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Commission on  
International  
Trade Law**

**YEARBOOK**

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**NOTE**

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

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

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## INTRODUCTION

This is the seventeenth volume in the series of Yearbooks of the United Nations Commission on International Trade Law (UNCITRAL).<sup>1</sup>

The present volume consists of three parts. Part one contains the Commission's report on the work of its nineteenth session, which was held in New York from 23 June to 11 July 1986, and the action thereon by the United Nations Conference on Trade and Development (UNCTAD) and by the General Assembly.

Part two reproduces most of the documents considered at the nineteenth session of the Commission. These documents include reports of the Commission's Working Groups dealing with international payments, the new international economic order and liability of operators of transport terminals, as well as working papers that were before the Working Groups.

Part three contains the draft Convention on International Bills of Exchange and International Promissory Notes, as revised by the Commission at its nineteenth session, summary records of this session for meetings devoted to the draft Convention, a bibliography of recent writings related to the Commission's work, a list of documents before the nineteenth session as well as of other documents referred to in the present volume and reproduced in an earlier volume.

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

<i>Volume</i>	<i>Years covered</i>	<i>United Nations publication, Sales No.</i>
I	1968-1970	E.71.V.1
II	1971	E.72.V.4
III	1972	E.73.V.6
III Suppl.	1972	E.73.V.9
IV	1973	E.74.V.3
V	1974	E.75.V.2
VI	1975	E.76.V.5
VII	1976	E.77.V.1
VIII	1977	E.78.V.7
IX	1978	E.80.V.8
X	1979	E.81.V.2
XI	1980	E.81.V.8
XII	1981	E.82.V.6
XIII	1982	E.84.V.5
XIV	1983	E.85.V.3
XV	1984	E.86.V.2
XVI	1985	E.87.V.4

## THE NINETEENTH SESSION (1986)

### A. Report of the United Nations Commission on International Trade Law on the work of its nineteenth session (New York, 23 June–11 July 1986) [Original: English]<sup>a</sup>

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<sup>a</sup>Official Records of the General Assembly, Forty-first Session, Supplement No. 17 (A/41/17) (11 August 1986) (hereinafter referred to as “Report”).

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## INTRODUCTION

1. The present report of the United Nations Commission on International Trade Law covers the nineteenth session of the Commission, held in New York, from 23 June to 11 July 1986.

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

### Chapter I. Organization of the session

#### A. Opening

3. The United Nations Commission on International Trade Law (UNCITRAL) commenced its nineteenth session on 23 June 1986. The session was opened on behalf of the Secretary-General by Mr. Carl-August Fleischhauer, Under-Secretary-General, the Legal Counsel.

#### B. Membership and attendance

4. General Assembly resolution 2205 (XXI) established the Commission with a membership of 29 States, elected by the Assembly. By resolution 3108 (XXVIII), the General Assembly increased the membership of the Commission from 29 to 36 States. The present members of the Commission, elected on 15 November 1982 and 10 December 1985, are the following States:<sup>1</sup> Algeria,\*

Argentina,\*\* Australia,\* Austria,\* Brazil,\* Central African Republic,\* Chile,\*\* China,\* Cuba,\*\* Cyprus,\*\* Czechoslovakia,\*\* Egypt,\* France,\* German Democratic Republic,\* Hungary,\*\* India,\*\* Iraq,\*\* Iran (Islamic Republic of),\*\* Italy,\*\* Japan,\* Kenya,\*\* Lesotho,\*\* Libyan Arab Jamahiriya,\*\* Mexico,\* Netherlands,\*\* Nigeria,\* Sierra Leone,\*\* Singapore,\* Spain,\*\* Sweden,\* Union of Soviet Socialist Republics,\* United Kingdom of Great Britain and Northern Ireland,\* United Republic of Tanzania,\* United States of America,\*\* Uruguay\*\* and Yugoslavia.\*\*

5. With the exception of the Central African Republic and the Libyan Arab Jamahiriya, all members of the Commission were represented at the session.

6. The session was also attended by observers from the following States: Bangladesh, Bulgaria, Burma, Cameroon, Canada, Colombia, Côte d'Ivoire, Finland, Germany, Federal Republic of, Ghana, Greece, Guatemala, Holy See, Honduras, Indonesia, Oman, Panama, Peru, Philippines, Poland, Republic of Korea, Sudan, Switzerland, Syrian Arab Republic, Turkey and Venezuela.

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

(a) *Specialized agency*

International Monetary Fund (IMF)

(b) *Intergovernmental organizations*

Asian-African Legal Consultative Committee (AALCC)  
Hague Conference on Private International Law  
Organization of American States (OAS)

(c) *International non-governmental organizations*

Chartered Institute of Arbitrators  
European Banking Federation  
Inter-American Bar Association

\*Term of office expires on the last day prior to the beginning of the twenty-second session of the Commission in 1989.

<sup>1</sup>Pursuant to General Assembly resolution 2205 (XXI), the members of the Commission are elected for a term of six years. Of the current membership, 17 were elected by the Assembly at its thirty-seventh session on 15 November 1982 (decision 37/308) and 19 were elected by the Assembly at its fortieth session on 10 December 1985 (decision 40/313). Pursuant to resolution 31/99 of 15 December 1976, the term of those members elected by the Assembly at its thirty-seventh session will expire on the last day prior to the opening of the twenty-second regular annual session of the Commission in 1989, while the term of those members elected by the Assembly at its fortieth session will expire on the last day prior to the opening of the twenty-fifth regular annual session of the Commission in 1992.

\*Term of office expires on the last day prior to the beginning of the twenty-second session of the Commission in 1989.

\*\*Term of office expires on the last day prior to the beginning of the twenty-fifth session of the Commission in 1992.



International Bar Association  
 International Chamber of Commerce (ICC)  
 International Federation of Consulting Engineers  
 Latin American Banking Federation

### C. Election of officers

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

*Chairman:* Mr. P. K. Kartha (India)

*Vice-Chairmen:* Mrs. G. O. Adebajo (Nigeria)  
 Mr. Luis A. Delfino-Cazet (Uruguay)  
 Mr. Hellmut Wagner (German Democratic Republic)

*Rapporteur:* Mr. Alfred Duchek (Austria)

### D. Agenda

9. The agenda of the session, as adopted by the Commission at its 335th meeting, on 23 June 1986, was as follows:

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

### E. Adoption of the report

10. The Commission adopted the present report at its 357th meeting, on 11 July 1986, by consensus.

## Chapter II. International payments

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

#### Introduction

11. The United Nations Commission on International Trade Law, at its seventeenth session in 1984, considered over a three-week period the draft Convention on Inter-

<sup>2</sup>The elections took place at the 335th and 344th meetings, on 23 and 27 June 1986. In accordance with a decision taken by the Commission at its first session, the Commission has three Vice-Chairmen, so that, together with the Chairman and Rapporteur, each of the five groups of States listed in General Assembly resolution 2205 (XXI), sect. II, para. 1, will be represented on the bureau of the Commission (see report of the United Nations Commission on International Trade Law on the work of its first session, *Official Records of the General Assembly, Twenty-third Session, Supplement No. 16 (A/7216)*, para. 14.

<sup>3</sup>The Commission considered this subject at its 335th to 353rd meetings and at its 355th and 356th meetings, from 23 June to 9 July 1986. Summary records of these meetings are contained in documents A/CN.9/SR.335-353, 355 and 356.

national Bills of Exchange and International Promissory Notes, which had been prepared by the Working Group on International Negotiable Instruments. The Commission decided that further work should be undertaken with a view to improving the draft Convention and entrusted that work to the Working Group on International Negotiable Instruments.<sup>4</sup> At its eighteenth session in 1985, the Commission requested the Working Group to complete its work with a view to submitting a draft Convention to the Commission in a form suitable for consideration at its nineteenth session.<sup>5</sup> The Working Group on International Negotiable Instruments held its fourteenth session at Vienna from 9 to 20 December 1985, at which it completed its deliberations on and revision of the draft Convention on International Bills of Exchange and International Promissory Notes.

12. At its current session, the Commission had before it the report of the Working Group on International Negotiable Instruments on the work of its fourteenth session (A/CN.9/273), a note by the secretariat containing the text of the draft Convention on International Bills of Exchange and International Promissory Notes as revised by the Commission at its seventeenth session and by the Working Group at its thirteenth and fourteenth sessions (A/CN.9/274), and a note by the secretariat in response to requests of the Working Group to undertake certain inquiries or to prepare certain draft provisions in implementation of decisions made by it (A/CN.9/285).

13. The Commission elected Mr. Willem Vis (Netherlands) as Chairman of the Committee of the Whole for the discussion of the draft Convention.

#### Discussion at the session

14. The Commission commenced its deliberations on the draft Convention on International Bills of Exchange and International Promissory Notes by discussing the draft articles that had been considered by the Working Group and the decisions taken by the Working Group concerning those articles, as reflected in the provisions of the draft Convention set forth in document A/CN.9/274. It then discussed other articles of the draft Convention. The Commission entrusted a drafting group with the implementation of its decisions and with the establishment of corresponding language versions in the six official languages of the Commission.

#### 1. Review of decisions of the Working Group on International Negotiable Instruments on issues previously identified as major controversial issues

##### Forged endorsements (article 23)

15. In connection with article 23(1), it was generally agreed that, in addition to a person whose endorsement was forged, any party who signed the instrument before

<sup>4</sup>Report of the United Nations Commission on International Trade Law on the work of its seventeenth session, *Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 17 (A/39/17)*, para. 88.

<sup>5</sup>Report of the United Nations Commission on International Trade Law on the work of its eighteenth session, *Official Records of the General Assembly, Fortieth Session, Supplement No. 17 (A/40/17)*, para. 336.

the forgery should have the right to recover compensation for damage that he might have suffered because of the forgery. As an example of damage suffered by a party who signed the instrument before the forgery, a drawer or maker of an instrument could be liable to pay a holder who took the instrument after a forgery of the payee's signature (by virtue of article 14(1)(b), a transferee of an instrument could be a holder even if a prior endorsement was forged) and also to pay the debt to the payee. Such a maker or drawer should be able to recover compensation under article 23(1).

16. In connection with article 23(1)(c), the Commission noted that payment to a forger through a collecting bank might be considered as not having been made "directly to the forger", and thus not covered by subparagraph (c). It was generally agreed that a party or the drawee should be liable to pay compensation under subparagraph (c) not only when he paid the forger in person, but also when he paid the forger through one or a series of collecting banks. Accordingly, the Commission adopted a proposal of the drafting group to amend article 23(1)(c) to read as follows:

"(c) A party or the drawee who paid the instrument to the forger directly or through one or more endorsees for collection."

17. Based on a proposal of the drafting group, the Commission decided that, in order to facilitate drafting in languages other than English, article 23(2) should be amended to read as follows:

(2) However, an endorsee for collection shall not be liable under paragraph (1) if at the time at which:

"(a) He pays the principal or advises the principal of the receipt of the proceeds of the instrument, or

"(b) He receives the proceeds of the instrument,

whichever comes later, he is without knowledge of the forgery, provided that such absence of knowledge is not due to his negligence."

18. With respect to article 23(3), it was agreed in principle that the liability of a party or the drawee to pay compensation should depend upon whether or not he knew of the forgery. However, the view was expressed that there was an inconsistency between article 23(3) and article 68(3). It was noted that under article 23(3) a party or the drawee who paid an instrument to a forger was not liable to pay compensation if he was without knowledge of the forgery, provided that the absence of knowledge was not due to negligence. Under article 68(3) a party paying an instrument to a holder who had acquired the instrument by theft or forged the signature of the payee or an endorsee or participated in such theft or forgery was discharged of liability on the instrument if he did not know of the theft or forgery whether or not the absence of knowledge was due to negligence. As an example of the inconsistency between the two provisions, it was stated that an acceptor who paid an instrument to a forger and who was negligent in not knowing of the forgery would be discharged of liability on the instrument

under article 68(3), but would be liable to pay compensation under article 23(3).

19. According to another view, there was no inconsistency between articles 23(3) and 68(3), since the concept of knowledge in article 68(3) must be construed in the light of article 5, which, by providing that a person was considered to have knowledge of a fact if he could not have been unaware of its existence, incorporated the element of negligence. A further view was expressed, however, that the concept contained in article 5 differed from the concept of negligence in that it covered, in addition to actual knowledge, only the case of wilful ignorance.

20. In order to deal with the question raised in connection with articles 23(3) and 68(3), a suggestion was made that the reference to negligence in article 23(3)—and also in article 23(2)—should be deleted and that the concept of knowledge in that provision should be construed in the light of article 5. It was noted, however, that the substance of article 5 had not yet been settled by the Commission. Accordingly, it was generally agreed that a decision on the question should be considered after the substance of article 5 had been settled (see paras. 63–70 below).

21. With respect to article 23(4), a view was expressed that the reference in that provision to articles 66 and 67 was meaningless, since the latter articles did not establish a means for determining the amount recoverable. It was pointed out, however, that articles 66 and 67 established a ceiling to the amount recoverable and that article 23(4) provided that the amount of damages could not exceed that ceiling. Article 23(4) was adopted.

#### *Endorsement by agent without authority (article 23 bis)*

22. The discussion in respect of article 23(1)(c), (2) and (3) (see paras. 16 to 20 above) related also to article 23 bis (1)(c), (2) and (3). Accordingly, the Commission decided that article 23 bis (1)(c) and (2) should read as follows:

"... (c) A party or the drawee who paid the instrument to the agent directly or through one or more endorsees for collection.

"(2) However, an endorsee for collection shall not be liable under paragraph (1) if at the time at which:

"(a) He pays the principal or advises the principal of the receipt of the proceeds of the instrument, or

"(b) He receives the proceeds of the instrument,

whichever comes later, he is without knowledge that the endorsement does not bind the principal, provided that such absence of knowledge is not due to his negligence."

23. It was noted that the provisions of article 23 bis, relating to endorsement by an agent without authority, paralleled those of article 23, relating to forged endorsements. A view was expressed that an endorsement by an

agent without authority should be treated differently from a forged endorsement. In particular, a transferee in good faith of an instrument endorsed by an agent of the transferor should not have the burden of ascertaining the authority of the agent and should not be strictly liable to pay compensation if the agent signed without authority. A view was expressed that, in most cases, there would exist some kind of relationship between the purported principal and the unauthorized agent; it was, therefore, more equitable and better public policy for the purported principal, and not the transferee in good faith, to bear the risk of unauthorized transfers by a purported agent.

24. It was accordingly proposed that article 23 *bis* (3) should be amended to read as follows:

“(3) Also, any person against whom compensation is sought, other than the agent, shall not be liable under paragraph (1) if, at the time he paid the instrument, he was without knowledge that the endorsement did not bind the principal, provided that such absence of knowledge was not due to his negligence.”

25. After deliberation, the Commission did not adopt this proposal.

*Definition of protected holder (article 4(7))*

26. A view was expressed that the reference in article 4(7) to completion of an incomplete instrument was superfluous and should be deleted. It was pointed out, however, that while a person who took an incomplete instrument could not be a holder, article 4(7) provided that he could become a holder if the instrument met the requirements of article 11(1) and if the instrument was completed in accordance with authority given. The reference in article 4(7) to completion of an incomplete instrument was therefore useful and necessary.

27. According to a further view, the reference in article 4(7) to completion of an instrument “in accordance with authority given” implied that a transferee of an instrument which had been completed by his transferor would have to inquire into whether the transferor had authority to complete the instrument; that would impede the international circulation of instruments covered by the Convention. It was pointed out, however, that article 4(7) dealt only with the question of whether a person who took an incomplete instrument could become a protected holder upon completing it. It did not deal with the question whether a transferee of an instrument which had been completed by his transferor could be a protected holder. Such a transferee could be a protected holder, even though the transferor completed the instrument without authority, if the transferee did not know of the lack of authority.

28. A suggestion was made that in order to clarify article 4(7) so as to reflect its intended meaning, the words “by him” should be added, so as to refer to an instrument “completed by him in accordance with authority given”. The prevailing view, however, was that the decision taken at the fourteenth session of the Working

Group to delete the words “by him” should be maintained (see A/CN.9/273, para. 22), since the instrument might not be completed by the holder himself but by a person acting under the authority of the holder, such as an escrow agent who took an instrument before the amount of a transaction was known and who was authorized to fill in the amount on that instrument. The Commission agreed upon the substance of article 4(7), but referred to the drafting group the task of devising appropriate wording to clarify the intended meaning of the article (see also later decision on article 4(7)(a), para. 57 below).

*Defences and claims that may be set up against a holder (article 25)*

29. In order to clarify that the right of a party to set up against a holder a defence under paragraph (1)(b) of article 25 or a claim under paragraph (2) of article 25 was subject to the provisions of paragraph (2 *bis*) of that article, the Commission requested the drafting group to consider incorporating the substance of paragraph (2 *bis*) in both paragraph (1)(b) and paragraph (2). In addition, it was noted that paragraph (3)(b) referred to the acquisition of the instrument by the holder by theft or forgery or by participation in the theft or forgery, but that paragraph (2 *bis*) did not contain a comparable reference. It was agreed that the substance of paragraph (2 *bis*) should include a comparable reference to theft.

30. Based upon a proposal of the drafting group, the Commission adopted article 25(1)(b) as follows:

“(b) Except as provided in paragraph (2 *bis*) of this article, any defence based on the underlying transaction between himself and the drawer or between himself and the party subsequent to himself or arising from the circumstances as a result of which he became a party;”

31. The drafting group proposed to amend article 25(2) to read as follows:

“(2) Except as provided in paragraph (2 *bis*) of this article, the rights to an instrument of a holder who is not a protected holder are subject to any claim to the instrument on the part of any person.”

32. An objection was raised to the omission from that wording of the reference to a “valid” claim, which appeared in the text of article 25(2) in document A/CN.9/274. The decision of the Commission in respect of that point is reflected in paragraph 41 below.

33. As regards the rule contained in paragraph (2 *bis*), it was proposed to make an exception for overdue instruments by adding wording along the following lines, “except that a holder who takes the instrument after the expiration of the time limit for presentment for payment is subject to any claim to or defence upon the instrument to which his transferor is subject”. It was stated in support of that proposal that the addition was necessary to further the intention underlying article 4(7)(b) and the philosophy of the draft Convention to discourage negotiation of

overdue instruments. Specific reference was made to article 53, according to which certain parties were discharged of liability if an instrument was not duly presented for payment. While some doubt was expressed as to the appropriateness of the proposed addition, the Commission, after deliberation, adopted the proposal.

34. The drafting group proposed that article 25(2 *bis*) should be amended to read as follows:

“(2 *bis*) A holder who is not a protected holder and who took the instrument before maturity is subject to a defence under paragraph (1)(b) or to a claim under paragraph (2) of this article only if he took the instrument with knowledge of such defence or claim or if he obtained the instrument by fraud or theft or participated at any time in a fraud or theft concerning it.”

35. It was noted that under this amendment the exposure of a non-protected holder to a defence or claim would be restricted to the cases set forth in paragraph (2 *bis*) only if he took the instrument before maturity. However, the intention of the original proposal as adopted by the Commission was to expose the holder who took an overdue instrument only to those defences and claims which may be set up against his transferor. Accordingly, the Commission decided that article 25(2 *bis*) should read as set forth in document A/CN.9/274, with the following additional sentence:

“However, a holder who takes the instrument after the expiration of the time-limit for presentment for payment is subject to any claim to or defence upon the instrument to which his transferor is subject.”

36. A view was expressed that paragraph (1)(c) of article 25 should be changed to correspond with paragraph (1)(b) of article 26 (see paras. 44–48 below). In support of that view, it was suggested that, in view of the decision that article 26(1)(b) was not intended to restrict the availability of set-off or counterclaim which might be available under national law (see para. 48 below), article 25(1)(c) and article 26(1)(b) in essence made the non-protected holder and the protected holder subject to the same defences. Thus, the wording of the two provisions should be consistent. It was noted that that had been the view of the Working Group at its fourteenth session (see A/CN.9/273, para. 20).

37. According to another view, however, such a change would be one of substance. A protected holder should be treated differently from a non-protected holder. Under most legal systems the equivalent of a non-protected holder was subject to all defences *vis-à-vis* his immediate transferor, and that was reflected in article 25(1)(c). With respect to a protected holder, however, the situation was different. In some legal systems the equivalent of a protected holder was subject to a broad range of defences *vis-à-vis* his immediate transferor, while in other systems he was subject only to very limited defences. Article 26(1)(b) reflected a compromise between those systems. Accordingly, it was generally agreed that the difference between articles 25(1)(c) and 26(1)(b) should be maintained.

38. In connection with paragraph (3) of article 25, a question was raised concerning the meaning of the phrase “asserted a valid claim” appearing in subparagraph (a), e.g., whether, in order for a party to be able to raise a *ius tertii* defence, the third person must have instituted legal proceedings to establish his claim to the instrument, or whether he must merely have notified the party of his claim to the instrument. A view was expressed that the word “valid” should be deleted, since that word implied that a party could not raise a *ius tertii* defence unless the third person’s claim to the instrument had been finally adjudicated as valid in legal proceedings. Such a result could not have been intended by the provision. Moreover, by virtue of the word “valid”, a party faced with a demand for payment of the instrument by a holder would face difficulty in deciding whether to pay the instrument if he had to evaluate whether a claim by a third person was valid. On the other hand, it was pointed out that the inclusion of the word “valid” would not require a party to delay deciding whether to pay the instrument until the validity of a claim to the instrument by a third person had been finally adjudicated. The effect of the word “valid” was that the party could decide either to pay or not to pay the instrument, but that such a decision would be at his peril if the claim to the instrument by the third person were subsequently adjudicated to be valid or invalid, as the case may be. A view was expressed that the word “valid” should be retained in order to prevent a party from raising a *ius tertii* defence that was palpably false.

39. According to a further view, article 25(3) should be read in conjunction with article 68(3), under which a party who paid an instrument without knowledge of a valid claim to the instrument by a third person was discharged. The intent of article 25(3)(b) was to establish the circumstances under which the party could invoke the claim to the instrument by a third person as a defence against a holder.

40. The Commission decided to refer to the drafting group the task of clarifying the language of subparagraph (a) of article 25(3) in the light of the questions raised concerning the word “valid”.

41. The drafting group proposed that the word “valid” should be deleted from article 25(3)(a). However, in view of the differing views expressed with respect to the use of that word, the Commission decided to retain, for the time being, the word “valid” in that article and also in articles 25(2), 26(2) and 68(3), and to refer the questions concerning the use of the word to the Working Group and the Commission when they considered the draft Convention further.

42. Subject to the drafting decisions referred to in the foregoing paragraphs, the Commission adopted article 25 (see, however, later decision on article 25(1)(c), paras. 50–57 below).

*Defences and claims that may be set up against a protected holder (article 26)*

43. The Commission agreed with the decision of the Working Group at its fourteenth session to add to article 26(1)(a) a reference to article 59 (see A/CN.9/273, para. 10).

44. In connection with article 26(1)(b), a view was expressed that the defences that could be asserted against a protected holder should be restricted in order to promote the usefulness and acceptability of an international negotiable instrument. In accordance with that view, the formulation of subparagraph (b) as it appeared in document A/CN.9/274 was preferable to the formulation considered by the Working Group at its fourteenth session (see A/CN.9/273, para. 16). The defences to which a protected holder was subject under subparagraph (b) should be limited to defences based on an underlying transaction between the protected holder and the party from whom payment was demanded, or arising from any fraudulent act on the part of the protected holder in obtaining the signature of that party on the instrument. A party should not be able to assert a defence arising out of a transaction between himself and the protected holder unrelated to the instrument. According to an additional view, a protected holder should be subject not only to defences arising out of the underlying transaction, but also to defences arising out of situations related to the underlying transaction, such as a prolongation agreement.

45. The Commission considered whether the defences to which a protected holder was subject under subparagraph (b) of article 26(1) should be exclusive or whether the protected holder should also be subject to additional defences that might be available under national law. In that connection, the Commission considered whether or not subparagraph (b) should affect defences such as set-off or counterclaim, which might be available under national law to a party facing a claim on an instrument by a protected holder. A view was expressed that if defences other than those referred to in subparagraph (b) were to remain available under national law, the subparagraph should expressly so provide in order to promote certainty as to the defences to which a protected holder was subject.

46. It was noted that, generally, set-off and counterclaim were matters of procedural law. However, it was also pointed out that in some legal systems such rights were regarded as matters of substance.

47. It was observed that the question of whether or not a protected holder should be subject to defences under national law in addition to those specified in subparagraph (b) was particularly important in some common law systems, where a protected holder was subject to very limited defences *vis-à-vis* his immediate party. It would be of concern to those legal systems if a protected holder were to be subject to defences under national law in addition to those referred to in subparagraph (b). It was noted that subparagraph (b) was a compromise between

those legal systems in which a protected holder was subject to a broad range of defences *vis-à-vis* his immediate party and those systems in which the protected holder was subject only to very limited defences. Accordingly, the view was expressed that a protected holder should not be subject to additional defences under national law.

48. It was generally agreed that subparagraph (b) was not intended to interfere with defences such as set-off and counterclaim that might be available under national law. It was also generally agreed that the wording of the subparagraph should remain as it stood, subject to the use of the word "transaction", which was referred to the drafting group.

49. Subparagraph (c) of article 26(1) was adopted.

*Reference to article 25 in article 4(7)(a)*

50. It was suggested that in the light of the text of article 25(1) as adopted, the definition of protected holder in article 4(7) might need amendment. In its present wording article 4(7) precluded a holder from qualifying as a protected holder if, when he became a holder, he had knowledge of any defence upon the instrument referred to in article 25. Accordingly, he would be precluded from qualifying as a protected holder if he had knowledge of a defence to contractual liability based on a transaction between himself and a party even though that transaction was unrelated to the issue or transfer of the instrument (article 25(1)(c)). It was suggested that the denial of the status of protected holder in those circumstances was undesirable and that article 4(7) might therefore be amended to avoid that result (e.g. by providing that a holder was precluded from qualifying as a protected holder if he had knowledge of a defence referred to in article 25(1)(a), (b) or (d)).

51. There was considerable support for this suggestion. The view was expressed, however, that the result of such an amendment might be that a holder would qualify as a protected holder even when he had knowledge of a defence to contractual liability that was available to the immediate party from whom he took the instrument on the basis of the underlying transaction between the holder and that party.

52. It was noted in reply that while the holder might in such circumstances qualify as a protected holder, an immediate party could set up as against the protected holder the defence based on the underlying transaction (article 26(1)(b)). It was observed, however, that while an action against the immediate party might not be available by reason of article 26(1)(b), the fact that the holder obtained the status of protected holder might have other consequences (e.g. a transfer by the protected holder might vest in a subsequent holder the rights of a protected holder: article 27(1)).

53. The view was also expressed that the phrase "a defence upon the instrument referred to in article 25" contained in article 4(7) needed further consideration.

Article 25(1) referred to a range of defences that any party, immediate or remote, might set up against a holder who was not a protected holder, and it was unclear whether knowledge of any of those defences would preclude a holder from becoming a protected holder.

54. After deliberation, the Commission decided that article 4(7) needed modification in the light of the difficulties noted above and entrusted this task to an *ad hoc* working party. The *ad hoc* working party concluded that the reference to article 25, as contained in article 4(7)(a), was appropriate, except for those defences arising from a transaction or relationship between the immediate party and the holder that was not related to the issue or transfer of the instrument. In order to express this exception, it was proposed that a distinction should be made in article 25(1)(c) between defences resulting from the underlying transaction and defences resulting from other transactions and to exclude this latter part of the provision from the reference contained in article 4(7)(a).

55. The Commission considered the following proposal of the *ad hoc* working party:

(a) To modify article 4(7)(a) as follows:

“(a) He was without knowledge of a claim to or defence upon the instrument referred to in article 25, other than in paragraph (i)(c)(ii), or of the fact that it was dishonoured by non-acceptance or non-payment; and”

(b) To modify article 25(1)(c) as follows:

“Any defence resulting from

“(i) the underlying transaction between himself and the holder;

“(ii) any other transaction between himself and the holder that would be available as a defence against contractual liability.”

56. It was observed that the proposed new text maintained in article 4(7) the words “a claim to or defence upon the instrument referred to in article 25”. In the earlier deliberations in the Commission, it had been noted that the reference to article 25 gave rise to difficulties in identifying the parties mentioned in article 4(7) within the context of article 25, although such identification was necessary to give effect to the reference.

57. It was observed in reply that any attempt to draft article 4(7) without such a reference led to extreme complexity of language in article 4(7). After deliberation, the Commission adopted the proposed text of articles 4(7) and 25(1)(c) that had been proposed by the *ad hoc* working party with a drafting amendment to article 4(7) proposed by the drafting group.

#### *Shelter rule (article 27)*

58. A view was expressed that under the present wording of article 27, its intended effect might not be clear. After deliberation, it was agreed that the effect of article 27 was that a transferee of an instrument from a

protected holder acquired the rights that the protected holder had at the time of the transfer; it did not confer protected holder status upon the transferee.

59. The Commission, after deliberation, adopted article 27.

#### *Presumption of protected holder status (article 28)*

60. A proposal was made to delete article 28 on the grounds that a person raising a defence should not have to prove knowledge by the claimant of facts that would prevent the claimant from being a protected holder. In opposition to the proposal, it was stated that the rule expressed in article 28 was contained in many legal systems and that the rule strengthened the transferability of an instrument. The proposal was not adopted.

61. The Commission, after deliberation, adopted article 28.

#### *Liability of transferor by endorsement or by mere delivery (article 41)*

62. The Commission approved of the approach taken in article 41 under which its provisions applied both to a transfer by mere delivery and to a transfer by endorsement and delivery. It was suggested that the opening language of the article needed amendment to make it clear that the article applied to both those categories of transfer. The Commission agreed that because the article applied to both categories of transfer, it should not be placed under the heading “The endorser” but should be placed under an independent heading. The Commission also agreed that the interest rate referred to in paragraph (3) of article 41 should be calculated in accordance with article 66. Subject to those agreed changes, the Commission adopted article 41.

#### *Article 5 (and its relationship to other articles)*

63. The Commission considered the definition contained in article 5 as to when a person is considered to have knowledge of a fact.

64. The view was expressed that while under the article a person is considered to have knowledge of a fact if he either has actual knowledge of a fact or could not have been unaware of its existence, the second element was in fact superfluous. If a person could not have been unaware of the existence of a fact, he would appear to have actual knowledge of the fact. The view was also expressed that the meaning of the phrase “could not have been unaware of its existence” was unclear, and that the phrase might therefore be interpreted differently in different jurisdictions. It was observed in reply that in some legal systems the term “actual knowledge” was given a very restricted meaning, and that a wider meaning was required in the contexts in which the word “knowledge” was used in the draft Convention. For example, where a person deliberately chose to ignore a fact, knowledge of the fact should

be imputed to him even though he could not be said to have actual knowledge of it. It was also noted that the phrase "could not have been unaware of its existence" had been used in the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980), and that the phrase had been found to be widely acceptable during the deliberations leading to the adoption of that Convention.

