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Towards a (Post)modern European Contract Law

Estonian and European contract law

A discussion of the development of a European private law and a European contract law is very appropriate here on Estonian soil. After regaining its independence, Estonia, together with the other newly independent states, has had the unique opportunity to completely recreate its private law system. Estonia has been forced to look at private law experiences in various parts of Europe and the world when making decisions concerning its own future. By necessity, Estonia as well as the other countries in the same position, have become showcases of the ongoing processes of the Europeanisation of private law.

Estonia has, for various reasons, including its pre-Soviet historical background, in principle decided to base the development of its private law on the German model.^{*1} From the point of view of Europeanisation, this seems, at the outset, like a step backwards — why look (back) toward the law of a certain country, when legal ideas are moving across borders in Europe at an ever-increasing rate. However, Estonia did not choose German law in order to find a model to copy as such, but rather to find a suitable and needed point to anchor its legal culture.^{*2} When making concrete substantive decisions, a comparative method and a plethora of sources from various places have been used.^{*3}

The Europeanisation of contract law is taking place today on many levels. The rapid rate at which the EC is issuing directives in areas like consumer law is well known.^{*4} However, the creation of a general structure and general rules for a possible European contract law has so far been a task which has been mainly performed by the European academic community. Collections of rules have been created, or are in the process of being created, by various more or less privately organised groups of comparative contract lawyers. For Europe^{*5}, the most important result so far is the collection of the Principles of European Contract Law (PECL), elaborated by the Commission of European Contract

¹ See P. Varul. Legal Policy Decisions and Choices in the Creation of New Private Law in Estonia. – *Juridica International. Law Review*. University of Tartu, V, 2000, p. 107 *ff.*

² As a Nordic citizen I am, of course, a little disappointed that we could not welcome Estonia into the Nordic legal family.

³ P. Varul (Note 1), p. 107.

⁴ See *e.g.* G. Howells, T. Wilhelmsson. *EC Consumer Law*. Aldershot. Ashgate, 1997.

⁵ A similar collection on international level is the very well known UNIDROIT Principles of International Commercial Contracts. Rome. UNIDROIT, 1994.

Law, sometimes also called the Lando Commission after its convener Ole Lando.^{*6} These principles have gained much attention and will certainly influence the legal development of Europe.^{*7}

The PECL have already been used as source material by various countries outside the EU in the development of their own contract legislation.^{*8} Their influence is visible in the drafting of the Estonian Law of Obligations Act as well.^{*9} If the PECL become an important guideline in the Europeanisation of contract law, Estonian law has been placed in the vanguard of such a possible development.

Today I would like to make some general comments on the possible role of the PECL in the Europeanisation of law. As the future is notoriously difficult to predict, I will not try to make any prognosis concerning the role of the PECL in this inevitable process. Instead, my discussion is normative in character. First, I will make some comments on the quality of the PECL, comments that are relevant when discussing a modern law of contract from the perspective of commercial contracts. I will claim that in this perspective, the PECL are fairly modern and useful.^{*10}

However, this does not imply any enthusiasm concerning the idea of the European Civil Code, based on the PECL — which is the vision of at least some of its creators.^{*11} I will, at the end of my paper, argue for a more “postmodern” vision of European contract law and private law that respects the pluralism of Europe while it also promotes the free movement of legal ideas across the European borders.

PECL as modern principles for commercial contracts

The drafters of the PECL have seen as one of the main aims of the Principles to provide a useful set of rules to be chosen by parties from different countries as the “law” governing the contract. According to the express provision in the PECL article 1:101, the Principles will apply both when the parties have expressly agreed to incorporate them into their contract and when they have agreed that the contract is to be governed by “general principles of law” or a *lex mercatoria*. They may even be applied by arbitrators when no explicit choice of law has been made, again as a kind of an elaborated *lex mercatoria*.

Although not all national legal systems would approve of a clause of this kind^{*12}, one may expect that in practice the PECL can become relevant in this way. As a comparison, one should note that the UNIDROIT Principles already have been applied in some arbitral awards as generally accepted principles, even if the parties have not expressly referred to them^{*13}, and that such an award has been upheld by an American court.^{*14} Through such practices, the PECL may also exert influence on the gradual development of national commercial law. And I think this is entirely appropriate. To my mind, the PECL do represent a modern European view on commercial contracting in many respects, and are therefore worthy of being influential in this area.

