms, the issue here is the jurisdiction to prescribe the law in international cases, and depends largely on an analysis of the facts and the circumstances of each case. This is also the approach adopted in Art 9 of the EU Regulation, (EC) No 593/2008 on the Law Applicable to Contractual Obligations, (Rome I) and in a more refined way in the American Restatements (Restatement (Second) of Conflict of Laws, s 6 and Restatement (Third) of Foreign Relations, ss 402–403).

[33] The EU has legislated fairly extensively in the area of consumer law, see n 443 below, and, since the 1992 Maastricht Treaty, considers it a legitimate preoccupation, although the Maastricht Treaty did not give the EU special legislative powers in private law formation. All such powers are still based on, and confined by, the promotion of the internal market. It means that in the consumer area, this is still primarily a question of setting uniform consumer standards to facilitate cross-border business rather than to protect consumers.

It may well be that in the EU, the DCFR with its codification approach and generally more prescriptive statist attitude, is relatively suitable in the area of consumer law from which it comes, and this may also be borne out in the CESL, but its fundamental problem is its lack of distinction in this regard with the result that consumer law concepts and domestic notions of protection in this area constantly spill over into the professional sphere. This is also demonstrated in the CESL and is wholly improper.

It has already been suggested that at least the general attitude in international dealings, therefore in the professional area, is becoming more like that of the traditional common law at least if the move towards a new *lex mercatoria* for these dealings is properly understood. That is not surprising because of the traditionally more pragmatic attitude and gradual approach of the common law to law formation and its bottom-up nature. Common law influence is apparent first in a greater reliance on practices, custom and party autonomy. It is further promoted by the fact that it has always been more result- and practitioner-oriented, is used to operating from case to case, is more sensitive to the facts—and perhaps therefore more used to supporting new business structures and their needs from a legal perspective (and not unduly encumbered by pre-existing legal notions, models or systems) and were comfortable with multiple legal sources.

The common law is in any event not given to confining system thinking, whatever the modern academic tendencies in England. It can therefore look with more confidence to new developments, at least in business. Particularly in equity, it also has a number of facilities such as trusts, floating charges and conditional or temporary proprietary interests that the civil law lacks. In fact, the common law's traditional mistrust of intellectual sophistication (although less so in the US) gives it flexibility, in the US through legal realism, which the civil law may now also need if it wants to progress. It is in any event more called for in the transnationalisation process of private professional law. A further important contributing factor is that the English language has become the lingua franca of the commercial and financial world. Its legal terminology is naturally geared more towards the common law than to any other system.

As already mentioned, the EU idea of codification (if the DCFR may be considered representative) runs counter to these modern developments at the transnational level and remains inspired by the concept of a system-driven unitary set of rules that is statist and territorial, the same in principle for consumers and professionals. It also poses the question of the status of the other sources of law.

In professional dealings, it further excludes the views and needs of all other countries. The USA and Japan, but also modern emerging countries, may have an interest as well and a view on how to proceed at least with regard to commercial and financial transactions which affect or play out on their territories or in which their businesses are involved when operating in the EU. The DCFR approach presents not only a statist but also an inward-looking mentality that seems distrustful of and unfriendly towards international business and the outside world more generally, even in international trade, commerce and finance on which the EU, like others, wholly depends.

In the meantime, it should be noted that there is no demand from practitioners for transnational codification in this formal manner, and that the DCFR and its progeny are driven purely by a particular strand of academic opinion, especially in Germany. Here policy dominates over quality, which compares poorly with what the UCC achieved in the US. In fact, it appears to be mainly an updating effort of the German Civil Code or BGB,

now extended to all dealings within the EU, even if, according to more profound German academic and practitioners opinion, it is as such not of sufficient quality as a new model. See more particularly Volume II, chapter 1, section 1.6 and chapter 2, section 1.11.

As a minimum, such an effort at EU level would appear to require a much more extensive discussion of the true underlying issues and methodology. Earlier, UNIDROIT and UNCITRAL initiatives ran along similar lines, although in narrower areas (including the Vienna Convention on the International Sale of Goods); they were never particularly successful; neither had they been asked for by the business community.[34] In Europe, only the work of the ICC, particularly in Incoterms and UCP,[35] driven by the business community itself, has been a major success. This participation appears to be a key element in more formal law formation efforts of this nature cross-border, at least if the result is to apply to international professional dealings and relationships. It is that participation in the American Law Institute that has made the UCC a success.

1.1.3 The Coverage of Domestic and Transnational Commercial and Financial Law

In commercial and financial law, other differences between the common and civil law approach derive from its coverage. In common law countries, commercial law is traditionally associated with the sale and transportation of goods (which in the English terminology are tangible movable assets only) and with the related shipping or other forms of transportation, insurance, and payment methods and therefore traditionally with the contract for the sale of goods, with specialised trade terms such as FOB and CIF, and with bills of lading, bills of exchange, promissory notes, and other methods of payment. It has already been said, that commercial law in a common law sense still allows for a considerable independence from the general system.

[34] Even the best known of these treaties, the 1980 Vienna Convention on the International Sale of Goods, see vol II, ch 1, s 2.3, although now ratified by 74 countries, has not been accepted by the UK and Brazil, nor by some smaller trading countries such as Portugal. More importantly, it was substantially rejected by the international commercial practice that commonly excludes its application. The UNIDROIT Mobile Equipment Convention (see vol III, ch 1, s 2.1.9) may hold some greater promise and there may also be some reasonable prospect for the UNIDROIT 2009 Geneva Convention on Substantive Rules Regarding Intermediated Securities, see vol II, ch 2, s 3.2.4, but it is altogether not a great harvest.

Again, the reason is probably that UNCITRAL and UNIDROIT seldom managed to respond to true needs, and the results were generally not asked for by commercial practice, nor were they sufficiently pace-setting; rather they were product of compromises between domestic notions, often formulated by academics with insufficient practical knowledge, or by practitioners with an insufficient conceptual grasp of newer developments. This may have applied in particular to the potentially significant 2001 UNCITRAL Convention on the Assignment of Receivables in International Trade. It provided an important opportunity to move forward, but in the end proved a disappointment. See vol II, ch 2, s 1.5.13 and vol III, s 2.4.5ff.

In practice, more important were the UNCITRAL Model Law on International Commercial Arbitration (1985) and the UNCITRAL Model Law on Cross-border Insolvency (1997). Perhaps the greater success of these model laws derived from the fact that they did not mean to impose a uniform system but were content with more modest forms of harmonisation. They did not seek to impose from above through treaty law but were rather meant to guide domestic reform legislation.

[35] See text preceding n 337 below.

Thus certain features of the ordinary common law of contract, such as the concept of consideration, never affected the agreement to transfer negotiable instruments, implemented through delivery or endorsement. Also, contrary to the more normal *nemo dat* rule, bona fide purchasers or holders of these instruments are generally protected. Indeed, this type of protection is better supported in commercial law than in the rest of the common law (equity excepted),[36] and underscores the point that integration between common law and commercial law does not fully exist in common law countries.

Commercial law in a common law sense is then likely to cover the entire area, that is to say the *contractual* as well as *proprietary* aspects of the trade in goods, therefore also the transfer of ownership and any secured interests in these assets, for example to protect payment or raise finance, and the protection of bona fide purchasers as a matter of transactional finality. Thus in common law, the transfer of property in goods is seen as essentially a commercial law issue and not as a matter that is dealt with primarily by a general system of property law (on which the common law traditionally lays less stress anyway).

This has led to a tendency to treat the *entire* law of chattels and intangible assets as a distinct commercial law matter within the common law. This more fractured approach to property law is also borne out by the operation of equitable proprietary interests as more incidental rights, which in commercial and financial law is especially relevant in the area of asset-backed financing, leading in movable property to floating charges, conditional or temporary ownership rights, and in the area of the assignment and payment of receivables to bulk assignments of present and future claims, and in the payment area to liberal set-off and netting facilities as we have seen.[37]

In fact, it has already been noted that in common law countries important features of commercial law derive from equity, a facility civil law crucially missed. Indeed, it suggests a more incidental approach and brings with it greater judicial discretion, activism and direction, especially in trust, company and bankruptcy law, even though this law is now largely statutory. Equity in this manner conferred a flexibility on commercial law that is still important and might otherwise have been lost in common law countries as well.

[36] Sale of goods, transportation and insurance law, considered the typical commercial law subjects in common law, developed from the trade between England and the European Continent and acquired some distinguishing features from that contact, in which there may still be some faint remnants of a Roman law orientation. As the common law mainly developed in connection with land law, it at first possessed more scope for the persuasive force of other law in these commercial areas. In fact, the treatment of the sale of goods, transportation and insurance as especially defined contract types was itself due to continental influence: traditionally the common law does not define different types of contract and does not endow each with its own special contractual regime.

Interestingly, English maritime law developed in this way the continental concept of the ship master based on the *patria potestas* of Roman law. However, as we have seen, this history no longer sets maritime contracts and maritime concepts apart as commercial law on the European Continent. In fact, in the nineteenth and twentieth centuries, these areas of law developed more strongly and separately in England as a trading nation than they did on the European Continent.

[37] It should be noted that in England, commercial law as such is also referred to as trade law. There is a terminology issue here within the common law family. In the US, trade law is first and foremost associated with tariffs and international trade restrictions and agreements, now centred on the operation of the World Trade Organization (WTO). The result is that trade law in English terms is private law and therefore more properly part of commercial and financial law, but it is in American terms rather public or regulatory law and thus the result of governmental involvement and international arrangements between states designed to facilitate trade or investments.

In civil law, the coverage of commercial law is traditionally different, being much broader in one way and narrower in another. It is broader in that it is not unusual, for example, to find company law and insolvency law and much of financial law and therefore also services, covered by commercial law. This is especially the case in the French tradition, which is more service- than sales-oriented. But the civil law notion of commercial law is also narrower, as its coverage is only partial, as already mentioned in terms of *lex specialis*, and major topics in the commercial law area remain part of the general law or legal system.

This particularly concerns the proprietary aspects (such as transfer of ownership in goods and investments and the creation of any security interests therein, even if connected with the sale of goods) and their operation in bankruptcy, and brings with it the civil law restriction to only a small number of internally closely connected property rights (the *numerus clausus* notion of proprietary right). But it also concerns the general notions of contract law and of partnerships and even corporate associations, which in the commercial law area are equally derived from the general private law system.

If we accept for the moment globalising or transnationalising forces in the private law, especially in commerce and finance and thus in professional dealings, in the manner as discussed in the previous sections, and then turn to what may now be considered more particularly *transnational* substantive commercial and financial law or the new law merchant or modern *lex mercatoria*, we see that not only in as far as method (see previous section) but also in as far as *coverage* is concerned, the common law approach provides the starting point.

This means that the sale of goods, or rather the operation of international market place especially in commoditised goods or physical movable assets remains central, as is demonstrated by the 1980 Vienna Convention on the International Sale of Goods (CISG) and by the other work of the United Nations Commission for International Trade Law (UNCITRAL), whatever its success, particularly in the areas of bills of lading, negotiable instruments, payments and receivables financing. It is also evident in the area of shipping and maritime law. In other words, this new law is primarily oriented towards the international market place.

While the *sale of goods* and the operation of the international market are thus the major starting points of transnational commercial law, it is also true that more recently *financing* and *financial instruments* have become an important part of transnational law and are increasingly driving it. Here we also move into the coverage of certain classes of intangible assets such as receivables. Euromarket products and practices are here especially indicative[38] but no less relevant are transnationalised assignment, payment, set-off and netting notions. Although the international market place remains here at the centre of developments, there is also an important move towards *services*, and therefore towards the French commercial law tradition. This suggests a broadening approach in terms of coverage, but also confirms a more incidental approach in terms of products.

There is here a clear shift, partly because the typical older mercantile function of commercial law instruments, like bills of lading and negotiable instruments, are losing much of their importance in trading environments that are increasingly paperless and electronic,

[38] See, for the autonomy of the international capital markets and for the operation of the eurobonds market vol III, ch 2, ss 2.1.1–2.1.2.

and that are, especially for payments and investment securities, closely connected with clearing, settlement and netting notions, now more commonly the subject of financial law as we shall see in Volume III.

Thus, in so far as shares and bonds are concerned, the traditional (bearer and other) investment securities are increasingly being replaced by securities entitlements in paperless book-entry systems, see Volume II, chapter 2, section 3.1, and are no longer transferred through physical delivery but rather through a system of debits and credits in securities accounts, a system that resembles to a large extent modern payments through bank transfers which move here to the centre and will be extensively discussed in Volume III, chapter 1, section 3.1. Even domestically, the greater impact of modern finance on commercial law is increasingly clear. In this connection, it may be noted that the direction of modern company law development in both common and civil law is also in the same financial (capital markets and corporate finance) direction.

These developments explain why this book pays close attention to financial products and services including their regulation, to the financial markets and their operation, and to the creation of ever-more sophisticated financial instruments and payment facilities internationally that have not only affected and transnationalised the way capital is raised (particularly in the eurobond markets) and payments are made, but also the manner in which investments are held, transferred and protected. This is the subject of Volume III.

It is clear that in this updated realm of international commerce and finance, the more important features of the new transnational law or modern *lex mercatoria* can no longer be predominantly the law of the sale of goods and related laws concerning commodity trading and shipping or indeed the merchant law. Financial law becomes here the core of commercial law. As already mentioned, this also means a move in the direction of services and ever newer proprietary structures especially in asset backed financing, including those using intangible assets, notably receivables.

1.1.4 Legal Dynamism as a Key Notion in Transnational Commercial and Financial Law. Law as a Dynamic Concept in Modern Contract and Movable Property

In fact, more important than its precise coverage, is the nature of this new professional law which is dynamic. Indeed, through its different sources, method and coverage, another significant aspect of this new transnational commercial and financial law, or new *lex mercatoria*, is that it embraces a more *dynamic concept* of law that operates, it is submitted, around a more objective but also more powerful concept of *party autonomy* that is itself transnationalised when operating amongst professionals and is here an original source of law.[39]

This modern 'privatisation' of private law at the transnational level is thus particularly connected with a reinforcement and extension of party autonomy in the international

[39] See for this concept and its autonomy s 1.4.9 below.

market place, which may subsequently fold into practices commonly accepted amongst professionals in their business, an approach that was largely lost in civil law countries when commercial and financial law was domesticated and incorporated into more formal and intellectual local legal frameworks that were mostly statutory. It has already been pointed out in the previous section that this more modern transnational attitude combines a more dynamic approach to law formation, which recognises different sources of law, with a more pragmatic approach to coverage, although it remains centred on the operation of the international market place now extended in the direction of international finance and professional services more generally.

In the law of personal or movable property, stronger party autonomy at the transnational level may do away with the civil law notion of a limited number of proprietary rights (the idea of the *numerus clausus*).[40] To the uninitiated, it might seem extraordinary that parties may in this way expand their rights against third parties, who in the nature of all proprietary rights would have to respect them, but it is less objectionable where there is a stronger protection of bona fide purchasers at the same time (as there always was in the common law approach in equity which has this flexibility) or even of purchasers in the ordinary course of business of commoditised products (who need not then be bona fide and in any event do not have a search duty). Proprietary rights are

[40] As will be discussed more extensively in vol II, ch 2 and vol III, ch 1, s 1.1.9, civil law has traditionally been opposed to an open system of proprietary rights, sees this as a public policy issue, and recognises only a limited number of these rights. This is the notion of the *numerus clausus* of proprietary rights that, however, has only operated since the nineteenth century and was formulated and discovered not much before the seventeenth century as we shall see. It goes into the fundamental distinction between the law of property and obligations in civil law at the level of the system.

In equity, in common law countries, the system is in essence open, important in modern finance especially in the law of chattels and intangibles. It means that third parties must respect the rights so created and acquire the assets as transferees subject to the rights of others, but only to the extent that they knew of them. It follows that in that (equitable) system, bona fide purchasers or assignees are generally protected. This is now commonly extended to transferees of commoditised products acquired in the ordinary course of business. There is here no search duty either, except for insiders such as banks and professional suppliers who should and can know better.

This means that the ordinary commercial flows are always protected against this type of proprietary interests which cannot be traced in them. A more open system of proprietary rights in this manner, allows for stronger risk management tools amongst insiders as we shall see.

Surprisingly, the idea of a *numerus clausus* of proprietary rights is now sometimes also advocated for common law by proponents of the law and economics school which favour standardisation; see TM Merrill and HE Smith, 'Optimal Standardization in the Law of Property: The *Numerus Clausus* Principle' (2000) 110 *Yale Law Journal* 1; see also H Hansman and R Kraakman, 'Property, Contract, and Verification: The *Numerus Clausus* Problem and The Divisibility of Rights' (2002) 31 *Journal of Legal Studies* 373. See for common law writers on the subject of the *numerus clausus*, B Rudden, 'Economic Theory v Property Law: The *Numerus Clausus* Problem' in *Oxford Essays in Jurisprudence*, 3rd Series (1987) 239. See further A Fusaro, 'The *Numerus Clausus* of Property Rights' in E Cooke (ed), *Modern Studies in Property Law, vol 1 Property 2000* (2001) 307.

As we shall see, it denies the strong risk management element inherent in party autonomy in the creation of (equitable) proprietary rights in modern finance, particularly in new forms of asset backed funding. Nevertheless, there is increasingly strong evidence of a more flexible use of proprietary rights in international finance. For the idea of contractualisation of proprietary rights in common law, see JH Langbein, 'The Contractarian Basis of the Law of Trusts' (1995) 105 *Yale Law Journal* 624; see further vol II, ch 2, s 1.10.