65. The Commission noted that where the words "without knowledge" were used in articles 23(2), 23 *bis* (2), 25(1)(d) and 26(1)(c), those articles also contained the following proviso: "provided that such absence of knowledge was not due to his negligence". The Commission first considered the relationship of the definition contained in article 5 to the proviso as contained in articles 25(1)(d) and 26(1)(c). The view was expressed that, in view of the definition contained in article 5, the proviso might be deleted. Where the absence of knowledge of a fact by a person was due to his negligence, knowledge of the fact might be imputed to that person by the application of the phrase "could not have been unaware of its existence" contained in article 5. Retaining both this phrase in article 5 and the proviso in articles 25(1)(d) and 26(1)(c) might lead to duplication of or inconsistency in language. The difficulty might be resolved either by deleting the proviso from articles 25(1)(d) and 26(1)(c) or by deleting article 5. Another approach to resolving the difficulty might be to add at the commencement of article 5 the words "unless otherwise stated in this Convention". It was also noted that use of the term "negligence" might lead to difficulties of interpretation in some legal systems.

66. Under another view, however, it was desirable to retain the words "provided that such absence of knowledge was not due to his negligence" in articles 25(1)(d) and 26(1)(c). It was possible to envisage situations where it could not be held that a person could not have been unaware of the existence of a fact (article 5), but where that person might be held to be negligent. For example, if a promissory note was placed before a person by a trusted employee with the nature of the document concealed and it was therefore signed by that person as maker, the circumstances might make it difficult to find that he could not have been unaware of the nature of the document that he was signing. Nevertheless, those circumstances might have imposed on that person a duty to make inquiry about the document he was signing and his signing without inquiry might have constituted negligence. It was also observed that if use of the term "negligence" might lead to difficulties of interpretation, a different term of equivalent meaning might be used. Furthermore, the addition of the words "unless otherwise stated in this Convention" to article 5 was undesirable because that addition would reduce the certainty of meaning that the definition as presently drafted gave to the term "knowledge".

67. After deliberation, the Commission decided that the proviso should be retained in articles 25(1)(d) and 26(1)(c).

68. The Commission recognized that the arguments advanced in respect of the relationship of the definition contained in article 5 and the proviso as contained in articles 25(1)(d) and 26(1)(c) also applied in regard to the proviso in articles 23(2) and 23 *bis* (2). It was noted that the following additional consideration was relevant in regard to the latter articles. Those articles covered the possible liability of a collecting banker when the instrument contained a forged endorsement. While different approaches were possible as to the extent of liability of a banker collecting such an instrument, the present text reflected a compromise solution that appeared to be acceptable to bankers. Deletion of the proviso, which would eliminate the compromise solution, was therefore undesirable.

69. After deliberation, the Commission decided that the proviso should be retained in articles 23(2) and 23 *bis* (2).

70. The Commission considered the definition contained in article 5 in relation to the word "knowledge" as used in articles 4(7), 11(2)(a), 41(1)(c), 41(2) and 68(3) and decided that the definition was satisfactory in the context of those articles.

## 2. *Review of other issues and draft articles considered by the Working Group*

### *Article 1*

71. It was proposed that a new subparagraph reading "is domiciled with a bank;" should be added after subparagraph (c) of article 1(2) and (3) and that article 51(d) should be deleted.

72. After deliberation, the Commission was of the view that the proposed amendment would unduly restrict the scope of the instruments to which the draft Convention would apply, and accordingly did not adopt the proposal.

73. The view was expressed that the provisions of article 1 defining when an instrument was to be regarded as international so as to attract the application of the Convention were unsatisfactory. An instrument in respect of which the places specified in article 1(2)(e) were exclusively within a single State would not attract the application of the Convention. However, the application of the Convention would continue to be excluded even if the instrument thereafter circulated in a different State (e.g. was endorsed in a different State). It was observed in reply that the provisions of article 1 gave autonomy to the parties to attract the application of the Convention at the time the instrument was issued by, *inter alia*, specifying that at least two of the places mentioned in article 1(2)(e) were situated in different States.

74. It was recognized that article 1(2)(e), which determined when an instrument was international so as to attract the application of the Convention, was the result of decisions taken by the Commission at earlier sessions

after extensive deliberation. Accordingly, the Commission decided to maintain the approach reflected in article 1.

75. The view was expressed that article 1 combined two different sets of requirements, namely, the international elements necessary for the application of the Convention and the conditions for the validity of an instrument. A proposal was therefore made to separate those two sets of requirements by dividing article 1 into two articles. The Commission noted that the same proposal had been placed before the Working Group on International Negotiable Instruments at its fourteenth session, but had not been adopted by the Working Group (see A/CN.9/273, paras. 61 and 62). While the proposal attracted some support, the prevailing view was that it should not be adopted.

76. The view was expressed that it was unclear whether article 1 required an instrument to show where all the places mentioned in article 1(2)(e) and (3)(e) were situated, and whether showing where those places were situated was an essential condition for the validity of an instrument. It was observed in reply that the provisions of article 1(2)(e) and (3)(e) were only directed to determining when an instrument was international so as to attract the application of the Convention and required that the instrument show that two of the places mentioned therein were situated in different States as a condition for such application. It was agreed that this meaning should be clarified by a suitable amendment to the opening words of article 1(2)(e) and (3)(e) and the matter was referred to the drafting group. The Commission adopted a proposal by the drafting group to amend the opening words of article 1(2)(e) and (3)(e) as follows:

“(e) Specifies at least two of the following places and indicates that any two so specified are situated in different States:”.

77. A suggestion was made that in order to attract the application of the Convention, article 1(2) and (3) should require the words “International bill of exchange (Convention of ...)” or the words “International promissory note (Convention of ...)” to be contained only in the heading of an instrument and not in the text of an instrument. A further suggestion was made that those words should be required to be in a single specified language, as that requirement would enable an instrument to which the Convention applied to be easily identified. The Commission did not accept those suggestions.

78. It was agreed that the draft Convention should not contain a definition of the term “writing”. Rather, the meaning of the word should be left open so that it could be interpreted in accordance with evolving practices and technological developments. It was stated that it would be difficult to arrive at a satisfactory definition of “writing”. Moreover, the word was usually not defined in national legislation concerning negotiable instruments, and the absence of a definition had not led to difficulties.

79. A view was expressed that a problem could arise where an instrument consisted of several pages. In some cases, for example, the essential terms of the instrument were contained in one or more pages, but the signature appeared only on the last page, and it was questionable whether such an instrument was valid under the draft Convention. It was suggested that if it were intended that the essential requirements of an instrument could be contained in separate pages, the draft Convention should expressly so provide.

80. According to another view, no problems arose with respect to the validity under the Convention of an instrument consisting of several pages, when all the pages were fixed together to form a single document. It was noted, however, that some of the terms of a multi-paged instrument might make the instrument conditional, contrary to article 1(2)(b) and (3)(b) of the draft Convention.

81. It was agreed that instruments consisting of several pages were covered by the draft Convention.

82. It was observed that a provision excluding cheques from the scope of application of the Convention was necessary for those legal systems where a cheque was regarded as a form of bill of exchange.

83. The Commission, after deliberation, adopted article 1 with the above-mentioned modifications.

#### *Questions relating to article 2*

84. A view was expressed that the Convention should require an instrument to be linked in some way with a contracting State in order for the Convention to apply to the instrument. According to that view, it was unacceptable for a drawer in a non-contracting State to be able to draw a bill on a drawee in another non-contracting State and to make the bill subject to the Convention.

85. In addition, it was also noted that some legal systems did not recognize the autonomy of a drawer or maker to choose the law to which an instrument was subject. If an action were brought on the instrument in such a State and that State was not a party to the Convention, it would not be bound to apply the Convention; rather, it would apply the rules of the legal system indicated by its own conflict of laws rules. Those conflict of laws rules were not likely to indicate the rules applied in a contracting State (i.e., the Convention) if there existed no link between the instrument and a contracting State. The possibility that a court in a non-contracting State would not apply the Convention, notwithstanding that a party had purported to make the instrument subject to the Convention, would lead to uncertainties with respect to the application of the Convention and the legal rules governing international negotiable instruments. Although that uncertainty could not be completely eliminated, it might be moderated by requiring, for example, that the place where the instrument was drawn or the place where it was to be paid was situated in a contracting State.



86. According to another view, the uncertainty referred to in the previous paragraph was not a major concern to bankers. They would prefer to be able to determine from the face of the instrument whether the Convention applied. They could do so with reasonable certainty under article 2 as it was drafted at present. If the Convention were to require a link between a place indicated on the instrument and a contracting State, bank personnel handling an instrument would have to ascertain whether or not the indicated place was in a State that was a party to the Convention.

87. Questions were raised as to the meaning and effect of article 2 as drafted at present. According to one view, article 2 was misleading, since it implied that a court in a contracting State would in all cases be compelled to apply the Convention if a party had made the instrument subject to the Convention, whether or not the places indicated on the instrument were situated in contracting States. It was stated that there were cases in which some States, even if they were parties to the Convention, would, by application of their conflict of laws rules, apply national legal rules rather than the Convention. For example, where an instrument was drawn in a non-contracting State, a court in the contracting State might apply the law of the State where the instrument was drawn, rather than the Convention.

88. The prevailing view, however, was that the intent and meaning of article 2 was that a court in a contracting State must apply the Convention to an instrument meeting the requirements of the Convention, even if the conflict of laws rules of that State would result in the application of some other law.

89. A view was expressed that under that interpretation of article 2, there would exist a conflict between the Convention now being drafted and the 1930 Geneva Convention for the Settlement of Certain Conflicts of Laws in Connection with Bills of Exchange and Promissory Notes. It was questioned, therefore, whether a State which was a party to that convention could also become a party to the Convention currently being drafted by the Commission.

90. Owing to the apparent lack of clarity with respect to the meaning and effect of article 2, the article was referred to the drafting group with instructions to clarify the article so as to reflect its intended meaning and effect. The drafting group proposed to amend the beginning of article 2 to read as follows: "A Contracting State shall apply this Convention without regard to whether ...".

91. During consideration of that proposal by the Commission, it was noted that since the Convention was addressed only to contracting States, the proposed wording would not preclude a non-contracting State from applying the Convention if its conflict of laws rules indicated that the Convention should apply. However, a view was expressed that the proposed wording did not conform to the wording usually found in private international law conventions and that the original wording of

article 2 as it appeared in document A/CN.9/274 was preferable, subject to replacing the word "applies" with the words "shall apply". The Commission decided to retain the original wording subject to the suggested change.

#### *Interpretation of the Convention (article 3)*

92. A view was expressed that the reference in article 3 to the observance of good faith in international transactions should be deleted. It was suggested that the obligation to observe good faith was incumbent upon the parties to a transaction and should not be directed to a tribunal interpreting the Convention, which was the object of article 3. In addition, it was unclear what was meant by the observance of good faith in international transactions. The prevailing view, however, was that the reference to the observance of good faith should be retained.

#### *Definition of "signature" (articles 4(10) and X)*

93. A view was expressed that the draft Convention should not contain a definition of the term "signature". In support of that view, it was stated that the methods of signature in use and legally recognized varied from State to State, and it would be difficult for the Convention to reflect those local practices and legal requirements; rather, the question of permissible methods of signature should be left to be resolved by national law. It was also stated that no problems had arisen from the absence of a definition of "signature" in the Uniform Law annexed to the 1930 Geneva Convention providing for a Uniform Law for Bills of Exchange and Promissory Notes. That point, however, was disputed.

94. According to another view, the word "signature" should be defined in the draft Convention. It was observed that, under article 1(2)(f) and (3)(f), the signature of the drawer or maker was an indispensable element for the Convention to apply to an instrument. It was, therefore, important for parties to have some certainty that a signature by a particular method would be valid in States where the instrument might be negotiated or sued upon. Without a definition specifying the methods of signature that were acceptable, that certainty would not exist.

95. The Commission considered various methods of signature that should be included in a definition of the term "signature". It was generally agreed that the definition should refer to handwritten signature, which was the most traditional method. A view was expressed that the mechanical methods of signature referred to in article 4(10) should also be included in the definition. Further suggestions were made that the definition should refer to "illegible signature", i.e., signature by characters or symbols, and to signature by electronic means. According to another view, however, signature by electronic means should not be included, since that might imply that an instrument need not be on paper.

96. Differing views were expressed with respect to article X. According to one view, if the Convention were to define signature as including both handwritten and non-handwritten forms of signature, article X must be included in order to meet the interests of those States that required signatures made in their territories to be handwritten. It was noted, however, that the concerns of those States might, to some extent, be met by article 30, under which a person whose signature was forged was not liable on the instrument.

97. According to another view, article X should not be included in the draft Convention. In support of that view, it was stated that inclusion of the article would produce uncertainty with respect to the validity of a signature and would impair the circulation of instruments. In dealing with instruments containing signatures by methods other than handwriting, bank personnel would have to determine whether the State where the signature was made had deposited a reservation pursuant to article X. Moreover, the Convention did not require the instrument to indicate the place where the signature was made; it would therefore be impossible in many cases to ascertain whether the signature had been made in a State that had deposited a reservation pursuant to article X.

98. A suggestion was made that if article X were retained, the draft Convention should require the instrument to indicate the place where the signature was made. According to another suggestion, it should be clarified whether or not a State that had not deposited an article X declaration must regard as invalid a signature by non-handwritten means made in a State that had deposited such a reservation.

99. Some of those objecting to article X stated that if retention of article 4(10) made it necessary to include article X to meet the interests of some States, it was preferable for article 4(10) to be deleted. Others preferred to retain article 4(10) and also to include article X, if necessary.

100. It was generally agreed that the most desirable approach would be to attempt to formulate, as a compromise, a definition of "signature" that would take into account the interests of those favouring a broad definition of the word and those favouring a restricted definition and that would make it possible to avoid including article X. In that connection, a view was expressed that the definition should refer expressly to handwritten signature and facsimile thereof, but should also be broad enough to include signatures effected by certain other methods in use in various parts of the world. However, to be satisfactory to those States that required signatures in their territories to be handwritten in order to protect against falsification, those other methods should be limited to methods that afforded a degree of authenticity equivalent to that afforded by handwritten signatures. It was stated that such an approach would allow courts or national legislatures to recognize the validity of methods of signature that might come into practice in the future but that conformed to the general parameters of the definition.

101. It was also suggested that the definition should provide a reasonable degree of certainty that a signature by a particular method would be regarded as valid, although it was recognized that the commercial risk with respect to methods that were not expressly mentioned in the definition could not be completely eliminated.

102. Taking into account these views and based upon a proposal of the drafting group, the Commission agreed to adopt the following definition of signature and to delete article X:

"Signature' means a handwritten signature, or a facsimile thereof, or any other means of effecting the equivalent authentication, and 'forged signature' includes a signature by the wrongful or unauthorized use of such means."

*Articles 4(11) and 71(1 bis)*

103. The Commission considered article 4(11), which sets forth a definition of "money" and "currency". It also considered a note by the secretariat (A/CN.9/285, paras. 1-4) prepared in response to a request to the secretariat by the Working Group on International Negotiable Instruments to consult with the International Monetary Fund (IMF) on the definition set forth in article 4(11).

104. The observer of IMF noted that article 4(11) enabled an instrument governed by the draft Convention to be drawn in a monetary unit of account established by an intergovernmental institution or by agreement between two or more States. In so far as the Special Drawing Right (SDR) established by IMF was concerned, it was intended to be the subject of transactions between States members of IMF who were also members of a special SDR department within IMF. IMF had laid down rules regulating the transfer of SDRs among members qualified to make transfers, and those rules related, for example, to exchange rates and the value dates for transactions. While the draft Convention permitted instruments to be drawn in monetary units of account and regulated the transfer of such instruments, it was not intended that the draft Convention should derogate from the rules laid down by IMF regulating the transfer of SDRs, or the rules laid down by any other intergovernmental institution or by two or more States regulating the transfer of a monetary unit of account established by such intergovernmental institution or States. In the view of the observer of IMF, it was desirable to reflect this intention in the draft Convention by adding a proviso to article 4(11) on the following lines: "provided that the Convention shall apply without prejudice to the rules of an intergovernmental institution or to the stipulations of an agreement between two or more States relating to a monetary unit of account established by such institution or agreement".

105. The view was expressed that the addition of the suggested proviso was unnecessary, since there was little danger that the draft Convention would be interpreted as derogating from the rules of an intergovernmental institution or the stipulations of an intergovernmental agree-

ment relating to a monetary unit of account established by such institution or agreement. The view was also expressed that the concerns of IMF might be met by the inclusion of a statement in the report of the Commission on the work of its current session to the effect that, in the understanding of the Commission, the draft Convention was not to be so interpreted. The prevailing view, however, was that the addition of a proviso clearly resolving the issue in question was preferable, and the Commission decided to include a proviso on the lines of that suggested by the observer of IMF.

106. The Commission also examined the following two considerations in respect of monetary units of account established by agreement between two or more States, which had been brought to the attention of the Commission by the secretariat (see A/CN.9/285, para. 4):

(a) The definition in article 4(11) would include the units of account denominated in specified quantities of gold found in several important liability conventions. Those did not appear to be among the units of account contemplated by the Working Group when they formulated the definition;

(b) Units of account created by agreement of two or more States for specific purposes might be terminated when that purpose was fulfilled. It was possible that no means of converting those units into replacement currencies or units of account would be devised, especially if the States concerned were unaware that private obligations had been created in that unit of account.

107. The Commission entrusted to an *ad hoc* working party the task of formulating a proviso to be added to the definition in article 4(11) (see paras. 104–105 above) and also the task of determining whether article 4(11) needed additional modification in the light of the considerations set forth in paragraph 106 above.

108. The view was expressed that the provisions of article 71(1 *bis*) regulating the payment of an instrument the amount of which was expressed in a monetary unit of account needed clarification. That article might be interpreted as providing that, when the amount of an instrument is expressed in a monetary unit of account that is transferable between the person who is to make payment and the person who is to receive payment and when the instrument specifies that payment is to be made in a currency of payment, payment nevertheless cannot be made in the specified currency. The wording of the article might therefore be modified to avoid this interpretation. The Commission referred that article for consideration to the same *ad hoc* working party examining article 4(11).

109. The Commission considered a proposal of the *ad hoc* working party and of the drafting group to add to the end of article 4(11) the following text:

“provided that this Convention shall apply without prejudice to the rules of the intergovernmental institution or to the stipulations of the agreement.”

and to replace paragraph (1 *bis*) of article 71 by the following text:

“(1 *bis*) When the amount of an instrument is expressed in a monetary unit of account within the meaning of article 4(11) and the monetary unit of account is transferable between the person making payment and the person receiving it, then, unless the instrument specifies a currency of payment, payment shall be made by transfer of the monetary unit of account. If the monetary unit of account is not transferable between those persons, payment shall be made in the currency specified in the instrument or, if no such currency is specified, in the currency of the place of payment.”

110. After deliberation, the Commission adopted those proposals.

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

111. The Commission considered article 6(b) and (c), which provides that the sum payable by an instrument is deemed to be a definite sum even though the instrument states that it is to be paid by instalments at successive dates (article 6(b)) or by instalments at successive dates with the stipulation on the instrument that upon default in payment of any instalment the unpaid balance becomes due (article 6(c)).

112. The view was expressed that those provisions were not acceptable because they led to technical difficulties (e.g. complexity in the provisions of the instruments, difficulties in calculating the interest due). Article 6(c) in particular was open to objection because it might encourage the drawing of instruments that operated harshly against the debtor.

113. The prevailing view, however, was that since the practices described in those two provisions were current in international trade, the usefulness of the draft Convention would be enhanced if instruments subject to it were permitted to include such provisions. Furthermore, while an acceleration clause under article 6(c) might be harsh in a given case, a debtor was free to object to such a term which the creditor wished to include in an instrument. After deliberation, the Commission adopted article 6(b) and (c).

#### *Instruments with floating interest rates (article 7)*

114. The Commission considered whether the draft Convention should include a provision permitting the issuance of instruments with floating (or variable) interest rates. In that connection the Commission had before it a note by the secretariat dealing with this issue (A/CN.9/285, paras. 5–12). The Commission considered the issue in the light of the following new article 7(5) proposed by the secretariat:

“(5) A rate at which interest is to be paid may be expressed either as a definite rate or as a variable rate. For a variable rate to qualify for this purpose, it must vary in accordance with provisions stipulated in the

instrument and those provisions must refer to one or more other rates of interest [that are both publicly available and not subject to the control of the payee].”

115. There was support for the view that the draft Convention should not include such a provision. The inclusion of a floating interest rate might lead to uncertainty as to the extent of the debtor's payment obligations. This uncertainty might in turn impede the circulation of instruments with such rates. Furthermore, unless safeguards were adopted, a floating interest rate might be influenced by the creditor in his own favour. In addition, since interest rates tended in general to increase and not decrease, a floating interest rate would probably not favour the debtor. As a result, the view was expressed that such a provision was not in the interest of developing countries. It was also noted that instruments with floating rates had not been regarded as significant in international trade by financial institutions in some countries.

116. The prevailing view, however, was that the inclusion of a provision permitting floating interest rates would greatly increase the attractiveness of the draft Convention to the financial community. Instruments with floating interest rates were currently in use in certain financial markets, although they did not qualify as negotiable instruments. Inclusion of a provision in the draft Convention permitting floating interest rates would allow such instruments to qualify as negotiable instruments and to circulate. This in turn could be expected to reduce the interest charged on those instruments. While a floating interest rate might introduce an element of uncertainty as to the extent of the debtor's payment obligations, article 6(d) of the draft Convention already countenanced an element of uncertainty by providing that a sum payable by an instrument is deemed to be a definite sum although it is to be paid according to a rate of exchange to be determined as directed by the instrument. Furthermore, recent experience had shown that interest rates often decreased, and therefore it could not be concluded that a floating interest rate would normally favour the creditor.

117. The Commission considered the requirements contained in the new article 7(5) proposed by the secretariat that in stipulating a variable interest rate, the provisions in the instrument “must refer to one or more other rates of interest [that are both publicly available and not subject to the control of the payee]”. The view was expressed that it was undesirable for the proposed paragraph to permit the variation of the interest rate on the instrument to be linked only to a variation in one or more other interest rates; in practice, floating interest rates were linked to commodity price indices or other sources. While there was some support for this view, the prevailing view was that a reference to only one or more other rates of interest should be permitted.

118. The Commission considered whether the proposed new paragraph in the draft Convention should require that the reference rates of interest were to be “both

publicly available and not subject to the control of the payee”. It was noted that both requirements were directed to reducing the possibility that the reference rate of interest might be influenced by an interested party. It was also noted that the meaning of “publicly available” might be uncertain. For example, there might be differences of view as to whether a rate used by only a few banks and available only upon inquiry from one of those banks was “publicly available”. In view of that uncertainty, the suggestion was made that the requirement should be deleted and that the parties should be given autonomy to select a reference interest rate, provided that that rate was determined or determinable on the instrument.

119. With regard to the words “not subject to the control of the payee”, the view was expressed that the concept of “control” was unclear, and it was suggested that the clearer phrase “not subject to unilateral variation by the payee” might be substituted. It was also noted that a reference solely to “control of the payee” was insufficient; protection against control of the reference interest rate by other parties to the instrument (e.g. endorsers) was also needed.

120. After deliberation, the Commission decided to retain the concepts underlying the use of the wording “both publicly available and not subject to the control of the payee”, but referred the text of article 7(5) prepared by the secretariat to an *ad hoc* working party for consideration in the light of the deliberations in the Commission.

121. The Commission considered the following new article 7(5) proposed by the *ad hoc* working party:

“(5) A rate at which interest is to be paid may be expressed either as a definite rate or as a variable rate. For a variable rate to qualify for this purpose, it must vary in relation to one or more reference rates of interest in accordance with provisions stipulated in the instrument and each such reference rate must be published or otherwise available to the public and not subject, directly or indirectly, to unilateral determination by the payee or by any person named in the instrument at the time the bill is drawn or the note is made.”

122. The question was raised as to the time that was relevant under the proposed paragraph for referring to the reference rate. It was stated in reply that the reference rate contemplated was one that would be published or available during the lifetime of the instrument whenever a need to refer to that rate arose (e.g. when it became necessary to calculate interest).

123. The question was raised as to what words were qualified by the phrase “at the time the bill is drawn or the note is made”. It was stated in reply that the phrase qualified the words “named in the instrument”. It was agreed that the text of the paragraph needed modification to make this clear.

124. It was observed that the phrase "any person named in the instrument" might lead to difficulties of interpretation where a person was named in the instrument only for the purpose of identifying a reference rate (e.g. the reference rate is identified as that published by a named bank). Since it was not intended that the phrase should cover a person named in the instrument only for that purpose, it was agreed that the text of the paragraph needed to be modified to clarify which persons were intended to be covered by the phrase.

125. After deliberation, the Commission adopted the new paragraph, entrusting to the drafting group the task of making the needed modifications referred to in the previous two paragraphs.

126. A proposal was made that the uncertainty as to the extent of the debtor's payment obligations and hardship to the parties created by extreme fluctuations of interest rates might be mitigated if the provision to be included in the draft Convention permitted the parties to stipulate that the interest rates applicable could neither exceed nor be less than specified rates of interest. Under another proposal, any instrument that provided for floating interest rates would be required to establish a reasonable minimum and maximum rate of interest. The view was expressed that imposing such limitations was undesirable because they were not currently found in the use of floating interest rates in commercial (as contrasted with consumer) loans.

127. The following specific proposals were made to add a new paragraph (5 *bis*) to article 7 in order to provide for limits on the amount by which variable interest rates on an instrument could fluctuate:

*Proposal A*

"In order for a floating interest to be agreed to, the instrument shall at the same time indicate the rules agreed on to prevent fluctuations, whether upwards or downwards, from having consequences which, according to reasonable criteria in international trade, are contrary to equity, to the detriment of any of the parties and of the holder of the instrument."

*Proposal B*

"Where the rate at which interest is to be paid is expressed as a variable rate, it may be stipulated that such rate shall not be less than or exceed a specified rate of interest."

128. In support of proposal A, it was stated that some parties to commercial transactions would be willing to agree to the use of instruments subject to variable interest rates only if the fluctuation of the interest rate, and thus of the amount of interest that they would be required to pay, was limited. The acceptability of instruments covered by the Convention, and of the Convention itself, would therefore be enhanced if the Convention provided for such limits. Proposal A allowed the parties the freedom to agree upon various techniques for limiting the amount of fluctuation in accordance with their commercial needs, while proposal B restricted them to one

particular technique. It was also stated that proposal A would require the parties to agree upon a limit to the amount the interest rate could fluctuate, thereby reducing the extent to which a variable interest rate provision on an instrument would depart from the fundamental principle of negotiable instruments law that an instrument should not be subject to circumstances external to it. According to another view, however, by providing for such limits, the Convention would depart even further from that principle.

129. In support of proposal B, it was stated that it was preferable to leave it to the parties to agree as to whether or not the amount of fluctuation of the rate of interest on an instrument should be limited, rather than to obligate them to agree upon such limits. If proposal A were adopted, parties who desired not to have such limits would not be able to use an instrument governed by the Convention. In addition, the criteria specified under proposal A for the validity of limits agreed upon by parties were vague and would lead to uncertainty as to whether a variable interest rate provision would be regarded as valid in particular cases.

130. Some representatives who favoured proposal B in principle suggested that the parties should not be restricted to formulating limits by stipulating a minimum or maximum rate of interest; they should also be permitted to agree upon other techniques. Some such representatives stated that the right of parties to agree upon limits of any nature was implicit in paragraph (5) of article 7 as adopted by the Commission; therefore, it might be preferable not to include a paragraph (5 *bis*).

131. After deliberation, it was decided to add paragraph (5 *bis*) to article 7 along the following lines:

"(5 *bis*) Where the rate at which interest is to be paid is expressed as a variable rate, it may be stipulated on the instrument that such rate shall not be less than or exceed a specified rate of interest, or that the variations are otherwise limited by express provisions."

132. The Commission considered what should be the consequences if the parties selected a floating interest rate that did not meet the requirements of the proposed article 7(5) (e.g. the parties selected a rate that was not publicly available). It was noted that in those circumstances article 7(4) would apply and the instrument would bear no interest. The Commission considered an alternative solution prepared by the secretariat (A/CN.9/285, para. 8) and reflected in the following proposed new article 7(6):

"(6) If a variable rate does not qualify under the preceding paragraph or for any reason it is not possible to determine the numerical value of the variable rate for any period, interest shall be payable for the relevant period at the rate specified in article 66(2)."

133. The Commission decided that the Convention should provide for a substitute rate of interest to apply when the variable rate selected by the parties did not meet the requirements of the draft Convention.

134. The drafting group, after considering the discussions of the Commission concerning new paragraphs (5), (5 *bis*) and (6) of article 7, proposed that those paragraphs be worded as follows:

“(5) A rate at which interest is to be paid may be expressed either as a definite rate or as a variable rate. For a variable rate to qualify for this purpose, it must vary in relation to one or more reference rates of interest in accordance with provisions stipulated in the instrument and each such reference rate must be published or otherwise made available to the public and not subject, directly or indirectly, to unilateral determination by any person who, at the time the bill is drawn or the note is made, is named in the instrument as payee, drawee, or actual or prospective party or other holder.

“(5 *bis*) Where the rate at which interest is to be paid is expressed as a variable rate, it may be stipulated expressly on the instrument that such rate shall not be less than or exceed a specified rate of interest, or that the variations are otherwise limited.

“(6) If a variable rate does not qualify under paragraph (5) of this article or for any reason it is not possible to determine the numerical value of the variable rate for any period, interest shall be payable for the relevant period at the rate calculated in accordance with article 66(2).”

135. A question was raised concerning the meaning of the words “prospective party” at the end of the proposed paragraph (5). It was stated that the intention in respect of the provision in which those words occurred was to refer to all persons named in the instrument at the time it was drawn or made who were to have rights on the instrument or were expected to have such rights and who should not be able unilaterally to affect the reference rate of interest. The provision was intended to exclude other persons, for example those mentioned in the variation clause, such as a bank, who would set the reference rate of interest.

136. Paragraphs (5), (5 *bis*) and (6) as proposed by the drafting group were adopted.

#### *Questions relating to article 8(2)*

137. A proposal was made to delete article 8(2) on the grounds that the legal effects of the rule contained in that provision were not clear, e.g., whether presentment, notice of dishonour or protest were necessary with regard to an endorser after maturity. Moreover, it was stated that the situation envisaged in article 8(2) was not likely to occur frequently. After deliberation, it was decided to retain article 8(2).

#### *Incomplete instruments (article 11)*

138. A proposal was made to add to article 11 a new paragraph providing that a holder may complete an instrument only before the instrument has matured. It

was contended that if, at the date of maturity, an instrument was not complete in accordance with the requirements of article 1, the instrument could not be regarded as covered by the Convention. That contention was, however, disputed. In opposition to the proposal, it was noted that it was possible for an instrument to be transferred after maturity; thus, it should be possible to complete an instrument after maturity. The proposal was not adopted.