A good set of European contract rules cannot be created by searching for the “average” European contract law. The strength of the PECL lies in the fact that the Lando Commission did not strive to make only such a compilation, but to design a modern set of principles that responds to the needs of business today — of course with due regard to national traditions. In a very interesting way, this can be seen, *e.g.* in the fact that the Commission members belonging to the common law tradition did not insist on doctrines like the doctrine of consideration, which is both rather strange for a Continental lawyer and impractical from the business point of view. Others, of course, made similar concessions. And what is perhaps most interesting: there are also principles in the PECL that do not reflect any

⁶ O. Lando, H. Beale (eds.). *Principles of European Contract Law*. Parts I and II. The Hague: Kluwer, 2000.

⁷ The most important ongoing activity, “The Study Group on a European Civil Code”, will follow the results of the Lando Commission. The leader of the Study Group, Christian von Bar, is a member of the Lando Commission.

⁸ Even the newly adopted Contract Law of the People’s Republic of China, of 15 March 1999, has been influenced by the PECL.

⁹ P. Varul (Note 1), p. 114; I. Kull. *Legal Remedies Provided in the Estonian Draft Law of Obligations Act for Breach of Contractual Obligations*. – *Juridica International. Law Review*. University of Tartu, IV, 1999, p. 147 *ff.*

¹⁰ As I have been a member of the Commission since 1995 — when Finland joined the EU — my objectivity may of course be questioned. Most of the provisions I will mention were, however, already in place at that time.

¹¹ O. Lando, H. Beale (Note 6), p. xxiii.

¹² See, *e.g.* R. Goode. *A New International Lex Mercatoria?* – *Juridisk Tidskrift*, 1999–2000, pp. 266–267.

¹³ *Ibid.*, p. 266.

¹⁴ M. J. Bonell. *UNIDROIT Principles: A Significant Recognition by a U.S. District Court*. – *Uniform Law Review*, 1999, p. 653 *ff.*

present law, but are taken instead from modern commercial practice. The rules on change of circumstances, which I will return to below, are good examples of this.

As to their substantive starting point, the PECL are certainly very traditional. The main substantive principle is freedom of contract, which is expressly spelled out in article 1:102. However, a collection of principles of this kind, developed primarily to meet the needs of international trade and meant to be used as a kind of soft law based on express or implied choices of the parties, could hardly have had any other starting point. As long as we are talking about soft law for international commercial contracting, the traditional principle of freedom of contract is a natural basic principle.

The modern features of the PECL should be sought elsewhere. First, one should note that the principle of freedom of contract and its corollary, the binding effect of the contract, are not adhered to *in absurdum*, despite the fact that the Principles are offered to the parties to be used at their discretion. The general part of the PECL already includes a provision on good faith and fair dealing (article 1:201) that is mandatory. The parties may not exclude or limit their duty to act in accordance with good faith and fair dealing.

In the Comments on the PECL, this principle is presented as a basic principle that runs through the whole PECL.¹⁵ The principle of good faith and fair dealing should be followed, both when the contract is made and when it is performed and enforced.

Of course, from the point of view of a Continental lawyer, it may seem strange that I mention this principle as an example of the “modern” character of the PECL. In fact, its model is taken from and it corresponds to the established Continental principles reflected, e.g. in the French concept of “*bonne foi*” and the German “*Treu und Glauben*”. In Nordic law as well, a similar concept has traditionally been used to infuse a minimum level of honesty and decency in commercial relations.¹⁶ However, from a common law point of view, this principle has introduced new patterns of thinking into contract law. It has been said that “the criterion ¼ of good faith is mysterious and exciting to an English lawyer”.¹⁷ The principle of good faith has — primarily because of the EC Directive on unfair terms in consumer contracts, but perhaps also because of the PECL — caused much discussion in the common law world.¹⁸

A good example of the practical relevance of the good faith principle can be found in the rules on liability for negotiations (article 2:301). Although the starting point is, and must be, that a party is free to negotiate and is not liable for failure to reach an agreement, the PECL also state that a party who has negotiated or broken off negotiations contrary to good faith is liable for the losses caused to the other party. Entering into or continuation of negotiations with no real intention of reaching an agreement has been expressly mentioned as an example. Rules of this sort reflect ideas of decency and loyalty that should be important in a modern set of rules on contract.