It may be noted in this respect that German case law opened up the system through its concept of floating charge or *Sicherungsuebereignung*, see vol III, ch 1, s 1.4, and at one stage also went the way of recognising proprietary expectancies or conditional ownership rights (or the *dingliche Anwartschaft*), see BGH, 22 February 1956, BGHZ 20, 88, although this important concept was not developed further and remains largely confined to the area of reservation of title; as it does in the Netherlands, see vol III, ch 1, s 1.2. An insufficient insight into the nature of the commercial flows and fear of breaking the *numerus clausus* notion (which is itself not expressed in the BGB) were here important contributing factors.

here not cut off at their creation but only at the level of their operation; see further the discussion in Volume II, chapter 2, section 1.10.

This may be considered as increasingly customary in professional circles and reflects equity in a common law sense. That suggests first a strong but also more objective notion of party autonomy in this area. Not everything goes and transnational public order restrictions may impose themselves, but there is the legitimisation through evolving transnational practice. Public order in particular protects here the *commercial flows* in the international market place against the effects thereon of greater freedom in the creation of proprietary rights. To repeat, they then only operate amongst a group of professional insiders such as banks and suppliers who are or become used to these newer techniques. The ordinary course of business is thus freed from the impact of adverse interests so created.

That is a crucial departure and denotes the limit of greater party autonomy in this area allowing property law nevertheless to become a *prime risk management tool*, especially clear in asset-backed funding where floating charges and conditional or temporary ownership rights freely operate side by side and next to more traditional security interests. It is indeed submitted that this is becoming a key facility in the modernisation of personal or movable property law at the transnational level. See again more particularly, Volume II, chapter 2, section 1.10.

If one keeps in mind the autonomous development of negotiable instruments and documents of title in the older *lex mercatoria*, this more modern development related to the operation of the international marketplace and its proprietary structures may be less surprising. It is now more especially relevant in modern financial transactions, even at the domestic level. In civil law countries, this is generally not yet identified and analysed, although it is even now sometimes found in the area of finance leasing and repo financing and in the area of receivables and their transfer, and in the interests[41] that may be created in them.[42]

[41] For assignments of receivables, greater latitude is now sometimes assumed in civil law, and parties might at least be able contractually to choose different domestic laws of assignment. See the discussion in vol II, ch 2, s 1.9.2 and vol III, ch 1, s 1.1.10.

In Dutch case law, for example, in proprietary aspects of assignments, the law of the underlying claim and in other cases the law of the assignment have sometimes been upheld as applicable following Art 12(1) and (2) of the 1980 Rome Convention on the Law Applicable to Contractual Obligations, now Art 14(1) and (2) of the 2008 EU Regulation (EC) No 593/2008 on the Law Applicable to Contractual Obligations (Rome I), rather than on the law of the debtor or that of the assignor. See for the legal nature of finance leasing, vol III, ch 1, s 2.4, and of repo financing, s 4.2.

[42] See for the bona fides requirement in England allowing the collecting younger assignee to retain its collections, which was only implicit in *Dearle v Hall* (1828) 3 Russ 1, *Rhodes v Allied Dunbar Pension Services Ltd* [1987] 1 WLR 1703. There is no investigation duty and acquiring knowledge of the earlier assignment after the second assignment but before notice is given thereunder is irrelevant for the entitlement to the collection. If there is a registered charge, there may be constructive or implied notice, although this is not automatically the case in England and in particular does not apply to any restrictive assignment covenants in a floating charge as these covenants need no filing. See further vol III, ch 1, s 1.5.9.

In this connection, it should be noted that especially the English equity rule protecting the first *collecting bona fide* assignee is not proposed to be adopted in the DCFR (it protects the bona fide assignee but forgets to require collection, see Art III-5:121 (1)), which would appear to be the necessary corollary of a more open system of assignment, see vol II, ch 2, s 1.11.3.

The 2001 UNCITRAL Convention on the Assignment of Receivables in International Trade suffered here from a lack of conceptual clarity and innovative spirit, see vol III, ch 1, s 2.4.5ff, which led to its failure. Its main problem is that it could not assimilate the receivable with the promissory note. The measure to which this is done determines the success of conventions of this nature. *cf* also s 2-110 UCC in the US.

Its major achievement was nevertheless a liberal identification requirement, which allowed the inclusion of future claims, but *major shortcomings* of the Convention were in its failure (not immediately clear from Art 8) to

For assets located in different countries, the technique is increasingly to locate them all at the place of the owner, now already often favoured for receivables, so that they can be transferred in bulk under one regime. That is important but may still suggest the application of a (reformed) national law although subject to fundamental adjustment of more traditional conflicts of law notions (here the *lex situs* rule for the applicable property rules). It still requires recognition of such interests at the place of their location or collection, however. In a more advanced legal environment, the owner's law could be transnationalised or formulated by the parties at the transnational level regardless of location in the manner just explained,[43] again subject to proper protection of the commercial flows as a public order requirement of the transnational commercial and financial legal order itself. This would result in an informal uniform regime, applicable everywhere, including in local bankruptcies.

It is the force of transnational practice that makes the difference here whilst imposing its own logic, ultimately entering, as we shall see, domestic legal regimes, even in bankruptcy where it is especially important, in this area buffeted by evolving *mandatory* transnational custom and general principle,[44] or even by the transnational public order itself.

provide for a uniform notification regime (or its waiver) and in its documentation or formalities regime (or their waiver). This was unfortunate, especially in the context of bulk assignments, all the more so as under Art 27 it is unclear which local law might be applicable. The reliance in these aspects on domestic law destroyed any notion of an international bulk assignment which was the true focus of the Convention. The DCFR also deals with the subject but does not manage to move it forward either, especially because of its lack of insight into the asset nature of claims and the operation and significance of bulk assignments.

Closely related was the UNCITRAL Convention's failure to establish a uniform regime for priorities. It concerns here the right of the assignee in the receivables over the right of a competing claimant. Instead, the Convention refers the matter to the law of the assignor (Arts 22 and 30), or leaves it to the Contracting States to opt for one of the systems set out in the Annex to the Convention (Art 42). Inspired by the UCC filing system, the Annex itself prefers a system based on registration of an assignment (Arts 1ff of the Annex). But states may also opt for a *prior tempore* rule based on the time of the contract of assignment (Arts 6ff of the Annex), which conforms to the German approach. Finally, they may also opt for a priority rule based on the time of the notification of the assignment (Arts 9ff of the Annex), which is wholly unconducive to bulk assignments and rather reflects old French law.

[43] See for receivables, n 42 above. See for this technique more generally vol III, ch 1, s 1.1.10.

[44] Indeed, the final test of such newer (prospectively internationalised) proprietary structures is in bankruptcy. Precisely because bankruptcy has hitherto been purely a matter of domestic law, this area is likely to encounter the greatest problems with transnationalised property rights and other new structures.

The idea of autonomy requires that in this area too, transnational law must increasingly demand recognition in domestic bankruptcy courts as customary law. In an earlier work, I dealt extensively with international bankruptcy from the perspective of recognition and enforcement in other countries and the internationalisation of concepts that exist in that connection, see *Dalhuisen on International Insolvency and Bankruptcy*, vol I (1986) 3.266.3ff. I shall revert to this in a fourth volume to this series.

Note in this connection also the Australian (Victoria) cases in *IATA v Ansett* [2005] VSC 113, [2006] VSCA 242, and [2008] HCA38, in which the Australian High Court ultimately accepted that, at least in a non-financial CCP (central counterparty, see also vol III, ch 1, s 2.6.4) in respect of mutual airline claims resulting from passenger cancellations and ticket changes, this transnational form of clearing and settlement and set-off trumped the Australian bankruptcy laws. This was and important precedent, see further C Chamorro-Courtland, "The Legal Aspects of Non-Financial Market Central Counter Parties", (2012) 27.4 *Banking and Finance Law Review*, and an advance notably on *British Eagle International Airlines Ltd v Compagnie Nationale Air France* [1975] 2 All ER 390, discussed in vol III, ch 1, s 3.2.3 in connection with novation netting and its limitations in bankruptcy in England.

In the meantime international bankruptcy principles are developing and are being written down. See IMF, *Orderly & Effective Insolvency Procedures* (1999) and World Bank, *Principles and Guidelines for Effective Insolvency and Creditors Rights Systems* May 2001 available at www.worldbank.org/ifa/ipg_eng.pdf. For another compilation, see also Koopman *et al* (eds), *Principles of European Insolvency Law* (2003).

If we concentrate on transnational commercial and financial law, we may note that a more diverse and fractured system of proprietary rights is evolving at that level, with different proprietary notions for different areas of the law or for different (financial) products and this system may eventually also be followed or recognised domestically in terms of transnational practice or custom. Again, it assumes and confirms a higher degree of party autonomy, even in proprietary matters, but it may also be more objective, that is, fenced in by the practices evolving at that level and the need of protection of the commercial flows as a transnational public order requirement.

This may affect in particular modern forms of (electronic) payment, securities entitlements and their transfer; the treatment of conditional and temporary ownership rights in finance leases and repurchase agreements; the (bulk) assignment of payment obligations, receivables financing and securitisations; the development of security interests in the form of non-possessory floating charges; the notion of agency (and the transfer of ownership in indirect or undisclosed agency); the evolution of fiduciary duties; and the important principle of segregation of assets in formal, resulting or constructive trusts and the facility of tracing. In this connection no less important are the modern notions of set-off and netting.

To repeat, one recognises here transnationally the innovative pull and challenge of *equity* in a common law sense, where, because civil law did not have this facility, the greatest differences between common and civil law resulted. It will be discussed more extensively in Volume II, chapter 2, section 1.3.1. Domestically, the more incidental and fractured attitude to proprietary rights and the absence of systemic thinking in this area have in more modern times been fundamentally supported by the different chapters or Articles of the UCC in the US, which are often particularly enlightening in these areas.

The French alone amongst major civil law countries, in their *Code Monetaire et Financier* of 1999 show here, largely for financial services purposes, a willingness to adjust. In the process they also acquired a level of comfort with different proprietary structures for different financial products leading to significant innovations in France in the laws concerning repos, securitisations, assignments and reservation of title, whilst in the French *Code Civil*, through more recent amendment, floating charges and trust structures have also been introduced. However, French law, although having become pragmatic in these areas,[45] still lacks the detail and also a clear academic support as to what

However, their usefulness will be limited if they do not manage to deal with the very concepts of proprietary or priority/separation or segregation rights, and their operation and acceptance in the international sphere. The same applies to the modern set-off and netting facilities in terms of preferences as we shall see in vol III, ch 1, s 3.2.7.

[45] See vol III, ch 1, s 1.3. The French, at least in commerce and finance, ultimately proved to be pragmatic by introducing in the last 25 years through amendments to their Bankruptcy Act, amendments to their *Code Civil* (CC), and the introduction of a new Monetary and Financial Code (CMF). It resulted in the following facilities: (1) the *reservation of title*, now in Arts 2367–2372 of the French CC (*Ordonnance* no 2006–346 of 23 March 2006) as a true payment protection devise (abandoning in the process the fundamental concept of '*solvabilite apparente*', see vol III, ch 1, s 1.1.9); (2) the *bulk assignment* for financial purposes (*Loi Dailly*) now in Arts L 313-23–L 313-35 CMF; (3) *securitisation* or *titrisation* through the creation or facilitation of *fonds communs de créances* (FCCs), now contained in Arts L 214-43–L 214-49 CMF; (4) *repos* or *pension livree* in Arts L 432-12–L 432-19 CMF; (5) *finance leases* (already earlier regulated by Law 66-455 of 2 July 1966 on the *credit-bail*), now in Arts L 313-7–L 313-11 CMF; (6) the *floating charge* since 2006 in Arts 2333–2366 CC, *Ordonnance* no 2006-346 *relative aux Sûretés* of 23 March 2006, see also *Rapport au Président de la République relative à l'ordonnance no 2006–346 du 23 Mars 2006 relative aux Sûretés*, JO no 71 of March 24 2006 (it was followed by a short Decree No 2007–404 of 22

is necessary to make such a system operate, notably in terms of party autonomy and the protection of the commercial flows.[46] Rather, it still captures these newer developments in static laws or formal legislation, not merely in a facilitating manner but in a limited and prescriptive way.

These adjustments are basically pragmatic and an instant reply to market pressure, also in terms of Paris keeping up with London as an international financial centre, and they are not necessarily more fundamental in terms of a new paradigm in respect of the system of private law property rights as a whole. They are nevertheless important indications of a less dogmatic approach in civil law. It should be noted in this respect that the Germans have made no such attempt so far, mainly for fear of destroying the unity of their system. This also transfers into the DCFR, which maintains a similar unworldly approach and even tries to undo whatever case law had achieved in Germany in terms of floating charges and bulk transfers of future (replacement) assets as we shall see.

Conceptually, at least at the transnational level, the result of newer thinking in this area is a more dynamic law of movable property in modern transnational commercial and financial dealings. However, legal dynamism and a less static approach to private law and its rules are *not* confined to personal property and are at least as necessary and demonstrable in *contract* law, where so far the modern notion of good faith has been used in major civil law countries domestically to create greater flexibility, behind which even other sources of law may re-emerge. That is likely to become ever more apparent at the transnational level, it is submitted, where in this area there are no pre-conceived system constraints either. Even pressing moral, social and especially efficiency considerations may then find readier acceptance in a more modern interpretation technique. That is indicative, although these considerations, except those concerning efficiency, may not always be highly relevant in international trade, commerce and finance and in any event may not always give more protection. It may even give less, as we shall see.

But a truly dynamic concept of contract law goes further and is more fundamental. One may think here especially of the infrastructure of modern contract requiring a more dynamic approach to contract formation, during which, depending on the phase of the negotiations,

March 2007 concerning some aspects of real estate mortgages); and now even (7) the *trust* or *fiducie* since 2007 in Arts 2011–2031 CC. See also P Matthews, 'The French Fiducie: and now for something completely different?' (2007) 22 *Trust Law International* 1.

It was followed in 2009 by the introduction of (8) the *fiducie-surete*, in Arts 2372-1–2372-6 (*mobiliere*) and Arts 2488-1–2488-6 (*immobiliere*) CC. It allows the setting apart of property with a trustee for the benefit of funding parties subject to the conditions of the arrangement. Appropriation is possible as an alternative to security interests, still subject, however, to the return of any overvalue but in the case of natural persons only, Art 2372-3 CC.

The introduction of these new facilities completely destroyed any idea of one system of proprietary rights in France (although this author is not aware of any study explaining the impact on the *Code Civil* and its proprietary system), whose 200-year anniversary was nonetheless celebrated in some style in 2004. Under the circumstances, one wondered why.

[46] No less 'damage' to traditional civil law system thinking in this area came with the EU Collateral Directive, see vol III, ch 1, s 1.1.8, which pulled the rug from under most Continental orthodoxy in the law of personal property in the context of finance. The Dutch and Germans were no longer able to integrate it into their 'systems' and the Directive's contents figure as a special section to their Codes.

pre-contractual duties emerge and parties assume steadily increasing obligations. They no longer depend on a ritual kind of mating dance in the offer and acceptance language, traditionally resulting in a fixed moment of contract formation.[47] This more recent approach accepts a progression in commitment during the entire contract period,[48] in which conduct and reliance,[49]

[47] As to the more traditional offer and acceptance notion, it is seldom recognised that it is relatively recent. On the European Continent, the natural law school of Grotius and Pufendorf in the seventeenth and eighteenth centuries had completed the theoretical structure of the law of contract based on consensus as we know it today in civil law. See Grotius, *De Iure Belli ac Pacis*, Lib II, Cap XI, iv.1, emphasising the mutuality of promises rather than the consensus idea itself or the more modern model and process of offer and acceptance, but *cf* also Cap XI, xiv and his *Inleidinge* or *Jurisprudence of Holland* (RW Lee trl 1953) III.10, where Grotius noted that by contract we mean a voluntary act whereby the one party promises something to the other with the intention that the other party should accept it and thereby acquire a right against the first party. *cf* also Pufendorf, *De Iure Naturae et Gentium* 1674, Lib III, Cap IV, s 2.7.

This resulted in the general applicability of the famous maxim *pacta sunt servanda*, itself derived from the early Canon law heading of the relevant chapter in the *Decretales* of Pope Gregory IX of 1234 which had been at the beginning of this development ('*Pacta quantumque nuda servanda sunt*'). Through the seventeenth-century works of the French jurist Domat, *Les Lois Civiles dans leur Ordre Naturel, Livre I Introduction* (Paris, 1777), the concept of consensus entered the French Codes.

One key is that it captured the contract and the rights and obligations arising thereunder at the moment of its formation, the determination of which then became a separate but prime issue. The other great French jurist, Pothier, formulated the notion of offer and acceptance in the eighteenth century more precisely, see *Traité des Obligations*, no 4, although the question of acceptance had already been raised by Bartolus in connection with the use of agents: *Commentaria* D.15.4.1.3. Only in the nineteenth century, was this insight described in terms of the will of the parties, see vol II, ch 1, s 1.2.1 which led to more refined offer and acceptance theories.

In common law, as we shall see in vol II, ch 1, s 1.2.2, there is no similar emphasis on consensus or a meeting of minds and the parties' will or intent relates there rather to the individual promises they make. In common law, it is the more objective doctrine of consideration, which is the notion of exchange or bargain (or sometimes the notion of sufficient reason), that still provides the main basis for the validity of contracts. Offer and acceptance language dates here only from the nineteenth century, imported from the Continent.

