

The Common European Sales Law and Party Choice: When Will Parties Choose the Proposed CESL?

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1. Introduction

The most important aspect of the Proposal for a Regulation on a Common European Sales Law (CESL), as published by the European Commission in 2011,¹ is its optional character. The CESL leaves the decision to adhere to a common European set of rules on cross-border sales with the contracting parties.² This is in clear contrast with existing methods to achieve convergence in the area of contract law, such as the traditional method of European harmonisation by way of directives, the creation of a model law that states can opt into (as in the case of the US Uniform Commercial Code) and unification by way of a treaty (of which the Vienna Convention on Contracts for the International Sale of Goods is the most important example). Despite severe criticism one can have on the details of the present Proposal,³ I believe that the fundamental choice to create an optional contract law regime should be met with enthusiasm.⁴ It does not only fit in with previously introduced

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¹ Proposal for a Regulation on a Common European Sales Law, COM (2011) 635 final (hereinafter: Proposal CESL).

² Art. 3 CESL: 'The parties may agree that the Common European Sales Law governs their cross-border contracts for the sale of goods (...)' Cf. Communication on a Common European Sales Law to Facilitate Cross-Border Transactions in the Single Market, COM (2011) 636 final (hereinafter: Communication CESL), at 7: 'choice of the Common European Sales Law will be voluntary (...)'.

³ See below, section 4, and e.g. *ZEUP* 20 (2012), no. 4 (special issue); *MJ* 19 (2012), no. 1 (special issue), 3 ff.; Horst Eidenmüller et al, *Der Vorschlag für eine Verordnung über ein Gemeinsames Europäisches Kaufrecht*, *JZ* 67 (2012), 269-289; Martin Schmidt-Kessel (ed.), *Ein einheitliches europäisches Kaufrecht?*, München (Sellier) 2012; Hans Schulte-Nölke et al. (eds.), *Der Entwurf für ein optionales europäisches Kaufrecht*, München (Sellier) 2012; *ERPL* 19 (2011), no. 6 (special issue), 709-1021.

⁴ See already European Commission, Communication: A more Coherent European Contract Law – an Action Plan, COM (2003) 68 final, par. 89 ff. and Jan M. Smits, *Toward a Multi-Layered Contract Law for Europe*, in: Stefan Grundmann & Jules Stuyck (eds.), *An Academic Green Paper on European Contract Law*, The Hague (Kluwer Law International) 2002, 387-398.

European optional legal regimes in other areas of the law,⁵ there are also good substantive arguments that speak in favour of the creation of 'optional law.'

The aim of this contribution is to show the potential and limits of a choice for the CESL by the contracting parties.⁶ My main question is which choices parties have to make in the case CESL would be introduced, including on what conditions it is dependent whether parties will choose for the CESL or not. It is clear that this question cannot be answered without a clear view of at least two things. First, we need to establish that there is added value in the creation of an optional European regime compared to traditional jurisdictional competition among national legal systems (section 2). Second, it is important to establish what an optional contract regime should look like in case it is to develop as an attractive competitor on the law market. This question requires knowledge of what it is that contracting parties maximise when they decide upon the legal design of their contract (section 3). This will lead to an assessment of the proposed CESL and to conclusions about its defects and possible ways to remedy these (section 4).

2. Vertical jurisdictional competition: is there added value in an optional European regime?

The creation of an optional European regime in the field of contract law fits in with previous initiatives to make '28th' legal systems, such as the European Company,⁷ European Economic Interest Grouping (EEIG),⁸ European Cooperative Society (SCE)⁹ and Community Trade Mark,¹⁰ as well as with the proposed European Private Company¹¹ and European Union patent.¹² The question is whether such European regimes, and the vertical competition they engender, have added value compared to traditional jurisdictional competition among national legal systems.

The rationale of competition among national legal systems (or rather among national legislatures) is well known.¹³ If differences exist among various laws, mobile private actors will move to the jurisdiction that best satisfies their

⁵ See Holger Fleischer, *Optionales europäisches Privatrecht ('28. Modell')*, *RabelsZ* 76 (2012), 235-252; Jan Smits, *Optional Law: A Plea for Multiple Choice in Private Law*, *MJ* 17 (2010), 347-352; Gregor Bachmann, *Optionsmodelle im Privatrecht*, *JZ* 63 (2008), 11-20.

⁶ Other actors (such as national legislatures, European and national courts and legal academics) also have to make important choices concerning the CESL. See on these choices Jan M. Smits, *The Common European Sales Law (CESL) Beyond Party Choice*, *ZEUP* 20 (2012) (forthcoming).

⁷ Council Regulation 2157/2001 on the Statute for a European company.

⁸ Council Regulation 2137/85 on the European Economic Interest Grouping (EEIG).

⁹ Council Regulation 1435/2003 on the Statute for a European Cooperative Society (SCE).

¹⁰ Council Regulation 207/2009 on the Community Trade Mark.

¹¹ *Proposal for a Council Regulation on the statute for a European Private Company (SPE)*, COM (2008) 396.

¹² *Proposal for a Council decision authorising enhanced cooperation in the area of the creation of unitary patent protection*, COM (2010) 790.

¹³ Cf. e.g. Anthony Ogus, *Competition between national legal systems: a contribution of economic analysis to comparative law*, *ICLQ* 48 (1999), 405-418; Eva-Maria Kieninger, *Wettbewerb der Privatrechtsordnungen im europäischen Binnenmarkt*, Tübingen (Mohr Siebeck) 2002; Norbert Reich, *Competition between Legal Orders: A new Paradigm of E.C. Law*, *CMLR* 29 (1992), 861.

preferences. Because of the competitive pressure this will put on the national legislature of the state that people opt out of, this state is expected to adapt its laws in order to keep capital and labour within its own borders. Legislatures thus have an incentive to attract foreign parties to their jurisdiction, leading to increased prestige and revenues of in particular the providers of legal services.¹⁴ In contract law, this means that if a state does not provide the functions parties are in need of, the costs of contracting will increase¹⁵ and parties will move to another jurisdiction or seek refuge in arbitration or other alternative dispute mechanisms. This process of learning by both suppliers and users of law is a continuous one (hence no convergence towards only one 'best' set of rules will occur) as it is highly unlikely that one model will be seen as optimal by all private actors.