The importance of the principle of good faith and fair dealing in an European instrument is underlined by the fact that basic patterns and customs for honest dealing in the marketplace may not yet be well established in the former socialist countries. In Estonia, section 108 of the General Part of the Civil Code Act prescribes an obligation to act in good faith which thus has been in force already since 1994. Despite this, as Irene Kull states: “the traditions of negotiations and the tradition of fair business relations in a wider sense have not yet developed.”¹⁹

A part of the idea of good faith is the perception of contract not only as a ground where conflicting interests are momentarily reconciled but also as an instrument for loyal co-operation. The more the parties in the marketplace found their relationships on the basis of long-term co-operation, the more important such an approach becomes. The PECL are modern in the sense that they reflect the growing importance of loyalty and co-operation. According to article 1:202, each party owes to the other a duty to co-operate in order to give full effect to the contract. Although the examples in the Comments tend to indicate that the main purpose of the article is to regulate a fairly traditional co-operation duty of the party who receives a performance, there is at least one example which hints that more extensive information duties may be based on this provision. According to the example, a party has

¹⁵ O. Lando, H. Beale (Note 6), p. 113.

¹⁶ See, e.g., T. Wilhelmsson. Good Faith and the Duty of Disclosure in Commercial Contracting — The Nordic Experience. — R. Brownsword, N. J. Hird, G. Howells (eds.). Good Faith in Contract. Concept and Context. Aldershot. Ashgate, 1999, p. 165 ff.

¹⁷ H. Collins. Good Faith in European Contract Law. — Oxford Journal of Legal Studies, 1994, p. 249. Collins here analyses the concept of good faith in the EC Directive on unfair terms in consumer contracts.

¹⁸ See, e.g., R. Brownsword, N. J. Hird, G. Howells (Note 16).

¹⁹ I. Kull. Legal Integration and Reforms — Innovation and Traditions. — Juridica International. Law Review. University of Tartu, V, 2000, p. 122.

to inform the other party if the latter may be unaware of the fact that certain acts in performance of the contract may involve a risk of harm to persons or property.^{*20}

Leaving the general part of the PECL and turning to its more concrete provisions, the choice of examples of modern provisions by necessity becomes extremely subjective. Obviously, I cannot, in this context, go through the whole collection of principles. I will only mention some examples of what I mean when I claim that the PECL are at least relatively modern.

The provisions on formation in Chapter 2 seem, *prima facie*, very traditional and old-fashioned. The chapter on formation which rests so strongly on refined rules concerning clearly separated acts of offer and acceptance does not seem to reflect the realities of the modern marketplace. However, these provisions are in line with those of the modern international basic law of contracts, the UN Convention on Contracts on the International Sale of Goods (CISG). Looking more closely at Chapter 2 of the PECL, one also finds more modern provisions, for example on the binding effect of standard form contracts (article 2:104). In that context, it is interesting to note the procedural fairness rule, according to which a mere reference to standard form terms in a signed contract document is not sufficient; the party invoking them should have taken reasonable steps to bring the terms to the other party's attention before or when the contract was concluded.

It is also worth noticing that the PECL contain a provision on the problem of the so-called "battle of the forms" (article 2:209) that ensues when both parties have referred to their own general conditions. In this provision, the PECL do not try to fit their solution into the traditional scheme of offer and acceptance — which would result in on/off rules preferring either the "first shot" or the "last shot" solution^{*21} — but have chosen a more flexible compromise that reflects recommendations in modern doctrine.^{*22} According to this provision, both sets of general conditions form a part of the contract to the extent that they are common in substance.