139. Article 11 was adopted.

#### *Clauses prohibiting further transfers (articles 16 and 20(3))*

140. A view was expressed that the treatment of the subject of a stipulation by a drawer or maker restricting transfer of the instrument (article 16) and the subject of a clause by an endorser restricting further transfer of an instrument (article 20(3)) should be maintained in separate articles. It was noted that the effect of article 16 was to restrict the transferability of an instrument *ab initio*, while the effect of article 20(3) was to restrict only transfer subsequent to the transfer under the endorsement. Treating the two subjects in separate articles would avoid any misunderstanding as to the time when the restriction on transfer became effective. According to another view, however, the use and understanding of the Convention would be facilitated if all provisions concerning clauses restricting the transfer of an instrument were included in article 16, which was contained in the chapter of the draft Convention entitled “Transfer”.

141. In connection with those articles, the Commission considered what should be the effect of an endorsement and transfer of an instrument that did not conform to the restrictive clause. According to one view, the endorsement and transfer should be regarded as ineffective. According to another view, the endorsement and transfer should be deemed to have been made for collection only. It was agreed that whatever solution was adopted, it should be expressly set forth in the draft Convention.

142. The Commission reached the following decisions on those issues. The subjects of stipulations by a drawer or maker restricting transfer of an instrument and of clauses by an endorser restricting further transfer should both be dealt with in article 16, in separate paragraphs. In both cases, the consequence should be that the instrument was not transferable except for purposes of collection. If an instrument was purported to be transferred with an endorsement that did not indicate that the transfer was for collection only, the endorsement should be deemed to be an endorsement for collection.

143. After considering these questions, the drafting group proposed that article 16 should read as follows:

“(1) When the drawer or the maker has inserted in the instrument such words as ‘not negotiable’, ‘not transferable’, ‘not to order’, ‘pay (X) only’, or words of similar import, the instrument may not be transferred except for purposes of collection, and any endorsement, even if it does not contain words authorizing the

endorsee to collect the instrument, is deemed to be an endorsement for collection.

“(2) When an endorsement contains the words ‘not negotiable’, ‘not transferable’, ‘not to order’, ‘pay (X) only’, or words of similar import, the instrument may not be transferred further except for purposes of collection, and any subsequent endorsement, even if it does not contain words authorizing the endorsee to collect the instrument, is deemed to be an endorsement for collection.”

144. It was noted that the proposed paragraph (2) consisted of an amended version of former article 20(3). The Commission adopted the proposal of the drafting group.

#### *Implied acceptance or representation (article 30)*

145. It was noted that references to implied waiver had been omitted from articles 52, 58 and 63, but that the reference to implied acceptance or representation had been retained in article 30. A view was expressed that that reference in article 30 should also be deleted. In support of that view, it was stated that uncertainty would exist if a person whose signature had been forged could be made liable on the instrument as a result of conduct from which his acceptance or representation could be implied. It would be difficult for a purported transferee to know whether such an implied act had occurred, and whether the forger or the person whose signature was forged was liable on the instrument. Moreover, covering such implication would be contrary to the scheme of the Convention, according to which matters affecting the rights and duties of the parties arising from the instrument must be explicit. It was noted that deleting the reference would not affect the liability for damages off the instrument of a person who, by his conduct, induced another person to believe that he had accepted or represented the forged signature to be his own.

146. According to another view, however, the reference in article 30 should be retained, on the grounds that it was appropriate for a person to be liable on the instrument when, by his conduct, he impliedly accepted or represented the forged signature to be his own. It was also stated that the underlying question dealt with by article 30 was simply one of authority to sign the instrument, and that such questions generally depended upon circumstances off the instrument. Another view, however, was that article 30 did not deal with the question of authority.

147. A proposal was made to delete the possibility of both express and implied acceptance or representation by deleting the second sentence of article 30. In support of that proposal, it was stated that to make the person whose signature was forged liable on the instrument without his actually having signed it was contrary to the scheme of the Convention. Such a person should only be liable for damages off the instrument. According to the prevailing view, however, at least a person who had expressly indicated that a forged signature was his own or that he

would be bound by it should be liable on the instrument. As a result, the proposal to delete the second sentence of article 30 was not accepted.

148. A proposal was made to delete the words “expressly or impliedly” from article 30. In opposition to that proposal, it was stated that the deletion of the words would result in uncertainty as to whether an implied acceptance or representation would be covered.

149. After discussion, it was generally agreed that article 30 should be redrafted without using the words “expressly or impliedly”, and in such a way as to enable a court to imply from the conduct of a person whose signature had been forged that he had accepted or represented the forged signature to be his own, with the result that he would be liable on the instrument.

150. A proposal was made to amend the second sentence of article 30 to read as follows:

“Nevertheless, where such person has accepted to be bound by the forged signature or represented that the signature was his own, he is liable as if he had signed the instrument himself, according to the terms of such acceptance or representation.”

151. It was stated that the words “according to the terms of such acceptance or representation” were intended to permit a person whose signature had been forged to accept the forged signature or represent that it was his own only towards particular holders. After deliberation, the Commission decided to adopt the proposal to amend the second sentence of article 30, but to exclude those words.

#### *Exclusion of liability by drawer (article 34(2))*

152. With respect to the last sentence of article 34(2), a view was expressed that a stipulation by the drawer of a bill excluding or limiting liability for payment should be operative only if the drawee had accepted the bill, or if the bill had been signed by a guarantor for the drawer or for the drawee since the drawer should not be able to disclaim his liability unless there was another primarily liable party. The prevailing view, however, was that the present text of article 34(2), under which the stipulation would be effective if another party was or became liable on the bill, should be retained. In support of that view, it was stated that it was sufficient if there was a party, whether he be an acceptor or an endorser, from whom payment of the bill could be claimed. In addition, it was noted that the present text reflected a compromise between the Geneva and the Anglo-American systems on this point. It was also in accordance with commercial practice.

#### *Article 42*

153. The view was expressed that in commercial practice guarantees were sometimes entered into which were not written on the instrument or on a slip affixed thereto (“*allonge*”). Under most national laws those guarantees were valid, although they might only be effective as

between the immediate parties to the contract of guarantee. Since, however, the present wording of article 42(2) might be interpreted as not permitting those guarantees, it was proposed that the article should be modified to prevent that interpretation. The prevailing view, however, was that the present wording of article 42(2) was satisfactory. In support of that view, it was observed that the draft Convention did not in general deal with agreements outside the instrument and that the addition of wording which clarified in one instance that those agreements were permitted might lead to the inference that, in other instances where no such words were added, the Convention would exclude agreements outside the instrument. It was also observed that any provision to be added to the draft Convention to permit the creation of guarantees outside the instrument might need to determine the nature of permitted guarantees, and this determination might lead to an undesired limitation on the autonomy of the parties to enter into guarantees of their choice. The Commission therefore did not adopt that proposal.

154. The Commission considered article 42(6), which was a provision introduced into the draft Convention by the Working Group at its fourteenth session (see A/CN.9/273, para. 110, and annex).

155. After deliberation, the Commission adopted article 42.

#### *Article 46*

156. The Commission considered article 46, which had been modified by the Working Group at its fourteenth session (see A/CN.9/273, paras. 112 and 113, and annex). There was support for the view that the possibility given to the drawer under the first sentence of article 46(1) to stipulate that a bill must be presented for acceptance before the occurrence of a specified event needed reconsideration, since the inclusion of such a term in the instrument might be regarded as making the order contained in the instrument conditional. The instrument would then not satisfy the requirement contained in article 1(2)(b) that it contain an unconditional order to pay from the drawer to the drawee.

157. It was noted in reply that the provision under consideration had been included because inquiries among banking and trade institutions had shown that stipulations requesting the holder not to present the bill before the occurrence of a specified event (e.g. that presentment was to be delayed until the merchandise sold under an underlying transaction had arrived or until the customs clearance of the merchandise) were not infrequently included in bills of exchange. If the specified event did not occur, presentment for acceptance as directed by the stipulation would obviously be impossible and be dispensed with under article 48(b), and the holder would acquire an immediate right of recourse by virtue of article 50(1)(b) and (2). The present wording was therefore a compromise solution directed to the needs of international trade and enjoyed the support of banking circles.

158. After deliberation, the Commission adopted article 46.

#### *Articles 51(h) and 58(2)(d)*

159. After deliberation, the Commission adopted article 51(h), which was a provision modified by the Working Group at its fourteenth session (see A/CN.9/273, paras. 115–117, and annex). The Commission also adopted article 58(2)(d).

#### *Article 66*

160. The Commission considered the following issues arising in relation to article 66(2). It was noted that the article dealt with the rate of interest payable on an unpaid instrument after maturity, and that the first two sentences of the article provided for rates of interest to be payable at 2 per cent per annum above certain rates specified in those two sentences. However, the figure two had been placed by the Working Group within square brackets, leaving it to the Commission to take a final decision on the rate of interest to be payable.

161. In its third sentence article 66(2) contemplated that a rate to be specified in the draft Convention would apply in the absence of the rates specified in the first two sentences of the paragraph; however, no decision had been taken by the Working Group as to what that rate might be, leaving it to the Commission to decide.

162. In regard to the rates set forth in the first two sentences of the article, the view was expressed that the reference interest rate given in those sentences (i.e. “the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country ...”) might not exist in some countries. In other countries there might be more than one official rate. In still other countries, it was uncertain whether there existed an official or “bank” rate. Accordingly, the interest rate to be specified in the last sentence, which applied in the absence of the rates set forth in the previous sentences, assumed great importance. The view was also expressed that the official rate effective in the main centre of the country where the instrument was payable (first sentence of article 66(2)) might not be an appropriate rate if the instrument was payable in a currency other than the currency of the country where the instrument was payable.

163. The view was also expressed that setting the rate payable by adding 2 per cent to the reference rate was unjustified and resulted in a rate that was excessive. Under another view, however, a rate of 2 per cent above the reference rate was justifiable, since the reference rate would usually be set by public financial institutions at a level below that set by commercial institutions for default in payment under instruments used in international trade transactions. An addition of 2 per cent to the reference rate was therefore needed to bring the rate payable into line with commercial practice.

164. In regard to the rate to be inserted in the last sentence of the article, there was general agreement that



it would be inappropriate for that sentence to contain a specific figure to be effective during the entire period the Convention would be in force. Any figure inserted, even though appropriate at the time it was inserted, might later cease to be appropriate because of changed economic conditions. It was therefore preferable for that sentence to refer to a rate that was determinable, but that would vary with changing economic conditions. It was observed in that connection that it would be desirable to select a determinable rate that would not vary widely in the process of determination in different countries.

165. The following proposals were made as to the rate of interest to be payable under the third sentence of article 66(2):

(a) The rate that would be adjudged by a court under national law for non-payment of an instrument;

(b) The rate that the creditor would have to pay if he borrowed in a commercial market the amount of money in regard to which there had been default in payment;

(c) A rate that would be set by each State at the time it became a party to the draft Convention. That rate would be applied under the Convention by the courts of that State;

(d) The prime rate of interest in a country;

(e) The reasonable commercial rate existing at the time interest had to be calculated.

166. Views were exchanged on those proposals. It was observed that banking circles in some countries were reluctant to accept a rate that was not clearly and immediately ascertainable at the time that interest had to be calculated. Accordingly, rates that could be identified only after court intervention, or on which there might be differences of view (e.g. reasonable commercial rates), were not acceptable.

167. In opposition to the proposal set forth in paragraph 165(a) above, it was noted that adoption of a rate that would be adjudged by a national court might result in wide disparities in the rates that were effective in different countries or even in the different constituent units of a federal state. Furthermore, the rates set under national legislation might not reflect the compensation actually awarded by courts for non-payment. For example, in some countries, the interest rates set under national legislation were low in comparison with rates that would adequately compensate creditors, taking into account prevailing commercial conditions. In some of those countries the courts would, in addition to the interest adjudged under the legislation, also award a sum by way of damages as additional compensation. Moreover, if a State had become a party to the 1930 Geneva Convention providing a Uniform Law for Bills of Exchange and Promissory Notes without making a reservation under article 13 of annex II thereto, adoption of this proposal would result in the award of interest at only 6 per cent (article 48 of the Uniform Law), although this rate was not in line with current commercial rates of interest.

168. There was some support for the adoption of the rates referred to in paragraph 165(b) and (e). The adoption of those rates was opposed on the ground that they might not be easily ascertainable.

169. There was greater support for the following rate devised on the lines of that described in paragraph 165(a): the rate that would be adjudged under national law in respect of default of payment on an instrument in court proceedings instituted at the place where the instrument was payable. It was noted that court proceedings for default would normally be instituted at the place where the instrument was payable, and accordingly the rate in question would be easily ascertainable.

170. The Commission decided to refer to an *ad hoc* working party the revision of article 66(2) and (3) in the light of the deliberations in the Commission. The working party was also requested to consider the effect of modifications to article 66(2) and (3) on other articles of the draft Convention where article 66(2) and (3) was referred to. Another issue referred to the working party was whether the reference in article 66(1)(b)(ii) to "the sum specified in paragraph (1)(b)(i)" was appropriate or whether it should be limited to "the amount of the instrument".

171. In the light of proposals by the *ad hoc* working party and the drafting group, the Commission decided to amend article 66(2) to read as follows:

"The rate of interest shall be the rate that would be recoverable in legal proceedings taken in the jurisdiction where the instrument is payable."

172. In connection with article 66(3), which dealt with discount for payment of a bill before maturity, it was noted that the same problems concerning the existence of "the official rate (bank rate)" encountered in connection with article 66(2) did not exist with respect to "the official rate (discount rate)". However, observations were made with respect to the stipulation of a rate in the last clause of article 66(3) comparable to those expressed in relation to the last sentence of article 66(2). Accordingly, the Commission decided to amend the last clause of article 66(3) to read as follows:

"or, if there is no such rate, then at such rate as is reasonable in the circumstances."

173. The Commission adopted a proposal to add to article 66 a new paragraph (2 *bis*), as follows:

"(2 *bis*) Nothing in paragraph (2) prevents a court from awarding damages or compensation for additional loss caused to the holder by reason of delay in payment."

### 3. Consideration of further questions and draft articles

#### Conditional endorsements (article 17)

174. It was generally agreed that, under article 17, an endorsement for the purpose of transferring an instru-

ment to a holder must be unconditional. If an endorsement was made subject to a condition, the condition was to be disregarded with respect to the transfer of the instrument, and the transferee became a holder even if the condition was not fulfilled. However, differing views were expressed with respect to the effect, if any, of a condition upon the liability of the endorser to parties subsequent to the endorsee. According to one view, the condition should also be disregarded with respect to the liability of the endorser towards those parties. It was stated that that approach would promote the circulation of an instrument.

175. According to another view, however, a condition should not be disregarded with respect to the liability of the endorser towards parties subsequent to the endorsee. In support of that view, it was stated that if an instrument was transferred to an endorsee in connection with an underlying transaction between the endorser and the endorsee that was subject to a condition and the condition was not fulfilled, the endorser justifiably expected not to be liable, whether the condition was set forth in the endorsement on the instrument or was only contained in the underlying agreement. If the endorser had a defence against the endorsee based upon the non-fulfilment of the condition, holders subsequent to the transferee could also be affected by the condition by virtue of article 25; i.e., a subsequent holder who knew of the condition and that it had not been fulfilled would be subject to a defence based upon the condition.

176. It was stated that if a condition in an endorsement were to be prohibited and disregarded with respect both to the transfer of the instrument and the liability of the endorser, there would exist an inconsistency between article 17 and article 40(2), under which an endorser was able to exclude or limit his liability.

177. The Commission decided that article 17 should be redrafted in such a way that a condition in an endorsement was to be disregarded as to parties subsequent to the endorsee, and it referred the article to the drafting group.

178. The drafting group proposed the addition of the following sentence to article 17(2):

“The written condition is deemed not to have been written as to parties and transferees subsequent to the endorsee.”

179. Views were expressed in opposition to that wording, based upon the reasoning set forth in paragraph 175 above. It was stated that it might be wrong to disregard totally the condition in respect of the liability of the endorser towards parties subsequent to the endorsee since it may be relevant as a notice about a possible defence of the endorser. After deliberation, the Commission adopted the proposal of the drafting group.

#### *Pledge of instrument by endorsement*

180. A proposal was made to add a new article 20 *bis* reading as follows:

“When an endorsement contains the statements ‘value in security’ (*valeur en garantie*), ‘value in pledge’ (*valeur en gage*), or any other statement implying a pledge, the endorsee

“(a) Is a holder by virtue of article 4(6) and (7) and article 28;

“(b) May exercise all the rights arising out of the instrument;

“(c) May only endorse the instrument for purposes of collection;

“(d) Is subject to claims and defences which may be set up against the endorser only in the cases specified in articles 25 and 26.

Such an endorsee, having endorsed for collection, is not liable upon the instrument to any prior holder.”

181. In support of that proposal, it was stated that a pledge of an instrument by endorsement (“*endossement pignoratif*”) was used in international trade as a means of obtaining credit and that the draft Convention should contain special rules with respect to the rights and status of a pledgee by endorsement. According to another view, however, there was no practical need for such a provision, since the device contemplated by the provision was not in common use. A number of questions and objections were raised as regards certain elements of the proposed text, in particular the rules set forth in subparagraphs (a) and (b). The Commission decided not to entertain the proposal since it could not at the present stage engage in a careful consideration of the various elements of the proposal and its implications upon other articles of the draft Convention.

#### *Questions relating to articles 34(1), 35(1) and 40(1)*

182. A proposal was made to delete the word “subsequent” from article 34(1). It was stated that it was unclear whether the phrase “any subsequent party” referred to a party subsequent to the holder or one subsequent to the drawer. A further view was expressed that this article should also obligate the drawer to pay a guarantor of an endorser who had paid an instrument. Accordingly, it was agreed to amend article 34(1) along the following lines: by deleting the words “to any subsequent party” and to replace them with the words “to any endorser or the endorser’s guarantor”. It was also agreed that the same language should be used in article 35(1) and, with the word “subsequent” inserted, in article 40(1), since here it was necessary to clarify that the endorser was not obligated to prior endorsers or their guarantors.

183. The Commission adopted the following proposals of the drafting group:

(a) In article 34(1), to replace the words “any subsequent party” with the words “any endorser or any endorser’s guarantor”;

(b) In article 35(1), to replace the words “any party” with the words “any endorser or any endorser’s guarantor”.

(As regards article 40(1), see the proposal of the drafting group in para. 209 below.)

*Article 38(1) and its relationship with article 11*

184. The Commission considered the meaning of the term "incomplete instrument" in articles 11 and 38(1) and whether the provisions in article 38(1) dealing with the acceptance by a drawee of an incomplete bill of exchange before it had been signed by the drawer were satisfactory.

185. It was noted that different meanings were given to the term "incomplete instrument" in articles 11 and 38(1). Under article 11, an incomplete bill of exchange was one that satisfied the requirements of subparagraph (a) of article 1(2) that the bill contain in its text the words "international bill of exchange (Convention of ...)" and of subparagraph (f) that it be signed by the drawer, but that failed to satisfy one or more of the other requirements set out in article 1(2). Under article 38(1), however, a bill of exchange that satisfied only the requirements of article 1(2)(a) was regarded as an incomplete instrument that might be accepted by the drawee.

186. The view was expressed that as a result of the inconsistency in meaning of the term "incomplete instrument" as used in article 11 and in article 38(1), a drawee who accepted a bill before it had been signed by the drawer pursuant to article 38(1) did not receive the protection conferred by article 11(2), since the latter article conferred protection only on an incomplete instrument as defined in article 11(1). Since commercial needs sometimes made it desirable for a drawee to accept a bill before it had been signed by the drawer, it was desirable that a drawee who so accepted a bill should be given the protection conferred by article 11(2). That protection might be given by amending the opening words of article 11(1) to read: "An incomplete instrument which satisfies the requirements set out in subparagraph (a) of paragraph (2) of article 1, and bears the signature of the drawer or the drawee ...".

187. In reply, it was stated that the use of the term "incomplete instrument" in article 38(1) was inaccurate, since a bill of exchange that had not been signed by the drawer was not an incomplete instrument, but rather a writing that was not a negotiable instrument at all. A negotiable instrument came into being only after signature by the drawer. No attempt should therefore be made to bring within the definition of "incomplete instrument" in article 11 an instrument that had not been signed by the drawer. It was stated that neither article 11(1) nor article 38(1) contained a true definition of the term "incomplete instrument" and that it was therefore not inconsistent that the two provisions, for their different purposes, referred to instruments that were not complete as regards different requirements.

188. The Commission, after deliberation, decided to amend either article 11 or article 38(1) so as to provide that a writing that merely satisfied the requirement of article 1(2)(a) may be accepted by the drawee and that, in such case, the provisions of article 11 applied accordingly

to the signing by the drawer and any further completion by the drawer or another person. (See proposal by the drafting group to amend article 38(1), para. 209 below.)

*Article 48*

189. It was noted that while article 48 specified the situations in which a necessary or optional presentment for acceptance was dispensed with, it did not address the situation in which there was delay in making presentment for acceptance by the holder and in which the delay was excusable in that it was caused by circumstances that were beyond the control of the holder and that he could neither avoid nor overcome. In contrast, excusable delay was addressed by article 52(1) (in relation to presentment for payment), by article 58(1) (in relation to protesting an instrument for dishonour) and by article 63(1) (in relation to giving notice of dishonour). It was proposed that article 48 should be brought into line with the other articles referred to and that the holder should be obligated to make presentment for acceptance with reasonable diligence after the cause for delay ceased to operate.

190. It was noted in reply that article 48 did not address the question of excusable delay in making presentment for acceptance because article 47 required presentment within a fixed period of time rather than within a reasonable period of time, as was the case in some legal systems. The issue raised by excusable delay was resolved through article 48(b), under which presentment was completely dispensed with if it could not with reasonable diligence be made within the prescribed time-limits. It was also observed that the system reflected in articles 47 and 48 worked with fairness in most instances. For example, when a bill was drawn payable on demand or at a fixed period after sight, article 47(e) provided that it must be presented for acceptance within one year of its date. Thus the holder had sufficient time for presentment, and if presentment was prevented by excusing circumstances during the whole year, it was fair for the holder to be permitted to dispense with presentment for acceptance and to proceed against the parties to the instrument. It was observed, on the other hand, that the system might not work fairly in other instances. For example, if a bill provided on its face that it was to be presented within 30 days after the date of the instrument and presentment was prevented by excusing circumstances during the 30 days but became possible on the thirty-second day, it was unfair that the holder should be entitled immediately after the lapse of the 30 days to proceed against the parties to the instrument on the basis of constructive dishonour by non-acceptance.

191. In regard to article 48(b), it was proposed that the words "with reasonable diligence" be replaced by the words "because of circumstances which are beyond the control of the holder and which he could neither avoid nor overcome". In support of that proposal, it was noted that the former words had a subjective meaning while the latter words had an objective meaning; the latter words were therefore preferable. The retention of the words "with reasonable diligence" was supported for the reason

that they had a well-understood meaning. In addition, it was noted that a failure to present an instrument for acceptance might occur in two somewhat different situations: first, where circumstances of *force majeure* prevented presentment, and second, when the drawee could not be traced. The words "because of circumstances which are beyond the control of the holder and which he could neither avoid nor overcome" did not readily apply to the latter situation, but the words "with reasonable diligence" did so apply.

192. The following proposal was made with a view to resolving the difficulties noted above in regard to article 48:

(a) To add the following new paragraph to article 48:

"(1) Delay in making a necessary presentment for acceptance within the time-limit stated within the bill is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of the delay ceases to operate, presentment must be made with reasonable diligence."

(b) To transform subparagraph (a) of article 48 into paragraph (2);

(c) To replace subparagraph (b) of article 48 by the following new paragraph (3):

"(3) When a necessary presentment for acceptance cannot be effected within the time-limit prescribed in article 47(e) due to circumstances which are beyond the control of the holder and which he could neither avoid nor overcome, the necessary presentment for acceptance is dispensed with."

193. After deliberation, the Commission adopted the proposal, with the modification that reference should be made in the proposed new paragraph (3) to both article 47(d) and 47(e).

#### *Articles 68(3) and 73(2)*

194. The Commission considered the consequences of payment by a drawee who had accepted a bill (article 68(3)), as contrasted with the consequences of payment by a drawee who had not accepted a bill (article 73(2)). It was noted that in the former case, the drawee, as acceptor, who paid a holder who was not a protected holder, would be discharged of liability only if he did not know at the time of payment that a third person had asserted a valid claim to the instrument or that the holder had acquired the instrument by theft, forged the signature of the payee or an endorsee, or had participated in such theft or forgery (article 68(3)). Thus, other parties were discharged by virtue of article 73(1) only if the acceptor was without such knowledge. When the drawee had not accepted the bill, however, it appeared that payment by him, irrespective of such knowledge, discharged all parties (article 73(2)). It was suggested that this inconsistency was not justifiable and that, therefore, article 73(2) should be amended by adding wording along the following lines: "except where

the drawee pays a holder who is not a protected holder and knows at the time of payment that a third person has asserted a valid claim to the instrument or that the holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery".

195. The proposal was opposed on the ground that articles 68(3) and 73 were directed to different issues. Article 68(3) was directed to the issue of when a party was discharged by payment. Article 73(1), however, was directed to the relationship between the discharge of a party and the discharge of other parties who had rights of recourse against the discharged party. Article 73(2) in turn dealt with the relationship between payment by the drawee and the discharge of all parties.

196. The Commission, after deliberation, decided to adopt the proposal.

#### *Article 68(4)(a bis)*

197. The question was raised how a person other than the drawee, acceptor or maker who paid an instalment under an instrument payable by instalments at successive dates could exercise a right of recourse against prior parties. It was noted that under article 69(4), a party making a partial payment was entitled to receive from the holder a certified copy of the instrument and any authenticated protest (article 69(4)(b)) and could exercise his right of recourse by relying on that certified copy. It was agreed that a provision on the lines of article 69(4)(b) should be included in article 68.

#### *Articles 44, 68, 69 and 73*

198. It was stated that the draft Convention did not contain satisfactory rules covering the following situations or issues: discharge in case of payment by guarantor of the liability of the party for whom he became guarantor, the protection of a party paying an instrument payable by instalments at successive dates, and the effect of partial payment by the guarantor of the drawee. To cure these deficiencies, the following proposals were made:

#### *Article 44*

The present text of article 44 should be transformed into paragraph (2) and the following text should precede it as new paragraph (1):

"(1) Payment of an instrument by the guarantor in accordance with article 68 discharges the party for whom he became guarantor of his liability on the instrument to the extent of the amount paid."

#### *Article 68*

Add in paragraph (4) the following subparagraph (*a ter*):

"(*a ter*) If an instrument payable by instalments at successive dates is dishonoured by [non-acceptance or] non-payment as to any of its instalments and a

party, upon the dishonour, pays the instalment, the holder who receives the payment must give the party a certified copy of the instrument and any necessary authenticated protest in order to enable such party to exercise a right on the instrument."

#### Article 69

Amend paragraph (3)(a) to read as follows:

"(3) If the holder takes partial payment from the drawee, the guarantor of the drawee, or the acceptor or the maker:

"(a) The guarantor of the drawee, or the acceptor or the maker is discharged of his liability on the instrument to the extent of the amount paid; and"

Amend paragraph (4)(b) to read as follows:

"(4) If the holder takes partial payment from a party to the instrument other than the acceptor or the maker or the guarantor of the drawee:

(a) ...

(b) The holder must give such party a certified copy of the instrument and any necessary authenticated protest in order to enable such party to exercise a right on the instrument."

#### Article 73(1)

Replace in paragraph (1) the words "a right of recourse" by the words "a right on the instrument".

199. As regards the suggested modification of article 44, it was understood that payment by the guarantor would not discharge the party for whom he became guarantor of his liability on the instrument as against the guarantor himself.

200. As regards the proposed new subparagraph (*a ter*) of article 68(4), it was agreed to retain the words placed between square brackets (i.e. "non-acceptance or"), although dishonour by non-acceptance of an instrument payable by instalments at successive dates was probably rare in practice.

201. As regards the proposed changes in article 69(3) and (4), it was agreed that partial payment by the guarantor of the drawee should be covered by paragraph (3) since the liability of such guarantor was a primary liability in that he in fact guaranteed payment. The insertion of the word "necessary" in paragraph (4)(b) was justified by the fact that the party paying did not need any authenticated protest in all circumstances, for example where protest was dispensed with.

202. The proposed replacement in articles 69(4)(b) and 73(1) of the words "a right of recourse" by the words "a right on the instrument" was justified on the ground that it would enlarge the scope beyond the rights of recourse as covered by articles 55 to 64 so as to include rights against primary obligors and the rights of a guarantor against the party for whom he became liable.

203. The Commission, after deliberation, adopted the proposals, subject to drafting amendments.

#### Article 71

204. It was noted that article 71(1) provided that an instrument must be paid in the currency in which the amount of the instrument is expressed. If the currency in which an instrument was payable were not the currency of the country of the payee and if payment was demanded in currency notes, the person who had to make payment might find it impossible to make payment because he did not, at the time payment was demanded, possess sufficient foreign currency notes to pay the amount due. In that event, a dishonour of the instrument by non-payment would occur. Thus, the article in its present form gave an opportunity to a holder who wished to contrive a dishonour to do so by demanding payment in foreign currency notes without prior notice. This problem might be solved by including in article 71 a provision obligating the holder to give, prior to the demand for payment, notice to the party from whom payment would be demanded that he required payment in foreign currency notes.

205. The prevailing view, however, was that the difficulty sought to be addressed did not arise in practice, since holders of instruments did not usually wish to obtain currency notes when the amount of the sum payable was considerable. If it were decided that a provision should be included in article 71 under which a holder who required payment in foreign currency notes was obligated to give notice of this requirement to the party from whom payment was demanded, such a provision would have to address the following issues: the period of advance notice; whether notice had to be given even in cases where payment was demanded in the exercise of a right of recourse; and the effect of a failure to give notice. The Commission, after deliberation, decided not to include in the draft Convention a provision requiring advance notice.

#### Article 72(1)

206. It was noted that article 72(1) was intended to avert any derogation by the draft Convention of the right of a contracting State to enforce exchange control regulations applicable in its territory. However, some States had enacted provisions for the protection of their currencies that could not be regarded as exchange control regulations, and it was desirable that the draft Convention should not derogate from those regulations as well. To achieve this objective, it was proposed that the words "and provisions relating to the protection of its currency" be added after the words "exchange control regulations". After deliberation, the Commission adopted that proposal.

207. A proposal was made that the words "or may take into consideration" be added after the words "bound to apply". In support of that proposal it was noted that under certain conventions relating to the conflict of laws a contracting State may take into consideration certain legal regulations and, in particular, the mandatory regula-

tions of another State, while not being bound to apply them. While there was some support for this proposal, the prevailing view was that the addition of the proposed words would create uncertainty as to the meaning of article 72(1). That article was directed to enabling the enforcement of mandatory regulations applicable in the territory of a contracting State, and the article was not the appropriate place to seek to deal with mandatory regulations applicable outside the territory of a contracting State. After deliberation, the Commission did not accept the proposal.

*Article 80(1)(c)*

208. It was noted that this article provided that, against the acceptor of a bill payable on demand, a right of action arising on an instrument may no longer be exercised after four years had elapsed from the date on which it was accepted. The provision would not be workable, however, if the acceptor had not indicated the date of his acceptance or if, failing such indication by the acceptor, the drawer or the holder had not inserted the date of acceptance (article 38(3)). It was therefore proposed to add the words "or, in case no such date is shown, the date of the instrument" at the end of article 80(1)(c). After deliberation, the Commission adopted that proposal.