It is also well known how difficult this jurisdictional competition is achieved in practice.¹⁶ One often mentioned reason for this is a lack of mobility of actors: despite the attractiveness of another jurisdiction, not many actors are willing to move out if this means they have to physically exit their home jurisdiction. In contract law, however, this problem is less pervasive because choice is often possible while staying at home.¹⁷ Other reasons for deficient jurisdictional competition are a lack of information about the available options and the fact that most contracting parties do not choose another set of rules because they seek a high quality legal system. Their choice is rather dependent on coincidental factors, such as that they happen to know another legal system or because information on it is coincidentally available in their own language. This leaves legislatures with little incentives to change the national system under competitive pressure. Another problem is that it is difficult for legislatures to learn as a choice is usually made for an entire legal system, meaning that the legislature has no clue as to why its law is chosen or opted out of: it remains in the dark why a party is motivated to choose for another law. Finally, a more practical, problem is that private international law does not always allow a choice for another jurisdiction. Thus, the Rome I Regulation¹⁸ severely limits the effects of party choice in consumer law (art. 6 s. 2) and in a purely domestic contract (art. 3 s. 3).

It is against this background that we must ask what are the advantages of creating an optional regime at the European level. Could *vertical* competition (among national and European rules) avoid the problems I just sketched? The general point to make is that the rationale for jurisdictional competition also applies to optional regimes in so far as they differ sufficiently from any other jurisdiction

¹⁴ Nice examples of the European law market in action can be found at <www.lawsociety.org.uk> and at <www.lawmadeingermany.de>, on which Hein Kötz, *The Jurisdiction of Choice: England and Wales or Germany?*, *ERPL* 18 (2010), 1243-1257. See also Erin O'Hara and Larry E. Ribstein, *The Law Market*, Oxford (OUP) 2009 and Horst Eidenmüller, *Recht als Produkt*, *JuristenZeitung* 64 (2009), 641-653.

¹⁵ Cf. e.g. Robert E. Scott, *The Rise and Fall of Article 2*, *La. LR* 62 (2002), 1009-1063, at 1058.

¹⁶ Out of the extensive literature: Stefan Leible, *Kollisionsrecht und vertikaler Regulierungswettbewerb*, *RabelsZ* 76 (2012), 374-400, at 381 ff. and O'Hara & Ribstein, o.c.

¹⁷ See also Horst Eidenmüller, *The Transnational Law Market, Regulatory Competition, and Transnational Corporations*, *Indiana Journal of Global Legal Studies* 18 (2011), 707-749, at 710. On the argument that contract law may not matter to parties at all: below, section 3.2.

¹⁸ Regulation 593/2008 on the law applicable to contractual obligations.

that can be chosen. As I argued before,¹⁹ the main reason why jurisdictional competition should be stimulated is that the question of what is fair and just necessarily receives different answers from different people, also if these people live in the same country. This may of course always have been the case but globalisation, resulting in greater exposure to alternative views of justice, and a stronger focus on the individual²⁰ make it less and less convincing to force all citizens to accept the solution of 'their' own national parliament. This calls for a theory of justice that does not seek one ideal law, but will 'have something to say about the choices that are actually on offer.'²¹ In this respect, the advantage of optional regimes is that they can be designed with a view to being competitive. When national legislatures make laws, they usually only think of their own, national, constituency, not of foreigners considering to opt in. Regimes designed as optional can try to avoid this by offering high quality alternatives that differ considerably from existing options and thus reflect alternative views of justice.²²

Could vertical competition also avoid the specific problems that were just mentioned? It will in any event be easier to provide information on optional European regimes in more languages than is possible in case of national jurisdictions.²³ In addition, the marketing of an optional instrument as a European system may pre-empt lock in-effects among parties who are active on the European market: they may be better prepared to opt out of the law they use at present.²⁴ The problem of national legislatures not being able to react to a choice for the optional system because they do not know which aspect parties like best, could be remedied by allowing a partial choice for the optional regime (see below, section 4). Also the fact that a choice for a national jurisdiction is not always possible could be remedied by making the scope of application of the optional regime as wide as possible: a limitation to cross-border contracts appears wrong (see below, section 4).²⁵

All this means that vertical competition has the potential to avoid some of the problems of traditional jurisdictional competition, but that it all depends on how the instrument is shaped and when it is available to parties whether it will in fact do so.²⁶

¹⁹ See more elaborate Smits, o.c., *MJ* 17 (2010), 347-352.

²⁰ For a general account of what this means: Zygmunt Bauman, *The Individualized Society*, Oxford (Polity) 2001.

²¹ Amartya Sen, *The Idea of Justice*, Cambridge, Mass. (Harvard University Press) 2009, 106.

²² As we will see below, the present proposal for the CESL does not succeed in achieving this.

²³ The Proposal for the CESL is already available in all EU-languages. The proposed database of cases will also become available in all EU-languages.

²⁴ Gary Low, Will firms consider a European optional instrument in contract law?, *EJLE* 2012, online at DOI 10.1007/s10657-011-9276-1, makes the point that the use of an optional instrument is contingent on an actor's performance relative to its aspiration level.

²⁵ It is in my view also wrong not to allow a choice for a national legal system in a purely domestic situation. The economic rationale that parties having strong connections to the forum will limit their capacity to choose an inefficient forum (see Michael J. Whincop & Mary Keyes, Towards an Economic Theory of Private International Law, *Australian Journal of Legal Philosophy* 25 (2000), 1-35, at 15) no longer holds true in a globalised society like ours.

²⁶ More skeptical: Leible, o.c., *RabelsZ* 76 (2012), at 390 ff. More positive: Karl Riesenhuber, Wettbewerb für das europäische Vertragsrecht, *JZ* 66 (2011), 537-544, claiming however that vertical jurisdictional competition may be unfair ('you can't beat the house').