The modern principle of loyalty is also reflected in the provision on change of circumstances in article 6:111. According to this provision, a party is, subject to certain conditions, bound to enter into negotiations with a view to adapt or terminate the contract if performance becomes excessively onerous because of a change of circumstances. This provision is not based on examples from national law, but on commercial practice as expressed in "hardship clauses" connected with renegotiation duties.^{*23}

Finally, turning to the chapters on remedies, I would like to mention the very central rule on the basis of liability in the PECL article 8:108. According to this provision, a party's non-performance is excused if the party proves that the failure is due to an impediment beyond its control and that it could not reasonably have been expected to take the impediment into account at the time of the conclusion of the contract, or to have avoided or overcome the impediment or its consequences. This provision expresses the so-called control liability that is also used as the basic type of liability in the CISG (article 79). As the control liability of the CISG has found its way into many pieces of national legislation as well, it is in the process of becoming an internationally accepted basic principle of contract law. For example, the Nordic countries have adopted this principle in their new Sale of Goods Acts, at least for certain situations, and serious consideration is being given to generalising it as the basic liability principle of contract law.^{*24} It is considered to be especially suitable for judging behaviour in businesses. In a modern set of principles for commercial relationships, it is natural to base liability on the concept of control.^{*25}

PECL as model for Civil Code

On the basis of these considerations, as a collection of model rules for commercial contracts, the PECL have many merits. However, some of the drafters of the PECL have more far-reaching ambitions. The Lando Commission has expressed as one of its aims to offer a basis for the future

²⁰ O. Lando, H. Beale (Note 6), p. 120.

²¹ Such thinking is still applied in many national laws, see U. Göranson. *Kolliderande standardavtal* (Collision of Standard Form Contracts). Uppsala: Iustus förlag, 1988, p. 25 ff.

²² See for Nordic law, e.g., J. Hellner. *Standardavtal vid avtalslutande* (Standard Form Contracts When Contracts are Made). – Tidskrift, utgiven av Juridiska Föreningen i Finland, 1979, p. 297.

²³ Hardship clauses are mentioned also in the Comment, O. Lando, H. Beale (Note 6), p. 323.

²⁴ See, e.g., L. E. Taxell. *Skadestånd vid avtalsbrott*. Åbo, Åbo Akademi University Press, 1993, p. 133 ff.

²⁵ This principle is also expressed in the new Estonian legislation, see I. Kull (Note 9), p. 150.

European Code of Contracts.^{*26} In this respect, however, I do not consider the PECL to be as useful and modern as in serving as a model for commercial contracting.

This general aim of the PECL is reflected, *inter alia*, in the fact that the PECL, unlike the UNIDROIT Principles, are not limited in their scope to cover commercial contracts only, but are at least in principle said to cover the whole area of contract law, including consumer relations.^{*27} However, the PECL contain almost no attempt to distinguish between the rules for business relationships and for consumer contracts. This is fairly strange in a set of contract rules that purport to be modern.

The answer to this criticism is given in the PECL: specific rules for consumer contracts should be provided by special legislation.^{*28} This would, however, reinforce the traditionalist idea — in some sense — of a more important general contract law and a special, inferior area of consumer law (*Sonderprivatrecht*). The general rules are considered as main rules, and the consumer rules as exceptions, with unfortunate consequences for example concerning the interpretation of the latter. The said counterargument cannot remove the impression that this is not a very modern collection of rules.

In contrast to the conservative stance of the PECL, one might mention that consumer protection rules, *e.g.* stemming from EC law, are being incorporated in the Estonian legislation for a civil code.^{*29}

As just one concrete example of the (relative) shortcomings of the PECL in this respect, I would like to mention the provision on adjustment of unfair contracts (article 4:110): a party may avoid a term of the contract if, contrary to the requirements of good faith and fair dealing, it causes a significant imbalance in the parties' rights and obligations arising under the contract. This adjustment rule is basically copied from the EC Directive on unfair terms in consumer contracts, and it extends the provision of the Directive to other contracts besides consumer contracts. This extension seems to increase the role of welfarist principles in the PECL. However, the (other) important limitations of the scope of the Directive, which make it relatively traditional and very conservative, *e.g.* from a Nordic point of view, but which are only minimum requirements in the Directive, are all retained and even converted to rules in the PECL.

The strong respect for freedom of contract, as traditionally understood, is contained in the basic solution adopted in the Directive, according to which the unfairness control of contract terms is applied only to the contract terms that have not been individually negotiated. However, as a minimum directive, it does not force national legislations to delimit the power of the courts and supervisory authorities to cover only standard form terms and other non-negotiated terms. It is probably not even the purpose of the delimitation adopted in the Directive to promote such restrictions. The basis for the delimitation was mainly the difficulty in finding unanimity with respect to the need to regulate the fairness of individually negotiated contracts.^{*30} However, the PECL emphasise this very traditional contract philosophy, as they do not present it only as a part of a minimum requirement that can be improved by national law, but as a rule that will eventually become a part of a future European Code of Contracts (and thereby decreasing the protection offered today by, *e.g.* Nordic contract and consumer law).