[48] It means amongst other things that the moment a contract is concluded or formed may not be as clear as it used to be and the conclusion may show a progression. More formal notions of offer and acceptance also recede into the background, both in common and civil law, replaced as they are by a longer drawn out negotiation or formation process especially in respect of larger duration contracts. Rights and obligations appear here more gradually, depending on the stage reached in the negotiations.

A closely related aspect is the credit that must now more generally be given to the *raising of expectations* and any *detrimental reliance* on them by others. It is also clear that the way one party chooses to *organise* itself may itself give rise to these expectations. Thus the buying of a ticket on the bus and the purchase of groceries in a supermarket can often best be explained by reliance on the organisation that the seller of these service or of the goods has put in place and the choice and selection power that is in this manner given to the buyer rather than in terms of offer and acceptance or of bargain and consensus. The way the seller has *organised* itself in these situations does not, for example, allow the ticket seller or cash attendant discretion in refusing the travel service or the taking away of the groceries if the correct price is offered unless there are special reasons which the ticket seller or cash attendant would then have the burden of explaining. Intent of the ticket seller or cash attendant is here largely irrelevant.

It more generally poses the question of when reliance by others becomes justified and starts binding that party having given rise to the expectation. This will often depend on the circumstances and is therefore a factual issue, in which the type of parties may be significant and a beginning of performance may be required.

[49] Indeed, in the newer approaches, *reliance* on reasonable expectations (which again suggests the relevance of the circumstances and type of parties), is the basic issue in *contract formation* and its timing, whilst *culpable breach of reasonable expectations and duties* is the prime ground for actions for damages. It is clear that such actions may then be more closely related to tort than to more traditional, subjective concepts of contract. Conduct and reliance become here key in terms of contract formation and are themselves dynamic in determining the emerging rights and obligations of the parties and therefore the content of their contract. They do not merely operate besides offer and acceptance, but the latter become a subcategory of the former.

disclosure duties,[50] a beginning of performance,[51] and acceptance of risk of future developments[52] also figure.[53]

It is possible to move even further and put the whole emphasis (not just in terms of formation) on justified expectations, detrimental reliance, duties of care and co-operation, of disclosure, investigation and loyalty, and on the contractual purpose and consider them to be the basic source and *essence* of modern contractual rights and obligations, *only the details* of which would then depend on the more specific objectives of the parties. At least professionals may be able to do that. In this connection, they may also insist on a more literal interpretation of their contract if not already implied in a good faith approach, especially where the contract functions as a road map and risk management tool between them.[54]

This newer contractual approach or model will be discussed more extensively under modern contract theory in Volume II, chapter 1. It involves a process of *objectivation* of norms in which in a largely corporate modern environment traditional will theories and

[50] In later phases of the contract too, new rights and obligations emerge, although, as for pre-contractual disclosure duties, perhaps less between professionals than between professionals and weaker unsuspecting parties. The European and UNIDROIT Contract Principles simply accept consumer notions and do not distinguish between consumer and professional dealings. That is also the basic approach of the DCFR, see more particularly vol II, ch 1, s 1.6.

As for these contractual negotiation duties, see vol II, ch 1, ss 1.3.12ff. Modern contract theory differentiating between the types of parties in this instance may explain the English case *Walford v Miles* [1992] 2 WLR 174, and the denial in it of the duties of pre-contractual negotiation and co-operation between professionals, although it did not rule out claims in negligence for costs incurred unnecessarily.

[51] In particular, reliance might need a response in some *beginning of performance* by the relying party and cannot be merely in the mind or on a piece of paper. It is an aspect of reliance having to be detrimental. See for this requirement PS Atiyah, 'Contract, Promises and the Law of Obligations' (1978) *LQR* 193. In the early *droit coutumier* in France, where the promise itself became binding, this extra requirement (besides that of a lawful cause) was not unknown either, at least in the law of sales. See A Esmein, *Etudes sur les contrats dans les tres ancien droit francais* 5, 29 (1883). The codification dropped it and may therefore be considered to have a lesser requirement for contract enforceability than the immanent transnational law may have.

[52] Another key modern insight is that *entering into a relationship* of whatever nature implies acceptance of much of what follows and for which one may not have bargained, and in any event much may happen which could not have been foreseen. That is risk acceptance. When signing a contract, parties thus take a risk which may be considerable especially between professionals. It will not give them a way out of the contract on the mere basis of lack of original intent except in extreme cases (when holding a party to the contract would become manifestly unreasonable). In such relationships, much unknown risk must be considered discounted. See further vol II, ch 1, s 1.3.14. Any detriment falls where it falls and that must be accepted as a risk one took.

The European and UNIDROIT Contract Principles and DCFR appear to be little aware of this and the Vienna Convention in Art 79 only operates with a broadened *force majeure* concept, which, as it concerns here professional sales, may, still have to be interpreted narrowly.

[53] Yet another aspect of modern contract theory is the importance of the *demonstrable contractual purpose* in determining the contract's content and effect, again as some objective standard regardless of what the original intent of one of the parties may or may not have been. This is the essence of *teleological* interpretation.

[54] As we have seen, in a more objective contract interpretation, parties may also face pressing external *ethical, social and efficiency* standards in the implementation of their transaction, although the impact will again depend on the situation, including the type of parties and taking into account the standards they may have set amongst themselves. This is sometimes called the *normative* interpretation technique which goes well beyond a mere teleological one.

The term 'normative' when used in this connection, does not refer to any ideal type or to ethical aspirations per se, as it usually is in the positivist tradition, but rather refers to to legally or objectively binding considerations or correctives which may have an extralegal origin in moral, social, cultural or economic considerations. It could also simply relate to rationality or common sense. Again, it is more than a merely purposive or teleological interpretation, which looks for the objective of the agreement in terms of its interpretation (although this is also important in this context). See also s 1.2.14 below.

an anthropomorphic attitude to private law[55] and to contract formation in particular are abandoned, and at least duration contracts may be seen as a form of partnership or a framework in which new obligations emerge in a continuous process of law formation that is not solely guided by the parties' will at a fixed moment in time but rather by conduct, reliance and acceptance of risk, especially of ever changing circumstances. It may still give rise to post-contractual renegotiation duties, although in professional dealings, short of a contractual hardship clause, only when the risk of new developments becomes manifestly unreasonable for one party to bear,[56] which in professional dealings is not likely to occur soon.

It has already been said that good faith but also market practices now often operate as a front behind which legal dynamism is rekindled, at least in contract. A liberal interpretation technique is soon accompanied by the revival of other autonomous sources of law.[57] Good faith case law can often be analysed in this manner in civil law countries[58] and the more

[55] The strong emphasis on the will is a typical nineteenth-century Continental European idea, connected with romantic philosophy, and suggests a thoroughly anthropomorphic attitude to contract law that is now out of place for professional dealings in a largely corporate environment. See also n 196 below. See for the more modern idea of party autonomy and present day meaning and operation, s 4.9 below.

[56] In the case of hardship due to intervening unforeseeable, unavoidable and undiscounted circumstances, re-negotiations may be sought under the UNIDROIT Contract Principles (written for professional contracts) as soon as the contractual equilibrium is disturbed, whilst there need not even be severe financial consequences (Art 6.2). This is hard for professionals to understand. One may wonder whether this rule is also considered to be related to good faith and therefore mandatory. Again this could at most be so in clear cases. This is consumer thinking. At least the DCFR avoids good faith language, Art III.-1:110.

In a similar vein, surprising (standard) terms must be expressly accepted even amongst professionals (Art 2.19), whilst Arts 7.1.6 and 7.4.13 limit their freedom with respect to exemption clauses and agreements to pay fixed sums for non-performance. These rules also seem to be mandatory amongst professionals. This is also the attitude in the DCFR. The question is why? Who needs protection here, and against what? See further vol II, ch 2, s 1.6.

[57] In countries such as Germany, Austria, Switzerland and the Netherlands, in contract law, the modern, more dynamic approach is now closely associated with the good faith notion in the interpretation and supplementation of contracts. In its extreme form, it may even lead to contractual adjustments on the basis of what may be considered fair and reasonable in objective terms, or even rational and common sense, or what may be required in a social sense in terms of (re-)distribution or is morally demanded in an advanced society. In Germany in particular, that plays a role in terms of pre-contractual disclosure duties as it had earlier in the case of profound changes of circumstances. This has been an area of statutory law since 2002. The problem is that consumer law thinking quickly spills over into professional dealings. This is also true of the DCFR as we shall see.

[58] Although in civil law, the notion of good faith is often considered just one (other, open but mandatory) norm that supplements the codes (but is only in interpretation authorised by them to do so), it has in truth acquired a *multifaceted* character and is by no means always mandatory. It (a) supplements the contract; but may sometimes (b) also derogate from it if the result would be manifestly unreasonable; (c) may activate other sources of law; and (d) stretches existing norms to new situations by selecting new facts as being legally relevant.

In operating in these ways, 'good faith' is sometimes judicial discretion and sometimes judicial limitation. It may be legal principle or a more precise legal rule. It is sometimes the highest norm (if morally, socially or economically sufficiently pressing, and may then be mandatory), sometimes practical norm (if promoting good sense, co-operation and reasonable care, and is then directory). It is sometimes legal refinement and differentiation, sometimes generalisation and system building. It may be rule formulation, or rule application, selecting and weighing the relevant facts and defining the legal consequences (*Konkretisierung*). It may even be subjective, although it is mostly objective. It sometimes looks at the nature of legal relationships of the parties and their special interests and sometimes at the nature of their transaction and its particular features. At one time it may set rules for judicial decision making but at other times provides only judicial direction and guidance. It looks for fairness, particularly in consumer and small company cases, and for what makes sense and is practical, particularly in business cases. It is sometimes structure, but mostly movement. It is always inter-relational but is probably more important in human relationships than in business dealings. See further vol II, ch 1, s 1.3.4.

modern civil law literature is aware of these developments.[59] Some of these ideas can also be identified in England[60] although they are expressed differently.[61] They are clearer in the US, where they are closely connected with legal realism.[62] As already noted, they receive insufficient

[59] Misuse of the notion of good faith is not excluded, however, and intellectual prejudice may be as rampant in its application as in the application of the legal model good faith is meant to correct or expand, eg by referring to certain behaviour as '*obviously* contrary to good faith', see also J Vranken, *Exploring the Jurist's Mind* (2006).

[60] See Lord Hoffmann in *ICS Ltd v West Bromwich BS* [1998] 1 WLR 896, 912, referring to the reasonable man approach, with a preference for contextual interpretation to abstract literalism, but also in *BCCI v Ali* [2001] 2 WLR 735, 749 restating the principle of literal interpretation on the basis of a narrow view of the parties' intent, at least as a starting point. Similarly, Lord Steyn in *Total Gas Marketing Ltd v Arco British Ltd* [1998] 2 Lloyd's Rep 209 alluded to the contractual language, the contractual scheme, the commercial context and the reasonable expectations of the parties.

This is relationship thinking. The path finding approach of Lord Bingham in terms of relationship thinking in formation of contracts was demonstrated in *Interfoto Picture Library Ltd v Stiletto Visual Programmes Ltd* [1989] 1 QB 433, 439. English case law is careful to avoid broad concepts, however, such as the one to teleological interpretation (of statutes), and prefers to use the term 'purposive' instead, which may denote a more limited concept. See further the comment of Lord Denning in *Bulmer v Bollinger* [1974] Ch 401, s 1.3.3 below.

[61] The common law's emphasis on the nature of the relationship between the parties means that it needs the notion of good faith *much less* than civil law in this connection. Implied terms, fiduciary duties, notions of reliance, and sometimes resort to natural justice do the rest. Protection of small investors against their brokers may present here a case in point. Good faith notions in civil law do not reach as far as fiduciary duties traditionally do in common law. Moreover, the common law is less unfriendly to other sources of law, as we have seen. The often heard proposition on the European Continent that English contract law is primitive, because it does not even accept the notion of good faith, is therefore ill informed and imperceptive. See further vol II, ch.1, s 1.3.7.

[62] See MA Eisenberg, 'The Emergence of Dynamic Contract Law' (2000) 88 *California Law Review* 1747.

In the USA, the notion of good faith now operates more directly than in England: see for a fuller discussion vol II, ch 1, s 1.3.7. In the UCC under German influence, a general reference to good faith was inserted in s 1-304. It imposes an obligation of good faith in the performance or enforcement of every contract or duty under the UCC, but strictly speaking *not* in the formation. Interestingly, s 1-201(b)(20) UCC defines the concept as 'honesty in fact in the conduct or transactions concerned'. The 'in fact' language suggested a subjective approach ('empty head, pure heart'), but has gradually acquired a more normative or objective meaning, see s 1-201(19) (old), whilst s 1–201(a)(20) (new) now adds after 'honesty in fact' a reference to 'the observance of reasonable commercial standards of fair dealing'.

Indeed, for sales, s 2-103(1)(b) UCC had done so earlier, now repeated in its new version (s 2-103 (1)(j)); see also s 3-103(a)(6) UCC (for negotiable instruments), s 5–102(a)(7) UCC (for letters of credit) and s 9-102 (a)(43) UCC (when used in the area of secured transactions. See for a more limited use of the concept in this area of proprietary rights, Comment 10 to s 8-102 UCC (for adverse claims in security entitlements).

There are several other references to good faith in the UCC, eg for the sale of goods, in ss 2-603 and 2-615. It remains exceptional in the common law of contract, however, and is substantially statutory and even then, as in the UCC, incidental, as the many individual references to it show. At least in the UCC, good faith does *not* cover pre-contractual duties or strictly speaking even gap-filling but *only* the performance or enforcement of the contract, here joined by a general provision on the unenforceability of *unconscionable clauses* in contracts for the sale of goods, see s 2-302 UCC, particularly (but not only) relevant in sales to consumers.

On the other hand, in the US, the non-binding Restatement (Second) of Contracts of 1981 s 205, stated for the first time more generally that every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement. This was then followed in the 1990 revision of s 3-103(a)(4) UCC (for negotiable instruments) which, as far as the UCC is concerned, was first in accepting the idea that good faith could also means the observance of reasonable commercial standards of fair dealing, but good faith remained here also a matter of performance and enforcement of the contract only. This is now the general UCC approach.

It follows that in the interpretation of intent, the normative approach is now increasingly followed in the USA. Australia and New Zealand also have abandoned the narrow common law approach in this area. More limited notions of foreseeability and reasonableness may, however, commonly still be found in most legal systems as possible correctives to the parties' exposure in this connection when it comes to any assessment of damages even where the requirements of good faith are deemed violated in a more objective sense.

For the US see also EA Farnsworth, 'Good Faith in Contract Performance' in J Beatson and D Friedmann (eds), *Good Faith and Fault in Contract Law* (1995) 153. See for a case that could more readily be explained as covering a pre-contractual situation, *Teacher's Ins & Annuity Ass'n v Butler* 626 F Supp 1229 (SDNY 1986) in which a developer refused to close a loan deal whilst objecting to a pre-payment fee in the closing documents. The court recognised a duty of good faith and fair dealing in every commercial transaction and found a breach of this duty

acknowledgement in the DCFR (and earlier in the Principles of Contract Law (PECL)) which now stands for the latest, more classical, example of codification thinking in Europe. The reason for this is its anthropomorphic idea of contract and a prescriptive consumer law ethos which makes these texts unsuitable for professional dealings.

For professionals, the contract itself is likely to be primarily a road map and prime risk-management tool. Good faith interpretation does not then always provide more rights; it can also be restrictive, especially when predictability requires it. Proper risk management through contract is an overriding aim in all professional dealings. Particularly in this respect, the initiative of the parties remains paramount whilst good faith notions or corrections recede in importance, although it has already been observed that in civil law the notion of good faith is often still perceived as unitary, therefore operating for both professionals and consumers in a similar manner. This is a serious mistake. On the other hand, it can easily be maintained that good faith underlies all contract interpretation, including professional contracts as long as it is understood that it may work out very differently in consumer and business dealings. Again, proper relationship thinking is the key here and should move to the centre of the good faith concept itself. Civil law has still some way to go in this respect.

Indeed in modern contract theory, the notion of party autonomy is recast primarily in terms of initiative and organisation.[63] It is no longer psychological and is therefore more objective, locked in, in particular, by conduct and reliance notions and supplemented (and sometimes corrected) by other sources of law. The modern notion of good faith, if properly understood, supports this and may thus extend as well as limit the protections of the parties depending on the nature of their relationship (different in professional and consumer dealings) and on the type of their deal (different therefore in duration contracts and sale of individual goods). In this vein, the commercial contract will often be interpreted literally, especially if operating as a road map and risk management tool. Good faith itself requires it; it may mean fewer rights, not more.

Thus modern contract theory[64] generally underwrites a dynamic concept of contract law, see Volume II, chapter 1, section 1.1.4, often accepted in more ambitious domestic

on the basis of commercial practice which accepted pre-payment fees in loan agreements even if not normally included in a bank's commitment letter. The court, therefore, rejected the borrower's argument as a pretext for getting out of the deal also taking into account that the draft loan agreement had included the fee and that the problem had never been raised until the eve of closing. The case can, however, also be seen in the context of performance pursuant to the commitment letter.

[63] Especially in terms of risk allocation, including the risk of unforeseeable events, particularly in duration contracts, *party autonomy* thus remains an important concept, fully recognised by modern contract theory, especially between professionals including their right to set standards or even eliminate adjustment possibilities except in extreme cases. Only if the situation gets totally out of hand will there be redress under more objective good faith notions, which may include termination of the agreement, but again it is unlikely to be an issue of lack of intent. Parties retain here a sense of *initiative* and *imagination* and will use their contract as a tool of risk management in as far as they can foresee these risks, but intent is here no longer central as a notion in itself.