This account of the values of optional instruments would not be complete without attention for two other arguments, unrelated to jurisdictional competition. One argument often used in favour of optional law is that it is less disruptive for the national legal order.²⁷ Harmonisation of substantive private law has until now mostly taken place by way of European directives. This method of harmonisation is not seen as very satisfactory: not only does it endanger the coherence of the national legal system, also from the European perspective directives often remain a political compromise having adverse effects on the internal market. Optional law could then offer an alternative. It leaves national systems intact and makes it dependent on the wish of private actors themselves whether they want to make the European regime applicable (with the additional advantage that it makes clear in a bottom up way whether parties are in need of a European regime at all). This is not only better for the coherence of national law, it can also lead to a higher quality of the optional regime: if Member States' own legal systems are not affected, they may be more likely to accept the rules of European origin.²⁸

The argument of the European Commission in favour of the adoption of the CESL is still another one. It does not focus on the advantages that suppliers (member states) and users (parties) of law can derive from its introduction, but it is obsessed with the idea that the CESL will improve the functioning of the internal market by facilitating cross-border trade for business and cross-border purchases by consumers.²⁹ Whether this objective will be pursued is of course entirely dependent on how attractive it will be for parties to opt-in to the CESL. It is therefore surprising that the European Commission does not pay more attention to the added value of an optional regime compared to competition among national laws.³⁰

3. What do contracting parties maximise? On the ideal design of an optional sales law

3.1 What do parties maximise? On lemons on the law market

It was made clear in the previous section that there could be added value in the creation of an optional European regime on the law of sales, but that its success as an attractive competitor to national jurisdictions wholly depends on how the instrument is designed. This merits first of all attention for the needs of contracting

²⁷ Cf. Green Paper on Policy Options for Progress Towards a European Contract Law for Consumers and Businesses, COM (2010) 348 final (hereinafter: Green Paper 2010), 10: 'Such an optional instrument could bring about important internal market benefits without necessitating further inroads into national law (...).'

²⁸ Although this is also dependent on a member state's willingness to move away from a nationalist view of law: see in more detail *ERCL* 8 (2012), issue 2 (special issue).

²⁹ Proposal CESL, art. 1 s. 3: the CESL is to 'encourage consumers to shop across borders'; cf. p. 4. The argument is used in a consistent way ever since the European Commission's Communication (...) on European Contract Law, COM (2001) 398 final. See also European Commission, Green Paper on Policy Options for Progress Towards a European Contract Law for Consumers and Businesses, COM (2010) 348 final.

³⁰ See also Richard A. Epstein, in this issue, ...

parties: what do they maximise when they decide upon the legal design of their contract? Only when this is clear, we can consider the ideal design of an optional regime on sales law.

Economic analysis assumes that contracting parties are rational maximisers of their own self-interest³¹ and have full information about the alternatives among which they can choose as well as about the effects of each of these alternatives. This is a viable starting point for an analysis of the choices that parties have to make when designing their legal relationship. It is useful to distinguish between business-to-business (B2B)- and business-to-consumer (B2C)-relationships although, as we shall see, these two types of relationships do not differ on the point of what it takes to have a successful vertical competition.

In commercial relationships, parties are arguably mostly interested in a transparent and predictable law that is substantively uniform. Parties need to know at the time of concluding the contract that courts deciding a possible dispute (including courts in other jurisdictions) will interpret the contract in a uniform way (territorial dimension) and that they will continue to do so over time (temporal dimension).³² Thus, a more 'formal' law will probably better maximise the utility of businesspeople than a law with many open-ended standards that leaves wide discretion to the courts. The ability to predict the legal outcome is more important than its fairness.³³ This not only explains the preference of commercial parties to draft detailed general conditions, but also various aspects of international commercial contract practice, such as the desire to have arbitrators decide the dispute, the common exclusion of the CISG,³⁴ and the general preference of business for the more 'formal' English law.³⁵

In B2C-relationships, it is more disputed what the consumer maximises. Economic analysis could be applied in two different ways. On the one hand, one could reason that the main incentive for the consumer is to obtain the product at the lowest possible price, which would speak against a legal regime with costly consumer protection – that will undoubtedly be reflected in the price of the product and could even lead to suppliers of products and services leaving the market, reducing general welfare. On the other hand, it is also consistent with economic theory to argue that the consumer is in need of protection, not because it is a weaker

³¹ Richard A. Posner, *Economic Analysis of Law*, 6th ed., New York (Aspen), 4; cf. Louis Kaplow & Steven Shavell, *Fairness versus Welfare*, Cambridge Mass. (Harvard University Press) 2002, 155.

³² Scott, o.c., *La. LR* 62 (2002), 1058. Cf. also Robert E. Scott, The Uniformity Norm in Commercial Law, in: Jody S. Kraus & Steven D. Walt (eds.), *The Jurisprudential Foundations of Corporate and Commercial Law*, Cambridge (CUP) 2000, 149-192.

³³ Cf. John Linarelli, The economics of uniform laws and uniform lawmaking, *Wayne LR* 48 (2003), 1387-1448 and Whincop & Keyes, o.c., *Austr. J. Leg. Phil.* 25 (2000), at 15: parties prefer ex ante specification versus ex post discretion.

³⁴ See e.g. Martin F. Koehler, Survey regarding the relevance of the United Nations Convention for the International Sale of Goods (CISG) in legal practice and the exclusion of its application, 2006, available at <www.cisg.law.pace.edu/cisg/biblio/koehler.html>.

³⁵ Stefan Vogenauer & Christopher Hodges, *Civil Justice Systems in Europe: Implications for Choice of Forum and Choice of Contract Law*, 2008, available at <www.iecl.ox.ac.uk> show that English law is the most popular among companies with cross-border activity, supposedly because of its greater sensitivity to the needs of commerce.

party, but because it knows less about the product (or the law) than the professional party and must therefore be put at the same level of information. Only if, based on this information, the consumer is able to ascertain that the quality of the product is higher, or that it receives more legal protection, it will be willing to pay a higher price.³⁶

It follows from the above that a commercial party will usually only choose for an optional regime such as the CESL if it believes it will provide more certainty than another (usually national) jurisdiction (or is beneficial to it in another significant way). A consumer will probably only choose for the applicability of the CESL if the price of the product is lower or if it believes it will receive higher protection than under a national law. In other words: actors must be able to distinguish easily between the available legal regimes and ascertain the differences in quality. If it is not possible to identify 'good' and 'bad' legal regimes, a similar phenomenon as with normal products arises: the overall quality of the law will decrease as there is no longer an incentive for the (European) provider of law to continue offering and maintaining the CESL. With a variation on Akerlof,³⁷ one is tempted to speak of a market for legal lemons.