In the PECL, the traditional, market-rational approach to the problems of contract law can also be seen in another important restriction of the scope of the adjustment provision. Terms which define the main subject matter of the contract and adequacy in value are expressly excluded from the scope of the Directive, and therefore also from the scope of the adjustment provision of the PECL. In other words, neither set of rules extends the application of the adjustment provision to the most central parts of the contract, that is, to the price/performance relationship. In this respect as well, the Directive is a minimum directive and as such does not preclude the more comprehensive view on adjustment that prevails, for example, in Nordic law in this matter. However, the PECL again make a rule of what was only a minimum requirement in the Directive. The developers of a European Code of

²⁶ O. Lando, H. Beale (Note 6), p. xxiii.

²⁷ *Ibid.*, p. xxv.

²⁸ *Ibid.*

²⁹ P. Varul (Note 1), p. 115.

³⁰ The Preamble to the Directive notes that national laws allowed only partial harmonisation and that it was therefore necessary to restrict the Directive only to contractual terms that have not been individually negotiated. In its Communication to the Parliament, the Commission openly regretted that it had to include this limitation in the Directive; see COM(92) 66 final.

Contracts again offer a traditional solution in which the fairness principle is clearly subordinated to the principle of freedom of contract.^{*31}

Toward flexible and fragmented (postmodern) Europeanisation

Not only are the PECL unsuitable to serve as a model for the common European Civil Code or Contract Code, one may even question the idea of a complete harmonisation of European private law altogether.

I have elsewhere more extensively criticised such ideas^{*32}, and I will not repeat all details of the arguments here. The general thrust of my reasoning is the following.

Firstly, a large codification is as such fairly static in nature. This feature would surely affect the European Code in an even more drastic way. The creation of the European Civil Code would mean a shift of legislative power in this area from the parliaments of the Member States to the European Union. This would reduce the power of the Member States to react to socio-economic changes^{*33} within large parts of the central areas of the legal order. Changes could be made only through the cumbersome legislative mechanisms of the Union. Not only would the harmonisation of European contract law be created on the basis of traditional values; it would in addition form an obstacle to the piecemeal experimental development of, for example, consumer protection provisions, which has been so typical of modern European contract law.

Secondly, one may claim that the strength of Europe and the core of its identity is the recognition of the plurality of its languages, social structures and cultures. A systematic harmonisation of law would, in this view, destroy rather than strengthen the identity of Europe, resulting in “abolishing the Idea of Europe”.^{*34}

Some have seen the EU as an emerging new type of “Post-modern State”^{*35}, which “is abstract, disjointed, increasingly fragmented”.^{*36} This is in line with the claim that the European “idea” as such is one of pluralism.^{*37} In this view, the idea of the unified harmonisation of the law of Europe — if one believes in these claims — may even be at odds with the basic function and idea of the EU itself. A person with a positive attitude towards the idea of the EU as such might very well, without being inconsistent, be opposed to the project of systematic harmonisation of the law within the Union.

The postmodern and pluralist alternative to systematic harmonisation is, in other words, to take fragmentation seriously. The rejection of a European codification of private law does not necessarily imply a defence of traditional national structures.^{*38} Instead, as the pluralism of Europe offers a wealth of opportunities, the pluralism of European law can be seen as creating a field of new legal possibilities. EC law as well as ideas from the other European countries can be used in a creative way to break up petrified structures of national law that are hampering the development.

³¹ The EC Council actually justified the inclusion of this limitation of the scope of the Directive by the wish to exclude from the scope of the Directive “anything resulting directly from the contractual freedom of the parties”. See the Common Position adopted by the Council on 22 September 1992 with a view to the adoption of Council directive 93/13/EEC on unfair terms in consumer contracts, the Council’s reasons, p. 5.

³² T. Wilhelmsson. *Europeisering av privaträtten: för ett fragmenterat utbyte av erfarenheter* (Europeanisation of Private Law: for a Fragmented Exchange of Experience). – *Tidsskrift för Rettsvetenskap*, 2001.