[64] For modern contract theory, see esp Eisenberg, n 62 above, 1743, 1747 and earlier S Macauley, 'Non contractual Relationships in Business', (1963) *American Sociological Review* 55 and 'Contract Law and Contract Techniques; Past, Present and Future' (1967) *Wisconsin Law Review* 805; G Gilmore *The Death of Contract* (1974); PS Atiyah, *The Rise and Fall of Freedom of Contract* (Oxford, 1979) and *Essays on Contract* (Oxford, 1986); RA Hillman, 'The Crisis in Modern Contract Theory' (1988–89) 67 *Texas Law Reporter* 103 (1988/89) and 'The Richness of Contract Law: an Analysis and Critique of Contemporary Theories of Contract Law' (1999) *Michigan Law Review*; J Beatson and D Friedman, 'Introduction: From 'Classical' to 'Modern' Contract Law', in J Beatson and D Friedman (eds), *Good Faith and Fault in Contract Law* (Oxford, 1994); S Styles, 'Good Faith:

academic writing, although in practice the notion of good faith is by no means everywhere similarly extended or unchallenged as we shall also see, but it is true that under pressure of circumstances, domestic courts have often been forced to implement it in a liberal manner in order to remain credible and responsive, although even then in the civil law way of system thinking, at least in academia, there also remains an urge to use the new case law to complete or reinvent the system through extrapolation and reinterpretation.[65] Again, transnational commercial and financial law is here more likely to be responsive and ultimately to lead. It takes in *both* contract and movable property law the *risk management perspective*, which connects both the contractual and proprietary examples of legal dynamism given above. It should be noted, in this connection, that at the more formal level, even for contract law, the CISG is not up to date but this is no less true for the UNIDROIT and European Principles of Contract Law and the more recent DCFR as model for a uniform European (EU) private law, followed in 2011 by CESL, all of which will be more extensively discussed in Volume II, chapter 1, section 1.6 for contract and chapter 2, section 1.11 for movable property, including receivables.

In summary, in terms of modern legal dynamism, it could perhaps be said for modern commerce and finance that what the civil law concept of good faith is doing for contract as a transforming concept, making the (civil) law in this area adapt to modern realities, ultimately allowing for different types of relationships to be taken more significantly into account and, therefore, at least in professional dealings, accepting a continuous process of law formation, is at the transnational level increasingly matched by some similar transforming force in respect of movable proprietary structures, which allows for a degree of

A Principled Matter' in ADM Forte, *Good Faith in Contract and Property Law* 157 (1999); R Brownsword, *Contract Law: Themes for the Twenty-first Century* (London, 2000); Hugh Collins, *The Law of Contract*, 4th edn (London, 2003); E McKendrick, *Contract Law*, 6th edn (Basingstoke, 2005).

[65] Thus German academics typically look for system everywhere, even in more open textured provisions and often talk in this connection, for example, of the inner system (*Binnensystematik*) of the good faith notion, referring in particular to the reliance option, pre-contractual duties, normative interpretation, supplementation and correction techniques, the (continued) validity of the contract, the performance obligations and excuses of the parties, and, in appropriate cases, to their re-negotiation duties, all originally developed on the basis of the concept of good faith.

In German doctrine, see the major commentary of Palandt/Heinrichs, *Bürgerliches Gesetzbuch* (2011), at s 242, nos 2 and 13, there follows then some attempt at classification of the functions of good faith (*Funktionkreisen*), like interpretation, supplementation and correction of duties or adjustment in case of a profound change of circumstances, functions which are by no means new and are now expressed in specific provisions of the BGB: ss 241(2), 280, 311(2) and (3), 313. They had already appeared in the *Justinian Digests*, in connection with the definition of the powers of the Roman praetor in contract law (D.1.1.7 Papinianus). See also F Wieacker, *Zur Rechtstheoretischen Präzisierung des sec 242, Recht und Staat in Geschichte und Gegenwart* (Tübingen, 1956) 20. Within these good faith functions, there is a further effort to distinguish classes of cases (*Fallgrupen*), like, in the supplementation function, the development of pre-contractual and post-contractual rights and duties and of consumer or workers' rights (not necessarily, however, along the lines of altogether clear rules or new contract types), and, in the correction function, the emphasis on estoppel, abuse of rights, own co-operation duties, and on the manner in which rights were acquired or are invoked like in the case of standard terms.

But only some clear notions were identified in this manner, such as the abuse of rights (*exceptio doli*), the notion of clean hands, of own misbehaviour and of lack of co-operation; none very original. Also the loss of a right to performance became accepted if there was contrary conduct or if there were declarations on which the other party could rely as an excuse. Another development was the loss of rights whilst not timely invoking them (*Verwirkung*). All are of limited application, however, and it is altogether not a large crop. The search for rules in the above manner ignores not only the dynamic character of the concept of good faith but also good faith's modern multifaceted nature, see n 58 above.

party autonomy in proprietary matters creating room in particular, for typical asset backed financial products, a development more akin to that of equity in common law.[66]

1.1.5. Legal Pragmatism at the Transnational Level. Notions of Certainty, Finality and Predictability. The Need to Find Structure, Not System

Altogether the emerging new transnational law merchant or modern *lex mercatoria*, based on its various sources and the hierarchy of norms deriving from them, that is the law of international professional dealings, is less systemic and more pragmatic, particularly in its method, coverage and responsiveness, which all go to legal dynamism, especially in contract and movable property as submitted in the previous section. The resulting law is less concrete and cannot avoid some flux if only because it is still in its formative era and is particularly geared to respond to new situations. It embodies a way of thinking and presents an environment in which existing rules are foremost *guidelines* (unless the situation is fully repetitive) and subject to a good deal of party autonomy, but the new *lex mercatoria* also espouses firm notions of finality especially for payments and title transfers as we shall see. It should be noted, however, that even domestically, a similar state of fluidity is becoming clearer in respect of much black-letter private law except perhaps in the few areas where the law remains absolutely settled, such as in the area of conveyancing of real estate or where mandatory law is imposed especially through regulation. Even then, texts are seldom fully clear, policies poorly expressed or unattainable, and their meaning evolves in any event in interpretation.

In private law, greater fluidity is the unavoidable consequence of factual patterns becoming ever more diverse and complex, and of practical needs evolving ever more quickly. In the area of what we might term 'directory law' (or default rules), where the legal system has a mere support function, this may be more easily accepted and can also be more easily handled through the use of party autonomy in choosing or amending the applicable rules, but it is also unavoidable in the law's application in areas where it is (semi-)mandatory, even in private law, as in personal property law or even in contract, when the contractual infrastructure is an issue, for example, in terms of legal capacity to contract, in issues of validity and legality, or in matters of the continued existence of the agreement and obligations thereunder.

There is now more movement and this is also more readily understood, especially by the so-called 'legal realists' in the US, already mentioned,[67] who present the view that the private law is only legitimate in its operational adequacy and ethical, social and economic sufficiency. Thus, pressing ethical, economic, efficiency, utilitarian and social factors had to be

[66] It may also be said that, although this good-faith concept has (except in the US) so far met with less favour in common law countries (which, as noted in n 61 above, have other techniques that may lead to similar results, especially the emphasis on the nature of the relationship of the parties, fiduciary duties, implied terms, and the notion of estoppels and reliance), in movable property on the other hand this equitable transformation process has not yet been recognised in civil law countries, with the exception perhaps at the formal level of modern developments in France, as demonstrated in n 45 above, whilst in particular the EU Collateral Directive of 2002, discussed more fully in vol II, ch 2, Part III, may give some indication of what is to come. So may the 2001 UNIDROIT Mobile Equipment Convention, see vol III, ch 1, s 2.1.8.

[67] See n 23 above.

accepted as having an impact on private law, affecting the application of both statute and precedent. Ever evolving values, policies and needs then become key issues in the interpretation process (of statute, property law and contract), even if in commerce and finance, and therefore in the law between professionals, value considerations may often be less relevant, but issues of efficiency and utility or abuse and fraud may still be overriding. Cost/benefit considerations may then also become more relevant in the operation of this law.

Although this perspective was first articulated in the US in the 1930s (see section 1.3.4 below), it has also been accepted (albeit often reluctantly) in one form or another in countries such as Germany, Austria and the Netherlands, which, in the civilian law tradition, still work in essence with a statutory text and its system. This is so at least in the law of obligations as applied by the courts. The ensuing flexibility is therefore clearer in contract (especially because of the good-faith concept) than in movable property law.

Indeed, it is manifested foremost in a *liberal interpretation technique* in respect of codified texts, especially in the law of obligations, that could otherwise no longer be considered complete, nor operate as such. But the re-systemising tendencies in academia at the domestic level were also noted,[68] and at least in civil law countries nationalistic system thinking remains a prime academic preoccupation. There is here considerable tension in civil law as there continues to operate a belief in national academic models adequately capturing and guiding reality,[69] even for international transactions in respect of future fact patterns. As we have seen, this attitude has also spilled over into countries like England, where, especially in circles around the Law Commission which means to articulate law reform, statutory law, and thus legal texts, are also popular and a system mentality has been cultivated.

Greater fluidity in the rules raises everywhere the issue of *legal certainty* or lack thereof, and predictability. In modern international transactions (given their ever greater frequency and value), this problem is aggravated by the fact that legal certainty can no longer come from domestic laws that were never written for them and often operate at the cost of limited sophistication. The traditional conflict rules of private international law, always pointing to the applicability of a national law, here reach their useful end or suggest a certainty that may be of such a low quality that it may destabilise the relevant commercial and financial transactions for solely dogmatic reasons, often being no more than pure nationalism supported by domestic system thinking.

Certainty of this nature is often supported by the notion of law as pure technique or a logical framework that, when properly applied, always arrives at the correct answers. It has already been said that codification in the civil law manner was its culmination. To repeat, the idea is here that human behaviour can be systematically captured for the present and the future—a particular academic ideal and preoccupation in Germany—but for the social sciences this attitude and its idea of certainty have been fundamentally questioned, not only by Popper and his followers.[70] One may also recall in this connection the reference of Jerome Frank to the childish dread of uncertainty and unwillingness to face legal realities.[71] In fact, a search for certainty of this nature may hold everything back.

Rather, it is for professional parties through extended notions of party autonomy to chart a course through the risks of their international transactions, on both the contractual

[68] See n 65 above.
[69] For the connected problems see section.1.2.12 below.
[70] See n 208 below.
[71] J Frank, *Law and the Modern Mind* (1930) 41 and 159.

and proprietary side, in the manner that was discussed in the previous section, where it was also noted that their contract is likely to become a road map and may need literal interpretation. Even good faith may require that. It was further pointed out that their proprietary structures, especially in international finance in asset-backed finance, also become in this way tools of risk management that could be extended trans-border, supported by industry practices and subject to a more sophisticated protection of the ordinary course of business against hidden charges. There are of course also the tax and regulatory complications to be considered.

In the absence of a proper supranational legislator, and given the insufficient and often backward-looking spirit of much existing local black-letter law or even treaty law, we may instead have to get used to the idea that the certainty that commercial (or more generally professional) law requires must in a modern internationalised environment in private law increasingly come from the understanding, discipline, and practices of the participants themselves, helped by fundamental and more general legal principles that transcend national laws. As we have seen, this suggests in particular, a greater role for industry practices or custom and party autonomy, even in proprietary matters, always subject to the requirements of the commercial flows and their promotion and to legitimate public order concerns, particularly in terms of market abuse, which concept itself is likely to be transnationalised in professional dealings. That is the future if globalisation holds and should be better understood by all.

Instead of certainty of this nationalistic nature, which may now often only be obtained at too low a level in terms of quality, it is submitted that the emphasis should be on *finality* of title transfers and payments, therefore on transactional certainty,[72] which is a much narrower (proprietary) concept,[73] and on *predictability* for the rest. Finality is a key issue

[72] Only in terms of the narrower issue of the *finality* of their transactions, especially in respect of title transfers and payments, is there an overriding need for certainty which the law merchant was always prone to provide, *viz* the law of negotiable instruments and bills of lading.

Certainty of this nature has traditionally been stressed in English case law ever since Lord Mansfield, especially in mercantile transactions; see *Vallejo v Wheeler* [1774] 1 Cowp 143, 153 (KB); see more recently *Homburg Houtimport BV v Agrosin Private Ltd, The Starsin* [2003] 1 Lloyd's Rep 571, 577 (Lord Bingham of Cornhill) and *Compania de Neviera Nevasa SA v Tradex Internacional SA, The Tres Flores* [1974] QB 264, 278 (Roskill LJ). For the US, see *Mc Carthy, Kenney & Reidy, PC v First National Bank of Boston* 524 NE 2d 390 (Mass 1988). Again, it should be noted that it concerns here often negotiable instruments and letters of credit, all related to payments, or bills of lading, therefore a narrower strand of commercial law where *finality* is indeed of special importance. See also *Pero's Steak and Spaghetti House v Lee* 90 SW 3d (Tenn 2002).

In this context, emphasis on finality is not incompatible with the transnationalisation of commercial and financial law, see also JH Sommer, 'A Law of Financial Accounts: Modern Payment and Securities Transfer Law', (1998) 53 *Business Law* 1181. It is submitted that the concept of finality may be enhanced by it. It would also seem misconceived to ask in this context for clearer rules of conflicts of laws and be satisfied even with arbitrary rules and therefore an arbitrary choice of some domestic law whatever its quality and responsiveness. That is a step backwards and contrary to the basic tenants, history and true needs of international commerce and finance. They are nationalistic academic fabrications. The recent and new references in this connection to 'certainty' in the Preamble (6 and 16) of the EU Regulation (EC) No 593/2008 on the Law Applicable to Contractual Obligations (Rome I) are misconceived and disappointing, but typical for traditional conflicts of law thinking.

[73] In terms of the legal characterisation of transfers and their *finality*, important issues arise in securities transfers and in payments, especially those through the banking system. They centre on fraudulent or defective instructions, the meaning of acceptance of the transfer or payment, the question of capacity and intent, and the transfer and its formalities (eg, in terms of existence, identification and delivery of the assets) and acceptance.

In terms of *transnational general principle*, which may well be in the process of becoming customary in a *mandatory* manner, the necessary *finality* may here be underpinned by: (a) de-emphasising the role and subjectivity of capacity and intent whilst giving these notions an objective meaning; (b) the abstract nature of all transfers in the German tradition (separating them from any underlying contractual or instruction defects); (c) the indepen-

in transactions, including payment, as we shall see throughout this book, and is therefore a central theme and concern of the new *lex mercatoria* besides, and closely connected with, the protection of the ordinary commercial and financial flows against adverse interests. It is a proprietary issue. The concept of predictability on the other hand, is less absolute and assumes rationality and sensibility. It rests on the idea of law as sufficient guidance for parties to determine their behaviour and for arbitrators and judges to reach a conclusion in dispute resolution. It is a different concept from certainty, which as just mentioned sees law as pure technique with inbuilt automaticity in result. This is unrealistic, even undesirable. One could argue that it is also anti-social. Predictability assumes, on the other hand, movement, and can deal with legal dynamism. Some degree of legal uncertainty is a fact of life and not necessarily to the detriment of the legal profession. It is unavoidable in incongruent factual patterns or in newer situations,. It is increased by the ever greater internationalisation of trade and commerce, itself mostly seen as an important and irreversible process. It is also enhanced by the uncertain grip of domestic regulation in international transactions.[74]

Yet the lack of certainty in a technical sense should not be more destabilising than absolutely necessary. It is one reason why the professional community may prefer to live with its own rules to the extent it can. Again, it suggests a measure of spontaneous transnationalisation and a larger reliance on (transnational) custom and practices and, further, a greater degree of party autonomy at that level. Aiming at better risk management tools, it is for this community to decide what it prefers (unless there are major public order or public policy issues involved) and it is likely to find it better to operate under more flexible rules than under the wrong rules. At least professionals come from a community that is used to taking and managing risks and they may be better able to deal with greater uncertainty than with the wrong rule.[75]

Indeed, it appears that professionals can normally handle these risks, aided by an ability to devise better structuring and protection schemes amongst themselves. It is also the essence of enhanced party autonomy in the law of movable property, as we have seen, and it is much of the international transaction lawyers' activity promoted by their clients':

(a) understanding of the trade, the market infrastructure, and the requirements of the commercial flows, whilst developing and formulating custom and practices in these areas and enforcing them amongst themselves;
(b) access to the international commercial arbitration practice in the case of disputes between them; and
(c) being better positioned to ask for help, when needed, from states in the form of supporting treaty law (or within the EU in the form of Directives or Regulations, of

dence of the transfer or payment obligation and of the transfer and payment itself, as derived from the negotiable instrument and the letter of credit practice; (d) the *bona fides* of transferees once they have been credited or have received the assets in respect of any defect that may attach to the title, in other words the underlying assets (securities and cash) may assumed to be clean; and (e) justified reliance of transferees and especially payees who were owed the relevant assets or moneys and received them.

Thus it may be shown that transnationalisation may provide a considerable support function especially in this key aspect of finality of international transactions, see more particularly vol II, ch 2, s 1.4.6.

[74] In international situations, uncertainty may be compounded by the question of how far domestic mandatory *regulatory* laws or public policy may still impact on international transactions, see also n 32 above. It creates uncertainty of a different kind and raises issues of relevant contact, conduct and effect that, at present, are only capable of resolution on a case by case basis. See more particularly ss 1.5.6 and 2.2.6ff below.