This tells us that the two essential elements of successful vertical competition in both B2B and B2C-relationships are the extent to which the optional regime is significantly different from other options and the ability and willingness of parties to recognise this. In addition to this, it is important to consider the costs of choice for an optional regime compared to a choice for a national law or no choice at all. These three elements make up the design of an ideal optional sales law.

3.2 On the ideal design of an optional sales law

This subsection further develops the three elements that are in my view decisive for a successful optional sales law. As we just saw, the first aspect is the extent to which the optional regime is significantly different from other available options. Contracting parties will not easily deviate from the laws they are used to if the perceived benefits of an opt-out are only little. This is consistent with the idea of 'sticky nation-state laws'³⁸ as caused by several psychological biases. Among these is the bias that actors have a preference for inertia due to the perception that losses caused by departing from the status quo bias are greater than possible gains (status quo bias)³⁹ and the sunk cost effect (time and energy invested in the existing system may stand in the way of a willingness to accept another one).⁴⁰ This resistance

³⁶ Cf. Giesela Rühl, Consumer Protection in Choice of Law, *Cornell International Law Journal* 44 (2011), 569-601, at 572; Pamaria Rekaiti & Roger Van den Bergh, Cooling-Off Periods in the Consumer Laws of the EC Member States: A Comparative Law and Economics Approach, *Journal of Consumer Policy* 23 (2000), 371-407, at 379.

³⁷ George J. Akerlof, The Market for 'Lemons': Quality Uncertainty and the Market Mechanism, *QJ Econ* 84 (1970), 488-500.

³⁸ Erin O'Hara O'Connor, The Limits of Contract Law harmonization, *EJLE* 2012, online at DOI 10.1007/s10657-011-9277-0.

³⁹ See e.g. Russel Korobkin, Behavioral Economics, Contract Formation and Contract Law, in: Cass Sunstein (ed.), *Behavioral Law and Economics*, Cambridge (CUP) 2000.

⁴⁰ See in more detail Gary Low, The (Ir)relevance of Harmonization and Legal Diversity to European Contract Law: A Perspective from Psychology, *ERPL* 18 (2010), 285-305.

against change can only be overcome if the benefits of a choice for another legal regime are sufficiently high. Such benefits could lie in the different scope of application of the legal regime (enabling parties to make use of one uniform set of rules regardless of the counterpart's place of residence or status) or in the major substantive differences it shows compared to existing laws. Without these major differences, parties will not even start thinking about opting into another set of rules, but will instead expose 'rational ignorance': the expected potential benefits of informing oneself about the alternative system are too small relative to the costs.⁴¹

The second aspect concerns the ability and willingness of parties to recognise the differences among the available options. Even if clear differences among the various options exist, competition will not occur if a party does not recognise these. This aspect raises several interesting questions. The first is whether contract law matters to parties at all, or that they are largely immune to differences among legal systems. Although one should not overstretch the importance of contract law⁴² – and the European Commission tends to do so⁴³ – surveys show that commercial parties do care about the design of their contractual relationships.⁴⁴ The same is true for consumers. A recent survey shows that although the main concern of consumers when buying goods or services online from foreign companies is the security of the website and payment system, the factor 'the laws governing the terms and conditions of sale' is also relevant.⁴⁵

If we therefore assume that contract law is to some extent important to parties, the next question is what it takes to recognise differences among various legal systems. In my view, merely providing information about an optional regime is not very helpful. In particular SME's and consumers are only able to make rational decisions about choice of law if they can tell the differences between the law that is applicable by default and any other law they can choose.⁴⁶ This calls for providing information by way of comparison: parties should be able to clearly see the advantages and disadvantages of a choice for a specific legal regime, allowing them to choose from a menu of options.⁴⁷ The difficulty that must then be overcome is that in the view of law as a product, law is a so-called credence good: it is impossible to determine the quality by inspection (as with inspection goods) or immediately after the completion of the contract (as with experience goods), but only at the time a possible dispute is solved in a satisfactory way.⁴⁸ This could be years after the contract was concluded.

⁴¹ Pioneered by Anthony Downs, *An Economic Theory of Democracy*, New York (Harper) 1957.

⁴² See e.g. Stewart Macaulay, Freedom from Contract: Solutions in Search of a Problem?, *Wisconsin LR* 2004, 777-820; H. Beale and T. Dugdale, Contracts between businessmen, *British Journal of Law & Society* 2 (1975), 45-60.

⁴³ See e.g. Smits, ...

⁴⁴ ...

⁴⁵ Allen & Overy, Ipsos More Online consumer research January 2011.

⁴⁶ See Whincop & Keyes, o.c., *Austr. J. Leg. Phil.* 25 (2000), at 31.

⁴⁷ As is not uncommon in *choice architecture*. See Richard H. Thaler and Cass R. Sunstein, *Nudge: Improving Decisions About Health, Wealth and Happiness*, New Haven (Yale University Press) 2008.

⁴⁸ See on this distinction Michael R. Darby & Edi Karni, Free Competition and the Optimal Amount of Fraud, *J. L. & Econ.* 16 (1973), 67-88.

I can see two possible ways⁴⁹ of providing parties with comparative information about different jurisdictions. The first is to give rather specific legal information about e.g. the level of consumer protection in different legal systems or about the extent to which courts in different countries are generally willing to enforce the party agreement. This method may be suited for parties willing and able to pay legal experts to interpret this information and adapt sophisticated contracts accordingly, but not for smaller SME's and consumers.⁵⁰

The second, less traditional, method is to rely on experiences of users of legal systems, leading to screening and signalling mechanisms⁵¹ and in particular to ranking of different jurisdictions. Ranking has the advantage that laypeople and SME's can rely on the experiences of others and do not need to carry out extensive research themselves. This is in line with the repeatedly made point that the traditional business model of lawyers advising individual clients will fundamentally change as a result of new technologies.⁵² Information will be increasingly drawn from reliable sources outside of the legal profession and legal actors will become more proactive in setting their rights and obligations and in avoiding and deciding conflicts.⁵³ To create optional European regimes is an excellent way to empower the end-users of the law, but this also means that these end-users should be provided with information in novel ways. The more information there is available about the benefits of a choice for the CESL, the more likely it is that the necessary network effects are produced. To my mind, new technologies can play an important role in making such comparisons. Much in line with existing websites for comparison⁵⁴ and reviewing⁵⁵ of products, it would be useful if interactive websites exist that offer rankings of jurisdictions based on their attractiveness for parties and share experiences of 'users' of these legal systems with others.⁵⁶ This means that each person adds more value to the common network of users of the proposed CESL. Parties will then be able to rank the qualities of the CESL compared to making use of a national jurisdiction. Unfortunately, there are at present no accepted criteria for making such a ranking.⁵⁷

⁴⁹ Price mechanism...