4. *Certain drafting proposals not considered by the Commission*

209. The Commission did not have time at the current session to consider the following recommendations of the drafting group as to the formulation of substantive decisions of the Commission with respect to articles 38(1), 40(1), 41, 48, 66, 72(1), 73(2) and 80(1)(c):

*Article 38(1)* (see para. 188 above):

*Add* as a second sentence the following:

"In such case, article 11 shall apply accordingly to completion by the drawer or another person."

*Article 40(1)* (see paras. 182–183 above):

*For* "any subsequent party" *read* "any subsequent endorser or such endorser's guarantor"

*Article 41* (see para. 62 above):

*Before* article 41 *insert* the following heading:

"F. *The transferor by endorsement or by mere delivery*"

*Amend* paragraph (1) *to read* as follows:

"(1) Unless otherwise agreed, a person who transfers an instrument, by endorsement and delivery or by mere delivery, represents ..."

*Amend* the end of paragraph (3) *to read* as follows:

"plus interest calculated in accordance with article 66, against return of the instrument."

*Article 48* (see paras. 189–193 above):

*Amend* the text of the article *to read* as follows:

"(1) Delay in making a necessary presentment for acceptance within the time-limit stated within the bill is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of the delay ceases to operate, presentment must be made with reasonable diligence.

"(2) A necessary or optional presentment for acceptance is dispensed with if the drawee is dead or has no longer the power freely to deal with his assets by reason of his insolvency, or is a fictitious person or a person not having capacity to incur liability on the instrument as an acceptor, or if the drawee is a corporation, partnership, association or other legal entity which has ceased to exist.

"(3) When a necessary presentment for acceptance cannot be effected within the time-limit prescribed in subparagraph (d) or (e) of article 47 due to circumstances which are beyond the control of the holder and which he could neither avoid nor overcome, the necessary presentment for acceptance is dispensed with."

*Article 66* (see paras. 160–173 above):

*Replace* paragraphs (2) and (3) with the following paragraphs (2), (2 *bis*) and (3):

"(2) The rate of interest shall be the rate that would be recoverable in legal proceedings taken in the jurisdiction where the instrument is payable.

"(2 *bis*) Nothing in paragraph (2) prevents a court from awarding damages or compensation for additional loss caused to the holder by reason of delay in payment.

"(3) The discount shall be at the official rate (discount rate) or other similar appropriate rate effective on the date when recourse is exercised at the place where the holder has his principal place of business, or if he does not have a place of business his habitual residence, or, if there is no such rate, then at such rate as is reasonable in the circumstances."

*Article 72(1)* (see para. 206 above):

*After* "in its territory" *insert* "and its provisions relating to the protection of its currency"

*Article 73(2)* (see paras. 194–196 above):

*Amend* the end of the sentence *to read* as follows:

"the same extent, except where the drawee pays a holder who is not a protected holder and knows at the time of payment that a third person has asserted a valid claim to the instrument or that the holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery."

Article 80(1)(c) (see para. 208 above):

Amend the end of the text to read as follows:

"it was accepted, or, if no such date is shown, from the date of the instrument;"

210. The Commission decided to incorporate the above drafting proposals into the text of the draft Convention to be circulated to Governments and international organizations for their comments and to indicate that those proposals had not been reviewed by the Commission.

211. The text of the draft Convention as revised by the Commission at the current session is set forth in annex I to this report.

#### 5. Procedure for adopting the draft Convention as a convention

##### (a) Choice of procedure to be followed

212. The Commission considered the various procedures that might be followed for the adoption of the draft Convention.

213. The Secretary of the Commission indicated that informal consultations held between delegates had shown that there was support for each of three possible procedures. The first possible procedure was that the Commission recommend to the General Assembly that the Assembly convene a diplomatic conference to adopt as a convention the draft Convention as finalized at the current session of the Commission. The second possible procedure was that the draft Convention as finalized at the current session of the Commission be reviewed by the Working Group on International Negotiable Instruments prior to the twentieth session of the Commission and be thereafter considered and approved by the Commission at its twentieth session. The Commission would then recommend to the Assembly that the draft Convention be adopted by the Assembly without a review of the substance of the text. The third possible procedure was that the draft Convention as finalized at the current session of the Commission be considered and approved by the Commission at its twentieth session without any intervening review by the Working Group, but with the necessary preparatory work, including the establishment of draft final clauses, being done by the secretariat. The Commission would then recommend to the General Assembly that the draft Convention be adopted by the Assembly without a review of the substance of the text. Support and opposition was expressed for each of these procedures.

214. There was support for the view that the Commission should recommend the convening of a diplomatic conference to finalize the work engaged in by the Commission during more than 10 years. It was noted that the convening of a diplomatic conference was the normal procedure for the adoption of a universal convention on private law matters. It was also noted that the higher cost of a diplomatic conference would be offset by better

methods and conditions of work. The conference, which might be for a duration of three or four weeks, would give all States an opportunity to participate in a very detailed review of the draft Convention. A text that emerged after such a discussion was likely to command wide acceptance. A recommendation for the convening of a diplomatic conference was opposed on the ground that the holding of a conference was the most expensive method proposed and that such an expenditure could not be justified in the light of the current financial difficulties facing the Organization. The view was also expressed that the holding of a diplomatic conference might not be the best procedure for adopting as a convention a text of the extreme technical complexity of this draft Convention. There was no certainty that such a text would be improved by the deliberations at a diplomatic conference. It was also observed that a recommendation for the convening of a diplomatic conference would only be made if the Commission was satisfied that the draft Convention had been reviewed and perfected by the Commission so far as it lay within the powers of the Commission. The deliberations in the Commission had revealed, however, that certain States were of the view that the draft Convention might still have inconsistencies and *lacunae*. A diplomatic conference, providing a forum for international negotiation with wide participation, was required when a convention had to establish a balance between parties with opposed economic or political interests, but no such opposition of interests was involved in the draft Convention. In reply to the argument that the holding of a diplomatic conference was expensive, it was observed that the proper body to decide whether the expenditure of the sum required was justified or not was the General Assembly; the Commission was not competent to decide on that question.

215. There was wide agreement that if the holding of a diplomatic conference was to be dispensed with as envisaged in the second and third possible procedures noted in paragraph 213 above, those procedures should ensure, to the extent possible, that the draft Convention would receive the same careful examination by all States that it would receive if a diplomatic conference were convened.

216. There was general agreement that whether the second or third possible procedure were to be adopted, a necessary element in both procedures would be the transmission of the text as finalized at the current session to all States for their comments. That would enable States that had not participated in the seventeenth and the current sessions of the Commission to express their views on the draft Convention. The receipt of comments from all States and their consideration by the Commission would enable the Commission to state to the General Assembly that in finalizing the draft Convention account had been taken of the views of all States. It was noted that such transmission could be effected on the authority of a decision of the Commission, although under another view such transmission should more appropriately be made after the consideration of the present report by the Assembly.

217. It was observed that the significant difference between the second and third possible procedures noted in paragraph 213 lay in the fact that, under the second possibility, the draft Convention as finalized at the present session would be reviewed by the Working Group prior to the twentieth session of the Commission; the third possibility did not provide for such a review. A review by the Working Group was supported on the ground that a review might considerably lessen the burden on the Commission at its twentieth session in finalizing and approving the draft Convention. It was noted that the work of the Working Group at its thirteenth and fourteenth sessions had considerably facilitated the work of the Commission at its present session. Furthermore, the Working Group could consider the comments received from Governments after the draft Convention had been transmitted to them and make recommendations to the Commission as to how any concerns expressed in those comments might be satisfied.

218. Views were expressed opposing a review by the Working Group. It was observed that developing countries experienced difficulties in financing the attendance of their delegates at sessions of working groups. It was also observed that because of the time constraints involved in the transmission of the draft Convention to States and the receipt and analysis of the comments sent in response to the transmission, it might not be possible to place those comments before the Working Group at a session scheduled to be held early in 1987. The usefulness of a Working Group session would be greatly reduced if the comments of Governments could not be placed before the Working Group for examination. It was also observed that a two-week session of the Working Group, combined with two weeks of the Commission's twentieth session at which the final text of the draft Convention would be approved, would result in additional expense, thereby reducing the financial advantages to be gained from following that procedure rather than recommending the convening of a diplomatic conference.

219. It was generally agreed that whether the second or the third possible procedure referred to in paragraph 213 were to be adopted, the draft Convention should be discussed at the twentieth session of the Commission article by article. Such discussion would provide a substitute for the article-by-article discussion that would take place at a diplomatic conference. The view was expressed that in order to limit the deliberations within the Commission to a reasonable time period, it might be desirable that, except in exceptional cases, decisions taken by the Commission at earlier sessions should not be reopened at the twentieth session.

220. At the conclusion of the deliberations on the three possible procedures referred to in paragraph 213, there appeared to be approximately equal support for each of the three possible procedures, with slightly greater support for the adoption of the second procedure. Accordingly, the second procedure was adopted.

(b) *Implementation of that procedure*

221. The view was expressed that some States members of the Commission might not send delegates to participate in a session of the Working Group as observers. However, if those States were members of the Working Group, they might send delegates to the session of the Working Group. Participation would thereby be enlarged. Accordingly, the Commission decided that the Working Group should be expanded to include all States members of the Commission. The invitation to all States not members of the Commission to participate as observers should indicate the desirability of their attendance if they wished to participate in the preparation of the final text of the draft Convention. That would encourage all States who wished to participate in the session to do so and would result in wide participation in the discussion of the draft Convention. The invitation to participate as observers in the twentieth session of the Commission should be similarly worded.

222. The Commission considered the mandate to be given to the Working Group. It was agreed that the Working Group should consider the comments received from Governments on the draft Convention and should make recommendations to the Commission as to how any concerns expressed in those comments might be satisfied. The Working Group should also examine the draft Convention with a view to discovering any inconsistencies among its provisions or any *lacunae*. The Working Group should also be at liberty to suggest improvements to the draft Convention.

223. The Commission requested the secretariat to transmit the draft Convention as finalized at the current session to all States as soon as possible after the conclusion of the session, with a request that comments on the draft Convention be submitted to the secretariat by 15 November 1986, since the Working Group would be scheduled to meet early in January 1987. To the extent that time constraints permitted the preparation of the necessary documentation and translation, the comments received should be submitted to the Working Group in the official languages of the Commission. The secretariat was also requested to submit to the Working Group draft final clauses to be included in the draft Convention. One of those clauses might reflect the results of consultations between States that were parties to the 1930 Geneva Convention providing a Uniform Law for Bills of Exchange and Promissory Notes and the 1930 Geneva Convention for the Settlement of Certain Conflicts of Laws in connection with Bills of Exchange and Promissory Notes as to the procedures to be followed by those States in becoming parties to the draft Convention under discussion. Such consultations, which had been informally commenced on the occasion of the current session of the Commission, were aimed at discussing and overcoming the possible conflict between the two 1930 Geneva Conventions and the draft Convention under discussion.

224. The Commission further decided that a period of two weeks should be allotted at its twentieth session for a discussion article by article of the draft Convention,



taking into account the report of the Working Group on the work of its fifteenth session and the comments submitted by Governments. It was expected that the draft Convention, as finalized at the twentieth session, would be transmitted to the General Assembly with the recommendation that it be adopted as a convention by the Assembly without amendment of the substance of the text. A view was expressed that the recommendations to be made for the adoption of the draft Convention by a diplomatic conference or the Assembly might be decided at the twentieth session, after having ascertained in particular whether the Assembly would be prepared to adopt the Convention without amending the substance of the draft text.

## B. *Electronic funds transfers*<sup>6</sup>

### *Introduction*

225. The Commission, at its fifteenth session in 1982, had before it a report of the Secretary-General that considered several legal problems arising out of electronic funds transfers (A/CN.9/221). In the light of those problems, the report suggested that, as a first step, the Commission should prepare a legal guide on the problems arising out of electronic funds transfers. The guide, it was suggested, should be oriented towards providing guidance for legislators or lawyers preparing the rules governing particular systems for such transfers.

226. The Commission accepted that recommendation and requested the secretariat to begin the preparation of a legal guide on electronic funds transfers in co-operation with the UNCITRAL Study Group on International Payments.<sup>7</sup> Several chapters of the draft legal guide were submitted to the Commission at its seventeenth session in 1984 (A/CN.9/250 and Add.1-4) and the remaining draft chapters were submitted to the Commission at its eighteenth session in 1985 (A/CN.9/266 and Add.1 and 2).

227. At its eighteenth session in 1985, the Commission requested the Secretary-General to send the draft legal guide on electronic funds transfers to Governments and interested international organizations for comment.<sup>8</sup> It also requested the secretariat, in co-operation with the UNCITRAL Study Group on International Payments, to revise the draft in the light of the comments received for submission to the Commission at its nineteenth session for consideration and possible adoption.

228. At the current session, the Commission had before it a report of the Secretary-General concerning the legal

guide and possible future work by the Commission in the area of electronic funds transfers (A/CN.9/278). The report contained a brief summary of the replies received from Governments and international intergovernmental and non-governmental organizations and, in an annex, proposed various modifications to the legal guide in the light of those replies. The report recommended that the Commission consider adopting the legal guide and requesting that it be published in an appropriate manner. In addition, the report concluded that to the extent that the use of electronics had led to changes in banking procedures, new legal rules in the area of electronic funds transfers were needed. It discussed possible approaches and procedures for formulating model legal rules in that area.

### *Discussion at the session*

229. The Commission welcomed the completion of the Legal Guide on Electronic Funds Transfers. It was suggested that in setting forth the various practices worldwide with respect to electronic funds transfers and in pointing out the legal issues arising from those practices, the Legal Guide would itself promote the international harmonization of practices and legal rules with respect to such funds transfers. It was generally agreed that the Legal Guide should be published in such a way as to achieve a wide distribution to interested circles. A view was expressed that the widest distribution could be achieved if the Legal Guide were adopted by the Commission and published as a United Nations publication. The prevailing view, however, was that it would be inappropriate for the Commission to adopt the Legal Guide as a product of the work of the Commission itself without having engaged in substantive discussions on it. Accordingly, the Commission authorized the secretariat to publish the Legal Guide as a product of the work of the secretariat, in all official languages of the United Nations.

230. With respect to possible future work by the Commission in the area of electronic funds transfers, a view was expressed that the Legal Guide was, for the present, sufficient for the promotion of harmonization and unification of national practices and laws in this area and that the formulation of model legal rules need not now be attempted. The prevailing view, however, was that by addressing the relevant issues and suggesting possible solutions at an early stage, such model rules could influence the development of and help prevent disparities in those practices and laws. Therefore, the Commission decided to undertake work on the formulation of model legal rules on electronic funds transfers and to entrust this work to the Working Group on International Negotiable Instruments, which might be renamed for this purpose the Working Group on International Payments. The priority to be given to the work would depend on the other decisions on future work to be adopted at the current session. The Commission agreed that the Working Group should begin its work by considering the legal issues set forth in the last chapter of the Legal Guide as well as any other issues the secretariat might consider appropriate to place before the Working Group.

<sup>6</sup>The Commission considered this subject at its 352nd meeting, on 7 July 1986.

<sup>7</sup>Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17 (A/37/17)*, para. 73.

<sup>8</sup>Report of the United Nations Commission on International Trade Law on the work of its eighteenth session, *Official Records of the General Assembly, Fortieth Session, Supplement No. 17 (A/40/17)*, para. 342.

231. The Commission also agreed that the rules should be flexible and should be drafted in such a way that they did not depend upon specific technology. Where appropriate, the rules should present alternative solutions in order to take into account differences in banking systems. A view was also expressed that the model rules should deal with the relationship between banks as well as the relationship between banks and their customers.

### Chapter III. New international economic order<sup>9</sup>

#### A. Industrial contracts

##### *Introduction*

232. The Commission had before it the report of its Working Group on the New International Economic Order on the work of its eighth session (A/CN.9/276). The report set forth the deliberations of the Working Group on the basis of the introduction to the legal guide on drawing up international contracts for the construction of industrial works and draft chapters of the guide, which had been prepared by the secretariat (A/CN.9/WG.V/WP.17 and Add.1-9). It was noted that at its ninth session the Working Group would complete its examination of the draft chapters of the guide and thereby discharge the mandate entrusted to it by the Commission. The draft chapters would then be placed before the Commission for adoption at its twentieth session.

##### *Discussion at the session*

233. The Commission expressed its appreciation to the Working Group for the progress made in the preparation of the guide. It was noted that due to the anticipated length of the guide, it would not be possible for the Commission at its twentieth session to review the guide in detail to ensure consistency throughout the guide with respect, for example, to the analysis contained in the various chapters and the terminology used. In that regard, it was noted that the secretariat was engaged at present in revising all the draft chapters of the guide and that it was paying close attention to the matter of consistency within the guide. It was also noted that the secretariat would distribute the draft chapters as early as possible in order to allow delegations and observers sufficient time to review the guide for consistency as well as substance prior to the ninth session of the Working Group.

234. The Commission took note of the report of the Working Group on the work of its eighth session and welcomed the intention of the Working Group to submit the legal guide to the Commission at its twentieth session for its consideration.

#### B. Future work in the area of the new international economic order

##### *Introduction*

235. In view of the fact that the work of the Commission on the legal guide on drawing up contracts for the construction of industrial works was approaching its conclusion, the Commission considered possible subjects in the area of the new international economic order on which work might be undertaken in the future. The Commission had before it a note by the secretariat entitled "Future work in the area of the new international economic order" (A/CN.9/277). The note considered four possible subjects on which work might be undertaken: contracts for industrial co-operation; joint ventures; countertrade; and procurement.

236. With regard to contracts for industrial co-operation, the note suggested that work be deferred until the need for it was more clearly established. With regard to joint ventures, the note suggested that where an enterprise from a developing country had combined with an enterprise from a developed country in a joint venture whose objects included the construction of industrial works, the legal guide on drawing up contracts for the construction of industrial works would provide sufficient assistance to the enterprise from the developing country. With regard to the legal aspects of joint ventures in general, the note suggested that very different forms of joint venture agreements might be entered into and that, accordingly, it was difficult to envisage work that the Commission might usefully undertake in that area.

237. It was noted that countertrade currently formed an increased part of the trade of many developing countries, and the note suggested that work might be undertaken to ascertain and resolve legal difficulties that might be experienced by developing countries in that area. The note also suggested that procurement was an area of great importance to developing countries and that a study of major issues arising in procurement might be beneficial.

##### *Discussion at the session*

238. There was support for commencing work in the areas of procurement, countertrade and joint ventures. There was little support for work in the area of contracts for industrial co-operation.

239. A view was expressed that it would be useful to request the secretariat to prepare information relating to all the issues in the long-term programme of work of the Commission in the field of the new international economic order adopted in 1981 and that the decision on the future work of the Commission in that field should be taken only after that information had been considered.

240. There was very wide support for the view that work on procurement should be given priority. That subject was of great importance for the economic development of developing countries. Furthermore, depending on the results of preliminary studies on the major issues in

<sup>9</sup>The Commission considered this subject at its 354th meeting, on 8 July 1986.

procurement, it might be possible to prepare model regulations on procurement in the context of international trade. Work on procurement would therefore yield a concrete end-product. It was also noted that procurement was a subject of interest both to developed and developing countries, and work in that area would give developed countries an opportunity to present their experience in the area, which might be of value to developing countries. Moreover, as procurement was a procedure antecedent to and closely linked with the drawing up of contracts for industrial works, work on procurement would be a natural sequel to the work on the legal guide on drawing up contracts for industrial works. The Working Group on the New International Economic Order already had a certain degree of expertise in regard to procurement, and it might be anticipated that work on procurement would proceed expeditiously.

241. There was considerable support for undertaking work in the areas of countertrade and joint ventures. The view was expressed that countertrade had become of increased importance to developing countries, in particular because of shortages of convertible currency to finance international trade. Under another view, however, countertrade was not of great significance to some developing countries. It was also suggested that the Economic Commission for Europe (ECE) had under consideration a proposal to prepare a guide to compensation transactions, and it was suggested that work by the Commission might be deferred until it was ascertained whether ECE would undertake the preparation of that guide. If the preparation of a guide were to be undertaken by ECE, then the need for work by the Commission might be assessed after the guide had been prepared.

242. The view was expressed that the creation of joint ventures between enterprises of developed and developing countries was an important instrument for increasing investment in developing countries and that the creation of such joint ventures was encouraged by many developing countries. The subject of joint ventures was therefore of importance to developing countries, and preliminary studies might accordingly be undertaken with a view to identifying legal issues on which the Commission might work. Under another view, however, joint ventures were of such different types that it was difficult to visualize work which would lead to a useful end-product.

#### *Decision of the Commission*

243. The Commission noted that the secretariat did not have the resources to undertake work simultaneously on procurement, countertrade and joint ventures, and that the Working Group on the New International Economic Order could not commence work on more than one subject. Accordingly, it was decided that priority be given to work on procurement. It was also decided that the subjects of countertrade and joint ventures should be placed on the Commission's work programme and that preliminary studies prepared by the secretariat on those subjects should be placed before the Commission at a future session. In the light of the preliminary studies, the Commission could decide on priority between those subjects.

### **Chapter IV. Liability of operators of transport terminals<sup>10</sup>**

244. The Commission, at its sixteenth session in 1983, decided to include the topic of liability of operators of transport terminals in its programme of work and to assign work on the preparation of uniform rules on that subject to a working group.<sup>11</sup> At its seventeenth session in 1984, the Commission decided to assign that work to its Working Group on International Contract Practices.<sup>12</sup>

245. The Commission had before it the report of the Working Group on International Contract Practices on the work of its ninth session (A/CN.9/275). The report set forth the deliberations and decisions of the Working Group with respect to the draft articles of uniform rules on the liability of operators of transport terminals, which had been prepared by the secretariat. The Commission took note with appreciation of the report of the Working Group.

### **Chapter V. Co-ordination of work<sup>13</sup>**

#### **A. General co-ordination of work**

##### *Introduction*

246. The Secretary of the Commission reported on the co-ordination of work accomplished in the field of international trade law during the preceding year. He noted that this co-ordination was one of the principal tasks entrusted to the Commission and that the General Assembly, in its resolution 40/71 of 11 December 1985, had reaffirmed the mandate of the Commission in this field.

247. The reputation of the Commission both as the core legal body in the field of international trade law and as the principal organ for co-ordination of activities was now well established. Consultations with a view to co-ordination continued on a regular basis with organizations such as the Asian-African Legal Consultative Committee (AALCC), the Hague Conference on Private International Law, the Organization of American States, the International Chamber of Commerce and the International Institute for the Unification of Private Law (UNIDROIT), which had well-established relationships with the Commission for co-ordination of work. Consultative relationships had also been strengthened with bodies within the United Nations system such as the United Nations Industrial Development Organization (UNIDO), the United Nations Conference on Trade and Development (UNCTAD) and the World Bank.

<sup>10</sup>The Commission considered this subject at its 356th meeting, on 9 July 1986.

<sup>11</sup>Report of the United Nations Commission on International Trade Law on the work of its sixteenth session, *Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17 (A/38/17)*, para. 115.

<sup>12</sup>Report of the United Nations Commission on International Trade Law on the work of its seventeenth session, *Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 17 (A/39/17)*, para. 113.

<sup>13</sup>The Commission considered this subject at its 356th meeting, on 9 July 1986.

*Discussion at the session*

248. The Secretary-General of AALCC made a detailed statement in which he described the long history of co-operation existing between the Committee and the Commission. He recalled the collaboration that had taken place between the two bodies in the course of the work on the major projects undertaken by the Commission: the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg); the UNCITRAL Arbitration Rules; the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980); and the UNCITRAL Model Law on International Commercial Arbitration. He recalled in particular the close co-operation in the development of the UNCITRAL Arbitration Rules, which had resulted in those rules being adopted as the rules of the Regional Centres for Arbitration established under the auspices of the AALCC at Kuala Lumpur and Cairo. The collaboration had existed not merely at an inter-institutional level, but had been very close and harmonious at the inter-secretariat level. He expressed the expectation that that collaboration would continue in the future.

249. The Deputy Secretary-General of the Hague Conference on Private International Law also made a statement on the collaboration existing between his organization and the Commission. He mentioned in particular the recent collaboration during the elaboration of the 1985 Hague Convention on the Law Applicable to the International Sale of Goods. The Hague Conference had invited all States members of UNCITRAL to participate in the Special Commission that had prepared the text submitted to the Diplomatic Conference. All States had been invited to participate in the Diplomatic Conference that adopted that Convention. In addition, the Secretary-General of the Hague Conference had transmitted to the Secretary-General of the United Nations the request of the Diplomatic Conference that the United Nations undertake a translation of that Convention into Arabic, Chinese, Russian and Spanish, which were not working languages of the Hague Conference. The Secretary-General of the United Nations had acceded to that request. Those translations, though not constituting authentic versions of the text of the Convention, would be extremely useful in securing wider acceptance of the Convention. He stated that his organization greatly appreciated that expression of the co-operation that currently existed with the Commission and the United Nations in general.

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

250. The Commission had before it a comprehensive report on the subject of the current activities of international organizations related to the harmonization and unification of international trade law (A/CN.9/281). That report updated the information contained in an earlier report on the same subject submitted to the Commission

at its sixteenth session (A/CN.9/237 and Add.1-3). The current report dealt with the activities under the following headings: international commercial contracts in general; commodities; industrialization; transnational corporations; transfer of technology; industrial and intellectual property law; international payments; international transport; international arbitration; products liability; European Economic Community (EEC); private international law; other topics of international trade law; and facilitation of international trade.

251. The Secretary of the Commission noted that a report of this nature was usually submitted to the Commission at periodic intervals and had been regarded as serving a very useful purpose.

252. Views were expressed supporting the publication of a report of that nature. It was noted that the report mentioned the preparation of model laws by several organizations, and it was observed that it would be useful if future reports were to indicate the extent to which this form of unification was successful through the adoption of the model laws.

253. The Commission took note of the report with appreciation.

**C. Current activities of other organizations in the field of international commercial arbitration**

*Introduction*

254. The Commission had before it a report of the Secretary-General that set forth the activities of other international organizations on certain aspects of international commercial arbitration (A/CN.9/280). The report covered activities of the Hague Conference on Private International Law, the International Bar Association, the International Chamber of Commerce and the International Council for Commercial Arbitration. The aspects of arbitration dealt with in the report were multi-party arbitration, taking of evidence in arbitral proceedings, international court assistance in taking of evidence in arbitral proceedings, the law applicable to arbitration agreements, adaptation or supplementation of contracts by third persons, and a code of ethics for arbitrators in international commercial arbitration.

255. The purpose of the report was to provide information on the activities of other organizations and to invite consideration by the Commission of whether any of the issues warranted closer examination from the point of view of co-ordination of work and possible future work by the Commission itself. If such further examination were decided upon, the secretariat could prepare an in-depth study on the issue or issues selected by the Commission, which would include consideration of the desirability and feasibility of possible future efforts in co-operation with the international organizations concerned.

*Discussion at the session*

256. It was agreed that the Commission, which had made major contributions in the field of international commercial arbitration, should continue to play a role in that rapidly developing field of law. It was suggested, in that connection, that the secretariat continue to monitor developments and to submit from time to time reports of the kind contained in document A/CN.9/280.

257. As regards the choice of issues for closer examination, the Commission agreed that in-depth studies should be prepared by the secretariat on multi-party arbitration and on the taking of evidence in arbitral proceedings. It was stated in support that both issues were of considerable practical importance and that a closer examination was likely to show the desirability and feasibility of preparing rules, whether or not linked to the UNCITRAL Arbitration Rules. While there was some support for examining more closely the issue of adaptation or supplementation of contracts by third persons, the prevailing view was that such an undertaking was not promising, or at least premature. The Commission agreed that the remaining three issues (i.e. international court assistance in taking of evidence in arbitral proceedings, the law applicable to arbitration agreements and a code of ethics for arbitrators in international commercial arbitration) were not appropriate issues for further examination or future work by the Commission.

*Decision of the Commission*

258. The Commission requested the secretariat to submit to it at a future session in-depth studies on multi-party arbitration and on the taking of evidence in arbitral proceedings. Those studies should include the complete text of any rules prepared by other organizations, detailed comments on such rules, general considerations as to the desirability and feasibility of further efforts in co-operation with other international organizations concerned and suggestions as to any possible future work by the Commission itself. The Commission also requested the secretariat to continue monitoring developments in the field of international commercial arbitration and to report thereon to the Commission at appropriate intervals.

**D. Legal aspects of automatic data processing**

259. At its eighteenth session in 1985, the Commission considered a report of the Secretary-General on the legal value of computer records (A/CN.9/265) and adopted a recommendation on that subject. At the current session, the Commission had before it a further report on the legal aspects of automatic data processing, with suggestions for future action to co-ordinate work in this field (A/CN.9/279).

260. The report was divided into two parts, the first describing the work of international organizations active in the field of automatic data processing, and the second analysing the work undertaken by reference to the subject-matter covered by the work. It was noted that while many organizations were undertaking work in that

field, each organization dealt with a special area from the point of view of its own interests and needs. While a substantial degree of co-operation already existed between the organizations concerned through the exchange of documents and by attendance as observers at meetings organized by other organizations, a further degree of co-ordination was desirable. Leadership in the effort at co-ordination might be undertaken by the Commission, and it was proposed that that might take the form of a meeting organized by the secretariat in late 1986 or early 1987 to which all interested international organizations might be invited.

261. The view was expressed that the efforts of the secretariat in co-ordinating the work in that area were to be commended. The Commission took note with appreciation of the report submitted to it and generally approved of the course of action proposed therein.

**Chapter VI. Status of conventions<sup>14</sup>**

262. The Commission considered the status of conventions that were the outcome of its work, that is, the Convention on the Limitation Period in the International Sale of Goods (New York, 1974) (hereinafter referred to as "the Limitation Convention"); the Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980); the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg) (hereinafter referred to as "the Hamburg Rules"); and the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980) (hereinafter referred to as "the United Nations Sales Convention"), as well as the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958). The Commission had before it a note by the secretariat on the status of those Conventions, which set forth the status of signatures, ratifications and accessions to them as at 12 May 1986 (A/CN.9/283).

263. The Secretary of the Commission noted that, subsequent to the issuance of that note, Zambia had become a party on 6 June 1986 to the Limitation Convention and the United Nations Sales Convention. Thus, only one more party was needed for the Limitation Convention to come into force, and two more parties were needed for the United Nations Sales Convention to come into force. Several delegations reported on progress being made within their countries towards ratification of the United Nations Sales Convention. Noting that trend, the Secretary of the Commission expressed optimism that both Conventions would receive the required number of ratifications and accessions by the time of the twentieth session of the Commission in 1987.

264. The Secretary of the Commission reported on activities of the secretariat towards promotion of the Hamburg Rules. It was co-operating in the preparation by UNCTAD of promotional materials on the Hamburg

<sup>14</sup>The Commission considered this subject at its 356th meeting, on 9 July 1986.