[75] For the notion of professional, see s 1.1.8 below.

which the Settlement Finality and more particularly the Collateral Directives were prime examples).[76] Organisations like UNCITRAL, UNIDROIT and especially the ICC may provide a useful supporting function in this connection as well, but only if activated upon such requests.

It is a situation that has, in fact, been in practice for quite some time, has not led to disaster, and is unlikely to do so in the near future. This evolution should therefore be approached with confidence and imagination.

In truth, at least at the transnational level in the private law amongst professionals, the search is on for a new legal framework that is closer to present-day international reality, to how society works for them, and is thus capable of supporting their transactions in a more responsive and imaginative manner for the benefit of all participants. It has already been said that, theoretically, the formation, operation and application of the new transnational law merchant or *lex mercatoria* in the professional sphere in this manner takes its cue from the development and application of public international law. It is about how commercial (and financial) law is escaping the grip of domestic systems and is being transformed to better support international transactions and to provide a reasonable degree of predictability and finality where it matters, particularly in title transfers and payments. The limit is the public policy and public order which themselves may be transnationalised.

In private law, this takes us back to the time before the great nineteenth-century codifications when lawyers like Grotius accepted many sources of law and sought to find *structure* in them, not *system*. This is an important distinction. Finding structure is a dynamic forward-moving process. Finding system, on the other hand, is based on the idea that the system represents or can find reality and has in it all answers. In this way it seeks to set present-day law in concrete and is retrospective by definition. At best, it means to extrapolate newer law from past experiences but always assumes an existing intellectual model, framework or system that can handle all eventualities. It assumes that life is basically repetition.

The new law merchant rejects this approach and is dynamic and forward-looking, but it will also be shown that it is not averse to structure, and even seeks it by type of relationship, subject or product. The law of assignment or set-off and netting may be a prime example. It follows that the content and operation of the modern *lex mercatoria*, if properly understood, is by no means as vague, novel, uncertain or incomplete as is sometimes argued. As we shall also see, its hierarchy of sources and norms, with local law remaining the residual rule, presents a full operative legal system (for those who still wish to see one), no less than any domestic one: see section 1.4.13 below. But even then it does not claim to have all the answers.

1.1.6 Social, Economic, Intellectual or Democratic Legitimacy

A recurrent theme in discussing immanent law formation in the manner attempted here, and the operation of the modern *lex mercatoria* is the question of its legitimacy. In this connection it is often thought that statist law is more legitimate because it is democratic, at

[76] See also n 46 above.

least in democracies. This underpins in the minds of some the argument for codification, an issue that will be further discussed in section 1.2.13 below. It must be doubted, however, whether this is the correct perspective. In any event, the major modern civil codes—those of France and Germany—did not come about through a democratic process. The common law emanating principally from the courts could not possibly be so characterised. Where through legislation social values are incorporated into private law, there is clearly much to be said for democratic support, but social values enter through case law just as much and that has proven to be very necessary.

Rather, codification in the German manner had intellectual coherence and system thinking at its core, the idea being that in this manner society could operate better, but there was also a more transcendental aspect: states having the deeper insights in society and how it works. As has already been said, in this view, the state speaks here primarily through its academies and rubber-stamps their efforts, which derive their legitimacy from the academic effort itself and its search for 'truth' in that sense and its models to represent it. Legitimacy does not come, in this approach, primarily from the democratic process.

Other strong claims to legitimacy may derive from law as a community product and therefore, especially in customary law, from being more truly participatory. Efficiency considerations may also underpin this type of law. Although in the academic perceptions custom and practices are often declared inferior or primitive, nothing suggests that they are so in their operation. They have much to do with the infrastructure of the market place and stand for a more diverse society and for a multifaceted and more dynamic system of law.

The view has already been expressed that the modern *lex mercatoria* is in essence based on a number of non-territorial autonomous sources of law, notably fundamental and general principle, custom and practices and party autonomy, sometimes joined by uniform treaty law, whilst the residual rule remains territorial local law. This will be elaborated below in section 1.5 on the operation of the international commercial and financial legal order and its autonomy. It may thus be seen that some of the rules as well as the structure of this new law, are based on fundamental values or on more universal public order requirements; others on societal and efficiency forces; and yet others on statist action either through a legislature or through the court system. That is the simple consequence of having different sources of law and legal diversity in that sense, a theme that will be elaborated throughout this book and about which there is nothing per se undemocratic or illegitimate.

1.1.7 The Traditional Civil and Common Law Notions of Commercial Law. The Notion of Commerciality

The previous sections have looked at the different notions and coverage of commercial law in both civil and common law, and at this type of law formation at the transnational level, its reaction to system thinking, its need for more dynamic law, and its legitimacy. Its expanding international coverage was also considered.

This may merit some further consideration and a discussion of the more traditional theoretical notions that are still used in domestic laws to set commercial law apart even if, as we have seen, its independence in both civil and common law countries is in question,

although for different reasons. As we shall also see, these more traditional notions do not best serve the transnationalisation concept, which depends rather on the concept of professionalism (see section 1.1.8 below).

However, these more traditional notions cannot yet be completely discarded. If one starts by looking at some civil law commercial codes, for example at the French *Code de Commerce* (CdC) of 1807 (redrafted in 2000) and the German *Handelsgesetzbuch* (HGB) of 1900, as well as at a common law commercial code like the US UCC of 1962, one may see considerable differences even between civil law countries.

As regards the *coverage* of commercial law, which even differs markedly between the CdC in France and the HGB in Germany, in civil law it is always related to commerce, in which connection a notion of *commerciality* is used, which may, as compared to common law, produce limitations; as a consequence the concept of commercial law may be narrower and more *service*-oriented in civil law. In France, there is particular importance in the distinction, as commercial disputes are still brought before separate commercial courts.

On the other hand, in the absence of a clear *commerciality notion* or concept, in the modern *common law*, there is *no single overriding criterion* that determines the coverage of commercial law. Importantly, non-merchants engaged in the sale of goods, using cheques, and yielding security interests in their personal property are covered as much by commercial law as are merchants and this is borne out by the UCC in the US.[77]

In common law, there is still a difference in the approach to custom which has a broader and more independent meaning in commercial law going conceivably beyond mere contract term and therefore also operating in other areas. It has already been said that in documents of title and negotiable instruments there is no need for consideration for their trading whilst bona fide purchasers of these instruments are protected. Here again, one detects special concern with the commercial flows and finality, but beyond this, in common law, it is now often tradition or statutory convenience that determines whether a matter is considered part of commercial law. There are hardly any particular consequences or special features left in the law deriving from the mere commercial law qualification. There are none in the type of courts before which commercial cases are brought, although, as in England, there may be commercial law divisions in the ordinary courts.

In the USA, the modern UCC (1962, but frequently revised since), which applies as uniform law (exceptionally) in all states of the USA (civil and commercial law being state

[77] Within the US, the UCC from the beginning separately defined the notion of merchants and dealings between merchants in s 2-104, but *only* in the context of the law of the sale of goods and not in any broader sense. However, the UCC did not eliminate consumer sales from Art 2 UCC, but only has some special rules concerning merchants.

A merchant is here defined as a person who normally deals in goods of the kind or otherwise holds himself out by his occupation as having knowledge or skill peculiar to the practices or goods involved in the transaction or to whom such knowledge or skill may be attributed by his employment as an agent or broker or other intermediary who by his occupation holds himself out as having such knowledge or skill. Dealings between merchants are transactions with respect to which both parties are chargeable with the knowledge and skills of merchants.

In earlier versions of Art 2 UCC, a broader distinction between consumer and professional sales was proposed: see ZB Wiseman, 'The Limits of Vision: Karl Llewellyn and the Merchant Rules' (1987) 100 *Harvard Law Review* 465. Art 2 UCC is therefore less professional-oriented than originally planned, reflecting the reality that in domestic sales professional dealings have so far acquired fewer distinctive features. Consumers have in the meantime obtained special protection under broader consumer laws, often at the federal level. In this manner, commercial law has indirectly regained a place of its own.

matters),[78] covers in this connection only a number of products, specifically negotiable instruments, bills of lading and warehouse receipts, and letters of credit as well as the sale of goods. It also deals with secured transactions in moveable property (including intangibles) and now even with finance (equipment) leases, which were eventually distinguished from secured transactions, and with payment systems and investment securities. On the other hand, it does not cover transportation, either on land or by sea, nor the related insurance. Company law and bankruptcy were never part of commercial law in the common law sense.[79]

As mentioned, in civil law countries that still have a separate commercial law, there is usually a *more substantive criterion of commerciality* and therefore at least in theory a clearer view of what is commercial. In France this is provided by the notion of the 'commercial act'; in Germany by the idea of 'dealings with merchants'. These definitions form the intellectual basis of the coverage by the commercial codes of these countries as we shall see in the next section, but fundamental distinctions have become much less important here also, and the coverage by the commercial codes is in both France and Germany often incidental, if not erratic. Non-merchants may sometimes also find themselves covered by these codes, for instance in writing cheques. Again, there is no doubt that in France the most important factor is not coverage by the commercial code itself, but rather the jurisdiction of the commercial courts in mercantile matters still with lay judges, and an accelerated procedure. These courts no longer exist in Germany. There are still commercial sections in the lower courts of that country, with some lay input, but they otherwise operate much like normal courts.

In view of the limited modern impact of the distinction between commercial and civil law, some civil law countries such as the Netherlands, Switzerland, Italy, and Brazil have done away with it altogether. However, as has already been mentioned several times, and as we shall see in the following sections, in the modern internationalised market place, the

[78] It means that the UCC was promulgated separately in each state of the Union and that the text may still vary between states. Also amendments are not always introduced simultaneously in all states. Some have repealed part of it (especially Art 6 on Bulk Transfers), but others have not. The UCC was itself a joint project of the American Law Institute and the National Conference of Commissioners on Uniform State Laws, started in 1942. The American Law Institute is a private body, since 1923 devoted to the harmonisation of legal concepts among the various states of the USA, especially through producing Restatements of the law as it has done in various areas such as tort, contract, agency and (interstate) conflicts of law. The Restatements are non-binding, but have nevertheless had a considerable impact on the further development of the law in the relevant areas and serve as guidelines for the courts.

The National Conference of Commissioners on Uniform State Laws, on the other hand, which has existed since the end of the nineteenth century, has drafted a number of Uniform Laws for adoption in the different states. The UCC is by far the most important of these Uniform Laws and is now accepted (with certain modifications) in all 50 states of the Union.

The UCC uses the term 'Article' in the sense of chapter or book. Each is divided into individual sections. Besides the chapter on sales (Art 2); there is the one on Bills of Exchange and similar types of payment instruments (Art 3); on Bank Deposits and Collections (Art 4); on Letters of Credit (Art 5); on Bulk Transfers (Art 6); on Documents of Title including Bills of Lading and Warehouse Receipts (Art 7); on Shares, Bonds and similar types of investment securities (Art 8); and on Secured Transactions (Art 9). Art 1 contains definitions. It is no exaggeration to say that Art 2 and especially Art 9 were at the time of their first publication (1952) original pieces of legislation. They were substantially introduced in the various states of the USA after 1962 and are regularly updated. Some new chapters have been added, particularly Art 2A on the Equipment Lease (a form of leasing) and Art 4A on Fund Transfers (payments).

[79] The UCC is in fact often considered bipolar with on the one extreme the sale of goods in Art 2 and on the other the security interests in Art 9, although the sale of goods remains here at the centre of commercial law itself; see also K Llewellyn, 'Problems of Codifying Security Law' (1948) 13 *Law and Contemporary Problems* 687.

distinction between professional and consumer dealings may have become more apt, with the former essentially being covered by a transnationalised legal regime or order and the latter remaining in essence subject to more prescriptive domestic laws.

Obviously, if there is to be any true meaning in distinguishing legally between commercial and other matters, it must be in some special legal regime applying to merchants and the dealings between them. At the very least, the commercial law regime should be more informal and custom-oriented, if not also more international. No less important would be the competence of special courts to hear commercial cases with simplified proceedings. They would be more specialised, less formal and speedier or be replaced by international commercial arbitration. Yet little is left of this in local laws.

As we have seen, in common law, the major difference is now in the role of commercial custom as an independent (although in England in practice often limited) source of law. There are no longer any autonomous courts. In the USA, the UCC reflects at least an accommodating approach to custom. To repeat, in, section 1-103(a)(2), the UCC envisages that the Code, for the areas it covers, is to be liberally construed to promote its underlying purposes and policies, one of them being to permit the continued expansion of commercial practices through custom, usage and agreement of the parties.

As just mentioned, France looks in this connection at *acts of commerce* and Germany at the dealing with and therefore *status of merchant*. Even in France, the German approach is often considered the more logical one, but at the time of the French codifications at the beginning of the nineteenth century, it was not considered proper to create a special class of people—in this case merchants—with different rights, even if these rights did not imply privileges but sometimes a less refined and harsher regime of enforcement. Nevertheless, treating merchants differently was considered counter to the then new notion of equality. The result was that the basic French concept of commercial law became tied to commercial acts or *actes de commerce* engaged in by otherwise equal people—at least that was the idea. There is no conceptual definition, however, and these acts are merely enumerated; compare Articles L 121-1 and L 110-1 (old Articles 1 and 632) CdC. They concern mainly the purchase of assets for resale and the intermediary services rendered in this connection, the renting of property, manufacturing activity, transportation and banking business.

Even though the basis was therefore *not* the concept of *merchants* or *commercants*, who are people or entities who habitually engage in commerce, the acts of commerce, as enumerated, are only covered by the CdC if they occur between merchants, except in so far as bills of exchange and cheques are concerned, which are commercial between all persons (except in a procedural sense). In France the result is that in their dealing merchants may not always be engaged in commercial acts as defined (even if they operate as merchants). On the other hand, persons not normally engaged in commerce may still engage in commercial acts but are not then covered in their activities by the CdC (except for bills of exchange and cheques). They are in any event sued in the ordinary courts.

In practice, the substantive relevance of the doctrine of commercial acts in France is modest, even in the law of sales. The most important aspects of commercial sales are that testimonial evidence against commercial contracts is admitted, which is unlike the situation under the *Code Civil* (Article 1341 CC). Furthermore case law[80] established that registered mail notice rather than court action is sufficient to put a party to a commercial contract in

[80] *Cour de Cass Req* 28 Oct 1903, DP 1.14 (1904).

default, thus creating the condition in which the remedies of rescission of the contract and/or damages become available. Another point is that joint and several liability of commercial debtors is presumed, thus derogating from the rule in Article 1202 CC. Since 1925, Article 631 CdC (old) has provided further that agreements to arbitrate future disputes are valid and enforceable in matters in which the commercial courts are otherwise competent.

Tying commercial law to acts of commerce (as enumerated) is often presented as the *objective* approach, as distinguished from the *subjective* approach, to commercial law—in France, *droit réel* versus *droit personnel*. This latter approach ties commercial law to the activities of merchants. France has opted for the objective approach (enumeration of the acts of commerce) with a subjective twist and limitation (in the indirect reference to these acts having to take place between merchants). In Germany it was the reverse: all merchants are governed in principle by the commercial code, but only of course for the activities it covers. Here, the term 'merchant' remains largely undefined, however, though case law looks for an element of independence, of business activity, and of repetitiveness of the activity.

Thus in Germany the coverage of the commercial code is primarily based on the activities of merchants as such (if both parties are merchants or at least the party making commitments), but only in those areas covered by the commercial code, which also in Germany is somewhat haphazard. It follows that commercial law does not cover activities between merchants which are not commercial in terms of that code. So, even in Germany, a definition of commercial acts (*Handelsgeschäfte*) comes in, although some activity is considered commercial per se. On the other hand, some commercial activity may also be engaged in by non-merchants, such as the writing of cheques or the drawing of bills of exchange, which is now covered by a separate statute. Where non-merchants engage in commercial activity that activity may still be covered by the commercial code, but the activity is then considered commercial only in a more generic or wider sense. In fact, many provisions of the HGB do not cover specific commercial matters at all and apply equally to non-merchants. The distinctions are therefore not so clean and clear in Germany either. Much is historical accident, not fully cleared up in 1897 when the current German civil and commercial codes were put in place. There are many voices in Germany arguing for an abandonment of the distinction between civil and commercial law altogether.[81]

In Germany, as in France, the substantive law effect of commercial acts between merchants is thus also limited and incidental. Of particular interest, however, is that the transfer of a business activity implies the liability of the transferee for all its outstanding debt (section 25 HGB). This is a much contested rule. Another interesting feature is that interest and fees are implied in business activity and need not expressly be agreed (section 354 HGB).

The *real problem* in all this, in both France and Germany and in all countries that still maintain similar abstract criteria for the application of commercial law, is that merchants are not only engaging in commercial activity but also in non-commercial acts. On the other hand, non-merchants also engage from time to time in commercial activities. The consequence is that neither the concept of merchant nor the concept of commercial activity can be defined exclusively in terms of the other. Hence the confusion.

[81] See CW Canaris, *Handelsrecht*, 22nd edn (1995) 8ff, *cf* also K Schmidt, *Handelsrecht* (1999) 5.

Another notable aspect of commercial law in France and Germany is the absence of any general reference to the status and impact of custom and industry practices, even in commerce. As we have already seen, this is entirely in line with codification thinking that is suspicious of, and uncomfortable with other sources of law, and particularly with an internationalist approach. But beyond pure system thinking, especially in commerce, this attitude was always curious.