⁵⁰ Also sceptical about the consumers comparing different systems of protection: Eidenmüller et al, o.c., *JZ* 67 (2012), 286.

⁵¹ On screening: Francesco Parisi & Larry E. Ribstein, Choice of Law, in: Peter Newman (ed.), *The New Palgrave Dictionary of Economics and the Law*, vol. I, London (Macmillan) 1998, 236-241.

⁵² See in particular Richard Susskind, *The End of Lawyers? Rethinking the Nature of Legal Services*, Oxford (OUP) 2008. See for what follows also Smits, o.c., *ZEUP* 2012 (forthcoming).

⁵³ Susskind, o.c., 226 ff. and Bruce H. Kobayashi & Larry E. Ribstein, Law's Information Revolution, *Arizona Law Review* 53 (2011), 1169-1220, at 1203. See also the Opinion of the Economic and Social Committee on The Proactive Law Approach: A Further Step Towards Better Regulation at EU Level, INT/415, CESE 1905/2008.

⁵⁴ Cf. e.g. <www.pricerunner.co.uk> and <www.kelkoo.com>.

⁵⁵ Cf. e.g. <www.epinions.com> and <www.booking.com>.

⁵⁶ Cf. Omri Ben-Shahar, The Myth of the 'Opportunity to Read' in Contract Law, *ERCL* 5 (2009), 1-28.

⁵⁷ One method of comparing jurisdictions is to look at the extent to which they ease doing business: see World Bank Doing Business 2012, available at <www.doingbusiness.org>. The used indicators are criticised: see e.g. Michael Faure & Jan Smits (eds.), *Does Law Matter?*, Oxford-Antwerp (Intersentia) 2011.

The third and final aspect relevant for a successful vertical competition deals with the costs of choice for an optional regime compared to a choice for a national law (or to no choice at all). More in general, the European Commission's argument that transaction costs will decrease if an optional regime is put into place must be set off against the costs of creating an optional legal regime.⁵⁸ My focus here is specifically on the costs for parties when entering the optional regime. These will necessarily involve not only the costs of obtaining information by way of comparison with existing alternatives (see above), but also (for commercial parties) the costs of changing general conditions, websites and standardised contracts and of training employees.⁵⁹ In addition, the costs of the uncertainty⁶⁰ surrounding the application of the optional regime may be high as the right interpretation of the optional regime can only be given by way of court decisions. All these costs must be justified in view of the perceived benefits of opting into the optional regime.

4. The proposed CESL: defects and possible solutions

The above can be easily summarised: the proposed CESL is only likely to be used by parties if it meets the three requirements that any type of (vertical) jurisdictional competition must meet: the CESL must be substantively different from the other pre-existing options, parties must have sufficient information to recognise this (requiring the parties' willingness and ability to compare), and finally the costs of choice for an optional regime must justify the perceived benefits. I will now test whether these requirements are met in the 2011 Proposal of the European Commission and, if not, how this could be rectified.

4.1 Does the proposed CESL differ sufficiently from existing options?

The European Commission gives two reasons why it would be advantageous for a business to opt into the proposed CESL.⁶¹ First, it would allow a trader to consider only one set of rules without the need to look at the national mandatory consumer law of the state in which it wants to do business. This will lead to a simpler legal environment and therefore to less transaction costs. Second, a choice for the CESL would ease negotiations as it could be easier to agree on a neutral law available in the language of both parties. For consumers, the benefits of choice supposedly lie in the high level of protection that the CESL offers, promoting consumers' willingness to buy across borders. Additional benefits would be that under the CESL the seller will always inform the consumer about its core rights by way of an information

⁵⁸ See for an analysis of costs involved in harmonization Jan M. Smits, *Diversity of Contract Law and the European internal market*, in: id. (ed.), *The Need for a European Contract Law: Empirical and Legal perspectives*, Groningen (Europa Law Publishing) 2005, 153-186.

⁵⁹ See Walter Doralt, *Rote Karte oder grünes Licht für den Blue Button?*, *AcP* 211 (2011), 1-34, at 22.

⁶⁰ On which Helmut Wagner, *Economic Analysis of Cross-Border Legal Uncertainty*, in: Smits, *The Need for a European Contract Law*, o.c., 25-..., at 30 ff.

⁶¹ Communication CESL, at 9-10.

notice and that the lower transaction costs for business will lead to more traders entering the market, resulting in more choice of products and lower prices.⁶²

Are these sufficient reasons for a party to opt into the proposed CESL? It should be made clear at the outset that the reasoning of the Commission is fundamentally flawed. It is simply not true that by applying the proposed CESL parties can 'use one single set of contract law rules across the EU'⁶³ and no longer have to 'adapt to different national contract laws.'⁶⁴ This is because the scope of the CESL is limited to certain parties (only consumers and SME's), to certain relationships (only cross-border sales contracts) and certain topics (legal personality, lack of capacity, illegality, non-discrimination, representation, assignment and transfer of ownership are still completely governed by the applicable national law⁶⁵). Having said this, the advantage of a choice for the CESL is that in B2C-transactions, a business no longer needs to do research into the national provisions of consumer protection in the area of sales law because the CESL will provide full harmonisation.⁶⁶