Rules and the United Nations Convention on International Multimodal Transport of Goods. The materials would be designed to promote greater international understanding of and interest in those two Conventions. The secretariat, assisted by a consultant, was preparing the portion of the materials dealing with the Hamburg Rules. In addition, the secretariat had engaged in discussions with the World Bank concerning means by which the World Bank might promote the Hamburg Rules during its contacts with Governments, particularly in connection with the Bank's transport-related activities. The Secretary expressed the belief that as a result of activities such as those, greater international interest in the Hamburg Rules might be expected.

### Chapter VII. Training and assistance<sup>15</sup>

265. At the eighteenth session of the Commission, in 1985,<sup>16</sup> there was general agreement that the sponsorship of symposia and seminars on international trade law should be continued and strengthened. It was noted that such symposia and seminars were of great value to young lawyers and government officials from developing countries.

266. By its resolution 40/71 of 11 December 1985 on the report of the Commission on the work of its eighteenth session, the General Assembly reaffirmed the importance, in particular for developing countries, of the work of the Commission concerned with training and assistance in the field of international trade law. It also reaffirmed the desirability for the Commission to sponsor symposia and seminars, in particular those organized on a regional basis, to promote training and assistance in the field of international trade law. The Assembly also expressed its appreciation to those Governments, regional organizations and institutions that had collaborated with the secretariat of the Commission in organizing regional seminars and symposia, and invited Governments, international organizations and institutions to assist the secretariat in financing and organizing seminars and symposia, in particular in developing countries. The Assembly also invited Governments, relevant United Nations organs, organizations, institutions and individuals to make voluntary contributions that might be utilized to enable candidates from developing countries to participate in symposia and seminars.

267. The Commission had before it a report of the Secretary-General on training and assistance (A/CN.9/282), which described the measures taken by the secretariat to implement the decisions of the Commission and of the General Assembly. The report noted, in particular, the association of the secretariat with the holding of two regional seminars. A regional seminar on international trade law and foreign trade

(22–23 April 1985, Bogota) was organized by the Chamber of Commerce of Bogota and the UNCITRAL secretariat, with the support of the Organization of American States. A regional seminar on international commercial arbitration (20–22 January 1986, Cairo) was organized by the Asian-African Legal Consultative Committee and the Cairo Centre for International Commercial Arbitration, with the co-operation of the UNCITRAL secretariat.

268. It was noted that the subject-matter of the majority of the symposia and seminars reflected the considerable interest in the work of the Commission in the field of international commercial arbitration and in particular the current interest in the UNCITRAL Model Law on International Commercial Arbitration.

269. The Commission took note with appreciation of the report.

### Chapter VIII. Relevant General Assembly resolutions and future work<sup>17</sup>

#### A. General Assembly resolutions on the work of the Commission

270. The Commission took note with appreciation of General Assembly resolution 40/71 on the report of the Commission on the work of its eighteenth session and of Assembly resolution 40/72 of 11 December 1985 on the Model Law on International Commercial Arbitration of the United Nations Commission on International Trade Law.

#### B. Date and place of the twentieth session of the Commission

271. It was decided that the Commission would hold its twentieth session for four weeks from 20 July to 14 August 1987 at Vienna. The Commission noted that by holding the session so late in the summer with a duration of four weeks, it was expected that the Commission would complete the two major items on its agenda for that session:

(a) Adoption of the final and definitive text of the draft Convention on International Bills of Exchange and International Promissory Notes for submission to the General Assembly;

(b) Adoption of the legal guide on drawing up international contracts for the construction of industrial works, which would be submitted to it by the Working Group on the New International Economic Order.

#### C. Sessions of working groups

272. It was decided that the Working Group on International Contract Practices would hold its tenth session

<sup>17</sup>The Commission considered this subject at its 356th meeting, on 9 July 1986.

<sup>15</sup>The Commission considered this subject at its 356th meeting, on 9 July 1986.

<sup>16</sup>Report of the United Nations Commission on International Trade Law on the work of its eighteenth session, *Official Records of the General Assembly, Fortieth Session, Supplement No. 17 (A/40/17)*, paras. 366 and 367.

from 1 to 12 December 1986 at Vienna. It was decided that the eleventh session of that Working Group should be held in 1987 at a date to be set by the secretariat that would enable the transmission to Governments for their comments of the text of the uniform rules on the liability of operators of transport terminals expected to be finalized at that session and the receipt of the comments in sufficient time to be placed before the Commission at its twenty-first session, in 1988.

273. It was decided that the Working Group on International Negotiable Instruments would hold its fifteenth session from 5 to 16 January 1987 at Vienna. The sixteenth session of the Working Group would be held in 1987 after the twentieth session of the Commission, at which time it would begin its consideration of the topic of electronic funds transfers.

274. It was decided that the Working Group on the New International Economic Order would hold its ninth session from 30 March to 16 April 1987 at Vienna. The Working Group had to consider all the draft chapters of the legal guide as revised by the secretariat, and the

Commission decided that a session of three weeks duration was essential if the Working Group was to complete its task and be able to submit the completed text to the Commission at its twentieth session. It was noted that that single session of three weeks would replace the normal authorization of two sessions of two weeks each.

#### ANNEX I

##### Draft Convention on International Bills of Exchange and International Promissory Notes

[Annex reproduced in part three, I, of this volume.]

#### ANNEX II

##### List of documents of the session

[Annex reproduced in part three, IV, A, of this volume.]

### B. United Nations Conference on Trade and Development (UNCTAD): extract from the report of the Trade and Development Board on its thirty-third session (TD/B/L.810/Add.9)

*“Progressive development of the law of international trade: nineteenth annual report of the United Nations Commission on International Trade Law*

*(Agenda item 8 (c))*

“20. At the 694th meeting, on 3 September 1986, the President drew attention to the nineteenth annual report of the United Nations Commission on International Trade Law (UNCITRAL) (A/41/17) circulated under cover of document TD/B/1109).

“21. The spokesman for the Group of 77 (Uruguay), noting that the UNCITRAL report described efforts undertaken on the draft convention on International Bills of Exchange and International Promissory Notes, said that his Group shared the view expressed in the report that standards in electronic funds transfers should be flexible.

“22. Referring to chapter III of the report on the New International Economic Order (paragraphs 235–243) he said that, while he understood that UNCITRAL could not examine more than one subject concurrently, he wished to reiterate the interest of his Group in the efforts

pursued in determining and solving legal difficulties facing trade compensation.

“23. He also emphasized the work done on the liability of operators of transport terminals (chapter IV), in particular the collaboration between UNCITRAL and the UNCTAD secretariat. He stressed that such joint action should continue.

“24. Finally, with regard to co-ordination of work (chapter V), he noted the current activities of international organizations related to the harmonization and unification of international trade law and in the field of international commercial arbitration, as well as the work accomplished on legal aspects of automatic data processing and the status of conventions.

*“Action by the Board*

“25. At the 698th meeting, on 8 September 1986, the Board took note of the report of the United Nations Commission on International Trade Law on its nineteenth session (A/41/17) and of the comments made thereon.”

**C. General Assembly: report of the Sixth Committee (A/41/861)**  
**[Original: Spanish]**

I. INTRODUCTION

1. On the recommendation of the General Committee, the General Assembly decided at its 3rd plenary meeting, on 20 September 1986, to include in the agenda of its forty-first session the item entitled "Report of the United Nations Commission on International Trade Law on the work of its nineteenth session" and to allocate it to the Sixth Committee.

2. In connection with this item, the Sixth Committee had before it the report in question, which was introduced by the Chairman of the United Nations Commission on International Trade Law at the 3rd meeting of the Committee, on 23 September 1986.<sup>1</sup>

3. The Sixth Committee considered the item at its 3rd to 7th meetings, from 23 to 30 September and at its 34th meeting, on 5 November 1986. The summary records of those meetings (A/C.6/41/SR.3-7 and 34) contain the views of the representatives who spoke during the consideration of the item.

<sup>1</sup>Official Records of the General Assembly, Forty-first Session, Supplement No. 17 (A/41/17). The report was submitted pursuant to a decision by the Sixth Committee at its 1096th meeting, on 13 December 1968 (see Official Records of the General Assembly, Twenty-third Session, Annexes, agenda item 88, document A/7408, para. 3).

**D. General Assembly resolution 41/77 of 3 December 1986**

**41/77. REPORT OF THE UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW**

*The General Assembly,*

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

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

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

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

<sup>1</sup>Official Records of the General Assembly, Forty-first Session, Supplement No. 17 (A/41/17).

II. CONSIDERATION OF DRAFT RESOLUTION  
A/C.6/41/L.3

4. The Committee had before it draft resolution A/C.6/41/L.3, sponsored by *Argentina, Australia, Austria, Brazil, Cyprus, Czechoslovakia, Egypt, Finland, Germany, Federal Republic of, Greece, Guyana, Hungary, India, Italy, Japan, Morocco, Netherlands, Sweden, Turkey and Yugoslavia*, later joined by *Chile, France, Kenya, Libyan Arab Jamahiriya, Philippines, Spain and Sudan*, which was introduced and orally revised by the representative of Austria at the 34th meeting, on 5 November 1986.

5. At the same meeting, the Committee adopted draft resolution A/C.6/41/L.3, as orally revised, by consensus (see para. 7).

6. Statements in explanation of position were made by the representatives of Mexico and Canada.

III. RECOMMENDATION OF THE  
SIXTH COMMITTEE

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

[Text not reproduced in this section. The draft resolution was adopted, with editorial changes, as General Assembly resolution 41/77. See section D, below.]

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

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

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

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



# I. INTERNATIONAL PAYMENTS

## A. International negotiable instruments

### 1. Report of the Working Group on International Negotiable Instruments on the work of its fourteenth session (Vienna, 9–20 December 1985) (A/CN.9/273) [Original: English]<sup>a</sup>

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## INTRODUCTION

1. The United Nations Commission on International Trade Law, at its seventeenth session (New York, 25 June - 10 July 1984), considered the draft Convention on International Bills of Exchange and International Promissory Notes as Regarding by the Working Group and contained in document A/CN.9/211. As regards its future course of action, the Commission decided that further work should be undertaken with a view to improving the draft Convention and entrusted this work to the Working Group on International Negotiable Instruments.<sup>1</sup>

2. The mandate of the Working Group was to revise the draft Convention on International Bills of Exchange and International Promissory Notes in the light of decisions and discussion at the seventeenth session of the Commission,<sup>2</sup> and also taking into account those comments of Governments and international organizations in documents A/CN.9/248 and A/CN.9/249/Add.1 which were not discussed at that session.

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its seventeenth session, *Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 17 (A/39/17)*, para. 88.

<sup>2</sup>The discussion and conclusions on major controversial and other issues are set forth in *ibid.*, paras. 21-82.

3. In the execution of the mandate entrusted to it, the Working Group held its thirteenth session at United Nations Headquarters in New York from 7 to 18 January 1985. At that session the Working Group commenced its work by considering the major controversial issues relating to the draft Convention, as set forth in document A/CN.9/249 and as discussed by the Commission at its seventeenth session, and some related questions. The deliberations of the Working Group are set forth in the report of the Working Group on the work of that session (A/CN.9/261).

4. The Working Group held its fourteenth session at Vienna from 9 to 20 December 1985. The Working Group consists, according to the decision of the Commission at its seventeenth session,<sup>3</sup> of the following 14 members of the Commission: Australia, Cuba, Czechoslovakia, Egypt, France, India, Japan, Mexico, Nigeria, Sierra Leone, Spain, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland and United States of America. With the exception of Sierra Leone, all members of the Working Group were represented at the fourteenth session. The session was also attended by observers from the following States: Argentina, Austria, Brazil, Canada, Chile, China, Ger-

<sup>3</sup>*Ibid.*, para. 88.

many, Federal Republic of, Holy See, Hungary, Indonesia, Iran (Islamic Republic of), Italy, Kuwait, Netherlands, Panama, Peru, Poland, Republic of Korea, Romania, Sweden, Switzerland, Thailand, Cameroon and Venezuela, as well as by observers from the following international organizations: Hague Conference on Private International Law, European Banking Federation, International Bar Association, International Chamber of Commerce, International Law Association and Regional Centre for International Commercial Arbitration, Cairo.

5. The Working Group elected the following officers:

*Chairman:* Mr. Willem Vis (Netherlands)<sup>a</sup>

*Rapporteur:* Mrs. G.O. Adebajo (Nigeria)

6. The Working Group had before it the following documents:

A/CN.9/WG.IV/WP.29—Provisional agenda;

A/CN.9/WG.IV/WP.30—Draft Convention on International Bills of Exchange and International Promissory Notes: Some considerations and suggestions relating to major controversial issues: note by the secretariat;

A/CN.9/211—Draft Convention on International Bills of Exchange and International Promissory Notes: Text of draft articles as adopted by the Working Group on International Negotiable Instruments: note by the secretariat;

A/CN.9/213—Commentary on draft Convention on International Bills of Exchange and International Promissory Notes: report of the Secretary-General;

A/CN.9/248—Draft Convention on International Bills of Exchange and International Promissory Notes and draft Convention on International Cheques: analytical compilation of comments by Governments and international organizations;

A/CN.9/249—Draft Convention on International Bills of Exchange and International Promissory Notes and draft Convention on International Cheques: major controversial and other issues;

A/CN.9/249/Add.1—Draft Convention on International Bills of Exchange and International Promissory Notes and draft Convention on International Cheques: major controversial and other issues—Addendum: summary of the comments of Romania and Switzerland;

A/CN.9/261—Report of the Working Group on International Negotiable Instruments on the work of its thirteenth session (New York, 7–18 January 1985);

A/39/17—Report of the United Nations Commission on International Trade Law on the work of its seventeenth session (1984), *Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 17*.

## DELIBERATIONS AND DECISIONS

7. The Working Group continued its review of the draft Convention on International Bills of Exchange and International Promissory Notes, and its consideration of the major controversial issues. It took into account a note

<sup>a</sup>The Chairman was elected in his personal capacity.

by the secretariat setting forth some considerations and suggestions relating to the major controversial issues (A/CN.9/WG.IV/WP.30). The deliberations of the Working Group relating to the major controversial issues are set forth below in part I of this report, and the deliberations relating to other issues are set forth in part II of this report. In the course of its deliberations, the Working Group prepared revised versions of certain articles of the draft Convention on International Bills of Exchange and International Promissory Notes as contained in document A/CN.9/211 based upon decisions of the Commission at its seventeenth session and of the Working Group at its thirteenth and fourteenth sessions. The revised articles are set forth in the annex to this report and will be incorporated into the complete text of the draft Convention, to be submitted to the Commission as document A/CN.9/274.

8. During the present session the Working Group completed the task entrusted to it by the Commission. The Working Group was of the view that the revisions suggested by it to the draft Convention on International Bills of Exchange and International Promissory Notes would in large measure meet the concerns expressed by Governments during the deliberations in the Commission at its seventeenth session, and in their written comments.

9. The Working Group wished to note the constructive atmosphere of its thirteenth and fourteenth sessions and the increased level of satisfaction that many representatives and observers had expressed with the draft text and with the entire project. The Working Group expressed the opinion that the review of the draft Convention at the nineteenth session of the Commission should be the final consideration of the full text prior to its adoption as a convention. For this reason it requested the Secretary-General, when he informed member States of the nineteenth session and invited observer States to that session, to suggest that experts in the field of negotiable instruments be named to the delegations. In making this request, the Working Group recalled that resolution 2205 (XXI), by which the General Assembly created the Commission, provided in its paragraph 4 that “The representatives of members of the Commission shall be appointed by Member States in so far as possible from among persons of eminence in the field of the law of international trade”.

## DRAFT CONVENTION ON INTERNATIONAL BILLS OF EXCHANGE AND INTERNATIONAL PROMISSORY NOTES: CONSIDERATION OF MAJOR CONTROVERSIAL AND OTHER ISSUES

### I. Major controversial issues

#### A. Defences available against holder or protected holder and related issues

##### 1. Article 26(1)(a): failure to make protest

10. The Working Group agreed to amend article 26(1)(a) by adding a reference to article 59, thereby

making failure to make a necessary protest a defence against the protected holder of a bill or a note.

2. *Article 26(1)(b): arising out of other transactions*

11. The Working Group recalled that at its thirteenth session it had requested the secretariat to consider which defences should be available to an immediate party against a holder or protected holder (under articles 25 and 26), with particular regard to the provisions of article 25(1)(c) and article 26(1)(b) (A/CN.9/261, para. 26). The Working Group considered the proposal of the secretariat, made in implementation of that request, to modify article 26(1)(b) as follows:

“(1) A party may not set up against a protected holder any defence except:

(a) ....

(b) Defences resulting from a transaction between himself and such holder that would be available as defences against contractual liability or defences arising from any fraudulent act on the part of such holder in obtaining the signature on the instrument of that party;”

12. It was noted that the proposed redraft of paragraph (1)(b) would allow as a defence only those defences which arose out of transactions between the protected holder and the party against whom he was claiming. This proposal would enlarge the text as found in document A/CN.9/211 by permitting that party to raise defences arising out of transactions with the protected holder which did not involve the instrument. It was also suggested that the proposal would restrict somewhat the defences available to that party which arose out of the underlying transaction between himself and the protected holder in that only those defences available against contractual liability would be recognized. In some countries, certain defences arising out of the underlying transaction might be based on tort and not be available as a defence against contractual liability.

13. During the discussion it was noted that there was a wide variety of positions taken on this point in national law. In some countries, the special nature of a negotiable instrument was emphasized and no defences were permitted to a claim on the instrument, not even when they arose out of the underlying transaction between the protected holder and the party against whom he was claiming. In other countries all claims of any type arising directly between the two parties could be interposed as a defence to an action on the instrument by the protected holder. In yet other countries only a restricted number of claims arising out of other transactions could be interposed as a defence against the protected holder. In some cases the available defences were described by type. In other cases the rule was that the only defences which could be raised were those that could be settled promptly by the tribunal before which the action on the instrument was brought so as not to delay the action on the instrument.

14. The Working Group was in agreement that the status of the protected holder under the draft Convention was a high one and that his ability to enforce the instrument promptly should not be unduly interfered with. At the same time there was general agreement that some defences which did not arise out of the underlying transaction should be permitted. It was recognized that those defences would be based on the national law applicable to the transactions, but it was suggested that the effect of such a defence on the substantive rights of the protected holder was a matter for the draft Convention.

15. The suggestion was made that, although the question arose in large measure because of the procedural advantages of claiming on a negotiable instrument, no attempt should be made to unify procedural rules. However, it was also suggested that the proposed modification of subparagraph (1)(b) would pose a substantive rule which the national procedural law would have to accommodate. It was stated that this would mean that the summary procedure for enforcement of a negotiable instrument currently used in some countries which recognize few if any defences to an action by a protected holder would not be available for enforcement of an instrument under this Convention without some modification.

16. In the light of the discussion the observer from Canada, at the request of the Working Group, prepared a revised version of paragraph (1)(b) which read as follows:

“(1) A party may not set up against a protected holder any defence except:

(a) ....

(b) (i) A defence based on the underlying transaction between himself and such holder;

(ii) A claim or defence in a liquidated amount resulting from a [business] transaction between himself and such holder that is available in accordance with the proper law of that transaction;

(iii) A defence arising from any fraudulent act on the part of such holder in obtaining the signature on the instrument of that party.”

17. It was stated in explanation of the draft that the use of the term “liquidated amount” in subparagraph (1)(b)(ii) was intended to restrict defences not arising out of the underlying transaction to those that could normally be settled promptly by the court. It was noted, however, that the term was unknown in many legal systems and would be hard to apply. After a further discussion of this proposal a working party consisting of the delegates of Australia, Czechoslovakia and Mexico and the observers from Canada and Switzerland, along with the Chairman of the Working Group, were asked to prepare a further revision.

18. The working party reported that they had attempted a number of formulas for re-drafting subparagraph (1)(b)(ii) of the Canadian proposal, but had been unable to express the desired concept in an acceptable manner. As a consequence, a majority of the working party

favoured the text as proposed by the observer from Canada with subparagraph (1)(b)(ii) deleted. A minority of the working party favoured the retention of the text originally proposed by the secretariat.

19. The Working Group was divided on the preferable approach. In response to a concern that was expressed, it was understood that under either formula a party could base a defence on the grounds, for example, that the protected holder had agreed with him to defer payment, even though that agreement was subsequent to the transfer of the instrument to the protected holder. Accordingly, the Working Group decided to present to the Commission both solutions referred to in paragraph 18.

3. *Article 25(1)(c): arising out of other transactions*

20. In view of its decision in respect of article 26(1)(b), the Working Group decided not to consider redrafting article 25(1)(c) but to bring to the attention of the Commission that article 25(1)(c) should be in accord with article 26(1)(b).

4. *Article 4(7): effect of knowledge of such a defence on status as protected holder*

21. The Working Group noted that if article 25(1)(c) was redrafted to permit some defences to be raised against a holder that did not arise out of the underlying transaction, the definition of protected holder in article 4(7) should be modified so that a party could be a protected holder in spite of having knowledge of such a defence.

22. The Working Group decided to delete from the definition as adopted by it at its thirteenth session the words "by him" since in some cases the completion of the instrument might be done by a person acting under the authority of the holder but whose actions might not be considered to be the actions of the holder.

23. It was noted that an instrument that was incomplete may not be an instrument under the Convention. Therefore, the Working Group decided to use the words of article 11(1) which speak of "an incomplete instrument".

5. *Article 25(3)(b): forgery*

24. The Working Group agreed to modify article 25(3)(b) by adding at the end the words "or forgery". It noted that this addition would correct what appeared to be a legislative oversight and would align the provision with the "mirror image" provision of article 68(3).

6. *Article 27: shelter rule*

25. The Working Group was in agreement that it should retain the shelter rule of article 27. It was noted that after a protected holder had acquired an instrument it might become common knowledge that there was a defence arising out of the transaction which underlay the issuance of the instrument. The example was given of notes issued to finance a large project which were in the hands of a

protected holder when a dispute in respect of the project was reported in the financial press. No subsequent holder might qualify as a protected holder because of knowledge of the dispute. Without article 27, which would permit a subsequent holder to have the rights of a protected holder in spite of knowledge of the dispute, the protected holder might not be able to sell the notes except at a substantial loss and might be forced to hold them to maturity when he could collect their face value.

26. The Working Group was also in agreement that a party who had at one time been in possession of an instrument, but not as a protected holder, who later reacquires the instrument from a protected holder should not have the rights of a protected holder and that this rule should be expressed in the article.

27. The Working Group agreed to delete paragraph (2) as unnecessary by reason of the fact that an instrument is not transferred to a party who pays it and such party does not become a holder of it.

28. The question was raised whether it was compatible with the principle of good faith that the present scope of the shelter rule would also give protection to a holder who had, when obtaining the instrument, knowledge of a fraud committed by a prior party. In a response, it was said that a restriction of the shelter rule would impair the transferability of instruments.

**B. Definition of "knowledge"**

29. The Working Group, at its thirteenth session, requested the secretariat to prepare a revised draft of the definition of knowledge in article 5 which would recognize that, while knowledge should in principle be actual knowledge, the courts should also have the power to deduce from the circumstances of the case that a person, despite his denial, had actual knowledge of a fact and that, without covering negligence, it should allow imparting knowledge to a person who did not have actual knowledge because he had wilfully disregarded relevant facts (A/CN.9/261, para. 67).

30. The Working Group, at its present session, considered a revised draft of article 5 prepared by the secretariat in response to that request which read as follows:

"For the purposes of this Convention, a person is considered to have knowledge of a fact if he has actual knowledge of that fact or

*Variant A:* if he deliberately disregarded facts or circumstances known to him which, but for such disregard, would have given him actual knowledge.

*Variant B:* if there exist facts or circumstances which would have given him actual knowledge had he not deliberately disregarded them.

*Variant C:* if he does not have actual knowledge because he wilfully disregarded facts or circumstances known to him."

31. The ensuing discussion focused on the differences between the three variants and the extent to which they adequately implemented the Working Group's request at its thirteenth session. The view was expressed that it was not appropriate to say that a person knew something he did not know, but that it was a different question whether a person should be responsible for not knowing what he should have known. The view was also expressed that the use of terms such as "deliberately" and "wilfully" in variants B and C did not make clear the strength of the inference to be drawn. Furthermore, it was stated, there is a danger in preparing a definition of knowledge that would require a party to inquire extensively as to possible additional facts on the basis of those facts which did come to his attention.

32. At the request of the Working Group the observer from Canada prepared a new draft article 5 which would have added to the end of the text in A/CN.9/211 the words "or he has deliberately disregarded other facts known to him which would have given him knowledge of that fact, unless such disregard was commercially reasonable."

33. It was explained that the real innovation of this proposal lay in the last clause. What was commercially reasonable must be tested by local standards, how one would act in regard to a local transaction. It was stated, however, that if the law required something to be done, no proof that it was commercially reasonable not to do that thing should be permitted.

34. After deliberation the Working Group decided to retain the original text of article 5. It was felt that under that text a court could reach the desired result in any given case.

#### **C. Forged endorsements: limit of liability in articles 23(4) and 23 bis (4)**

35. The Working Group was in agreement that the damages recoverable in articles 23(4) and 23 bis (4) should be limited to those mentioned in articles 66 and 67, and should not include interest or costs incidental to the giving of security under article 74 as had been suggested by the secretariat (A/CN.9/WG.IV/WP.30, para. 16). Although some representatives and observers viewed the use of cross references as a questionable practice, it was decided that the limit of recoverable damages would be expressed by referring to those articles.

#### **D. Liability of a transferor by mere delivery (article 41)**

36. The Working Group considered article 41 in the light of the explanatory notes and the revised draft prepared by the secretariat.<sup>4</sup> The discussion focused on the following issues: (1) whether a provision like article 41 should be retained which imposed liability on persons who transferred the instrument by mere delivery, i.e. without endorsing it; (2) if so, what should be the nature

and extent of such liability, and in which circumstances should it be incurred; and (3) should such liability be imposed also upon endorsers.

#### **1. Retention of provision on liability of transferor by mere delivery**

37. While some doubt was expressed about the appropriateness of regulating in the draft Convention the liability of a transferor by mere delivery, the Working Group, after deliberation, reaffirmed its decision, taken at its thirteenth session, to retain a provision along the lines of article 41.<sup>5</sup>

#### **2. Nature and extent of liability**

38. The Working Group considered the content and scope of the representation of the transferor on which the transferee would be entitled to rely. As regards the infirmities listed in subparagraph (a) of paragraph (1), divergent views were expressed as to whether forged or unauthorized signatures of all parties should be covered or only those of certain parties such as the maker and the acceptor and, possibly, the drawer of an unaccepted bill. The Working Group, after deliberation, was agreed that the signatures of all parties should be covered since any restriction to certain signatures would be contrary to the interest and legitimate expectations of the transferee who may place particular reliance on the quality of a specific signature such as that of a given guarantor or endorser.

39. Regarding the infirmity listed in subparagraph (b) of paragraph (1), the Working Group was agreed that not only an alteration of the amount of the instrument should be covered but also any other kind of material alteration, since such other alterations could equally affect the value of the instrument.

40. As regards the infirmities listed in subparagraph (c) of paragraph (1), it was noted that the protection afforded to a transferee was not needed if the transferee was a protected holder since, due to this status, he would not be subject to any claim or defence covered by that provision.

41. Divergent views were expressed as to whether the infirmities listed in this provision formed an acceptable basis for liability of the transferor. Under one view, the transferee of an instrument should be able to rely on the absence of a valid claim to the instrument or a defence against him since his expectations as to the value of what he received were the same and as justified as those of a buyer of any other item. Some proponents of this view pointed out that liability in this respect was appropriate if it was limited to the value received by the transferor and was conditioned on the return of the instrument to him.

42. The prevailing view, however, was that the scope of subparagraph (c) was too wide to be acceptable to most countries, in particular, if an immediate action for damages were envisaged as remedy. It was also pointed out that the expectations of a buyer of an instrument were

<sup>4</sup>A/CN.9/WG.IV/WP.30, paras. 18-53.

<sup>5</sup>A/CN.9/261, para. 51.

directed at getting payment at maturity and that the detrimental consequences of any infirmity listed in this provision may occur or be assessed with certainty only at the time of maturity.

43. The Working Group decided not to retain subparagraph (d).

44. It was realized that under some existing laws a transferor by mere delivery incurred liability for certain infirmities other than those relating to the genuineness and validity of the instrument as covered by subparagraphs (a) and (b).

45. In this context, the Working Group considered the general question whether the draft Convention should provide an exhaustive list of infirmities or whether a transferee may benefit from a rule in a national law other than the Convention embracing other kinds of infirmities. The Working Group, after deliberation, was agreed that, for the sake of uniformity, the liability under the draft Convention should be exclusive.

46. With this aim in mind, various proposals were made for inclusion of further infirmities in a new subparagraph (c). One proposal was to have the transferor represent that he was entitled to transfer the instrument. The Working Group did not adopt this proposal in view of the fact that under the system of the draft Convention, unlike certain national laws, transfer of title was not a precondition for becoming a holder.

47. Another proposal was to have the transferor represent that the instrument was in conformity with what it purported to be, that the claim in respect of which it was issued in fact existed, and that there was no impediment, even if unknown, to its payment. The Working Group did not adopt this proposal because it was regarded as too vague or too wide.

48. Yet another proposal was to impose liability on a transferor who knew of any fact which rendered the instrument valueless or significantly reduced its value. While there was some support for this proposal, the prevailing view was that this proposal was too far-reaching, in particular by covering instances of insolvency or similar facts affecting the chances of payment.

49. It was agreed that the gist of the basis of liability in the new subparagraph (c) should be the representation that the transferee acquired the rights to payment, as purported by the instrument, against the party primarily liable or, in the case of an unaccepted bill, against the drawer. It was agreed that the precise representation of the transferor envisaged in new subparagraph (c) was that, at the time of transfer, he had no knowledge of any fact which would impair such right of the transferee; one representative expressed the view that this liability should not depend on knowledge.

50. The Working Group was agreed that liability on account of any infirmity referred to in paragraph (1)(a),

(b) or (c) was incurred only to a holder who took the instrument without knowledge of such infirmity.

51. Divergent views were expressed as to the appropriate point of time at which liability under article 41 was incurred and the transferee had a right of recovery against the transferor. Under one view, the decisive point of time should not be before the date of maturity because it was only then that any detrimental effect of the defect or infirmity would materialize and the extent of that effect on the transferee's rights and expectations to obtain payment could be clearly assessed.

52. The prevailing view, however, was that the transferee should be given an immediate right of recovery. This was not only of practical importance but also in conformity with the basis of liability, namely that the transferee did not receive an instrument of the value it purported to have. While the precise reduction in value caused by the infirmity in question may not be easily determined at that early point of time, such possible difficulty was no convincing reason against an immediately available action since it could be taken care of in deciding on the appropriate type of remedy which the draft Convention should accord to the transferee.

53. As regards the decision on the type of remedy, the Working Group was agreed that the transferee's right to recover should not be characterised or labelled in a certain way such as action for damages or right to rescind the contract. Article 41 would simply state the content of the remedy which was agreed to be that the transferee may recover, against return of the instrument, the value originally received by the transferor for that instrument, plus interest calculated at a certain rate (to be determined by the Commission).