It has already been said that in France, commercial law as a separate body of law remains more important than elsewhere because of the special court system. Historically, French commercial law originated on two fronts: in trade with England, through the Channel ports, leading to maritime and insurance law; and in trade with Italy, through the fairs of Brie and Champagne, later moved to Lyons, in the East, leading to laws concerning transportation on land, bills of exchange and bankruptcy.[82] These were codified in the *Réglements de la Place de Change de la Ville de Lyon* of 1667, largely copied in the first all-French commercial code (*Ordonnance de Commerce de Terre*) of 1673, promulgated by Louis XIV and amended in 1716 and 1739. It was the result of an initiative of Minister Colbert who also ordered an *Ordonnance sur la Marine*, which was promulgated in 1681. They served as main sources for the French CdC of 1807.

As a consequence, the French Commercial Code still maintains the distinction between land and sea transportation law (in Books I and II old), although maritime law is now the subject of many different statutes. In the meantime, company law was put in a separate statute in 1966, bankruptcy in 1967 and banking in 1984. Many other provisions were repealed and the CdC was, as a consequence, much depleted, but it still covered commercial intermediaries and exchanges, negotiable instruments and the jurisdiction of the commercial courts. These subjects have recently been regrouped in the new French CdC of 2000, which again also covers company and bankruptcy law.

As for the specialised French commercial courts, there are many commercial courts throughout the country. Their presidents are elected by the local business community and they have lay judges. These courts have their origin in an Edict of Charles IX of 1563, which established in Paris an elected lay commercial court to decide the smaller commercial cases. This set-up was subsequently copied in many provincial towns. The commercial courts hear the commercial cases, including matters of company and bankruptcy law regarding merchants. The proceedings are informal and geared to speed. Parties need not be represented by counsel. The system has worked well and traditionally had a good reputation, although in modern times it has not remained free from scandal and accusations of rigging.

Belgium also has a system of commercial courts, but they were abandoned in the Netherlands. As in Switzerland and Italy, which took the step earlier, there is no longer a separate commercial code. Some of the content of the former commercial codes has been shifted to the civil codes or otherwise to separate statutes.

As regards the history of commercial law in Germany, there was enormous diversity in civil and commercial law between the different German States and Northern German (Hanseatic) towns, well into the nineteenth century. After 1848 there was at least a Bill of Exchange Act as a uniform law, therefore promulgated per state and not at national level. From 1861, there was a General German Commercial Code, itself at first a uniform law, but

[82] See, for the history of French bankruptcy, *Dalhuisen on International Insolvency and Bankruptcy*, vol 1 (1986) 1–60.

it acquired federal status in the North German Bund in 1869 and became the all-German Commercial Code after Germany's unification in 1871. A commercial Supreme Court was established in Leipzig in 1871. After 1879 it was converted into the German Supreme Court or *Reichsgerichtshof* (now *Bundesgerichtshof* in Karlsruhe) and the separate commercial court system disappeared. Thus in Germany there are no longer special commercial courts but there are special commercial chambers within the courts. They deal with commercial cases pursuant to the *Gerichtsverfassungsgesetz* of 1877. Each contains two lay judges who need not be lawyers. They are appointed for a term of four years, which may be extended.

As already mentioned, the German Commercial Code was adapted in 1897 at the time of the general German private law codification (*Bürgerliches Gesetzbuch* or BGB), without a fundamental re-orientation, and was then called the *Handelsgesetzbuch* or HGB. Both entered into force on 1 January 1900. In 1937, company law (the AG but not the GmbH) was put in a separate statute. In Germany, bankruptcy law had always been separate.[83]

1.1.8 Old and New Commercial and Financial Law. Transnational Notion of Professionality, a Separate Legal Order for Professional Dealings

We saw that the contract for the sale of moveable tangible assets (or goods in a common law sense) is often still considered to be at the heart of commercial law in common law countries where this law is trade-oriented. In civil law, there are only some limited special rules for sales in the commercial codes which otherwise have a bias towards the commercial rendering of services but also cover other subjects like (sometimes) company, insurance, banking and bankruptcy law.

Professionality of the contracting parties is *not* a feature per se of traditional commercial law of this type, especially not in common law, but if, as in France and Germany, special commercial law rules are sometimes still applied to these contracts, it is because in essence they are concluded between merchants, therefore in more modern terminology between professionals in their trade. Whatever the traditional differences between the French and German approaches in this respect (see the previous section), this suggests *greater expertise*, *business contact*, *and regular activity for financial gain* and therefore an activity between professionals or businessmen, even if sales may also be concluded between private persons under the normal private law rules, and cheques drawn, and services of transportation and insurance contracted for under the same commercial code.

For *domestic* activities, one may conclude, however, as many have, that the distinction between business (or professional) and private (or non-professional) activity as such has gradually become *less* important for the law. This is reflected in commercial law having become less significant as a different branch of the law everywhere, even if France still

[83] For a history of German commercial law, see Goldschmidt, 'Universalgeschichte des Handelsrechts' in his *Handbuch des Handelsrechts*, 3rd edn (1891). See, for the nineteenth-century discussions on the relationship between BGB and HGB, P Raisch, *Die Abgrenzung des Handelsrechts vom bürgerlichen Recht als Kodifikationsproblem im 19 Jahrhundert* (1962). The first more theoretical treatises on commercial law appeared from the sixteenth and seventeenth centuries, notably in Italy: see Straccha, *Tractatus de Conturbatonibus sive Decoctoribus* (1553), and Casaregis, *Discursus Legales de Commercio* (1740). See, for older French commercial law, J Savary (who largely drafted the *Ordonnance* of 1673), *Du Parfait Negociant* (1695).

maintains a separate court system for commercial disputes. It has already been noted that some civil law countries, such as Italy, Switzerland, the Netherlands and Brazil have therefore abandoned any such distinction and there is no longer a separate commercial code in these countries. Many writers in Germany also argue for this, as noted above. In modern times, domestically, special treatment has often become relevant, *not* for business dealings, but rather for consumers or non-professionals in their dealings with each other and particularly with professionals—therefore outside commerce. The result is that professionals and their dealings are again differently treated, although that is now not so much by design on the basis of special commercial or customary considerations, but rather by default, on the basis of special needs for others, especially consumers.

This may be relevant for instance in the application of modern notions of good faith to determine the rights and duties of the parties to a contract, when expertise and reasonable expectations may be taken into account, compare in particular sections 157 and 242 of the German BGB. This was considered especially important for the protection of weaker parties but may even now be much less relevant for professional dealings, see section 1.1.4 above and in particular Volume II, chapter 1, section 1.3.3. In civil law, the good faith notion may thus result in the nature of the relationship of the parties and the legal effect thereof on their dealings becoming a distinctive feature, as it is in common law where this was done, however, without using the doctrine of good faith; see Volume II, chapter 1, section 1.1.1. As we have seen, the result may be *less* protection for professionals all around. The notion of good faith in civil law is here only at its beginning as we shall see and there is commonly still a serious danger of a spill-over effect of consumer protections into professional dealings.

It was already been noted (in section 1.1.1) that in recent times financial rather than trade or mercantile considerations emphasise the special nature of modern commercial law and is introducing new notions not only of contract but also of proprietary law. Again, this is particularly relevant for professionals. In the financial world, leases, repos, secured transactions (including floating charges), and investment securities entitlements, have thus given rise to new notions of proprietary rights, which are alien particularly to traditional civil-law thinking and its systematic unitary approach and which pay no regard to the traditionally closed nature of its proprietary system. In section 1.1.4 above, the dynamic nature of modern contract and movable property law in the professional sphere was further introduced as another major modern development typical for professional dealings.

To repeat, at this stage, this is mostly relevant for professionals, with commercial law merely the likely conduit, but it is another reason why modern commercial law as a separate part of private law is once more in the ascendant. The additional reason is *transnationalisation*. Under the pressures of financial innovation and internationalisation, not only is a transnationalised system of substantive law being created, but this system is at the same time acting as a laboratory in which experimentation is taking place separated from the rest of private law in its domestic variants. This is the new *lex mercatoria* or law merchant; a law for international professional dealings whose features are legal transnationalisation, dynamism and, unavoidably at this stage also, experimentation.

As will be discussed in greater detail below, this law and its new structures are indeed largely meant to operate between *professionals* who are more likely to be able to deal with them and to fashion them. They are also able better to deal with risk and manage it, even legal risk. It reinforces the emphasis on *professional* dealings as the essence of *all* commercial law and of its separateness from the rest of private law and may be connected also with

the operation for them increasingly of a distinct new commercial and financial legal order which is transnationalised, see section 1.5.5 below.

In any event, special (but not necessarily better) treatment of professionals has always remained more important in *international* dealings, of which the international sale of goods is perhaps still the best example, even if financial dealings may have exceeded them in importance or at least in legal attention. Even if the new 2011 EU proposal for a Regulation on the Law of Sales (CESL) may well now have a different approach to cross-border sales within the EU, international sales present a clear instance of a situation where extra risks and complications gave rise to a different legal regime. In a *technical sense*, international sales have indeed always been considered to be contracts between *professional* parties only, therefore between parties who are both knowledgeable in the area of their sale and its risks, are likely and able to make the special arrangements necessary in this connection and are aware of and able to develop *special industry practices* to this end, for which in international sales one should always be on the look-out (compare Volume II, chapter 1, sections 2.1.4 to 2.1.5). Furthermore, in the additional arrangements completing an international sale, such as transportation and insurance, one may also see differences in treatment as compared to domestic dealings which are now likely to be more consumer-influenced.[84]

Unlike domestic sales, the subject of *international* sales in this sense is indeed not commonly thought to cover consumer sales at all, or even sales of goods concerning which an otherwise professional party does not have special knowledge. To the extent that a distinct pattern has developed, the international sale is further limited in scope in that, as a term of art, it is not believed to cover the sale of real estate, negotiable instruments, other documents of title, bonds and shares, or assignments of intangible property (like receivables) either. This is clearly reflected in the 1980 (UNCITRAL) CISG, Article 2, which offers a part-codification of the applicable directory law and is meant as a uniform law. As we shall see (in Volume II, chapter 1, section 2.3.1) it has been adopted by many countries, even if in practice it is often still expressly excluded by the parties to these sales, meaning that the larger actors remain sceptical of the result. One particular reason is the subjective nature of the concept of fundamental breach in Article 25 and of force majeure in Article 79. Another is the unilateral right of the buyer to reduce the price under Article 50. The smaller seller is here particularly at risk. But there is also the confusion about the relationship of the text to other sources of law, evidenced in Articles 4, 7 and 9, the old fashioned offer and acceptance language in Part II which is still directed towards spot sales between private individuals, and the partial coverage of the subject of sales in the text which does not deal with the title transfer and key notion of transactional finality.

Other types of sales may, of course, also be the subject of international sales contracts, including consumer sales (which may require a whole set of other safeguards, increasingly important in cross-border internet transactions) and the rendering of connected cross-border services. However, they are not commonly included in a reference to international sales in a *technical* sense, which, as to subject matter, is therefore limited to tangible *moveable assets sold between professionals located in different states.* In such sales, there are traditionally different rules as to delivery and passing of risk. In view of the distance, there may also result some special *duties of care* of the buyer to protect the goods upon arrival should disputes arise and

[84] See for the concept of merchant and its importance in Art 2 of the UCC, n 77 above. As just mentioned, domestically its importance is now often de-emphasised, but internationally it revives.

goods be rejected. On the other hand, the seller might have a special duty of care if the buyer delays taking delivery in order to preserve the assets, even if the risk has passed to the latter (for example, upon tender of delivery); compare Article 85ff of the CISG. The subject of international sales will be dealt with more extensively in Volume II, chapter 1, Part II.

As just mentioned, much more obvious is the professionalisation in connection with modern financial dealings, even domestically, which is particularly reflected in the law of movable property. If one takes the UCC as an example, it is clear that Article 2 on the sale of goods still maintains a general notion of ownership and its transfer that also obtains between non-professionals, but in Article 2A on equipment leases and in Article 8 on the trading and holding of modern investment securities entitlements, the emphasis is on professional activities (of intermediaries and on the relationship of investors with them). Proprietary rights are then only defined incidentally, that is, for each structure specifically without any resort to general proprietary principles or a unitary system of proprietary rights. That is also true in Article 9 on secured transactions that in its latest text tends to address itself more particularly to professionals (thus excluding consumer transactions; compare, for example, section 9-109(d)(13)). Again, this is all about finance. In Article 4A (section 4A-108) on electronic payment, consumers are explicitly excluded. They are also excluded in Article 5 from the practice of issuing letters of credit (section 5-102 (9)(b)). It confirms the assumption that because of the specialised nature of these financial arrangements, they cannot be handled or are less suitable or even dangerous for non-professionals.

In the meantime, separating out international professional dealings has become increasingly common, even outside finance. Sensitivity to the special nature of activities of *professionals* operating internationally is, for example, suggested in the 1995 UNIDROIT Principles of Contract Law. According to the Preamble, they apply only to international commercial contracts, a restriction not contained in the 1998 European (Lando) PECL, which also apply to consumer dealings but are otherwise quite similar. In the UNIDROIT Principles, internationality and commerciality are not defined but the idea is clear, even though many of the rules seem to come straight from domestic consumer laws. This explains the similarity with the European Principles. Both sets of Principles will be analysed in greater detail in chapter 2, section 1.6.

Thus, in these various areas, the distinction between professional and other dealings has become important, at least transnationally.[85] A *more radical* approach altogether is the *distinction in general* between the *professional sphere* on the one hand and the *private or consumer sphere* on the other with emphasis therefore on: (a) the types of parties rather than

[85] The notion of commerciality has also been defined in the context of sovereign immunity in terms of the distinctions between acts *de jure imperii* and *de jure gestionis*, but the aim is then to distinguish public and commercial acts of sovereigns and their agencies, not to distinguish between (international) commercial and other private law acts.

In the EU, the notion of consumer is of considerable importance, notably in the protection of consumers through consumer contract law. The ECJ has defined 'consumers' as natural persons acting outside the range of professional activity: see Case 361/89 *De Pinto* [1991] ECR I-1189. Problems may arise where individuals also act professionally, raising the question whether such activities may still benefit from consumer protection. Protection is not afforded unless the professional activity was insubstantial: see Case C-464/01 *Gruber* [2005] ECR I-439. The counterparty may here rely on his good faith when an individual contracts for his business. It is also relevant whether the goods are or could be used for professional purposes, require delivery at a business address, or there is VAT registration. This suggests that the buyer may have raised wrong expectations and accordingly bears the risk, but in internet transactions it may be simply the nature of the goods and the likelihood of professional use that will determine the issue.

on the nature of their dealings; and (b) the qualification of the one as essentially globalised and legally transnationalised, and of the other as remaining in essence domestic.

Modern commercial law is then typically tied to *all* flows of goods, services, knowledge, and money *between professionals*, who increasingly conform here to internationally established patterns. This may become relevant even if on occasion they may still be operating purely domestically, yet under internationalised standards. There is here no basic other limitation in scope. This is the preferred approach in this book and ties the new transnational law to the emergence of a *new legal order* for all professional dealings, whether or not playing out domestically or transborder. See further the discussion in section 1.5 below.

The result in so far as the applicable law is concerned, is the application of transnationalised legal concepts to *all* dealings of professionals to support their legitimate needs (which are needs that do not offend public order and policy in the place of operation). That is the modern concept of the *lex mercatoria* as here defended, in which, as we shall see, there are several sources of law amongst which local laws may still play the residual role, but, crucially, these local laws are then transnationalised and may accordingly be adjusted and transformed to fulfill their role in that context and at that level.[86]

Professional dealings are here considered to be all dealings in the international flows of goods, services, capital and technology between individuals or entities that:

(a) make it their business to do so;
(b) regularly engage in that activity; and
(c) are sufficiently expert in it.[87]

The direct consequence is a less subtle legal attitude to these professionals who are used to dealing in risk. It may also mean specialised proprietary structures not used in other parts of private law, and a more dynamic approach to contract as summarised in section 1.1.4 above and as will be more extensively the subject of Volume II. In sales, this leads to the basic distinction between professional and consumer sales, with the legal regime applicable to professionals being considered increasingly transnationalised. Importantly, this would be so even on those occasions when the relevant transaction may not have any international aspects; again, in this approach, it would be unrealistic to consider local professional dealings to remain subject to different rules if they concern the same business and are similarly structured. Economically speaking, there is indeed ever less justification to subject professional dealings to a different legal regime depending on the origin of the parties and their location in one or more countries. The result of the underlying flows being internationalised is thus a unitary legal approach for all operations in the professional sphere in which *internationality* need no longer be defined. Neither needs commerciality. Arbitrary distinctions in this connection may thus be avoided.[88]

[86] See JH Dalhuisen, 'What Could the Selection by the Parties of English Law in a Civil Law Contract in Commerce and Finance Truly Mean?' in M Andenas and D Fairgrieve, *Tom Bingham and the Transformation of the Law* (2009) 619.

[87] Another feature is here that only companies are likely to be involved in international dealings (therefore not individuals, certainly not consumers), whose business requires some expertise, is on some scale, whilst the interests to be defended are considerable but it also means that these issues primarily arise between parties that are aware of and used to taking some risk and apt to handle it professionally.

[88] The considerable confusion that is here arising in the EU in the context of its Draft Common Frame of Reference (DCFR) as a proposal for the codification of private law in EU and the more recent carve out for the law of sales in the Oct 2011 EU proposal for a Regulation in this area, will be discussed in nol II, ch 1, s 1.6. It may suffice here to say that in these texts no proper distinctions are made between consumer and professional dealings

It should be clear that these transactions are no longer confined to the sale of goods or other forms of trading or even financial transactions, but may also include agreements between, for example, large law firms and accounting firms in the realm of services even within the same country.