It is useful to briefly sketch the available options for parties in case the CESL would be introduced in its present form. In a cross-border B2B-relationship, the following options exist:

a) Parties do nothing. This means that the default rule of art. 4 Rome I-Regulation applies. The contract is then usually governed by the law of the country where the seller has his habitual residence. As most European countries are a party to the CISG, the practical effect of this is that the CISG governs formation and remedies, and that the applicable national law governs any other aspect of the contract.

b) Parties decide to explicitly exclude the application of the CISG. This has the effect that the entire contract and its consequences are governed by the default national law applicable through art. 4 Rome I-Regulation.

c) Parties choose a national law under art. 3 Rome I-Regulation. This will not implicitly exclude the applicability of the CISG,⁶⁷ making it dependent on whether the country of choice is a party to the CISG or not whether it will apply. If the chosen jurisdiction is not a party to the CISG, its law will govern the entire contract and its consequences.

d) Parties opt for the proposed CESL. This has the effect that the CISG is excluded.⁶⁸ The contract of sale is substantively mainly governed by the CESL, but for some important aspects parties still have to rely on national law. Substantively,

⁶² Communication CESL, at 10.

⁶³ Proposal CESL, at 11.

⁶⁴ Proposal CESL, at 4.

⁶⁵ Consideration 27 of the Proposal states: 'All the matters of a contractual or non-contractual nature that are not addressed in the Common European Sales Law are governed by the pre-existing rules of the national law outside the Common European Sales Law.'

⁶⁶ Proposal CESL, at 4.

⁶⁷ See on this (disputed) point e.g. Peter Schlechtriem, Requirements of Application and Sphere of Application of the CISG, Victoria University of Wellington LR 2005, 781-794, at 784.

⁶⁸ Proposal CESL, Consideration 25.

the CESL resembles the CISG, but offers some additional rules on e.g. defects of consent and prescription.

e) A fifth option is available in the United Kingdom. Because the UK ratified (in 1973) the Hague conventions on Uniform Law on the International Sale of Goods (ULIS) and on Uniform Law on the Formation of Contracts for the International Sale of Goods (ULFIS), contracting parties can choose to opt in to these in case of a cross-border transaction. There is no case law indicating that a UK party ever did this.⁶⁹

Overlooking this menu of options, it is difficult to see why a choice for the CESL in its present form would be attractive in a B2B-relationship. As a matter of substantive law, the CESL does not differ significantly from the CISG⁷⁰ or from some existing national laws that are equally available for parties in a cross-border relationship. In addition, a choice for the CESL necessarily means that some national law is still applicable for topics not covered by it, unlike is the case with a choice for a national law.

In my view, there are two points at which the CESL could make a difference compared to available legal systems. The first is its scope of application:⁷¹ if the CESL would also be available for domestic contracts and regardless of the type of parties (SME or consumer) involved, it would probably offer enough incentive for parties to change their behaviour. At the moment, a choice for the CISG or for another national contract law is only possible in a cross-border situation. The CESL could change this,⁷² in particular when the proposed rules would be more self-standing (thus: cover more topics) than they are now. The second point at which the CESL could make a difference is in the substantive rules it has to offer. If these are sufficiently innovative, or clearly reflect a type of justice that (certain types of) contracting parties like, this will increase their use. Perhaps the elaborate part in the proposed CESL on contracts for the supply of digital content will turn out to be innovative enough.

In a cross-border B2C-contract, the available options are more limited. The following options exist:

a) Parties do nothing. As a result of the default rule of art. 6 Rome I-Regulation, the law applies of the country where the consumer has its habitual residence. This law will offer a high minimum level of consumer protection as a result of the implemented European *acquis*. Some member states offer an even higher protection.

⁶⁹ See Nathalie Hofmann, Interpretation Rules and Good Faith as Obstacles to the UK's Ratification of the CISG and to the Harmonization of Contract Law in Europe, *Pace International Law Review* 22 (2010), 145-181.

⁷⁰ Cf. Nicole Kornet, *MJ* 19 (2012), forthcoming.

⁷¹ On which e.g. Hans-W. Micklitz & Norbert Reich, The Commission Proposal for a 'Regulation on a Common European Sales Law (CESL' – Too Broad or Not Broad Enough', *EUI Working Papers Law* 2012/4 and Smits, o.c., *ZEUP* 20 (2012), forthcoming.

⁷² This assumes that the European legislature has the competence to create such a comprehensive instrument, for which art. 114 TFEU is not likely to provide a legal basis. See on this (and on art. 352 TFEU as an alternative basis) Jan-Jaap Kuipers, The Legal Basis for a European Optional Instrument, *ERPL* 19 (2011), 545-564.

b) Parties choose a national law under art. 3 Rome I-Regulation. This choice cannot deprive the consumer of the protection afforded to him by the mandatory law of his habitual residence (art. 6). This means that the chosen law is applicable if it gives the consumer on a certain point more protection than its own law; if the chosen law provides less protection, the governing law is a mix of the foreign law that was chosen and the mandatory law of the consumer's residence. The result of this is that the consumer is never worse off as a result of the choice.⁷³

c) Parties opt for the proposed CESL. This means that, except for the aspects it does not cover, the contract is governed by the CESL including its fully harmonised and supposedly high level of consumer protection.⁷⁴ Because the choice for the CESL takes place within the national jurisdiction itself (as a 'second' national regime⁷⁵), the applicability of art. 6 Rome I-Regulation is excluded. This avoids that the higher protection of some national law would remain applicable in case of a choice for the CESL.⁷⁶

Is it likely that the proposed CESL will be chosen from this menu of options? From the viewpoint of a business, it is difficult to see how a choice for the CESL will lead to a simpler legal environment. True, a trader will no longer have to scrutinise differences in the national levels of consumer protection when it offers products to consumers abroad, but – as said before – it still has to rely on national law for topics not covered by the CESL. In addition, scepticism about the extent to which the common rules will be interpreted is in place: a truly autonomous interpretation of the CESL is difficult to achieve without a European court deciding upon the facts of the case (see below, section 4). A business would truly benefit from a common set of rules if it could use these also in the domestic context, but this will depend on a choice by a national legislature,⁷⁷ again prompting the need to do research into national law.