### 3. Extension of article 41 to endorsers

54. Some doubts were expressed as to the appropriateness of extending the provisions of article 41 to persons who transferred the instrument by endorsement and delivery. It was questioned whether there was a real need for such extension in view of the fact that in such cases the transferee, in his capacity as endorsee, had a right to payment from the transferor as endorser if payment could not be obtained from the party primarily liable. It was also pointed out that liability under article 41 was not appropriate in those cases where the instrument was endorsed without recourse or for collection.

55. However, the Working Group, after deliberation, was agreed that liability under article 41 should be imposed also on an endorser. It was thought that the policy reasons underlying the liability of a transferor by mere delivery applied with similar force to a person who transferred the instrument by endorsement and delivery and thus was, after all, also a transferor by delivery. A further reason was that, without such liability, the transferor by endorsement and delivery would be treated more favourably than the transferor by mere delivery whose liability was an immediate one and not conditioned upon dishonour for non-acceptance or non-payment.

56. Regarding the case of an endorsement for collection, the extension of article 41 to endorsers would not create any hardship since the endorsee for collection suffered no loss, for lack of any value given to his endorser; if due to any of the infirmities listed in article 41(1) he could not collect, he would simply return the instrument to his endorser. Regarding the case of an endorsement without recourse, the situation was similar to that of a transfer by mere delivery in that there was no endorsement which would be sufficient to compensate the transferee. Yet, it was pointed out that persons (often banks) who endorsed without recourse usually did so for the purpose and with the understanding of excluding any liability connected with the instrument or its transfer.

57. In this connection, the Working Group considered whether the expression "without recourse" or words of similar import should be interpreted as excluding only the liability on the instrument (see article 40(2)) or also any liability off the instrument as the one provided for in article 41. Since divergent views were expressed on that point, a proposal was made to include in the draft Convention a clear rule of interpretation and, for example, require specific wording (e.g. "without liability") for an effective exclusion of liability off the instrument.

58. The Working Group, after deliberation, did not adopt this proposal since no agreement was reached on the content of such a rule or on a standard wording and because it was felt to be too burdensome and possibly confusing to require an express stipulation to that effect on the instrument. The Working Group, therefore, decided that the faculty of the endorser to exclude or limit his liability under article 41 was appropriately expressed in the draft Convention by the opening words of article 41 "Unless otherwise agreed by the parties".

## II. Other issues

59. The Working Group noted that, during the consideration of the draft Convention by the Commission at its seventeenth session, the Commission had decided a certain number of issues but had left other issues open for possible further consideration by the Working Group. The Working Group decided to review those issues to determine in respect of which issues it could add further clarification.

### A. Internationality and formal requisites

#### 1. Article 1(2) and (3): International elements

60. The view was expressed that the place at which a bill was drawn and the place at which it was payable should be shown on the bill to be in different countries for the bill to fall under the draft Convention. It was stated that this was not a question of internationality but of validity. The Working Group did not retain this suggestion since the Commission had already decided that an indication of those places should not be a pre-condition to the application of the draft Convention.

61. A proposal was made by the observer for the Hague Conference on Private International Law to divide article 1 into two articles. The first article would express the international elements necessary for the draft Convention to apply while the second article would contain the conditions for validity of an instrument as follows:

#### "Article 1

"(1) This Convention applies to an international bill of exchange when the instrument contains the words 'international bill of exchange (Convention of...)' and shows that at least two of the following places are in different States:

- (a) The place where the bill is drawn;
- (b) The place indicated next to the signature of the drawer;
- (c) The place indicated next to the name of the drawee;
- (d) The place indicated next to the name of the payee;
- (e) The place of payment.

"(2) This Convention applies to an international promissory note when the instrument contains the words 'international promissory note (Convention of...)' and shows that at least two of the following places are in different States:

- (a) The place where the note is made;
- (b) The place indicated next to the signature of the maker;
- (c) The place indicated next to the name of the payee;
- (d) The place of payment.

"(3) Proof that the statements referred to in this article are incorrect does not affect the application of this Convention.

#### "Article 1 bis

"(1) An international bill of exchange is a written instrument which:

- (a) Contains an unconditional order whereby the drawer directs the drawee to pay a definite sum of money to the payee or to his order;
- (b) Is payable on demand or at a definite time;
- (c) Is dated;
- (d) Is signed by the drawer.

"(2) An international promissory note is a written instrument which:

- (a) Contains an unconditional promise whereby the maker undertakes to pay a definite sum of money to the payee or to his order;



- (b) Is payable on demand or at a definite time;
- (c) Is dated;
- (d) Is signed by the maker.”

62. The view was expressed that the original text was preferable since all elements presently set out in paragraphs (2) and (3) of article 1 were essential elements for the validity of an instrument under this Convention. The Working Group decided to retain the present text but to bring the proposal to the attention of the Commission.

### 2. *Articles 1 and 2: application of Convention to parties other than maker or drawer*

63. The prevailing view in the Working Group was that it was already clear that once an instrument fell under the Convention, the rights of all persons in regard to that instrument would be governed by the Convention and that it was not necessary to modify the text in that regard.

### 3. *Article 1: definition of “writing”*

64. The question was raised whether it would be useful to have a definition of writing in the draft Convention. It was noted that many recent international texts have defined writing as including telegrams, telex, and more recently, data communication which provides a record of the communication. Under one view expressed in the Working Group it was better not to include a definition of writing so as to permit the application of the draft Convention to new methods of data transmission. Under another view a definition was not necessary since the context of the draft Convention could only apply to an instrument in a paper-based form. The Working Group, after deliberation, decided not to recommend that a definition of writing be included in the draft Convention.

### 4. *Article 1: invocation of the Convention*

65. There was general agreement that an international bill of exchange or international promissory note should be easily recognizable. It was noted, in particular, that some banking systems handle large amounts of commercial paper and they would need easy means to distinguish these instruments which might need special handling. It was also noted that article 1 required the words of internationality to be in the text of the instrument, which had certain advantages but which might mean they would be difficult to find.

66. Various suggestions were put forth: that the words of internationality be in a conspicuous place such as the heading, that the words of internationality be in a widely used international language such as English or French, that a distinctive symbol be used, that the instrument follow a prescribed form as contained in an annex to the Convention. It was stated that for technical reasons a previous suggestion that the instrument be in a distinctive colour could not easily be implemented in all countries.

67. The Working Group decided that the words of internationality should be in the heading of the instru-

ment as well as in the text. In order to reflect its decision the Working Group decided to re-word paragraph (2) as follows:

“An international bill of exchange is a written instrument with the heading ‘international bill of exchange (Convention of ...)’ which:”

with the rest of the paragraph unchanged. A similar modification of paragraph (3) would be made for the international promissory note. In order to aid users in designing a form which would satisfy the requirements of the draft Convention, it was decided to request the secretariat to submit to the Commission at its nineteenth session model forms to be included in an annex to the Convention. The Working Group also decided that use of the forms would not be mandatory. Reference should be made in the text of the draft Convention to the recommended forms in such manner as the Commission should consider appropriate.

### 5. *Express provision excluding cheques from the scope of application of the draft Convention*

68. It was noted that in common law jurisdictions a cheque was a species of bill of exchange (i.e. a cheque was a bill of exchange, which contained an order by the drawer to a bank to pay on demand a sum of money to the payee). It was suggested that, since the draft Convention was not intended to apply to cheques, a provision excluding the application of the draft Convention to cheques should be included therein. It was noted, however, that it was unlikely that the provisions of the draft Convention would be applied to cheques. One reason for this would be the fact that instruments to which the draft Convention applied would contain in the text thereof the words “international bill of exchange (Convention of ...)”. After deliberation, the Working Group decided that a provision excluding cheques from the scope of application of the draft Convention was needed, and should be added.

## B. *Questions relating to article 2*

69. The Working Group noted that, under article 2, the Convention applied without regard to whether the places indicated on an international bill of exchange or on an international promissory note pursuant to paragraph (2)(e) or (3)(e) of article 1 were situated in Contracting States. It was pointed out that this provision created uncertainty, with particular regard to its effect in a non-contracting State. The main reason for such uncertainty or limited effect was that the provision presupposed party autonomy which, however, was not recognized in respect of negotiable instruments by most systems of conflict of laws. The situation was aggravated by the fact that the draft Convention did not require any link between the instrument or its use and a Contracting State and that, by virtue of article 1(4), even those instruments may be covered which were not genuinely international. It was, therefore, suggested that a certain link between the use of the instrument and a Contracting State should be required. For example, one could limit the application of

the Convention to those cases where the bill was drawn or the note was made in one Contracting State and the place of payment was situated in another Contracting State, or one could require that one of these two places was in a Contracting State.

70. In reply to these concerns, reference was made to the commentary on draft article 2 which addressed the possible problems as to the effectiveness of this provision.<sup>6</sup> Above all, it was pointed out that the above concerns had been expressed in previous sessions of the Working Group and at the seventeenth session of the Commission; the Commission had not adopted any of the proposals requiring a certain link between the instrument and a Contracting State, and there was wide agreement in the Commission that the problems referred to with regard to the applicability of the draft Convention should be addressed by the Hague Conference on Private International Law in the course of its intended revision of the Convention for the Settlement of Certain Conflicts of Laws in connection with Bills of Exchange and Promissory Notes (Geneva, 1930).<sup>7</sup>

71. The Working Group, after deliberation, concluded that, in the light of these considerations, it was not appropriate for the Working Group to decide these questions, and that the Commission itself may wish to reconsider them.

### C. Addition to article 3: observance of good faith

72. The Working Group considered a proposal to add at the end of article 3 of the draft Convention the following words "and the observance of good faith in international trade".

73. There was wide agreement that the addition of these words would serve a useful purpose. It was noted that the observance of good faith by the parties formed the basis for the proper operation of many provisions of the draft Convention. A suggestion was made that the proposed text should refer expressly to the use of the instruments covered by the Convention. It was suggested that, in the context of the draft Convention, it was more appropriate to refer to the observance of good faith "in international transactions" rather than "in international trade".

74. The Working Group decided to accept the proposal that article 3 contain the words "and the observance of good faith in international transactions".

75. There was support for the view that, since the provision was in the nature of a recommendation, it should be made part of the preamble to the draft Convention and not placed in the body of the draft

Convention. The prevailing view was that, since provisions of this character had previously been placed in the body of the Conventions to which they related, this past practice should be followed.

### D. Articles 4(10) and X: definition of "signature"

76. The Working Group considered certain questions relating to the definition of signature in article 4(10) and the possible content and effects of the declaration by a Contracting State envisaged in article X. The Working Group noted that, when these two articles were considered by the Commission at its seventeenth session, there was general agreement that article X should be retained to accommodate States whose legislation required that a signature on an instrument be handwritten but that the text of article X might need some clarification.<sup>8</sup>

77. In the course of the deliberations of the Working Group, various observations and proposals were made with a view to clarifying matters. The observations concerned the appropriateness of the required link between a given signature and the Contracting State which had made a declaration under article X and concerned the possible effects of such declaration within and outside that Contracting State.

78. As regards the required link between a given signature and the Contracting State, doubts were expressed as to the appropriateness of the territorial criterion envisaged in article X. It was observed that a declaration by a State to the effect that a signature placed on an instrument in its territory must be handwritten presented practical problems in those frequent cases where the place at which the signature had been made was not apparent from the instrument. Any obligation of other persons who took the instrument to make enquiries as to that place were deemed to be too burdensome in the context of an international instrument and would adversely affect the desired ease of its circulation. Moreover, the territorial criterion might be too wide in view of the fact that a Contracting State in its legislation may not require that all signatures placed on the instrument in its territory be handwritten. It may, for example, impose this requirement only on its nationals or only on certain of its legal or physical persons or only on certain parties to the instrument.

79. In the light of these concerns, a proposal was made to envisage in article X a declaration to the effect that any particular signature on an international instrument made by a legal or physical person of the Contracting State be handwritten. However, doubts were expressed as to the appropriateness of using the nationality of a person, or the seat of a legal person, as the connecting factor for the purposes of article X. One concern was that this formula may embrace nationals of the Contracting State who signed the instrument outside that State. Above all, it was felt that such connecting factor would adversely affect the transferability and circulation of the instrument in that it obliged other persons to enquire about the nationality of

<sup>6</sup>Commentary on Draft Convention on International Bills of Exchange and International Promissory Notes, Report of the Secretary-General, A/CN.9/213, commentary on article 2, paras. 1-6.

<sup>7</sup>Report of the United Nations Commission on International Trade Law on the work of its seventeenth session, *Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 17 (A/39/17)*, para. 70.

<sup>8</sup>*Ibid.*, para. 45.

those who signed it. It was suggested that such obligation was even more burdensome than the one resulting from the use of the territorial criterion.

80. It was observed that the difficulties concerning the link between a given signature and article X were aggravated by the fact that, as was generally agreed, article X did not clearly set out the precise effects of a declaration under that article. For example, it was not clear whether such a declaration would have an extraterritorial effect in that it would cover the case where the validity of a signature made in violation of the legislation of the Contracting State would arise in another State which did not require signatures to be handwritten.

81. A proposal was made to adopt the approach of article 12 of the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980) and to provide that the provision of article 4(10) which allowed a signature to be made by stamp, symbol, facsimile, perforation or other mechanical means did not apply where a Contracting State had made a declaration in respect of any signature which under its legislation must be handwritten.

82. The proposal was objected to on the ground that its effect, namely to exclude the application of article 4(10) as regards signatures covered by the declaration even in jurisdictions outside the Contracting State, was undesirable in the area of negotiable instruments law which, unlike sales law, concerned not merely two persons but a plurality of persons interested in the transferability and circulation of the instrument.

83. It was pointed out that due to this special feature of negotiable instruments law the traditional method of a reservation, even if its effect were limited to the Contracting State, would not solve the problem. By way of illustration, it was asked whether the fact that a Contracting State regarded a certain signature, for example that of an acceptor, as invalid should be treated as a case of dishonour in any action brought against the drawer in another jurisdiction or whether the acceptance would be treated there as valid with the result that the drawer would not be liable and the holder in fact could not obtain payment in either of the two jurisdictions.

84. In view of the above difficulties, two suggestions were made with a view to rendering the declaration envisaged in article X unnecessary. One suggestion was to delete the definition of signature in article 4(10). It was stated in support of this suggestion that the Geneva Uniform Law did not contain such a definition and that this fact had not led to any difficulties in the fifty years of its application. In view of future technical developments it might even be an advantage to let the individual States decide which forms of signature they were prepared to allow. It was stated in reply that it was undesirable to delete the definition of signature and to leave this important question to the individual States since the ensuing disparity and uncertainty was detrimental to the use of an international negotiable instrument.

85. The other suggestion was based on the premise that in respect of signatures made by legal persons the use of means prohibited under the law of a Contracting State should be regarded as an unauthorized use with the consequences laid down in article 32(3) concerning the signature of an agent without authority. It was thought that the interest of a State whose legislation required certain signatures to be handwritten could be met by regarding signatures made by legal persons in other forms not as non-existent but as unauthorized and thus not binding on the principal. The suggestion, therefore, was to let Contracting States use the vehicle of a declaration or any other appropriate means of publicizing its signature requirements in order to provide certainty and to exclude the possibility of reliance by persons outside that State and thus of any possible finding of apparent or implied authority.

86. The Working Group, after deliberation, was agreed that the above questions and proposals needed further consideration. It decided to retain article X placed between square brackets and to invite the Commission to reconsider this provision in the light of the discussion and suggestions made in the Working Group.

#### **E. Definition of "money" and "currency"**

87. The Working Group considered article 4(11) dealing with the definition of "money" and "currency", which was at present placed between brackets. It was noted that the definition of "money" or "currency" was not a comprehensive definition but only inclusive. The Working Group noted that certain modifications to this article had been suggested during the discussions in the Commission.

88. The Working Group considered a modified draft of article 4(11) which had been previously proposed by the International Monetary Fund, which read as follows:

"Money" or "currency" includes a monetary unit of account which is established by an intergovernmental institution and which is transferable among the members of this institution or other entities as the institution may prescribe." (A/CN.9/249, para. 24).

89. There was wide agreement that the substance of this definition was acceptable. The view was expressed that in addition to monetary units of account established by intergovernmental institutions, other units of account were established by bilateral or multilateral agreements between Governments. Such units of account should also be included within the definition of "money" and "currency". The Working Group agreed with this view, and decided that the definition should be modified to include such units of account.

90. The Working Group was also of the view that the definition of "money" and "currency" need not include the requirement that the unit of account established by an

intergovernmental institution or intergovernmental agreement be expressly made transferable by the institution or agreement. The purpose of the definition was solely to extend for the purposes of the draft Convention the ordinary meaning of "money" and "currency" so that these terms included monetary units of account established by an intergovernmental institution or intergovernmental agreement. The Working Group therefore decided to delete this reference to the transferability of the unit of account in the definition. However, since there might be implications to its decision of which the Working Group was unaware, the secretariat was requested to consult with the International Monetary Fund and to report to the Commission.

91. The Working Group considered the possible effect of a definition of the kind set forth above on the operation of article 71(1). The question was raised as to how payment would be made under that article if the amount of the instrument was expressed in a unit of account. It was observed in reply that payment could be made in certain units of account (i.e. accounts can be currently maintained in those units of account and the units of account due could be credited to those accounts). It was also observed that there is currently no means by which payment could be made in certain other units of account. When the amount of the instrument was expressed in the latter units of account, the drawer or the maker could indicate on the instrument that it must be paid in a specified currency other than the unit of account (article 71(2)). It was decided that article 71 needed to be supplemented by a rule determining the currency of payment when the drawer or maker had failed to specify the currency of payment.

92. The view was expressed that in some countries the term "currency" meant physical currency in the form of coin or notes. The question might arise in such countries as to whether a payee was entitled under article 71(1) to demand payment in coin or notes. One approach to resolving this difficulty might be for the draft Convention to provide a comprehensive and extended definition of "currency" or "money" (e.g. as including immediately available credit). The Working Group was of the view that it would be difficult to formulate an acceptable definition of "currency" or "money" in view of the different meanings given to those terms under national legal systems. The Working Group decided to maintain the present approach under which the draft Convention contained no comprehensive definition of the term, but only provided that certain items which might be regarded as not being included within the meaning of those terms were in fact so included (article 4(11)).

#### **F. Rate of interest: instruments with floating rates of interest**

93. The Working Group noted that the Commission, at its seventeenth session, had considered the proposal that the draft Convention should allow the issuance of instruments with floating rates but had not taken a final

decision on this proposal.<sup>9</sup> The Working Group considered this general proposal with the following qualification added: It shall be required that any adjustments to the original stated rate relate directly to the movement of an index which is both publicly disclosed and not subject to control of interested persons, in particular, the payee.

94. Under one view, the proposal should not be adopted since it created uncertainty as to the amount due at maturity. Such uncertainty was contrary to the principle that instruments should be certain on their face and, above all, might turn out to be to the detriment of the debtor. Therefore, the draft Convention should not condone or encourage the use of such instruments. If the proposal were to be accepted, it should at least be accompanied by a further safeguard such as an absolute interest rate ceiling or a limit on the maximum adjustment allowed.

95. The prevailing view, however, was in favour of the proposal. It was stated that promissory notes, and more recently also bills of exchange, with floating rates were being issued in large numbers and that their use was likely to increase. These instruments would continue to be used whether or not they were covered by the draft Convention. However, if they were covered, the draft Convention would gain considerably in attractiveness and acceptability, in particular since almost none of the existing national laws permitted such instruments to be negotiable.

96. Regarding the uncertainty inherent in a variable rate of interest, it was pointed out that the real cause of uncertainty lay in the economic situation with its fluctuation of rates of interest and of currency exchange. Instruments with floating interest rates were the response to that situation and the necessary cover could be obtained by certain types of credit. It was noted that any future adjustment did not necessarily work to the detriment of the debtor. It was also pointed out that the imposition of an absolute ceiling would defeat the object of an instrument with floating rates and that it was well-nigh impossible to fix an adequate ceiling. Above all, the qualification added to the proposal would ensure that the determinative source of adjustment was easily ascertainable and could not be influenced by the payee or any interested party to the detriment of the debtor.

97. The Working Group, after deliberation, was agreed that the proposal warranted serious consideration and that the Commission should be invited to consider inclusion of a provision which the secretariat was requested to prepare in consultation with the Study Group on International Payments and other banking experts. The secretariat was also requested to consider the need for redrafting certain other provisions (e.g. articles 1(2)(b), (3)(b) and 7(4)) with a view to clarifying the applicability of the Convention to instruments with floating interest rates.

<sup>9</sup>*Ibid.*, para. 50.

### G. Questions relating to article 8(2)

98. The Working Group noted that article 8(2) allowed an instrument payable at a definite time to be accepted or endorsed or guaranteed after maturity with the result that the instrument was payable on demand as regards the acceptor, the endorser or the guarantor. It was pointed out that the precise effects of this rule, in particular with regard to the liability of an endorser, were not clearly set out in the draft Convention. It was asked, for example, whether the endorser in such case was secondarily liable and what exactly was the starting point and the duration of his liability. Since it was not clear whether the provision of article 51(f) applied or whether the effective time-limit was set by article 80(1)(d), a suggestion was made to include in the draft Convention a specific rule regulating this question.

99. The Working Group, after deliberation, decided not to include a specific rule in view of the fact that the situation envisaged in article 8(2) was not likely to occur frequently and that it was not feasible to provide specific rules for the many questions which possibly arose in this context.

### H. Article 11: incomplete instruments

100. The Working Group noted that the Commission, at its seventeenth session, was in agreement with the policy underlying article 11 but had also expressed the view that certain aspects regarding completion should be clarified.<sup>10</sup> One such aspect was the question as to who could complete the instrument so as to make it effective as a bill or a note. It was noted that the uncertainty arose from the fact that the object of the two paragraphs of article 11 was not immediately apparent.

101. The Working Group, after an exchange of views, was agreed that paragraph (1) dealt with the formal requisites of an instrument irrespective of whether the person completing it had authority to do so, while paragraph (2) dealt with the consequences of a completion by a person without any authority or by a person who had authority but completed the instrument in a way not conforming with the terms of authority. It was felt that the term "authority", which had been used in an earlier draft, was more appropriate than the term "agreement".

102. The Working Group decided that this understanding should be made clear by revising the opening words of paragraph (2) as follows: "When such an instrument is completed without authority or otherwise than in accordance with the authority given". The secretariat was requested to make the necessary revisions to paragraph (2)(a).

### I. Article 16: clauses prohibiting further transfer

103. During the discussion in the Commission,<sup>11</sup> it was noted that article 16 covered two situations: (a) the

drawer or the maker issues an instrument excluding its transferability, and (b) an endorser makes a restrictive endorsement prohibiting further transfer. The Working Group shared the doubts expressed in the Commission as to the appropriateness of combining these two situations, as it might lead to confusion and uncertainty about the legal effects of such clauses.

104. Regarding the first situation, the Working Group was agreed that the rule laid down in article 16 was correct in providing that the instrument was not transferable.

105. Regarding the second situation, divergent views were expressed as to the appropriate consequences of such a restrictive endorsement. Under one view, the instrument should remain transferable but the endorser would not be liable to any subsequent transferee except his immediate endorsee. The prevailing view, however, was that a stipulation of the kind envisaged in article 16 should be taken literally and, thus, exclude further transfer by the endorsee, except for purposes of collection.

106. The Working Group was agreed that this solution, which accorded with the rule laid down in article 16, should be expressed in the context of article 20.

### J. Articles 30, 52, 58 and 63: legal effects of implied act or omission

107. The Working Group was agreed that the exclusion of implied waivers in articles 52, 58 and 63 was justified, as had been generally agreed by the Commission.<sup>12</sup> However, as regards the exclusion of the words "or impliedly" in article 30,<sup>13</sup> the Working Group was agreed that the situation of an implied acceptance of a signature by a person whose signature was forged should be treated differently. While the appropriate result might be obtained from an applicable rule of general law based on a principle of estoppel or good faith, it was preferable to provide a uniform answer in the draft Convention.

### K. Article 34(2): exclusion of liability by drawer

108. The Working Group considered the question whether the drawer should be permitted to disclaim liability for non-payment of the bill, a question on which opinions had been divided during the discussion in the Commission.<sup>14</sup> Under one view, article 34(2) should not permit such disclaimer, since permitting such disclaimer would make it possible for a bill of exchange to be issued and to circulate without a person being liable on it. Under another view, article 34(2) was acceptable in that it reflected actual practice and found its counterpart in some legal systems. Under yet another view, the drawer should be permitted to disclaim his liability for non-payment by the drawee or the acceptor in instances where a party other than the drawer was liable on the bill.

<sup>12</sup>*Ibid.*, para. 57.

<sup>13</sup>*Ibid.*, para. 58.

<sup>14</sup>*Ibid.*, para. 59.

<sup>10</sup>*Ibid.*, para. 56.

<sup>11</sup>*Ibid.*, para. 73.

109. The Working Group was in accord with the view of the Commission that article 34(2) should be revised to reflect the policy that a disclaimer by the drawer of his liability for non-payment should be effective provided another party was liable on the bill whereas a disclaimer of liability for non-acceptance might be effective even though no other party was liable on the bill.

**L. Article 42: guarantee of incomplete instrument**

110. The Working Group considered a proposal which had been accepted by the Commission that the draft Convention contain a provision according to which an instrument may be guaranteed before it had been signed by the drawer or the maker or while otherwise incomplete.<sup>15</sup> It was noted that article 38(1) permitted an incomplete instrument which satisfied the requirements set out in article 1(2)(a) to be accepted by the drawee before it had been signed by the drawer, or while otherwise incomplete. The Working Group decided that a provision should be included permitting an incomplete instrument which satisfied the requirements set out in article 1(2)(a) to be guaranteed.

**M. Article 42(2): guarantee to be written on instrument or on slip affixed thereto**

111. The Working Group noted that article 42(2) might be construed as prohibiting guarantees which did not appear on the instrument (e.g. were created on a separate document). It was also noted that guarantees were so created in practice. In order to clarify that such guarantees were not affected by the draft Convention, it was suggested that the words "under this Convention" be added after the opening words "A guarantee". It was observed, however, that the draft Convention in general did not deal with agreements created outside the instrument, and that the addition of these words in one instance might give rise to the argument that, in other instances where no such words were added, the Convention would exclude agreements created outside the instrument. The Working Group agreed with an observation to the effect that a guarantee could be given outside the instrument on a separate document and decided to retain article 42(2) without change. It requested the secretariat to refer to this possibility in any commentary to the draft Convention.

**N. Article 46: stipulation by drawer prohibiting presentment for acceptance**

112. The Working Group considered article 46 with a view to clarifying the legal nature and effects of stipulations prohibiting presentment for acceptance. The Working Group noted that under article 45(2) presentment was mandatory in the cases specified therein. To permit the drawer under article 46 to stipulate that the bill must not be presented for acceptance in those specified cases led to inconsistency. Article 46 should therefore be amended so as to deprive the drawer of the power to so stipulate.

<sup>15</sup>*Ibid.*, para. 61(c).

However, it was agreed that even in the cases under article 45(2) the drawer should have the power to stipulate that the bill must not be presented for acceptance before a specified date or before the occurrence of a specified event.

113. When presentment for acceptance was optional (article 45(1)), the Working Group was of the view that stipulations prohibiting or restricting presentment for acceptance (article 46(1)) might be permissible. However, the legal consequences if a bill was presented for acceptance contrary to such stipulations and not accepted should vary with the nature of the stipulations. In practice, stipulations prohibiting presentment and motivated by commercial considerations were sometimes included in a bill. If a bill was presented for acceptance notwithstanding such a stipulation, and acceptance was refused, the bill should not thereby be considered dishonoured. The Working Group noted that the provisions of article 46(1) and (2) were appropriate for these cases, and should be retained to deal with them. Stipulations were also sometimes included which, while not prohibiting presentment, excluded the liability of the drawer if acceptance were refused upon presentment. If acceptance was refused, the bill would be considered to be dishonoured, but an immediate right of recourse against the drawer would be excluded. Rights of recourse which might be available against other parties would be unaffected. The Working Group noted that these cases were governed by article 34(2). It was suggested that the distinction between a stipulation which prohibits presentment for acceptance and a stipulation which excludes liability for non-acceptance was subtle and may be difficult to apply in practice.

**O. Articles 48 and 52: bankruptcy of drawee**

114. During the consideration of the draft Convention by the Commission,<sup>16</sup> it had been noted that where the drawee had accepted a bill and had, after such acceptance but before maturity, become bankrupt, the draft Convention did not provide for the exercise of a right of recourse by the holder before the date of maturity of the bill (article 54(1)(b), (2)). It had been proposed during the discussion in the Commission that the draft Convention should provide an immediate right of recourse, before maturity, where the holder of an accepted bill learned of the bankruptcy of the acceptor before the date of maturity. The Working Group was in accord with the prevailing view in the Commission that this proposal should not be accepted.

**P. Article 51(h): presentment for payment at a clearing-house**

115. The Working Group considered a proposal made during the discussion in the Commission to add to article 51(h) the words "if in conformity with the rules of that clearing-house".<sup>17</sup> In support of this proposal, it was

<sup>16</sup>*Ibid.*, para. 62.

<sup>17</sup>*Ibid.*, paras. 78-79.

noted that presentment for payment at a clearing-house might not be feasible under the rules of a particular clearing-house. There was wide agreement that due presentment at a clearing-house could occur only if such presentment could be made in conformity with the rules of the clearing-house or the applicable law.

116. The Working Group noted that under the law of some States an instrument was duly presented for payment when it was presented at a clearing-house in conformity with the rules of that clearing-house. Under the law of other States, however, due presentment occurred only when the instrument was conveyed through the clearing-house to the drawee or acceptor. It was noted that article 51(h) needed clarification as to when due presentment occurred under its terms. Certainty as to the time when presentment occurred was required for the application of other rules of the draft Convention (e.g. to ascertain the commencement of the time period within which protest for dishonour must be made: articles 54(1)(a) and 57(2)).

117. The Working Group decided that article 51(h) should be re-drafted with a view to providing that an instrument may be presented at a clearing-house when under the law of the place of the clearing-house or under the rules of the clearing-house such presentment constituted due presentment. However, the re-drafted article should not restrict the practice in some States under which instruments were presented to the drawer or acceptor through a clearing-house.

#### **Q. Article 66(2), (3): rate of interest recoverable**

118. The Working Group decided not to consider the rate of interest recoverable under article 66, as it was of the view that it was appropriate to decide this issue only at a future session of the Commission, or at a Diplomatic Conference which would consider the draft Convention.

#### **R. Article 68(3): "ius tertii"**

119. The Working Group considered a proposal made during the discussion in the Commission that article 68(3) should provide that, if the payer was notified of the claim of a third party to the instrument, the payer could make payment and be validly discharged unless the third person claiming the instrument provided security deemed adequate by the payer.<sup>18</sup>

120. It was noted that many legal systems provided a mechanism to deal with situations when a party to an instrument was faced with conflicting claims in respect of the instrument (e.g. the party may be permitted to discharge his obligations by depositing the sum claimed in court). Despite difficulties which might sometimes arise in using these mechanisms (e.g. it might be difficult to satisfy time-limits within which action had to be taken), it was preferable to rely on these mechanisms. The Working

Group therefore did not adopt the proposal, and retained article 68(3) in its present wording on the understanding that no serious objections had been raised against the text of article 68(3) during the discussions at the Commission's seventeenth session. There was some support in the Working Group for a new drafting approach to article 68(3).