³³ H. Kötz. *A Common Private Law for Europe: Perspectives for the Reform of European Legal Education*. – B. De Witte, C. Forder (eds.). *The Common Law of Europe and the Future of Legal Education*. Deventer: Kluwer, 1992, p. 32.

³⁴ H. J. Thue. *Norwegian Private International Law at the End of the 20th Century: Progress or Regress?* – S. C. Symeonides (ed.). *Private International Law at the End of the 20th Century: Progress or Regress?* The Hague: Kluwer Law International, 1999, p. 328.

³⁵ See J. A. Caporaso. *The European Union and Forms of State: Westphalian, Regulatory or Post-modern?* – *Journal of Common Market Studies*, 1996, p. 44 ff. See also I. Ward. *A Critical Introduction to European Law*. London: Butterworths, 1996, p. 182.

³⁶ J. A. Caporaso (Note 35), p. 45.

³⁷ I. Ward (Note 35), p. 191.

³⁸ See on this strategy of Member States D. Caruso. *The Missing View of the Cathedral: The Private Law Paradigm of European Legal Integration*. – *European Law Journal*, 1997, pp. 3–32.

EC directives, like the Directive on unfair terms in consumer contracts, may bring in useful new ideas in the various national settings, starting processes of development in that context.^{*39} Such ideas may also flow directly over national borders without making the detour through Brussels. Contract law ideas can move, for example, in connection with international trade and transnational standard form contracts. This movement of ideas presupposes openness in relation to impulses from other places, which is not possible within the framework of a strict system. A comprehensive European Civil Code would easily destroy — or at least weaken — the potentially experimental nature of European law.

The development of European consumer law — although from a Nordic perspective, it seems a little too modest in some, but not all respects — is a good example of how experiences from various European countries can be used in order to create European solutions: German and Nordic experiences of unfair contract terms regulation, the English experience of consumer credit regulation, *etc.* A continuous experimental development and improvement of the kind to be seen in this area — where new ideas not only flow via EC legislation, but also directly between the Member States — would naturally be much more difficult if the field was controlled by the general European Civil Code.

The idea of an experimental and learning law that makes use of experience from other countries presupposes a minimum basis of understanding between legal players from different national environments, a common “legal language”.^{*40} A project like the Lando Commission can, despite its commercial biases, be useful in creating a conceptual basis for a common European legal discourse.^{*41} As long as this and the other projects produce “soft law” and “soft legal knowledge”, they facilitate the experimental and fragmented movement of ideas within the EU rather than hamper it, as a petrified code would do. They may also be taken into account as useful guiding materials when developing national legislation, as the Estonian example shows.

In other words, I want to underline that the idea of a continuous free movement of legal concepts and ideas does not imply any dissociation from the academic European legal harmonisation projects, like the PECL, as such. On the contrary, I find them very important, both because they help to create a necessary conceptual basis for the free movement of ideas and because the work as such is already producing new thoughts and ideas. My criticism is directed only towards the final vision of a common and static European Code.

³⁹ See the very interesting paper G. Teubner. Legal Irritants: Good Faith in British Law or How Unifying Law Ends Up in New Divergences. – *Modern Law Review*, 1998, p. 11–32.

⁴⁰ M. Van Hoecke, M. Warrington. Legal Cultures, Legal Paradigms and Legal Doctrine: Towards a New Model for Comparative Law. – *The International and Comparative Law Quarterly*, 1998, p. 525 *ff.* See the development of “some conceptual legal meta-language” as a “necessary condition for a real development of comparative law.” They consider the development of such a language to be a task for legal doctrine (p. 530).

⁴¹ K. Riedl. The Work of the Lando Commission from an Alternative Viewpoint. – *European Review of Private Law*, 2000, p. 83, also emphasises the commission’s contribution to “a fruitful discourse culture”. In his commentary to the UNIDROIT Principles of International Commercial Contracts, M. J. Bonell also seems to emphasise their role as a framework for discourse, see M. J. Bonell. *An International Restatement of Contract Law*. New York: Transnational Juris Publications, 1994, p. 2 *ff.* – M. J. Bonell. The need and possibilities of a codified European contract law. – *European Review of Private Law*, 1997, p. 505 *ff.* The author expressly defends the idea of non-binding instruments as opposed to a formal Code.