In summary, the consequence of a transaction being in the professional sphere, or rather in the transnational commercial and financial legal order, is the increased likelihood of it being taken out of the domestic law context altogether, both on the contractual and proprietary side (for movable property). It will be governed by its own set of transnational legal concepts in a unified cross-border legal framework, even if within that new law the contractual and proprietary structures may not yet form a single coherent or closed system of rights and obligations. This precisely defines the scope and challenge of the new *lex mercatoria*, but it was argued before that the professional community is likely to be well able to deal with this challenge and devise the necessary protections and make good use of the flexibility it entails within the larger room for party autonomy it is being given. Indeed, this has become the major task of structuring or transaction lawyers in international commerce and finance and is supported in international commercial arbitrations.

1.1.9 The Role and Status of International Commercial Arbitration

Not only are international commercial and financial dealings increasingly taken out of a domestic legal environment, but their operation within the transnational commercial and financial legal order with its own *lex mercatoria*, is also proving to have a profound effect on the dispute resolution in that order. It is common still to domesticate international commercial arbitrations in the place of the seat, which continues to nationalise all arbitrations even if international,[89] Although these issues may remain contentious, in the laws of *arbitration* a special approach to international professional dealings is now commonly

and between domestic dealings and transnational dealings, all dealings within the EU for these purposes now being considered domestic. There is thus no room either for a separate transnational legal order also operating within the EU. The consequence is that consumer protection issues spill over into professional dealings, also where they are transnational within the EU, eg between Portugal and Finland. This is another world, however, with very different ideas of risk. Not recognising this makes these EU proposals untenable in the professional sphere.

[89] The notion of the 'seat' of an arbitration in the place where it is conducted (making its *lex arbitri* applicable and, in the view of many, founding the award in it also, that is always in a national law), is in itself a strange one and hardly rational. It corresponds with the Savignian notion that all legal relationships have a seat or *Sitz* in a national law and that notion is then expanded to all legal action. This became the mantra in a time of extreme nationalism but it was always axiomatic, no more than political philosophy where 50 years earlier people had held exactly the opposite view. Furthermore, extraterritoriality of this law is then automatically assumed, governing the international arbitration in all its effects. This is an expression of statutist thinking, see s 2.1.2 below, commonly limited, however, to status and real estate matters.

Seat notions also emerged later in company law, but there it remained uncertain whether it was completely formalised at the place of the registration of a company or whether the place of its real activity had to be considered instead. This remains internationally an unresolved issue till this day and there are two different views. It is also reflected in international bankruptcy, although there seat language is not commonly used, rather the notions of primary and secondary bankruptcy depending on the intensity of activity in the country concerned.

taken.[90] It is, in fact, implied in the reference to international commercial arbitration itself, but the true consequences remain disputed.

It is generally accepted, however, that different arbitration rules apply and that there is a special internationalised arbitration regime when the (professional) parties come from different countries; when the subject matter is of an international nature; or when the arbitration takes place in an unrelated country. Compare the French Decrees Numbers 80-345 and 81-500 (1981) and the new Decree Number 2011-48 (2011), setting international commercial arbitration fundamentally apart; see also Article 1(3) of the UNCITRAL Model Arbitration Law of 1985, updated in 2006.[91] This Model Law (which does not as yet dispense with the notion of the seat), although not a treaty text, is important in the furthering of a special regime for international arbitrations. It is now accepted in several common law countries including some states of the USA, in Scotland, and in some East European countries including Russia, and is much used as guidance elsewhere, even in countries like England and Germany that did not follow it literally but have new arbitration acts, although especially the English Act 1996 still does not maintain here a fundamental distinction between domestic and international arbitrations either.

The distinction leads increasingly to the application of additional or different arbitration rules for international commercial or professional disputes. In this connection the following special features of international commercial arbitration may be noted:

(a) the separability of the arbitration clause, which finds its true legal base in transnational law or in the international commercial and financial legal order and its public order, as does ultimately the jurisdiction of arbitrators, activated to that effect by the arbitration clause but not created thereby. This activation itself is then also a matter of transnational law;
(b) the same may be said for the foundation of the related concept of arbitrability, which now also covers competition, securities, and other public policy issues;
(c) the status and role of international arbitrators is equally founded in the international legal order itself and may compare more particularly to the role of equity judges in common law jurisdictions;[92]

[90] See for this internationalisation or delocalisation of international commercial arbitration J Lew, 'Achieving the Dream: Autonomous Arbitration', (2006) 22 *Arbitration Internationa'l*, 179(Freshfield Lecture, 2005); and earlier J Paulsson, 'Delocalisation of International Arbitration: When and Why it Matters' 22 (1981) *ICLQ*, 53, and more recently J Paulsson, 'Arbitration in Three Dimensions', (2011) 60 *ICLQ* 291, see further also n 95 below. See for the leading defence of legal nationalism in international arbitration, the denial of the latter's existence, and the belief in the dominance of the seat and its *lex arbitri*, FA Mann, 'Lex Facit Arbitrum', 2 *Arbitration International* (1986) 245. Yet the development has been steadily away from localisation ever since the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards did away with the double exequatur, meaning that recognition of awards elsewhere no longer depended on the prior sanction of the courts of the seat.

[91] The UNCITRAL Model Arbitration Law accepts that an arbitration is international when the parties (at the time of the conclusion of the arbitration agreement) have their places of business in different countries, or the place (or seat) of the arbitration or the place of (a substantial part) of the performance is outside the country of the parties. Parties may also expressly agree that the arbitration shall be international. As to 'commerciality', the Model Law states in a footnote to Art 1(1) that it should be given a wide interpretation so as to cover matters arising from all relationships of a commercial nature whether or not contractual. It then gives a number of non-exclusive examples. The idea clearly is that all international business is covered.

[92] It is posited in this connection that, ever since Roman law—the praetorian law or *ius honorarium*—this extra facility has proved to be a necessary institutional pre-requisite to the adequate operation of private law, especially in order to prevent it from stultifying and to underpin private law's dynamic character. Ordinary courts cannot

(d) this international status is also the cause of the procedural flexibility and discretion of international arbitrators in matters of admission of evidence and applicability of private international law rules;[93]
(e) it is equally the platform for the acceptance of multiple sources of law and the hierarchy of the new law merchant or the modern *lex mercatoria* in matters of substantive law application in international arbitrations;
(f) it leads further to the *limitation* as a matter of transnational public *order* of the impact of *lex arbitri* of the seat;
(g) similarly, it leads to a limitation of the review by the domestic courts, either when the awards are challenged in the country where they are rendered (of their seat or any other) or in the context of their recognition and enforcement in other countries; and
(h) notably the sanction of the courts of the seat is no longer required for the international standing of these awards and is no precondition to their enforcement elsewhere. It also follows that their annulment at the seat is no longer dispositive in recognition and enforcement elsewhere either.[94]

properly take this on, never mind how liberal they may be in their interpretation technique and legislators cannot adequately handle it—it would require a continuous process of updating which is beyond their purview. At the level of transnationalisation, there is in any event no formal legislator.

The special position of international commercial arbitrators in this regard is underlined by the opinion often expressed in the sense that at least international commercial arbitrators may rely on notions of the *lex mercatoria* whilst ordinary courts remain beholden to the application of national laws. This is a grave error which would in particular exclude resort to international custom and general principle in domestic courts unless authorised by a national law and thus seriously compromise the role of commercial courts in international commerce and finance, but the sentiment is correct in so far that international commercial arbitrators may have extra powers, which, as is here suggested, are institutionally founded in the international commercial and financial legal order itself and rely on their conscience, knowledge, and sensibility, as equity judges did: see further JH Dalhuisen, 'International Arbitrators as Equity Judges' in PH Becker, R Dolzer and M Waibel (eds), *Making Transnational Law Work in the Global Economy: Essays in Honour of Detlev Vagts* (210) 510.

In this connection, Preamble 13 of the EU Regulation of 2008 on the Law Applicable to Contractual Obligations (Rome I which replaced the earlier Rome Convention in this area) makes it at least clear that parties may now opt for non-state law as the law applicable to their contract, which state courts would then have to apply, but short of such an election, this could still be doubtful. International arbitration agreements and arbitrators are outside the scope of the Regulation and are not therefore subject to similar constraints and may not therefore depend here solely on a parties' choice of law to the effect in their contract.

[93] Importantly, this freedom may also concern the method of reasoning in the award. Unfortunately these awards are becoming longer and longer. One reason is that arbitrators seem to feel that they must answer each point raised by the parties. Judges operate differently: they identify the relevant facts and relevant laws and deem the rest of the arguments immaterial and irrelevant and leave them as they are. Arbitrators seem less confident.

It may matter in particular where the reasoning may give rise to annulmentas under Art 52(1)(e) of the ICSID Convention, which of all the grounds for annulment under this Article looks most like an ordinary appeal ground: 'the award has failed to state the reasons on which it is based'.

In *International Centre for Settlement of Investment Disputes Washington, DC Compañía de Aguas del Aconquija SA and Vivendi Universal SA v Argentine Republic* (ICSID Case No ARB/97/3, Annulment Proceeding), 10 August 2010, the Ad Hoc Committee found that the standard is that the 'reasoning used by the Tribunal must have been plausible, that means adequate to understand how the Tribunal reached its decisions, it being given the benefit of the doubt if there is room for a difference of opinion in the matter'. Nevertheless, the question of reasoning remains problematic in international arbitrations and seems to become ever more so.

[94] This is the French position culminating in the *Putrabali* decision of the French Cour de Cassation, n 11 above, but it is also the American position, see *Chromalloy Airoservieces Inc v Arab Republic of Egypt*, 937 F Supp 907 (DDC 1996) although the reasoning is different. In the US, it is considered a matter of domestic US public

Thus on a better view, these awards and the arbitration agreements on which they are based, as well as the power and status of international arbitrators, are founded in the international commercial and financial legal order itself from which they derive their legitimacy and the awards derive their international currency.[95] International arbitration is not then merely based on party autonomy which would limit the jurisdiction of international arbitrators. It follows that the arbitration clause activates but does not found the arbitration. Or at least, that would now appear to be the more satisfactory academic model to explain and clarify what is happening and to guide the process of international arbitration in respect of commercial and financial dealings between professionals in our times. Globalisation of commerce and finance goes together with transnationalisation of its legal regime and of its dispute resolution, review, and enforcement facilities.

In fact, there is little point in being a nationalist in an internationalist world. It produces ever more unsatisfactory or contradictory answers. We see here a historical trend: law, even commercial law, was nationalised in the nineteenth century and became territorial. That was the model and political philosophy of those days. This trend is now reversed, the movements of the international flows of goods, services, information, payments, and money (if not also of people) and their scale require it.

It earlier led in Europe to the conditions that made the EU in its present much extended form, possible and necessary and is also at the heart of its openly declared existence as a separate legal order. But the trend goes much beyond it. There is in international arbitration also the drift of French case law up to the Cour de Cassation which introduced the concept of an international arbitral order. It is much the same as the transnational and commercial legal order in respect of all professional dealings as proposed in this book,

policy that favours arbitration whether a foreign annulled award can still be recognised and enforced in the US and US courts exercise their discretion under the New York Convention in this manner.

The key is, however, that annulment by the court of the seat is not dispositive in the US either and that is more and more the international attitude and in fact the consequence of the NY Convention having abandoned the double exequatur of the 1927 Geneva Convention and having rendered annulment at the seat no more than a ground for refusal of recognition and enforcement elsewhere as a matter of discretion of the recognising court.

However, there is often still considerable confusion here. The need for support at the place of the arbitration from the courts of the seat is often confused with the question of where the arbitration and the award are founded. Support may be necessary in many countries. In fact, recognition and execution is only one example of it. Like the latter, this support is usually not necessary in the country of the seat where there are mostly no relevant asserts or activities. The seat will be chosen for its neutrality in this respect. Provisional measures and preservation matters equally do not normally concern the country of the seat but must be demanded wherever relevant. Many countries may thus have to support and the *lex arbitri* of any of them is then relevant, not merely and certainly not exclusively, the one of the seat.

It may be that the courts of the seat and their laws are the more appropriate when it comes to appointing arbitrators and dismissing them, if the applicable arbitration rules chosen by the parties do not provide for such eventualities, but even such measures have no force outside the countries of the seat. Extraterritoriality of the laws of the seat in this regard may not be assumed and it is quite possible—even if undesirable—that other arbitrators emerge elsewhere and that they, or dismissed arbitrators, proceed to an award. It will ultimately all be a matter for review and recognition in recognition countries, where indeed the true control is, not therefore in the country of the seat.

[95] See for the *Putrabali* case, n 11 above. In the literature, see Paulsson n 90 above. The idea has been defended that party autonomy itself carries the delocalisation, it then being seen as a legal order of its own. The pre-existence of an international commercial and financial legal order that sanctifies party autonomy of this nature and also founds the status and powers of the arbitrators, which are merely activated by the arbitration clause, is here preferred. See further the discussion in s 1.5.5 below.

even if the new French Arbitration Act of 2011 hesitates to draw the conclusion and still seems to think that international arbitration to the extent it operates in France remains a French product. The more modern trend is no longer concerned with definitions like 'internationality' and 'commerciality' (see the discussion in the previous section), but rather with professional dealings per se.

The special arbitration regime for professionals in their international dealings is indirectly, even if incompletely, confirmed in the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (Article 1.3). First, there is the reference to 'foreign' awards and abolition of the double exequatur. It also allows states to limit the application of the Convention to commercial awards (the 'commercial reservation'). Even if they do *not* do so, the common view is that disputes between states on boundary and similar political issues, perhaps including disputes with foreign investors (unless further treaties allow it in which connection bilateral investment treaties or BITs may be important), are excluded and so too are employment and family law issues unless incidental to the main dispute. The New York Convention thus limits itself to international (commercial) arbitral disputes, although expressed in the (imperfect) language of 1958 which could not have foreseen the direction international commerce and finance was to take, nor its modern scale and its ever more justified claim to constituting a legal order of its own as it did well into the eighteenth century, an approach to be explored further below in sections 1.4 and 1.5.

1.1.10 International Arbitration and International Commercial Courts

As has already been noted in the previous section, in international arbitrations, the transnationalisation of modern commercial law is often dealt with informally. International arbitrators tend to enjoy greater freedom in conducting these proceedings and in finding the applicable law. Accordingly, they commonly assume greater freedom in fashioning the rules of procedure and evidence and the applicable private international law rules wherever they may still be relevant. In finding or developing the applicable substantive law, they may then also more freely rely on transnational custom or principle where necessary or appropriate and operate with a different concept of party autonomy that may even extend into the proprietary area, as we have seen.

This is the area of the modern *lex mercatoria* with its various legal sources and their hierarchy, which then also covers the role and powers of international arbitrators. It was suggested in this connection that the role of international arbitrators is becoming here more akin to that of equity judges in a common law sense before the latters' role became much curtailed in England after the eighteenth century when legislation took over as the more normal corrective of the common law.[96]

[96] See n 92 above.

In international commercial cases, it is submitted, national courts should assume the same freedoms, but often hesitate.[97] This is also an issue of powers.[98] To support the new transnational law in the professional sphere, it would therefore not be a bad idea, nor too far-fetched a proposition,[99] to set up an international court system for professional dealings operating in a similar manner as the commercial courts once did in regionally divided countries.

[97] It is worth noting in this connection that there may be a formal attempt at approximation when parties choose a local court for the resolution of their international commercial disputes. This is the subject of the 2005 Hague Convention on Choice of Law Agreements which facilitates international recognition and enforcement of ensuing judgments in all Member States of the Convention, along the simplified ways of the New York Convention for international arbitration awards. This is considerable progress. The Convention has so far only been ratified by Mexico but has been signed by the US and the EU.

The difference remains, however, in the attitude to the applicable law, where arbitrators are likely to exercise greater freedom. It is submitted that ordinary courts chosen by the parties should do the same so that a real alternative results, the distinction then being only in the possibility of appeals in the ordinary courts, a facility, it is further submitted, the parties should be allowed to exclude (an issue with which the Convention unfortunately does not deal—such an exclusion is still against public order in many countries).

[98] Note also in this connection Judge Wilkey speaking for the majority in the Court of Appeals in the American case, *Laker Airways Ltd v Sabena Belgian World Airlines* 731 F2d 909 (DC Circuit 1984), at the same time as the English judiciary in *Amin Rasheed Shipping Corporation v Kuwait Insurance Company* [1983] 1 WLR 228, 241, see n 100 below: 'Despite the real obligations of courts to apply international law and foster comity, domestic courts do not sit as internationally constituted tribunals. Domestic courts are created by national constitutions and statutes to enforce primarily national laws. The courts of most developed nations follow international law to the extent it is not overridden by national law. Thus, courts inherently find it difficult neutrally to balance competing foreign interests'.

Note that this statement came within the explicit rejection of the balancing test of para 403 of the Restatement (Third) of the Foreign Relations Law of the United States (1987), even though a reasonable link between forum and controversy was considered to be an important limitation on US jurisdiction. This Restatement was in preparation at the time and is now more commonly accepted, *cf* the US Supreme Court in *Hartford Fire Insurance Co v California* 509 US 764 (1993), in which both the majority and the dissenting minority relied on it. See for a further and more particular discussion, the dissent of Justice Scalia in that case. To the extent this Restatement is now accepted, it puts the status of the courts in dealing with international commercial cases in a different light.