121. A view was expressed that the changes in the concepts of holder and protected holder decided upon at the thirteenth session of the Working Group required a re-consideration of article 68(3). Because of those changes, it might now be justifiable to give the holder greater rights by limiting the circumstances in which a party who paid a holder was not discharged of liability.

#### **S. Article 68(4)(a): delivery of instrument against payment**

122. The Working Group considered a suggestion that paragraph (4) should be reviewed as to its appropriateness in cases of instruments payable by instalments on successive dates (article 6(b)) and in cases of partial payment (article 69(1)).<sup>19</sup> It was noted that, on the one hand, the payee should not be required to deliver the instrument, and that, on the other hand, the payer needed to be protected in respect of his payment. It was noted that in respect of partial payment effect was already given to these considerations in article 69(5), which provided that the drawee or a party making partial payment may require that mention of the payment be made on the instrument and that a receipt therefore be given to him. It was decided that a provision on those lines should be included in respect of instruments payable by instalments.

#### **T. Article 69(1): partial payment**

123. The Working Group considered the divergent views expressed in the Commission as to the appropriateness of the rule contained in article 69(1).<sup>20</sup> Under one view, the holder should be obliged to take partial payment since that would, at least to some extent, be in the interest of prior parties. Under another view, the holder should not be obliged to take partial payment so as to leave it to the holder, who was entitled to full payment, to decide whether or not to accept partial payment in accordance with his interests and assessment of the risks involved. The Working Group decided that the holder should not be obliged to take partial payment, and retained the article in its present form.

### **Annex**

#### **Draft articles revised by the Commission or the Working Group**

This annex sets forth all modifications to the draft Convention, as found in document A/CN.9/211, irrespective of whether

<sup>18</sup>*Ibid.*, para. 65.

<sup>19</sup>*Ibid.*, para. 81.

<sup>20</sup>*Ibid.*, para. 82.

the modifications were decided by the Commission at its seventeenth session or by the Working Group at its thirteenth or fourteenth session. For ease of reference, the relevant paragraphs of the pertinent report of the Working Group are added.

*Article 1: opening words of paragraphs (2) and (3); new (5)*

(See A/CN.9/273, paras. 67–68)

(2) An international bill of exchange is a written instrument with the heading “International bill of exchange (Convention of ...)” which: ...

(3) An international promissory note is a written instrument with the heading “International promissory note (Convention of ...)” which: ...

(5) *This Convention does not apply to cheques.*

*Article 3*

(See A/CN.9/273, para. 74)

In the interpretation of this Convention, regard is to be had to its international character, the need to promote uniformity in its application and the observance of good faith in international transactions.

*Article 4(7)*

(See A/CN.9/261, paras. 13–14; A/CN.9/273, paras. 22–23)

(7) “Protected holder” means the holder of an instrument which, when he took it, was complete or, if an incomplete instrument within the meaning of article 11(1), was completed in accordance with authority given, provided that, when he became a holder:

(a) He was without knowledge of a claim to or defence upon the instrument referred to in article 25 or of the fact that it was dishonoured by non-acceptance or non-payment; and

(b) The time-limit provided by article 51 for presentment of that instrument for payment had not expired.

*Article 4(11)*

(See A/CN.9/273, paras. 88–92)

(11) “Money” or “currency” includes a monetary unit of account which is established by an intergovernmental institution or by agreement between two or more States.

*Article 11(2)*

(See A/CN.9/273, paras. 101–102)

(2) When such an instrument is completed *without authority or otherwise than in accordance with the authority given*:

(a) A party who signed the instrument before the completion may invoke *such lack of authority* as a defence against a holder who had knowledge of such lack of authority when he became a holder;

(b) ...

*Article 16*

(See A/CN.9/273, para. 104)

When the drawer or the maker has inserted in the *instrument* such words as “not negotiable”, “not transferable”, “not to order”, “pay (X) only”, or words of similar import, *the instrument may not be transferred except for purposes of collection.*

*Article 20, new (3)*

(See A/CN.9/273, paras. 105–106)

(3) *When an endorsement contains the words “not negotiable”, “not transferable”, “not to order”, “pay (X) only”, or words of similar import, the instrument may not be transferred further except for purposes of collection.*

*Article 23*

(See A/CN.9/261, paras. 38–39; A/CN.9/273, para. 35)

(1) If an endorsement is forged, *the person whose endorsement is forged or any party who signed the instrument before the forgery has the right to recover compensation* for any damage that he may have suffered because of the forgery against:

(a) The forger,

(b) The person to whom the instrument was directly transferred by the forger,

(c) *A party or the drawee who paid the instrument directly to the forger.*

(2) *However, an endorsee for collection shall not be liable under paragraph (1) if, at the later of:*

(a) *The time he receives the proceeds of the instrument or*

(b) *The time at which he accounts to his principal for them,*

*he was without knowledge of the forgery, provided that such absence of knowledge was not due to his negligence.*

(3) *Also, a party or the drawee who pays an instrument shall not be liable under paragraph (1) if, at the time he paid the instrument, he was without knowledge of the forgery, provided that such absence of knowledge was not due to his negligence.*

(4) *Except as against the forger, the damages recoverable under paragraph (1) may not exceed the amount referred to in article 66 or 67.*

*Article 23 bis*

(See A/CN.9/261, paras. 47–48; A/CN.9/273, para. 35)

(1) *If an endorsement is made by an agent without authority or power to bind his principal in the matter, the principal or any party who signed the instrument before such endorsement has the right to recover compensation for any damage that he may have suffered because of such endorsement against:*

(a) The agent,

(b) *The person to whom the instrument was directly transferred by the agent,*

(c) *A party or the drawee who paid the instrument directly to the agent.*



(2) However, an endorsee for collection shall not be liable under paragraph (1) if, at the later of:

- (a) The time he receives the proceeds of the instrument or
- (b) The time at which he accounts to his principal for them,

he was without knowledge that the endorsement did not bind the principal, provided that such absence of knowledge was not due to his negligence.

(3) Also, a party or the drawee who pays an instrument shall not be liable under paragraph (1) if, at the time he paid the instrument, he was without knowledge that the endorsement did not bind the principal, provided that such absence of knowledge was not due to his negligence.

(4) Except as against the agent, the damages recoverable under paragraph (1) may not exceed the amount referred to in article 66 or 67.

Article 25, new (2 bis), (3)

(See A/CN.9/261, paras. 18–19; A/CN.9/273, para. 24)

(2 bis) A holder who is not a protected holder is subject to a defence under paragraph (1)(b) or to a claim under paragraph (2) of this article only if he took the instrument with knowledge of such defence or claim or if he obtained the instrument by fraud or participated at any time in a fraud affecting it.

(3) A party may not raise as a defence against a holder who is not a protected holder the fact that a third person has a claim to the instrument unless:

- (a) Such third person asserted a valid claim to the instrument; or
- (b) Such holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery.

Article 26(1)(a)

(See A/CN.9/273, para. 10)

(1) A party may not set up against a protected holder any defence except:

- (a) Defences under articles 29(1), 30, 31(1), 32(3), 49, 53, 59 and 80 of this Convention;

Article 27

(See A/CN.9/273, paras. 26–27)

(1) The transfer of an instrument by a protected holder vests in any subsequent holder the rights to and upon the instrument which the protected holder had.

(2) Such rights are not vested in a subsequent holder if:

- (a) He participated in a transaction which gives rise to a claim to, or a defence upon, the instrument;
- (b) He has previously been a holder, but not a protected holder.

Article 34(2)

(See A/CN.9/273, para. 109)

(2) The drawer may exclude or limit his own liability for acceptance or for payment by an express stipulation on the bill. Such stipulation has effect only with respect to the drawer. A stipulation excluding or limiting liability for payment is operative only if another party is or becomes liable on the bill.

Article 41

(See A/CN.9/273, paras. 38–58)

(1) Unless otherwise agreed, a person who transfers an instrument represents to the holder to whom he transfers the instrument that:

- (a) The instrument does not bear any forged or unauthorized signature;
- (b) The instrument has not been materially altered;
- (c) At the time of transfer, he has no knowledge of any fact which would impair the right of the transferee to payment of the instrument against the acceptor or, in the case of an unaccepted bill, the drawer, or against the maker of a note.

(2) Liability of the transferor under paragraph (1) is incurred only if the transferee took the instrument without knowledge of the matter giving rise to such liability.

(3) Where the transferor is liable under paragraph (1), the transferee may recover, even before maturity, the amount paid by him to the transferor, plus interest calculated at the rate of ..., upon return of the instrument.

Article 42, new (6)

(See A/CN.9/273, para. 110)

(6) A guarantor may not raise as a defence to his liability the fact that he signed the instrument before it was signed by the person for whose account he is a guarantor, or while the instrument was incomplete.

Article 46

(See A/CN.9/273, paras. 112–113)

(1) The drawer may stipulate on the bill that it must not be presented for acceptance before a specified date or before the occurrence of a specified event. Except where a bill must be presented for acceptance under article 45(2), the drawer may stipulate that it must not be presented for acceptance.

(2) If a bill is presented for acceptance notwithstanding a stipulation permitted under paragraph (1) and acceptance is refused, the drawer, the endorser, and their guarantors are not liable for dishonour by non-acceptance.

Article 51(h)

(See A/CN.9/273, para. 117)

(h) An instrument which is presented at a clearing-house is duly presented for payment if the law of the place where the clearing-house is located or the rules or customs of that clearing-house so provide.

*Article 52(2)(a)*

(See A/CN.9/273, para. 107)

## (2) Presentment for payment is dispensed with:

(a) If the drawer, an endorser or guarantor *has expressly waived* presentment; such waiver: ...*Article 58(2)(a)*

(See A/CN.9/273, para. 107)

## (2) Protest for dishonour by non-acceptance or by non-payment is dispensed with:

(a) If the drawer, an endorser or guarantor *has expressly waived* protest; such waiver: ...*Article 63(2)(b)*

(See A/CN.9/273, para. 107)

## (2) Notice of dishonour is dispensed with:

(a) ...

(b) If the drawer, an endorser or guarantor *has expressly waived* notice of dishonour; such waiver: ...*Article 68(4), new (a bis)*

(See A/CN.9/273, para. 122)

(a bis) *In the case of an instrument payable by instalments at successive dates, the drawee or a party making a payment, other than payment of the last instalment, may require that mention of such payment be made on the instrument and that a receipt therefor be given to him.**Article 71, new (1 bis)*

(See A/CN.9/273, para. 91)

(1 bis) *When the amount of an instrument is expressed in a monetary unit of account within the meaning of article 4(11) and does not specify a currency of payment, the instrument is to be paid in the currency of the place of payment. However, this provision does not apply if, between the person making the payment and the person receiving it, the unit of account is transferable.*

**2. Draft Convention on International Bills of Exchange and International Promissory Notes: text of draft articles as revised by the Commission at its seventeenth session or by the Working Group on International Negotiable Instruments at its thirteenth or fourteenth session: note by the secretariat (A/CN.9/274)**

[Original: Chinese, English, French, Russian and Spanish]<sup>a</sup>

This note contains a consolidation of the 1981 draft text set forth in document A/CN.9/211 and the revised draft articles set forth in the annex to document A/CN.9/273. Incorporated are thus all modifications decided by the Commission at its seventeenth session or by the Working Group on International Negotiable Instruments at its thirteenth or fourteenth session. It should be noted that, apart from these modifications adopted by the Commission or the Working Group, there are a number of issues and proposals which the Working Group invited the Commission to consider at its nineteenth session and which are not incorporated in this note. Matters of this kind are, for example, suggestions for inclusion of new provisions (e.g. covering instruments with floating rates of interest; see A/CN.9/273, paras. 93–97) or proposals for redrafting accompanied by alternative wordings (e.g. on article 26(1)(b); see A/CN.9/273, paras. 11–19) or other submissions for possible consideration by the Commission at its nineteenth session (e.g. questions relating to article 2; see A/CN.9/273, paras. 69–71).

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

**Draft Convention on International Bills of Exchange and International Promissory Notes**

**Chapter I. Sphere of application and form of the instrument**

*Article 1*

(1) This Convention applies to international bills of exchange and to international promissory notes.

(2) An international bill of exchange is a written instrument with the heading “International bill of exchange (Convention of ...)” which:

(a) Contains, in the text thereof, the words “international bill of exchange (Convention of ...)”;

(b) Contains an unconditional order whereby the drawer directs the drawee to pay a definite sum of money to the payee or to his order;

(c) Is payable on demand or at a definite time;

(d) Is dated;

(e) Shows that at least two of the following places are situated in different States:

- (i) The place where the bill is drawn;
- (ii) The place indicated next to the signature of the drawer;
- (iii) The place indicated next to the name of the drawee;
- (iv) The place indicated next to the name of the payee;
- (v) The place of payment;
- (f) Is signed by the drawer.

(3) An international promissory note is a written instrument with the heading "International promissory note (Convention of ...)" which:

- (a) Contains, in the text thereof, the words "international promissory note (Convention of ...)";
- (b) Contains an unconditional promise whereby the maker undertakes to pay a definite sum of money to the payee or to his order;
- (c) Is payable on demand or at a definite time;
- (d) Is dated;
- (e) Shows that at least two of the following places are situated in different States:
  - (i) The place where the note is made;
  - (ii) The place indicated next to the signature of the maker;
  - (iii) The place indicated next to the name of the payee;
  - (iv) The place of payment;
- (f) Is signed by the maker.

(4) Proof that the statements referred to in paragraph (2)(e) or (3)(e) of this article are incorrect does not affect the application of this Convention.

(5) This Convention does not apply to cheques.

#### Article 2

This Convention applies without regard to whether the places indicated on an international bill of exchange or on an international promissory note pursuant to paragraph (2)(e) or (3)(e) of article 1 are situated in Contracting States.

## Chapter II. Interpretation

### Section 1. General provisions

#### Article 3

In the interpretation of this Convention, regard is to be had to its international character, the need to promote

uniformity in its application and the observance of good faith in international transactions.

#### Article 4

In this Convention:

- (1) "Bill" means an international bill of exchange governed by this Convention;
- (2) "Note" means an international promissory note governed by this Convention;
- (3) "Instrument" means a bill or a note;
- (4) "Drawee" means the person on whom a bill is drawn but who has not accepted it;
- (5) "Payee" means the person in whose favour the drawer directs payment to be made or to whom the maker promises to pay;
- (6) "Holder" means a person in possession of an instrument in accordance with article 14;
- (7) "Protected holder" means the holder of an instrument which, when he took it, was complete or, if an incomplete instrument within the meaning of article 11(1), was completed in accordance with authority given, provided that, when he became a holder:
  - (a) He was without knowledge of a claim to or defence upon the instrument referred to in article 25 or of the fact that it was dishonoured by non-acceptance or non-payment; and
  - (b) The time-limit provided by article 51 for presentment of that instrument for payment had not expired;
- (8) "Party" means any person who has signed an instrument as drawer, maker, acceptor, endorser or guarantor;
- (9) "Maturity" means the date of payment referred to in article 8;
- (10) "Signature" includes a signature by stamp, symbol, facsimile, perforation or other mechanical means\* and "forged signature" includes a signature by the wrongful or unauthorized use of such means;
- (11) "Money" or "currency" includes a monetary unit of account which is established by an intergovernmental institution or by agreement between two or more States.

\*[Article (X) A Contracting State whose legislation requires that a signature on an instrument be handwritten may, at the time of signature, ratification or accession, make a declaration to the effect that a signature placed on an instrument in its territory must be handwritten.]

### Article 5

For the purposes of this Convention, a person is considered to have knowledge of a fact if he has actual knowledge of that fact or could not have been unaware of its existence.

## Section 2. Interpretation of formal requirements

### Article 6

The sum payable by an instrument is deemed to be a definite sum although the instrument states that it is to be paid:

- (a) With interest;
- (b) By instalments at successive dates;
- (c) By instalments at successive dates with the stipulation on the instrument that upon default in payment of any instalment the unpaid balance becomes due;
- (d) According to a rate of exchange indicated on the instrument or to be determined as directed by the instrument; or
- (e) In a currency other than the currency in which the amount of the instrument is expressed.

### Article 7

- (1) If there is a discrepancy between the amount of the instrument expressed in words and the amount expressed in figures, the amount of the instrument is the amount expressed in words.
- (2) If the amount of the instrument is expressed in a currency having the same description as that of at least one other State than the State where payment is to be made as indicated on the instrument and the specified currency is not identified as the currency of any particular State, the currency is to be considered as the currency of the State where payment is to be made.
- (3) If any instrument states that it is to be paid with interest, without specifying the date from which interest is to run, interest runs from the date of the instrument.
- (4) A stipulation stating that the sum is to be paid with interest is deemed not to have been written on the instrument unless it indicates the rate at which interest is to be paid.

### Article 8

- (1) An instrument is deemed to be payable on demand:
  - (a) If it states that it is payable at sight or on demand or on presentment or if it contains words of similar import; or
  - (b) If no time for payment is expressed.
- (2) An instrument payable at a definite time which is accepted or endorsed or guaranteed after maturity is an

instrument payable on demand as regards the acceptor, the endorser or the guarantor.

- (3) An instrument is deemed to be payable at a definite time if it states that it is payable:
  - (a) On a stated date or at a fixed period after a stated date or at a fixed period after the date of the instrument; or
  - (b) At a fixed period after sight; or
  - (c) By instalments at successive dates; or
  - (d) By instalments at successive dates with the stipulation on the instrument that upon default in payment of any instalment the unpaid balance becomes due.
- (4) The time of payment of an instrument payable at a fixed period after date is determined by reference to the date of the instrument.
- (5) The maturity of a bill payable at a fixed period after sight is determined by the date of the acceptance.
- (6) The maturity of an instrument payable on demand is the date on which the instrument is presented for payment.
- (7) The maturity of a note payable at a fixed period after sight is determined by the date of the visa signed by the maker on the note or, if signature is refused, from the date of presentment.
- (8) Where an instrument is drawn, or made, payable at one or more months after a stated date or after the date of the instrument or after sight, the instrument matures on the corresponding date of the month when payment must be made. If there is no corresponding date, the instrument matures on the last day of that month.

### Article 9

- (1) A bill may:
  - (a) Be drawn upon two or more drawees;
  - (b) Be drawn by two or more drawers;
  - (c) Be payable to two or more payees.
- (2) A note may:
  - (a) Be made by two or more makers;
  - (b) Be payable to two or more payees.
- (3) If an instrument is payable to two or more payees in the alternative, it is payable to any one of them and any one of them in possession of the instrument may exercise the rights of a holder. In any other case the instrument is payable to all of them and the rights of a holder can only be exercised by all of them.

### Article 10

- A bill may:
- (a) Be drawn by the drawer on himself;
  - (b) Be drawn payable to his order.

**Section 3. Completion of an incomplete instrument***Article 11*

(1) An incomplete instrument which satisfies the requirements set out in subparagraphs (a) and (f) of paragraph (2) or (a) and (f) of paragraph (3) of article 1 but which lacks other elements pertaining to one or more of the requirements set out in paragraph (2) or (3) of article 1 may be completed and the instrument so completed is effective as a bill or a note.

(2) When such an instrument is completed without authority or otherwise than in accordance with the authority given:

(a) A party who signed the instrument before the completion may invoke such lack of authority as a defence against a holder who had knowledge of such lack of authority when he became a holder;

(b) A party who signed the instrument after the completion is liable according to the terms of the instrument so completed.

**Chapter III. Transfer***Article 12*

An instrument is transferred:

(a) By endorsement and delivery of the instrument by the endorser to the endorsee; or

(b) By mere delivery of the instrument if the last endorsement is in blank.

*Article 13*

(1) An endorsement must be written on the instrument or on a slip affixed thereto ("*allonge*"). It must be signed.

(2) An endorsement may be:

(a) In blank, that is, by a signature alone or by a signature accompanied by a statement to the effect that the instrument is payable to a person in possession thereof;

(b) Special, by a signature accompanied by an indication of the person to whom the instrument is payable.

*Article 14*

(1) A person is a holder if he is:

(a) The payee in possession of the instrument; or

(b) In possession of an instrument which has been endorsed to him, or on which the last endorsement is in blank, and on which there appears an uninterrupted series of endorsements, even if any of the endorsements was forged or was signed by an agent without authority.

(2) When an endorsement in blank is followed by another endorsement, the person who signed this last

endorsement is deemed to be an endorsee by the endorsement in blank.

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

*Article 15*

The holder of an instrument on which the last endorsement is in blank may:

(a) Further endorse the instrument either in blank or to a specified person; or

(b) Convert the blank endorsement into a special endorsement by indicating therein that the instrument is payable to himself or to some other specified person; or

(c) Transfer the instrument in accordance with paragraph (b) of article 12.

*Article 16*

When the drawer or the maker has inserted in the instrument such words as "not negotiable", "not transferable", "not to order", "pay (X) only", or words of similar import, the instrument may not be transferred except for purposes of collection.

*Article 17*

(1) An endorsement must be unconditional.

(2) A conditional endorsement transfers the instrument whether or not the condition is fulfilled.

*Article 18*

An endorsement in respect of a part of the sum due under the instrument is ineffective as an endorsement.

*Article 19*

When there are two or more endorsements, it is presumed, unless the contrary is established, that each endorsement was made in the order in which it appears on the instrument.

*Article 20*

(1) When an endorsement contains the words "for collection", "for deposit", "value in collection", "by procuration", "pay any bank", or words of similar import, authorizing the endorsee to collect the instrument (endorsement for collection), the endorsee:

(a) May only endorse the instrument for purposes of collection;

(b) May exercise all the rights arising out of the instrument;

(c) Is subject to all claims and defences which may be set up against the endorser.

(2) The endorser for collection is not liable upon the instrument to any subsequent holder.

(3) When an endorsement contains the words "not negotiable", "not transferable", "not to order", "pay (X) only", or words of similar import, the instrument may not be transferred further except for purposes of collection.

#### Article 21

The holder of an instrument may transfer it to a prior party or the drawee in accordance with article 12; nevertheless, in the case where the transferee was a prior holder of the instrument, no endorsement is required and any endorsement which would prevent him from qualifying as a holder may be struck out.

#### Article 22

An instrument may be transferred in accordance with article 12 after maturity, except by the drawee, the acceptor or the maker.

#### Article 23

(1) If an endorsement is forged, the person whose endorsement is forged or any party who signed the instrument before the forgery has the right to recover compensation for any damage that he may have suffered because of the forgery against:

- (a) The forger;
- (b) The person to whom the instrument was directly transferred by the forger;
- (c) A party or the drawee who paid the instrument directly to the forger.

(2) However, an endorsee for collection shall not be liable under paragraph (1) if, at the later of:

- (a) The time he receives the proceeds of the instrument or
- (b) The time at which he accounts to his principal for them,

he was without knowledge of the forgery, provided that such absence of knowledge was not due to his negligence.

(3) Also, a party or the drawee who pays an instrument shall not be liable under paragraph (1) if, at the time he paid the instrument, he was without knowledge of the forgery, provided that such absence of knowledge was not due to his negligence.

(4) Except as against the forger, the damages recoverable under paragraph (1) may not exceed the amount referred to in article 66 or 67.

#### Article 23 bis

(1) If an endorsement is made by an agent without authority or power to bind his principal in the matter, the principal or any party who signed the instrument before

such endorsement has the right to recover compensation for any damage that he may have suffered because of such endorsement against:

- (a) The agent;
- (b) The person to whom the instrument was directly transferred by the agent;
- (c) A party or the drawee who paid the instrument directly to the agent.

(2) However, an endorsee for collection shall not be liable under paragraph (1) if, at the later of:

- (a) The time he receives the proceeds of the instrument or
- (b) The time at which he accounts to his principal for them,

he was without knowledge that the endorsement did not bind the principal, provided that such absence of knowledge was not due to his negligence.

(3) Also, a party or the drawee who pays an instrument shall not be liable under paragraph (1) if, at the time he paid the instrument, he was without knowledge that the endorsement did not bind the principal, provided that such absence of knowledge was not due to his negligence.

(4) Except as against the agent, the damages recoverable under paragraph (1) may not exceed the amount referred to in article 66 or 67.

### Chapter IV. Rights and Liabilities

#### Section 1. The rights of a holder and of a protected holder

##### Article 24

(1) The holder of an instrument has all the rights conferred on him by this Convention against the parties to the instrument.

(2) The holder is entitled to transfer the instrument in accordance with article 12.

##### Article 25

(1) A party may set up against a holder who is not a protected holder:

- (a) Any defence available under this Convention;
- (b) Any defence based on an underlying transaction between himself and the drawer or a previous holder or arising from the circumstances as a result of which he became a party;
- (c) Any defence to contractual liability based on a transaction between himself and the holder;
- (d) Any defence based on incapacity of such party to incur liability on the instrument or on the fact that such

party signed without knowledge that his signature made him a party to the instrument, provided that such absence of knowledge was not due to his negligence.

(2) The rights to an instrument of a holder who is not a protected holder are subject to any valid claim to the instrument on the part of any person.

(2 *bis*) A holder who is not a protected holder is subject to a defence under paragraph (1)(b) or to a claim under paragraph (2) of this article only if he took the instrument with knowledge of such defence or claim or if he obtained the instrument by fraud or participated at any time in a fraud affecting it.

(3) A party may not raise as a defence against a holder who is not a protected holder the fact that a third person has a claim to the instrument unless:

(a) Such third person asserted a valid claim to the instrument; or

(b) Such holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery.

#### Article 26

(1) A party may not set up against a protected holder any defence except:

(a) Defences under articles 29(1), 30, 31(1), 32(3), 49, 53, 59 and 80 of this Convention;

(b) Defences based on the underlying transaction between himself and such holder or arising from any fraudulent act on the part of such holder in obtaining the signature on the instrument of that party;

(c) Defences based on the incapacity of such party to incur liability on the instrument or on the fact that such party signed without knowledge that his signature made him a party to the instrument, provided that such absence of knowledge was not due to his negligence.

(2) The rights to an instrument of a protected holder are not subject to any claim to the instrument on the part of any person, except a valid claim arising from the underlying transaction between himself and the person by whom the claim is raised or arising from any fraudulent act on the part of such holder in obtaining the signature on the instrument of that person.

#### Article 27

(1) The transfer of an instrument by a protected holder vests in any subsequent holder the rights to and upon the instrument which the protected holder had.

(2) Such rights are not vested in a subsequent holder if:

(a) He participated in a transaction which gives rise to a claim to, or a defence upon, the instrument;

(b) He has previously been a holder, but not a protected holder.

#### Article 28

Every holder is presumed to be a protected holder unless the contrary is proved.

### Section 2. The liability of the parties

#### A. General provisions

#### Article 29

(1) Subject to the provisions of articles 30 and 32, a person is not liable on an instrument unless he signs it.

(2) A person who signs an instrument in a name which is not his own is liable as if he had signed it in his own name.

#### Article 30

A forged signature on an instrument does not impose any liability thereon on the person whose signature was forged. Nevertheless, such person is liable as if he had signed the instrument himself where he has, expressly or impliedly, accepted to be bound by the forged signature or represented that the signature was his own.

#### Article 31

(1) If an instrument has been materially altered:

(a) Parties who have signed the instrument subsequent to the material alteration are liable thereon according to the terms of the altered text;

(b) Parties who have signed the instrument before the material alteration are liable thereon according to the terms of the original text. Nevertheless a party who has himself made, authorized, or assented to, the material alteration is liable on the instrument according to the terms of the altered text.

(2) Failing proof to the contrary, a signature is deemed to have been placed on the instrument after the material alteration.

(3) Any alteration is material which modifies the written undertaking on the instrument of any party in any respect.

#### Article 32

(1) An instrument may be signed by an agent.

(2) The signature of an agent placed by him on an instrument with the authority of his principal and showing on the instrument that he is signing in a representative capacity for that named principal, or the signature of a principal placed on the instrument by an agent with his authority, imposes liability on the principal and not on the agent.

(3) A signature placed on an instrument by a person as agent but without authority to sign or exceeding his authority, or by an agent with authority to sign but not showing on the instrument that he is signing in a

representative capacity for a named person, or showing on the instrument that he is signing in a representative capacity but not naming the person whom he represents, imposes liability thereon on the person signing and not on the person whom he purports to represent.

(4) The question whether a signature was placed on the instrument in a representative capacity may be determined only by reference to what appears on the instrument.

(5) A person who is liable pursuant to paragraph (3) and who pays the instrument has the same rights as the person for whom he purported to act would have had if that person had paid the instrument.

#### *Article 33*

The order to pay contained in a bill does not of itself operate as an assignment to the payee of funds made available for payment by the drawer with the drawee.

#### *B. The drawer*

##### *Article 34*

(1) The drawer engages that upon dishonour of the bill by non-acceptance or non-payment, and upon any necessary protest, he will pay to the holder, or to any subsequent party who pays the bill in accordance with article 66, the amount of the bill, and any interest and expenses which may be recovered under article 66 or 67.

(2) The drawer may exclude or limit his own liability for acceptance or for payment by an express stipulation on the bill. Such stipulation has effect only with respect to the drawer. A stipulation excluding or limiting liability for payment is operative only if another party is or becomes liable on the bill.

#### *C. The maker*

##### *Article 35*

(1) The maker engages that he will pay to the holder, or to any party who pays the note in accordance with article 66, the amount of the note in accordance with the terms of that note, and any interest and expenses which may be recovered under article 66 or 67.

(2) The maker may not exclude or limit his own liability by a stipulation on the note. Any such stipulation is without effect.

#### *D. The drawee and the acceptor*

##### *Article 36*

(1) The drawee is not liable on a bill until he accepts it.

(2) The acceptor engages that he will pay to the holder, or to any party who pays the bill in accordance with

article 66, the amount of the bill in accordance with the terms of his acceptance, and any interest and expenses which may be recovered under article 66 or 67.

##### *Article 37*

An acceptance must be written on the bill and may be effected:

- (a) By the signature of the drawee accompanied by the word "accepted" or by words of similar import; or
- (b) By the signature alone of the drawee.

##### *Article 38*

(1) An incomplete instrument which satisfies the requirements set out in article 1(2)(a) may be accepted by the drawee before it has been signed by the drawer, or while otherwise incomplete.

(2) A bill may be accepted before, at or after maturity, or after it has been dishonoured by non-acceptance or non-payment.

(3) When a bill drawn payable at a fixed period after sight, or a bill which must be presented for acceptance before a specified date, is accepted, the acceptor must indicate the date of his acceptance; failing such indication by the acceptor, the drawer or the holder may insert the date of acceptance.

(4) If a bill drawn payable at a fixed period after sight is dishonoured by non-acceptance and the drawee subsequently accepts it, the holder is entitled to have the acceptance dated as of the date on which the bill was dishonoured.

##### *Article 39*

(1) An acceptance must be unqualified. An acceptance is qualified if it is conditional or varies the terms of the bill.

(2) If the drawee stipulates on the bill that his acceptance is subject to qualification:

- (a) He is nevertheless bound according to the terms of his qualified acceptance;
- (b) The bill is dishonoured by non-acceptance.