But this is not all. In the view of the European Commission, it will be the seller who takes the initiative in opting to use the CESL, followed by the explicit consent of the buyer.⁷⁸ This is problematic: why would the seller offer the possibility to opt for the CESL if it offers (costly) higher protection for the consumer than national law⁷⁹ and if it has to continue to distinguish between cross-border and domestic contracts?⁸⁰ From the perspective of the consumer, the question is whether a choice for the proposed CESL would make a significant difference compared to the present situation. If we imagine a consumer who has the option to click the 'blue button'⁸¹ (probably at the time of payment) when buying a product

⁷³ Cf. Rühl, o.c., *Cornell International LJ* 44 (2011), at 592.

⁷⁴ Proposal CESL, Consideration 11 and at 7: 'the level of protection of these mandatory provisions is equal or higher than the current *acquis*.'

⁷⁵ Proposal CESL, p. 9, on which Giesela Rühl, *MJ* 19 (2012), forthcoming.

⁷⁶ See Proposal CESL, 6, on which Martijn Hesselink, How to Opt into the Common European Sales Law?, *ERPL* 20 (2012), 195-212.

⁷⁷ Art. 13 Proposal CESL.

⁷⁸ Communication CESL, 9.

⁷⁹ See also Eidenmüller et al, o.c., *JZ* 67 (2012), 286 and Doralt, *AcP* 211 (2011), 14.

⁸⁰ Cf. Doralt, *AcP* 211 (2011), 14.

⁸¹ See Schulte-Nölke, *Europäisches Vertragsrecht als blauer Button im Internet-Shop*, *ZGS* 2007, 81.

over the internet, the benefits of choice are relatively low in view of the already high minimum⁸² level of protection throughout the European Union on which the consumer can rely: this makes it irrational for consumers to put efforts into informing themselves about other possible regimes: they are protected anyway. The free choice of contractual remedies in the proposed CESL⁸³ may not be distinctive enough. It is also highly likely that some member states offer a higher level of protection than the proposed CESL. This means that if a consumer is to go through the trouble of opting into another jurisdiction anyway, it will better serve its own interests by choosing for this national jurisdiction. The problem that the consumer is not likely to take the initiative can be solved by new mechanisms of providing information (see below).

One final aspect that is not helpful in making the proposed CESL a sufficiently different and therefore attractive alternative to existing options is the fact that it can, in B2C-contracts, only be chosen as a whole. The Proposal indicates that this avoids a selective application of certain elements, which could disturb the balance between the rights and obligations of the parties and adversely affect the level of consumer protection.⁸⁴ This is different from the present situation under the Rome I-Regulation. In my view it should be possible to choose chunks in B2C-relationships as well as long as this does not affect the protection of the consumer (which is feasible because many provisions of the CESL are unrelated to this): the possibility to unbundle the CESL will help to initiate learning processes for the legislature (see above, section 2) and is in line with the freedom of contract the Commission so much emphasises.⁸⁵

The conclusion must be that the CESL in its present form is not sufficiently distinct from already available options. In order to make it an attractive competitor on the law market, its scope of application must be broadened, it must be made more self-standing and it must offer more innovative solutions or better reflect a type of contractual justice that present laws do not offer. In B2C-contracts, an additional problem is that the CESL offering distinctively higher protection than the existing *acquis* stands in the way of sellers deciding to offer the CESL to its customers.

4.2 Are parties able to recognise the distinctness of the proposed CESL?

The second requirement for a successful CESL is that parties have sufficient information to recognise the differences with existing legal regimes. It was explained in the above (section 3.2) that comparison is essential for this informed choice. Unfortunately, the European Commission adopts a very traditional approach towards providing information about the CESL.⁸⁶ It does not go much further than stating that there is a need for 'clear information' to allow consumers to understand

⁸² And increasingly maximum level: see e.g. directive 2011/83 on consumer rights.

⁸³ Art. 106 Proposal CESL; cf. Communication CESL, 10.

⁸⁴ Art. 8 s. 3 and Consideration 24 Proposal CESL.

⁸⁵ Proposal CESL, Art. 1 and Consideration 30.

⁸⁶ The Proposal is very elaborate on the obligation of the trader to draw attention to the intended application of the CESL (Art. 9), but this is something else. My concern is with information on the very possibility for parties to make use of the CESL.

their rights and make a decision about the applicability of the CESL⁸⁷ and announcing that it intends to organise training sessions for legal practitioners using the CESL.⁸⁸ I find this insufficient: unlike traditional law, an optional instrument derives its validity completely from being made applicable by the parties. This means it should be marketed in a more innovative way. I make two suggestions.

First, the diverging preferences of commercial parties and consumers make it unlikely that they are attracted by the same type of arguments in favour of applying the CESL. This calls for a separate treatment. One could even claim that B2B-contracts and B2C-contracts each deserve a separate optional regime.⁸⁹

Second, people should be able to share experiences on the use of the CESL in comparison with other legal systems. An interactive website combined with a ranking of the various available options would in this respect be of great use. In my view, an important function of such a ranking would be to empower the consumer (who in the view of the EU Court of Justice is 'reasonably well informed and reasonably observant and circumspect'⁹⁰) to make an informed choice among in particular the level of protection of the CESL and of national jurisdictions. This would also fit in with European initiatives to make the consumer more self-sufficient in enforcing its own rights through quick and inexpensive alternative dispute resolution and the European small claims procedure.⁹¹ ...

4.3 What are the costs of a choice for the proposed CESL?

A final requirement for the CESL being preferred by parties over existing alternatives is that the costs of choice are relatively low compared to the default situation and other possible choices. Apart from the already mentioned more general costs that businesses incur when they change applicable law (such as changing general conditions and websites and training of staff), two aspects merit a more elaborate discussion: the costs of making the CESL applicable and of uncertainty in its application.

It must be said that the proposed CESL does not make it easy on the parties to make it applicable.⁹² While in a B2B-relationship an agreement of the parties is sufficient (art. 8 s. 1), in case of a B2C-contract the trader must first draw the consumer's attention to the intended application of the CESL by providing him with a 'Standard Information Notice' (SIN) in a prominent manner (art. 9 s. 1). The SIN contains information on the CESL and the rights it gives to the buyer. Next, the consumer's consent must be given by an explicit statement separate from the

⁸⁷ Green Paper 2010, 10, while recognising that a European optional instrument might be criticised for 'complicating the legal environment.'