Note also that by using a forum selection clause, it is normally accepted (unless the forum selection would work out to be unfair or utterly unreasonable for one of the parties in the circumstances of a case) that parties may choose a court that balances the potentially involved governmental interests better or more neutrally, like an international commercial arbitration panel would do that has undoubtedly an international status, see further s 2.2.6 below. To the extent national courts are increasingly willing to do the same, again it is not illogical to impute to them a similar status. It would certainly seem fair to say that, especially under the influence of much increased internationalisation and globalisation since 1984, matters have moved on.

It should also be noted in this connection that, within the EU, domestic courts in EU matters sit as European courts subject to the guidance of the European Court of Justice, from which prejudicial opinions may be and frequently are asked. The notion of national courts sitting as international courts is therefore by no means new. Another issue that could be raised in this connection is whether domestic courts would have to be more conservative in developing international law than international courts or international arbitrators would have to be. In this connection the observation of Lord Slynn in the first *Pinochet* case [2000] 1 AC 61, which implied that the House of Lords in a case like this one did *not* sit as an international court and would therefore be more restricted in developing international law, may be of interest. The majority clearly did not see it this way, although it did not argue the point explicitly. *Cf* also L Collins, 'Foreign Relations and the Judiciary' (2002) *ICLQ* 509 with reference to the Court of Appeal in *Kuwait Airways Corp v Iraqi Airways Co* [2001] 3 *WLR* 1117, 1207 in which the further development by the English courts of international law as to what was justiciable or not was also not considered impeded.

[99] See in favour of such an international court to operate as an appellate court in the supervision and recognition of arbitral awards internationally Mauro Rubino-Sammartano, *International Arbitration Law and Practice* (2001) 980, and JH Dalhuisen, 'The Case for an International Commercial Court' in KP Berger et al (eds), *Festschrift Norbert Horn* (2006) 893. See further HM Holtzmann, 'A Task for the 21st Century: Creating a New International Court for Resolving Disputes on the Enforceability of Arbitral Awards', and SM Schwebel, 'The Creation and Operation of an International Court of Arbitral Awards', both in M Hunter et al (eds), *The Internationalisation of International Arbitration*, The LCIA Centenary Conference (1995) at 109 and 115.

The concern of these last two authors is the recognition of foreign awards under the New York Convention of 1958 and the possible bias of local judges. The idea is to replace their involvement with that of an international court, which would acquire exclusive jurisdiction in the matter. Enforcement of recognition orders of such an

One possibility in this context would be to accept that domestic courts in international commercial matters sit as international commercial courts.[100] Judgments of these courts should then become universally enforceable, much as international arbitration awards are

international court would, of course, remain a domestic affair. It would be logical that such a court would also become solely competent for challenges or setting aside petitions, which are now normally brought in the domestic courts of the place of the arbitration. Other forms of ancillary proceedings could be added, such as interim protection measures and compelling the attendance of witnesses, see also M Hunter et al (above) at 157. The proposal is important though more limited than what is proposed here.

[100] See for the idea of local courts operating as international courts in this connection, the English case of *Amin Rasheed Shipping Corporation v Kuwait Insurance Company* [1983] 1 WLR 228, 241. The case is of special interest in view of the important cast of judges expressing their (minority) views in the lower courts with the House of Lords ultimately re-establishing orthodoxy. The facts in this case are not of great import. There was an insurance contract concerning an insurer in Kuwait, drafted much along the lines of the relevant standard English policy, yet without a choice of law and competent forum clause. There thus arose concern about the applicable law and about the jurisdiction of the English courts.

In the lower courts, Judge (as he then was) Bingham [1982] 1 WLR 961, thought that the contract could be covered by an international regime inspired along English lines (although not so in this case), so that under the applicable English rules of international jurisdiction the competency of the English courts could be established on the basis of the application of English law. In the Court of Appeal, the Master of the Rolls Sir John Donaldson thought that English courts could have jurisdiction over an unwilling defendant because the English courts could, in cases like these, function as *international commercial courts*.

In the House of Lords [1984] 3 WLR 241, Lord Diplock thought, however, that contracts could not operate in a vacuum as they would then be only scraps of paper. International law was clearly considered vacuous in this connection and the implication was that only a domestic law could apply, which in this case was eventually thought to be English law, a view supported by Lord Wilberforce. Lord Diplock further thought that English courts could not operate as international commercial courts and thus force themselves on unwilling defendants. Also, for English jurisdiction in cases like these, there would have to be a solid basis, which could be, but need not be, and was in this case was *not*, found to be in the application of English law, especially since in this case there was a Kuwaiti court available.

In a later unrelated case, *EI du Pont de Nemours v Agnew* [1987] 2 Lloyd's Rep 585, Lord Bingham, then in the Court of Appeal, borrowed some of the 'legal vacuum' language but seemed to leave open entirely the question whether that vacuum could be filled by international law, including international general principles or custom, while in the same year in the *Deutsche Schachtbau- und Tiefbohrgesellschaft* case [1987] 3 WLR 1023, the Court of Appeal under Sir John Donaldson held unanimously that at least international arbitrators could rely for the applicable law on internationally accepted principles, thus accepting not only general principle as a source of law but allowing *international* principles and customs to operate in that connection also. Notably, this was not considered to be against English public order. See further the discussion in section 3.3.1 below.

It is sometimes submitted that this could only be so in international arbitrations and that at least the 1980 Rome Convention on the Law Applicable to Contractual Obligations did not allow it in ordinary courts: cf *Dicey and Morris on the Conflict of Laws*, 13*th* edn (2000) 1216 and 15th edn (2012) 1223, but in truth the text is inconclusive and the point seems never to have been considered. So much is clear, however, that, even in England, no true principle is involved any longer as it is inconceivable that there is any fundamental difference between the applicable law in courts of law and in arbitrations. As far as the 1980 Rome Convention on the Law Applicable to Contractual Obligations was concerned, it was a matter of interpretation on which there was much contrary opinion in the rest of Europe. In any event, where more substantive rules are introduced, as in Arts 5, 6 and 7, more general principles of protection or balance were used. The replacement of the Convention by an EU Regulation in 2008, has not clarified the issue, except that under its Preamble, parties may choose a non-statist law even though the relevant text was ultimately deleted from the body of the regulation itself. It left also open the question whether judges may do so in appropriate cases if no such choice has been made by the parties.

In the US, opinion also moves in the direction of accepting international principle as the applicable law, see eg DW Rivkin, 'Enforceability of Arbitral Awards based on *Lex Mercatoria*' (1993) 9 *Arbitration International* 67.

In connection with international arbitrations, the question has further arisen whether they themselves could operate in a legal vacuum, therefore, in this terminology, separate from a domestic law or legal system (or local arbitration Act), often perceived to be the domestic law of the seat of the arbitration: see also n 94. above and accompanying text; also A Redfern and M Hunter, *Law and Practice of International Commercial Arbitration*, 5th edn (2009) 188ff. ICSID arbitrations notably do not operate in a national arbitration framework. Again, the more significant issue would appear to be whether the vacuum may be filled in another manner, eg by transnational law emanating from the transnational commercial and financial legal order as the new law merchant setting also common international arbitration standards.

under the New York Convention of 1958 on the Recognition and Enforcement of Foreign Arbitral Awards or as *in rem* judgments are habitually enforced in admiralty worldwide.

The difference with international arbitrations is that there might be more stability in such a court system and there would also be the possibility of appeal. On the other hand, local courts might still be predisposed to apply their own regulatory laws even in international cases that have little contact with their own territory and may also not attain the status of equity judges that arbitrators may now have in the development of transnational law. See the previous section 1.1.8.

Such an international court system comprised of domestic courts sitting in international commercial cases (they could have some lay judges) could have a central highest international appeal court to test points of law (thus forgoing national layers of appeal). That would not apply to international commercial arbitrations, which normally do not provide for an appeal in this sense.

This International Commercial Court could also be enabled to give preliminary opinions on points of transnational private law or the modern international *lex mercatoria*, and on such issues as the reach of domestic mandatory and other regulatory laws in international cases and on matters of international procedure or public order, if the relevant court or arbitration tribunal or the parties in agreement on such a request so wished. In principle, this would follow the EU example of preliminary opinions under Article 267 TFEU.

This highest court could also deal with international enforcement of commercial judgments and arbitral awards if contested in the domestic courts of the place of enforcement (on the limited grounds set out in the New York Convention but substituting international public policy considerations for domestic ones) and take over the adjudicatory challenges and supervision of the arbitral process in the courts of the place of the arbitration (seat), although these courts could still function in support subject to a similar system of preliminary opinions which could also be requested by the arbitration tribunal if it considered its authority to be undermined in this manner. Interim measures, especially involving attachments or similar preservation orders, might also be sought from such an International Commercial Court, especially if assets were located outside the country of the seat of the

One thing is clear, there is in these international cases a close connection between the law applied and the status of the tribunal. If the law is transnational, it is not strange to assume that courts applying such law (be they national courts or arbitration panels) thereby acquire an international status as well. Thus when in *Amin Rasheed* [1983] 1 WLR 228, 241, there was a discussion of English law being applicable as common currency or lingua franca, this implied internationalisation of both the applicable law and the courts applying it. Seen from this perspective, it was not at all so strange that the commercial courts in London, in the minority opinion, were considered to operate as international commercial courts. Of course, commercial courts in other countries could then claim a similar status.

Neither is it strange that this may affect unwilling defendants assuming an adequate rule of jurisdiction could be formulated for these courts under international (customary) law or on the basis of general principles. The jurisdictional limits could then be found in a vibrant *forum non conveniens* approach in the courts asked to exercise this jurisdiction and in a broad concept of *lis pendens* operated in other international commercial courts subsequently petitioned and asked to intervene, or in an intelligent handling of subject-matter jurisdiction and comity requirements in the American manner. See also s 2.2.6 below.

One consequence which is often overlooked is that the ensuing judgment could then hardly be qualified as a domestic judgment and be asked to be enforced as such. In fact, judgments of this nature should be enforced in the manner of arbitral awards under the New York Convention or now also in the manner of the 2005 Hague Convention on Choice of Court Agreements. Ideally, the principles behind these Conventions should be extended to them, in which connection the question of proper (judicial) jurisdiction would also have to be further considered. Another idea would be to allow the parties to select the regime of these Conventions for the international recognition of commercial judgments.

arbitration. It would not be the idea, however, for this Court to operate otherwise as an appeals or review court, certainly not in the substance of the decision, except, as just mentioned, in respect of local commercial courts acting like international courts in international commercial disputes.

This International Commercial Court should have exclusive jurisdiction in the areas of its competence and be allowed to base its decisions on transnational or international principle and practice much as the ICJ does for public international law disputes under Article 38(1) of its Statute.

In terms of this book, it would be best to introduce here, in respect of substantive private law issues, the hierarchy of norms of the *lex mercatoria* (see sections 1.4.13 and 3.1.2 below) supplemented by a balancing facility or minimum international standards in respect of governmental interests (or regulatory issues) as an international public order requirement. A similar system could be envisaged in matters of procedure and evidence where any domestic *lex arbitri* would thus be preceded by other rules, especially by the practices and customs of international arbitration. It is conceivable that such an approach to procedural issues could also be accepted in domestic commercial courts dealing with international cases. As just mentioned, this system of rules should be supplemented by a uniform notion of international public order for challenges and recognition disputes.

The creation and operation of this International Commercial Court would require treaty status. Its findings should be accepted as final and be directly enforceable in all Contracting States, therefore in all states participating in this scheme. It follows that commercial judgments or arbitral awards ignoring such decisions would not be effective or would be remedied accordingly.

This new Court could thus become an important aid to the development of transnational commercial and financial law and its creation would at this stage probably be more important than codifying transnational law itself for which there is no sufficient direction in practice and theory and no sufficient platform amongst legal practitioners.[101] Although, as has already been noted, a number of eminent authors have given their support to the idea of creating an International Commercial Court for the supervision of international commercial arbitrations and the enforcement of international commercial arbitration awards under the New York Convention of 1958, the subject needs renewed attention. The extension of its jurisdiction to recognition problems in all commercial judgments worldwide (on similar grounds to those contained in the New York Convention) is a further possibility. Decisions would be published in principle (even though parts might still have to be anonymised to protect confidentiality). This jurisdiction could of course, still be expressly excluded by the parties in their agreements.[102]

[101] See for practitioners' input in limited areas the UNIDROIT Mobile Equipment Convention of 2002, vol III, ch 1, s 2.1.8 and the EU Financial Collateral Directive, vol II, ch 2, s 3.2.4. See for the lack of this input in the DCFR and CESL and their uncritically following of the established civil law codification ethos, s 1.4.19 below.

[102] There is some kind of example in the WIPO procedure concerning domain names conflicts. Under the classic rules of private international law great differences could arise, encouraging forum shopping. The WIPO procedure allows everyone to ask on line to be entitled to use a domain name registered in the name of someone else. The WIPO then appoints an arbitrator, who decides within six weeks. If he finds in favour of the claimant, the respondent may appeal to the normal state courts to get his domain name back. The first cases were decided on general principles and on those derived from national laws, but are now increasingly determined on the basis of the (transnationalised) case law of these arbitrators, which can be accessed online.

1.1.11 Structure of this Volume

Before the emergence and development of the new *lex mercatoria* is discussed in greater detail, it may be useful for those particularly interested to dwell a little longer on the traditional sources of private law in civil and common law countries, on the development of the codification approach and its significance in this regard, and the survival and significance of other sources of law. This is the subject of the next two main sections (section 1.2 for civil law and section 1.3 for common law), where a further explanation will also be offered for the limited room traditionally left in civil law for the application of fundamental and more general principles and custom. It will also seek to explain and compare attitudes in this regard in the common law and in the modern American variety.

In section 1.4, the sources of law will be discussed more extensively in their operation in civil, common and transnational law. In section 1.5, the discussion will move to the operation of international legal orders and the abandonment of an exclusively statist and territorial view of modern private law creation in favour of a more modern sociological and economic approach leading to greater universalism (at least in international business cases).

This will lead to a fuller introduction to the concept and operation of the hierarchy of principles and norms in the modern *lex mercatoria.* which theme will be further developed in Part III after the traditional conflicts of law approach and its problems have been more fully analysed in Part II, including the problems arising internationally (and therefore also in the application of the modern *lex mercatoria* as a hierarchy of norms) with governmental interests as expressed notably in domestic regulation and similar domestic public policy directives. It concerns here the competition and possible clashes with (domestic) regulatory laws or legal orders.

For the internationally-oriented student interested in the development and operation of different (commercial) legal systems, this lengthy excursion may also serve as an explanation for much of what may, at first glance, look unfamiliar or strange in other legal systems, which she or he has not previously encountered. In particular the different approaches in civil and common law to the sources of the law, statist attitudes and system thinking should be better understood by all.

The approach taken throughout this book is to identify a number of legal constructs, such as in contract the notion of offer and acceptance, *force majeure* and change of circumstances, or otherwise the special rules pertaining to the sale of goods and contractual agency (in Volume II, chapter 1), or in personal property the rules pertaining to assignments (in connection with receivables financing and securitisations), leases and repos (as example of modern finance sales), or floating charges in secured transactions (in Volume III, chapter 1). This is done first to highlight the intrinsic aims and problems in these constructs and their use, then to see what local laws have done with them, and ultimately to consider the requirements of and developments in the transnational practice, where in modern movable property, for example, party autonomy (therefore contractual clauses) is the beginning but where broader practices and fundamental and general principle may need to be demonstrated to underpin newer proprietary structures operating at the transnational level but also public order requirements at that level to protect the international flows of commerce against all kinds of unknown changes or other proprietary interests.

In a comparative sense (therefore in respect of the examples used as illustration and guidance and in identifying a trend), I confine myself in this book largely to the laws and practices of the major countries of the common and civil law, therefore to the laws of England and the USA on the one hand, and of France and Germany on the other. This is not done out of disrespect for any other, but not all can be covered and what is covered should, in my view, be covered in some considerable depth to have meaning. The focus is therefore on the laws in the major industrial, even post-industrial, nations, the development of whose legal systems has been of prime importance for the evolution of commercial and financial law so far.

These legal systems are also likely to provide the natural starting point for the globalised transnational legal structures developing in the international commercial and financial sphere, therefore for professional dealings worldwide, but it will also be shown that it is necessary to move well beyond what the laws of these countries can contribute to arrive at the *new lex mercatoria* which crucially depends on various other sources of law (see section 1.4 below).

1.2 The Origin of Civil Law. Its Traditional Approach to Law Formation and to the Operation of Private Law especially Commercial and Financial Law

1.2.1 The Evolution of Modern Private Law and its Sources

The development of modern international commercial and financial law as an autonomous transnational non-statist phenomenon and the problems it encounters in that connection may be better understood when greater light is shed on the development of the various sources of private law and their autonomy in the course of time.

Although we have become used to the idea that the law, even private law, comes from states—in civil law through codification, in common law of the English variety through the idea that all law ultimately emanates from sovereigns who would only accept and enforce their own laws (and those of others only to the extent incorporated in their own or recognised by them)—it was not always thus and is in fact a typical nineteenth-century nationalistic perception whose prevalence may now be ending, at least in international commerce and finance. As we shall see, it had found important support earlier, among eighteenth-century philosophers, but it is a more recent attitude that became connected with the emergence of the modern state. In England, by that time, it had already led to the absorption of the autonomous commercial (and church) laws into the common law, being the law of the King's courts,[103] even though in common law, the commercial law is, to this day, as we have already seen, not as completely integrated into the general body of the private law as it is in civil law.

[103] See n 18 above.