⁸⁸ Proposal CESL, 11.

⁸⁹ See Stefan Vogenauer, Common Frame of Reference and UNIDROIT Principles of International Commercial Contracts: Coexistence, Competition, or Overkill of Soft Law?, *ERCL* 6 (2010), pp. 143-183, at 176.

⁹⁰ CoJ EU, C-220/98, [2000] *ECR* I-117 (Estée Lauder).

⁹¹ See also Communication CESL, 10-11.

⁹² Cf. Eidenmüller et al, *JZ* 67 (2012), 276 and Hesselink, o.c., *ERPL* 20 (2012), 207 ff.

agreement to conclude a contract.⁹³ Finally, once the CESL is made applicable, the trader shall provide the consumer with a confirmation of the agreement on a durable medium (art. 8 s. 2). These are costly entry costs compared to making no choice at all or a choice for another national jurisdiction (for which the mere agreement of the parties suffices). A business that has the choice between simply making a national law applicable in its general conditions⁹⁴ and applying the CESL – requiring the three steps just mentioned – may not be tempted to do the latter.

The decision to make the CESL applicable is also influenced by uncertainty costs. As long as there is uncertainty about how the CESL will be interpreted by courts, parties would be ill-advised to choose it: a choice for a national jurisdiction would better satisfy a trader's preference for legal certainty and a consumer's preference for protection. This is why the Proposal emphasises the need for an autonomous interpretation of the CESL: it is to be interpreted 'in accordance with its objectives and the principles underlying it' without recourse to any national law (art. 4). Legal certainty should also be enhanced by the creation of a database comprising decisions of the EU Court of Justice and the national courts on the interpretation of the CESL.⁹⁵

Despite these good intentions, it is not difficult to predict that it will take considerable time before the 'high degree of legal certainty'⁹⁶ CESL is to provide, will be similar to that of national jurisdictions.⁹⁷ This has to do with the many open-ended terms in the Proposal, the time-consuming preliminary ruling procedure before the EU Court of Justice,⁹⁸ the absence of a highest European court that can decide upon the facts of the case, and a lack of clarity about how to achieve an 'autonomous' interpretation (also because of the lack of a commonly accepted European reference text⁹⁹). A 'homeward trend', as is also apparent in the case law on the CISG,¹⁰⁰ seems inevitable. This makes it unlikely – as the European Commission argues¹⁰¹ – that the 'compulsory jurisdiction' of the EU Court of Justice makes all the difference with the CISG in providing a uniform application.

The best possible way to avoid this problem – the fear of parties that, compared to a national law, it leaves too much room for varying interpretations – is to make a specialised court competent to decide on the facts of the case, turning national highest courts in CESL-related matters into appellate courts. This court would ideally be located at the European level with national branches in the member states, but if this is politically not feasible, an alternative would be to

⁹³ Proposal CESL art. 8 s. 2 and Consideration 22: the 'agreement should be subject to strict requirements.'

⁹⁴ It follows from art. 8 s. 2 that the CESL cannot be made applicable in general conditions; see also explicitly Proposal CESL, Consideration 22.

⁹⁵ See Proposal CESL, Art. 14 and Consideration 34 and Communication CESL, p. 11.

⁹⁶ Art. 1 s. 2 Proposal CESL.

⁹⁷ See also John Cartwright, Choice is good. Really? *ERCL* 7 (2011), 335-349.

⁹⁸ Micklitz & Reich, o.c., 28 rightly state that national courts will be more often obliged to seek guidance from an already overburdened Court of Justice.

⁹⁹ See Smits, o.c., *ZEUP* 20 (2012), forthcoming.

¹⁰⁰ Franco Ferrari, Homeward Trend: What, Why and Why Not, in: André Janssen & Olaf Meyer (eds.), *CISG Methodology*, München (Sellier) 2009, 171-206.

¹⁰¹ Communication CESL, 5.

imitate the existing judicial procedure in the area of the Community Trade Mark. This optional legal regime is enforced by specialised national courts in the member states¹⁰² that closely cooperate with each other. It is difficult to see how the necessary network effects needed to attract as many users to the CESL as possible could occur without such a European court system ensuring a uniform interpretation.¹⁰³

5. Conclusions

The proposed CESL must derive its success from the fact that it is chosen by contracting parties as the applicable law. This puts the CESL in competition with other available options such as adhering to the default legal system, a choice for a national jurisdiction, or the decision not to exclude the CISG. It was seen in the above that the present Proposal does not take this competition seriously: although the CESL is meant as a competitor on the European law market, its present design is fundamentally flawed and will, in view of the preferences of businesses and consumers, probably not entice parties to make it applicable. This is even more problematic in view of the fact that the value of an optional instrument is dependent on the number of other parties using it: the larger the network of users, the higher the legal certainty the CESL is likely to create, attracting even more users as a result.

The CESL would be a more attractive competitor if three requirements were met. First, it should be significantly different from existing options by offering more innovative solutions, reflect an alternative view of contractual justice or offer a wider scope of application. Second, parties should be able to easily recognise the benefits of a choice for the CESL. This calls not only for a separate marketing of the CESL for B2B- and B2C-relationships (and perhaps even for separate optional regimes), but also for providing information about the CESL based on comparison with other available options combined with rankings. Finally, the costs of making the CESL applicable must be lower than the present Proposal suggests. This could be realised by making it easier to opt-in to the CESL and by the creation of a European court system.

In conclusion, the above is a plea to make the CESL as competitive as possible. If it is optimally designed to enter into competition with alternative legal regimes, it has the inestimable value of satisfying party preferences, engendering learning processes for legislatures, and demonstrating in an experimental way the need or non-need for a European regime of sales law.

¹⁰² See art. 95 s. 1 of Council Regulation 207/2009 on the Community Trade Mark: 'The member states shall designate in their territories as limited a number as possible of national courts and tribunals of first and second instance, hereinafter referred to as 'Community trade mark courts,' which shall perform the functions assigned to them by this Regulation.'

¹⁰³ Cf. Anthony Ogus, *The Economic Basis of Legal Culture: Networks and Monopolization*, *Oxford Journal of Legal Studies* 22 (2002), 419-434.