(3) An acceptance relating to only a part of the amount of the bill is a qualified acceptance. If the holder takes such an acceptance, the bill is dishonoured by non-acceptance only as to the remaining part.

(4) An acceptance indicating that payment will be made at a particular address or by a particular agent is not a qualified acceptance, provided that:

- (a) The place in which payment is to be made is not changed;
- (b) The bill is not drawn payable by another agent.



E. *The endorser**Article 40*

(1) The endorser engages that upon dishonour of the instrument by non-acceptance or non-payment, and upon any necessary protest, he will pay to the holder, or to any subsequent party who pays the instrument in accordance with article 66, the amount of the instrument, and any interest and expenses which may be recovered under article 66 or 67.

(2) The endorser may exclude or limit his own liability by an express stipulation on the instrument. Such stipulation has effect only with respect to that endorser.

*Article 41*

(1) Unless otherwise agreed, a person who transfers an instrument represents to the holder to whom he transfers the instrument that:

- (a) The instrument does not bear any forged or unauthorized signature;
- (b) The instrument has not been materially altered;
- (c) At the time of transfer, he has no knowledge of any fact which would impair the right of the transferee to payment of the instrument against the acceptor or, in the case of an unaccepted bill, the drawer, or against the maker of a note.

(2) Liability of the transferor under paragraph (1) is incurred only if the transferee took the instrument without knowledge of the matter giving rise to such liability.

(3) Where the transferor is liable under paragraph (1), the transferee may recover, even before maturity, the amount paid by him to the transferor, plus interest calculated at the rate of ..., upon return of the instrument.

F. *The guarantor**Article 42*

(1) Payment of an instrument, whether or not it has been accepted, may be guaranteed, as to the whole or part of its amount, for the account of a party or the drawee. A guarantee may be given by any person who may or may not already be a party.

(2) A guarantee must be written on the instrument or on a slip affixed thereto ("*allonge*").

(3) A guarantee is expressed by the words "guaranteed", "*aval*", "good as *aval*" or words of similar import, accompanied by the signature of the guarantor.

(4) A guarantee may be effected by a signature alone. Unless the content otherwise requires:

(a) A signature alone on the front of the instrument, other than that of the drawer or the drawee, is a guarantee;

(b) The signature alone of the drawee on the front of the instrument is an acceptance; and

(c) A signature alone on the back of the instrument other than that of the drawee is an endorsement.

(5) A guarantor may specify the person for whom he has become guarantor. In the absence of such specification, the person for whom he has become guarantor is the acceptor or the drawee in the case of a bill, and the maker in the case of a note.

(6) A guarantor may not raise as a defence to his liability the fact that he signed the instrument before it was signed by the person for whose account he is a guarantor, or while the instrument was incomplete.

*Article 43*

(1) A guarantor is liable on the instrument to the same extent as the party for whom he has become guarantor, unless the guarantor has stipulated otherwise on the instrument.

(2) If the person for whom he has become guarantor is the drawee, the guarantor undertakes to pay the bill at maturity.

*Article 44*

The guarantor who pays the instrument has rights thereon against the party for whom he became guarantor and against parties who are liable thereon to that party.

**Chapter V. Presentment, dishonour by non-acceptance or non-payment, and recourse****Section 1. Presentment for acceptance and dishonour by non-acceptance***Article 45*

(1) A bill may be presented for acceptance.

(2) A bill must be presented for acceptance:

(a) When the drawer has stipulated on the bill that it must be presented for acceptance;

(b) When the bill is drawn payable at a fixed period after sight; or

(c) When the bill is drawn payable elsewhere than at the residence or place of business of the drawee, except where such a bill is payable on demand.

*Article 46*

(1) The drawer may stipulate on the bill that it must not be presented for acceptance before a specified date

or before the occurrence of a specified event. Except where a bill must be presented for acceptance under article 45(2), the drawer may stipulate that it must not be presented for acceptance.

(2) If a bill is presented for acceptance notwithstanding a stipulation permitted under paragraph (1) and acceptance is refused, the drawer, the endorser, and their guarantors are not liable for dishonour by non-acceptance.

(3) If the drawee accepts a bill notwithstanding a stipulation that it must not be presented for acceptance, the acceptance is effective.

#### Article 47

A bill is duly presented for acceptance if it is presented in accordance with the following rules:

(a) The holder must present the bill to the drawee on a business day at a reasonable hour;

(b) A bill drawn upon two or more drawees may be presented to any one of them, unless the bill clearly indicates otherwise;

(c) Presentment for acceptance may be made to a person or authority other than the drawee if that person or authority is entitled under the applicable law to accept the bill;

(d) If a bill is drawn payable on a fixed date, presentment for acceptance must be made before or on the date of maturity;

(e) A bill drawn payable on demand or at a fixed period after sight must be presented for acceptance within one year of its date;

(f) A bill in which the drawer has stated a date or time-limit for presentment for acceptance must be presented on the stated date or within the stated time-limit.

#### Article 48

A necessary or optional presentment for acceptance is dispensed with:

(a) If the drawee is dead or has no longer the power freely to deal with his assets by reason of his insolvency, or is a fictitious person or a person not having capacity to incur liability on the instrument as an acceptor, or if the drawee is a corporation, partnership, association or other legal entity which has ceased to exist;

(b) When, with reasonable diligence, presentment cannot be effected within the time-limits prescribed for presentment for acceptance.

#### Article 49

If a bill which must be presented for acceptance is not so presented, the drawer, the endorsers and their guarantors are not liable on the bill.

#### Article 50

(1) A bill is considered to be dishonoured by non-acceptance:

(a) When the drawee, upon due presentment, expressly refuses to accept the bill or acceptance cannot be obtained with reasonable diligence or when the holder cannot obtain the acceptance to which he is entitled under this Convention;

(b) If presentment for acceptance is dispensed with pursuant to article 48, unless the bill is in fact accepted.

(2) If a bill is dishonoured by non-acceptance the holder may:

(a) Subject to the provisions of article 55, exercise an immediate right of recourse against the drawer, the endorsers and their guarantors;

(b) Exercise an immediate right of recourse against the guarantor of the drawee.

### Section 2. Presentment for payment and dishonour by non-payment

#### Article 51

An instrument is duly presented for payment if it is presented in accordance with the following rules:

(a) The holder must present the instrument to the drawee or to the acceptor or to the maker on a business day at a reasonable hour;

(b) A bill drawn upon or accepted by two or more drawees, or a note signed by two or more makers, may be presented to any one of them, unless the instrument clearly indicates otherwise;

(c) If the drawee or the acceptor or the maker is dead, presentment must be made to the persons who under the applicable law are his heirs or the persons entitled to administer his estate;

(d) Presentment for payment may be made to a person or authority other than the drawee, the acceptor or the maker if that person or authority is entitled under the applicable law to pay the instrument;

(e) An instrument which is not payable on demand must be presented for payment on the date of maturity or on the business day which follows;

(f) An instrument which is payable on demand must be presented for payment within one year of its date;

(g) An instrument must be presented for payment:

(i) At the place of payment specified on the instrument; or

(ii) If no place of payment is specified, at the address of the drawee or the acceptor or the maker indicated on the instrument; or

(iii) If no place of payment is specified and the address of the drawee or the acceptor or the maker is not indicated, at the principal place of business or habitual residence of the drawee or the acceptor or the maker;

(h) An instrument which is presented at a clearing-house is duly presented for payment if the law of the place where the clearing-house is located or the rules or customs of that clearing-house so provide.

#### Article 52

(1) Delay in making presentment for payment is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, presentment must be made with reasonable diligence.

(2) Presentment for payment is dispensed with:

(a) If the drawer, an endorser or guarantor has expressly waived presentment; such waiver:

(i) If made on the instrument by the drawer, binds any subsequent party and benefits any holder;

(ii) If made on the instrument by a party other than the drawer, binds only that party but benefits any holder;

(iii) If made outside the instrument, binds only the party making it and benefits only a holder in whose favour it was made;

(b) If an instrument is not payable on demand, and the cause of delay in making presentment continues to operate beyond 30 days after maturity;

(c) If an instrument is not payable on demand, and the cause of delay continues to operate beyond 30 days after the expiration of the time-limit for presentment for payment;

(d) If the drawee, the maker or the acceptor has no longer the power freely to deal with his assets by reason of his insolvency, or is a fictitious person or a person not having capacity to make payment, or if the drawee, the maker or the acceptor is a corporation, partnership, association or other legal entity which has ceased to exist;

(e) If there is no place at which the instrument must be presented in accordance with article 51(g).

(3) Presentment for payment is also dispensed with as regards a bill, if the bill has been protested for dishonour by non-acceptance.

#### Article 53

(1) If a bill is not duly presented for payment, the drawer, the endorsers and their guarantors are not liable thereon.

(2) If a note is not duly presented for payment, the endorsers and their guarantors are not liable thereon.

(3) Failure to present an instrument for payment does not discharge the acceptor or the maker or their guarantors or the guarantor of the drawee of liability thereon.

#### Article 54

(1) An instrument is considered to be dishonoured by non-payment:

(a) When payment is refused upon due presentment or when the holder cannot obtain the payment to which he is entitled under this Convention;

(b) If presentment for payment is dispensed with pursuant to article 52(2) and the instrument is unpaid at maturity.

(2) If a bill is dishonoured by non-payment, the holder may, subject to the provisions of article 55, exercise a right of recourse against the drawer, the endorsers and their guarantors.

(3) If a note is dishonoured by non-payment, the holder may, subject to the provisions of article 55, exercise a right of recourse against the endorsers and their guarantors.

### Section 3. Recourse

#### A. Protest

#### Article 55

If an instrument has been dishonoured by non-acceptance or by non-payment, the holder may exercise a right of recourse only after the instrument has been duly protested for dishonour in accordance with the provisions of articles 56 to 58.

#### Article 56

(1) A protest is a statement of dishonour drawn up at the place where the instrument has been dishonoured and signed and dated by a person authorized in that respect by the law of that place. The statement must specify:

(a) The person at whose request the instrument is protested;

(b) The place of protest; and

(c) The demand made and the answer given, if any, or the fact that the drawee or the acceptor or the maker could not be found.

(2) A protest may be made:

(a) On the instrument itself or on a slip affixed thereto ("*allonge*"); or

(b) As a separate document, in which case it must clearly identify the instrument that has been dishonoured.

(3) Unless the instrument stipulates that protest must be made, a protest may be replaced by a declaration written

on the instrument and signed and dated by the drawee or the acceptor or the maker, or, in the case of an instrument domiciled with a named person for payment, by that named person; the declaration must be to the effect that acceptance or payment is refused.

(4) A declaration made in accordance with paragraph (3) is deemed to be a protest for the purpose of this Convention.

#### Article 57

(1) Protest for dishonour of a bill by non-acceptance must be made on the day on which the bill is dishonoured or on one of the two business days which follow.

(2) Protest for dishonour of an instrument by non-payment must be made on the day on which the instrument is dishonoured or on one of the two business days which follow.

#### Article 58

(1) Delay in protesting an instrument for dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, protest must be made with reasonable diligence.

(2) Protest for dishonour by non-acceptance or by non-payment is dispensed with:

(a) If the drawer, an endorser or guarantor has expressly waived protest; such waiver:

(i) If made on the instrument by the drawer, binds any subsequent party and benefits any holder;

(ii) If made on the instrument by a party other than the drawer, binds only that party but benefits any holder;

(iii) If made outside the instrument, binds only the party making it and benefits only a holder in whose favour it was made;

(b) If the cause of delay under paragraph (1) in making protest continues to operate beyond 30 days after the date of dishonour;

(c) As regards the drawer of a bill, if the drawer and the drawee or the acceptor are the same person;

(d) If presentment for acceptance or for payment is dispensed with in accordance with article 48 or 52(2).

#### Article 59

(1) If a bill which must be protested for non-acceptance or for non-payment is not duly protested, the drawer, the endorsers and their guarantors are not liable thereon.

(2) If a note which must be protested for non-payment is not duly protested, the endorsers and their guarantors are not liable thereon.

(3) Failure to protest an instrument does not discharge the acceptor or the maker or their guarantors or the guarantor of the drawee of liability thereon.

### B. Notice of dishonour

#### Article 60

(1) The holder, upon dishonour of a bill by non-acceptance or by non-payment, must give notice of such dishonour to the drawer, the endorsers and their guarantors.

(2) The holder, upon dishonour of a note by non-payment, must give notice of such dishonour to the endorsers and their guarantors.

(3) An endorser or a guarantor who receives notice must give notice of dishonour to the party immediately preceding him and liable on the instrument.

(4) Notice of dishonour operates for the benefit of any party who has a right of recourse on the instrument against the party notified.

#### Article 61

(1) Notice of dishonour may be given in any form whatever and in any terms which identify the instrument and state that it has been dishonoured. The return of the dishonoured instrument is sufficient notice, provided it is accompanied by a statement indicating that it has been dishonoured.

(2) Notice of dishonour is duly given if it is communicated or sent to the party to be notified by means appropriate in the circumstances, whether or not it is received by that party.

(3) The burden of proving that notice has been duly given rests upon the person who is required to give such notice.

#### Article 62

Notice of dishonour must be given within the two business days which follow:

(a) The day of protest or, if protest is dispensed with, the day of dishonour; or

(b) The receipt of notice given by another party.

#### Article 63

(1) Delay in giving notice of dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

(2) Notice of dishonour is dispensed with:

(a) If after the exercise of reasonable diligence notice cannot be given;

(b) If the drawer, an endorser or guarantor has expressly waived notice of dishonour; such waiver:

(i) If made on the instrument by the drawer, binds any subsequent party and benefits any holder;

(ii) If made on the instrument by a party other than the drawer, binds only that party but benefits any holder;

(iii) If made outside the instrument, binds only the party making it and benefits only a holder in whose favour it was made;

(c) As regards the drawer of the bill, if the drawer and the drawee or the acceptor are the same person.

#### *Article 64*

Failure to give notice of dishonour renders a person who is required to give such notice under article 60 to a party who is entitled to receive such notice liable for any damages which that party may suffer from such failure, provided that such damages do not exceed the amount referred to in article 66 or 67.

### **Section 4. Amount payable**

#### *Article 65*

The holder may exercise his rights on the instrument against any one party, or several or all parties, liable thereon and is not obliged to observe the order in which the parties have become bound.

#### *Article 66*

(1) The holder may recover from any party liable:

(a) At maturity: the amount of the instrument with interest, if interest has been stipulated for;

(b) After maturity:

(i) The amount of the instrument with interest, if interest has been stipulated for, to the date of maturity;

(ii) If interest has been stipulated to be paid after maturity, interest at the rate stipulated, or in the absence of such stipulation, interest at the rate specified in paragraph (2), calculated from the date of presentment on the sum specified in paragraph (1)(b)(i);

(iii) Any expenses of protest and of the notices given by him;

(c) Before maturity:

(i) The amount of the bill with interest, if interest has been stipulated for, to the date of payment, subject to a discount from the date of payment to the date of maturity, calculated in accordance with paragraph (3);

(ii) Any expenses of protest and of the notices given by him.

(2) The rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country where the instrument is payable. If there is no such rate, the rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country in the currency of which the instrument is payable. In the absence of any such rates, the rate of interest shall be [ ] per cent per annum.

(3) The discount shall be at the official rate (discount rate) or other similar appropriate rate effective on the date when recourse is exercised at the place where the holder has his principal place of business, or if he does not have a place of business his habitual residence, or if there is no such rate then at the rate of [ ] per cent per annum.

#### *Article 67*

A party who pays an instrument in accordance with article 66 may recover from the parties liable to him:

(a) The entire sum which he was obliged to pay in accordance with article 66 and has paid;

(b) Interest on that sum at the rate specified in article 66, paragraph (2), from the date on which he made payment;

(c) Any expenses of the notices given by him.

## **Chapter VI. Discharge**

### **Section 1. Discharge by payment**

#### *Article 68*

(1) A party is discharged of liability on the instrument when he pays the holder, or a party subsequent to himself who has paid the instrument and is in possession thereof, the amount due pursuant to article 66 or 67:

(a) At or after maturity; or

(b) Before maturity, upon dishonour by non-acceptance.

(2) Payment before maturity other than under paragraph (1)(b) of this article does not discharge the party making the payment of his liability on the instrument except in respect of the person to whom payment was made.

(3) A party is not discharged of liability if he pays a holder who is not a protected holder and knows at the time of payment that a third person has asserted a valid claim to the instrument or that the holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery.

(4) (a) A person receiving payment of an instrument must, unless agreed otherwise, deliver:

- (i) To the drawee making such payment, the instrument;
- (ii) To any other person making such payment, the instrument, a receipted account, and any protest.

(a bis) In the case of an instrument payable by instalments at successive dates, the drawee or a party making a payment, other than payment of the last instalment, may require that mention of such payment be made on the instrument and that a receipt therefor be given to him.

(b) The person from whom payment is demanded may withhold payment if the person demanding payment does not deliver the instrument to him. Withholding payment in these circumstances does not constitute dishonour by non-payment under article 54.

(c) If payment is made but the person paying, other than the drawee, fails to obtain the instrument, such person is discharged but the discharge cannot be set up as a defence against a protected holder.

#### Article 69

- (1) The holder is not obliged to take partial payment.
- (2) If the holder who is offered partial payment does not take it, the instrument is dishonoured by non-payment.
- (3) If the holder takes partial payment from the drawee or the acceptor or the maker:
  - (a) The acceptor or the maker is discharged of his liability on the instrument to the extent of the amount paid; and
  - (b) The instrument is to be considered as dishonoured by non-payment as to the amount unpaid.
- (4) If the holder takes partial payment from a party to the instrument other than the drawee, the acceptor or the maker:
  - (a) The party making payment is discharged of his liability on the instrument to the extent of the amount paid; and
  - (b) The holder must give such party a certified copy of the instrument and of any authenticated protest.
- (5) The drawee or a party making partial payment may require that mention of such payment be made on the instrument and that a receipt therefor be given to him.
- (6) If the balance is paid, the person who receives it and who is in possession of the instrument must deliver to the payor the receipted instrument and any authenticated protest.

#### Article 70

- (1) The holder may refuse to take payment in a place other than the place where the instrument was presented for payment in accordance with article 51.
- (2) If in such case payment is not made in the place where the instrument was presented for payment in accordance with article 51, the instrument is considered as dishonoured by non-payment.

#### Article 71

- (1) An instrument must be paid in the currency in which the amount of the instrument is expressed.
  - (1 bis) When the amount of an instrument is expressed in a monetary unit of account within the meaning of article 4(11) and does not specify a currency of payment, the instrument is to be paid in the currency of the place of payment. However, this provision does not apply if, between the person making the payment and the person receiving it, the unit of account is transferable.
- (2) The drawer or the maker may indicate on the instrument that it must be paid in a specified currency other than the currency in which the amount of the instrument is expressed. In that case:
  - (a) The instrument must be paid in the currency so specified;
  - (b) The amount payable is to be calculated according to the rate of exchange indicated on the instrument. Failing such indication, the amount payable is to be calculated according to the rate of exchange for sight drafts (or, if there is no such rate, according to the appropriate established rate of exchange) on the date of maturity:
    - (i) Ruling at the place where the instrument must be presented for payment in accordance with article 51(g), if the specified currency is that of that place (local currency); or
    - (ii) If the specified currency is not that of that place, according to the usages of the place where the instrument must be presented for payment in accordance with article 51(g);
  - (c) If such an instrument is dishonoured by non-acceptance, the amount payable is to be calculated:
    - (i) If the rate of exchange is indicated on the instrument, according to that rate;
    - (ii) If no rate of exchange is indicated on the instrument, at the option of the holder, according to the rate of exchange ruling on the date of dishonour or on the date of actual payment;
  - (d) If such an instrument is dishonoured by non-payment, the amount payable is to be calculated:
    - (i) If the rate of exchange is indicated on the instrument, according to that rate;

(ii) If no rate of exchange is indicated on the instrument, at the option of the holder, according to the rate of exchange ruling on the date of maturity or on the date of actual payment.

(3) Nothing in this article prevents a court from awarding damages for loss caused to the holder by reason of fluctuations in rates of exchange if such loss is caused by dishonour for non-acceptance or non-payment.

(4) The rate of exchange ruling at a certain date is the rate of exchange ruling, at the option of the holder, at the place where the instrument must be presented for payment in accordance with article 51(g) or at the place of actual payment.

#### Article 72

(1) Nothing in this Convention prevents a Contracting State from enforcing exchange control regulations applicable in its territory, including regulations which it is bound to apply by virtue of international agreements to which it is a party.

(2) (a) If, by virtue of the application of paragraph (1) of this article, an instrument drawn in a currency which is not that of the place of payment must be paid in local currency, the amount payable is to be calculated according to the rate of exchange for sight drafts (or, if there is no such rate, according to the appropriate established rate of exchange) on the date of presentment ruling at the place where the instrument must be presented for payment in accordance with article 51(g).

(b) (i) If such an instrument is dishonoured by non-acceptance, the amount payable is to be calculated, at the option of the holder, at the rate of exchange ruling on the date of dishonour, or on the date of actual payment.

(ii) If such an instrument is dishonoured by non-payment, the amount is to be calculated, at the option of the holder, according to the rate of exchange ruling on the date of presentment or on the date of actual payment.

(iii) Paragraphs (3) and (4) of article 71 are applicable where appropriate.

### Section 2. Discharge of a prior party

#### Article 73

(1) When a party is discharged wholly or partly of his liability on the instrument, any party who has a right of recourse against him is discharged to the same extent.

(2) Payment by the drawee of the whole or a part of the amount of a bill to the holder, or to any party who has paid the bill in accordance with article 66, discharges all parties of their liability to the same extent.

## Chapter VII. Lost Instruments

### Article 74

(1) When an instrument is lost, whether by destruction, theft or otherwise, the person who lost the instrument has, subject to the provisions of paragraph (2) of this article, the same right to payment which he would have had if he had been in possession of the instrument. The party from whom payment is claimed cannot set up as a defence against liability on the instrument the fact that the person claiming payment is not in possession thereof.

(2) (a) The person claiming payment of a lost instrument must state in writing to the party from whom he claims payment:

(i) The elements of the lost instrument pertaining to the requirements set forth in article 1(2) or 1(3); for this purpose the person claiming payment of the lost instrument may present to that party a copy of that instrument;

(ii) The facts showing that, if he had been in possession of the instrument, he would have had a right to payment from the party from whom payment is claimed;

(iii) The facts which prevent production of the instrument.

(b) The party from whom payment of a lost instrument is claimed may require the person claiming payment to give security in order to indemnify him for any loss which he may suffer by reason of the subsequent payment of the lost instrument.

(c) The nature of the security and its terms are to be determined by agreement between the person claiming payment and the party from whom payment is claimed. Failing such an agreement, the court may determine whether security is called for and, if so, the nature of the security and its terms.

(d) If the security cannot be given, the court may order the party from whom payment is claimed to deposit the amount of the lost instrument, and any interest and expenses which may be claimed under article 66 or 67, with the court or any other competent authority or institution, and may determine the duration of such deposit. Such deposit is to be considered as payment to the person claiming payment.

#### Article 75

(1) A party who has paid a lost instrument and to whom the instrument is subsequently presented for payment by another person must notify the person to whom he paid of such presentment.

(2) Such notification must be given on the day the instrument is presented or on one of the two business days which follow and must state the name of the person presenting the instrument and the date and place of presentment.

(3) Failure to notify renders the party who has paid the lost instrument liable for any damages which the person whom he paid may suffer from such failure, provided that the damages do not exceed the amount referred to in article 66 or 67.

(4) Delay in giving notice is excused when the delay is caused by circumstances which are beyond the control of the person who has paid the lost instrument and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

(5) Notice is dispensed with when the cause of delay in giving notice continues to operate beyond 30 days after the last date on which it should have been given.

#### Article 76

(1) A party who has paid a lost instrument in accordance with the provisions of article 74 and who is subsequently required to, and does, pay the instrument, or who, by reason of the loss of the instrument, then loses his right to recover from any party liable to him, has the right:

- (a) If security was given, to realize the security; or
- (b) If the amount was deposited with the court or other competent authority or institution, to reclaim the amount so deposited.

(2) The person who has given security in accordance with the provisions of paragraph (2)(b) of article 74 is entitled to obtain release of the security when the party for whose benefit the security was given is no longer at risk to suffer loss because of the fact that the instrument is lost.

#### Article 77

A person claiming payment of a lost instrument duly effects protest for dishonour by non-payment by the use of a written statement that satisfies the requirements of article 74, paragraph (2)(a).

### 3. Working paper submitted to the Working Group on International Negotiable Instruments at its fourteenth session – draft Convention on International Bills of Exchange and International Promissory Notes: some considerations and suggestions relating to major controversial issues: note by the secretariat (A/CN.9/WG.IV/WP.30) [Original: English]

1. The Working Group, at its thirteenth session,<sup>1</sup> considered the major controversial issues, namely the concept of holder and protected holder, the effect of forged endorsements and the liability of the transferor by mere delivery or by endorsement. In this connection, it requested the secretariat to consider or study certain questions relating to the major controversial issues and to

<sup>1</sup>Report of the Working Group on International Negotiable Instruments on the work of its thirteenth session (New York, 7–18 January 1985), A/CN.9/261.

#### Article 78

A person receiving payment of a lost instrument in accordance with article 74 must deliver to the party paying the written statement required under article 74, paragraph (2)(a), received by him and any protest and a receipted account.

#### Article 79

(1) A party who has paid a lost instrument in accordance with article 74 has the same rights which he would have had if he had been in possession of the instrument.

(2) Such party may exercise his rights only if he is in possession of the receipted written statement referred to in article 78.

### Chapter VIII. Limitation (prescription)

#### Article 80

(1) A right of action arising on an instrument may no longer be exercised after four years have elapsed:

- (a) Against the maker, or his guarantor, of a note payable on demand, from the date of the note;
- (b) Against the acceptor or the maker or their guarantor of an instrument payable at a definite time, from the date of maturity;
- (c) Against the acceptor of a bill payable on demand, from the date on which it was accepted;
- (d) Against the drawer or an endorser or their guarantor, from the date of protest for dishonour by non-acceptance or non-payment or, where protest is dispensed with, from the date of dishonour.

(2) If a party has paid the instrument in accordance with article 66 or 67 within one year before the expiration of the period referred to in paragraph (1) of this article, such party may exercise his right of action against a party liable to him within one year from the date on which he paid the instrument.

draft or re-draft pertinent provisions.<sup>2</sup> This note has been prepared pursuant to that request.

#### A. Defences available against holder or protected holder; definition of protected holder (A/CN.9/261, paras. 23–26)

1. Article 26(1)(b)

2. The following modification of article 26(1)(b) is suggested:

<sup>2</sup>A/CN.9/261, paras. 26, 39, 48, 59, 63 and 67.



“(1) A party may not set up against a protected holder any defence except:

(a) ....

(b) Defences resulting from a transaction between himself and such holder that would be available as defences against contractual liability or defences arising from any fraudulent act on the part of such holder in obtaining the signature on the instrument of that party;”

3. Under this modified version of subparagraph (b), where the protected holder has dealt with a party, that party may set up against such holder not only defences derived from the transaction between them which gave rise to the issue or transfer of the instrument, but also defences based on another transaction, unrelated to the issue or transfer, provided that the defence is one that may be invoked against contractual liability. The rationale for this rule is that it would prevent circuitry of action. Following this rationale, there may be no need for limiting the modification, as was suggested in the Working Group,<sup>3</sup> to those defences deriving from agreements which were related to the underlying transaction such as agreements for prolongation.

4. Thus, if the maker (A) issued a note of SwF 100 to the payee (P) and P transferred the note to C in payment of a sale of goods transaction between P and C, P could, in a recourse action by C against P upon dishonour of the note by A, set up as a defence to his liability on the note the fact that, for instance, C owed P SwF 100 on account of a loan made by P to C, even though the loan was unrelated to the transfer of the instrument.

5. Therefore, if a defence would be available to P in an action by C based on contract, that defence would also be available to P in an action by C on the note. The question whether any defence and, if so, which ones would be available to P in an action by C based on contract is to be determined by the applicable national law.

#### 2. Article 25(1)(c)

6. If the above suggested modification of article 26(1)(b) were accepted, article 25(1)(c) could be brought into accordance with it as follows:

“(c) Any defence resulting

(i) from the underlying transaction between himself and the holder;

(ii) from any other transaction between himself and the holder that would be available as a defence against contractual liability;”

#### 3. Article 4(7)(a)

7. The following modification of article 4(7)(a) is suggested:

“(7) ‘Protected holder’ means the holder of an instrument which, when he obtained it, was complete or, if

incomplete as referred to in article 11(1), was completed by him in accordance with an agreement entered into, provided that, when he became a holder:<sup>4</sup>

(a) He was without knowledge of a claim to, or defence to liability on, the instrument referred to in article 25, other than in paragraph (1)(c)(ii), or of the fact that it was dishonoured by non-acceptance or non-payment; and”

8. The fact that, when the holder took the instrument, he had knowledge of a defence to liability on the instrument derived from a transaction between himself and the holder unrelated to the issue or transfer of the instrument (i.e. the defence available under the suggested redraft of article 25(1)(c)(ii)) should not prevent the holder from being a protected holder. As a protected holder he would not be subject to the defences available under article 25 but only to those available under article 26.

#### 4. Additional modifications of articles 25 and 26

9. The secretariat suggests modifying article 25(3)(b) as follows:

“(3) A party may not raise as a defence against a holder who is not a protected holder the fact that a third person has a claim to the instrument unless:

(a) ....

(b) Such holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery.”

10. This addition is intended to correct what appears to have been a legislative oversight and to align it with the corresponding “mirror image” provision of article 68(3).

11. The secretariat suggests modifying article 26(1)(a) as follows:

“(1) A party may not set up against a protected holder any defence except:

(a) Defences under articles 29(1), 30, 31(1), 32(3), 49, 53, 59 and 80 of this Convention;”

12. It appears that the reference to article 59, which had been included in an early draft version of article 26(1)(a), was deleted in the context of the draft Convention on International Cheques as being inappropriate in that context and subsequently, for the sake of harmony between the two draft Conventions, also omitted in the draft Convention on International Bills of Exchange and International Promissory Notes. However, it is submitted that failure to make a necessary protest as referred to in article 59 should be a defence against the protected holder of a bill or a note.

<sup>4</sup>The opening words of paragraph (7) are given here in the revised form as adopted by the Working Group at its thirteenth session, A/CN.9/261, paras. 9–14.

<sup>3</sup>A/CN.9/261, para. 25.

**B. Definition of knowledge, article 5 (A/CN.9/261, para. 67)**

13. The following modification of article 5 is suggested:

“For the purposes of this Convention, a person is considered to have knowledge of a fact if he has actual knowledge of that fact or

*Variant A: if he deliberately disregarded facts or circumstances known to him which, but for such disregard, would have given him actual knowledge.*

*Variant B: if there exist facts or circumstances which would have given him actual knowledge had he not deliberately disregarded them.*

*Variant C: if he does not have actual knowledge because he wilfully disregarded facts or circumstances known to him.”*

14. The proposed text, whichever drafting variant may be chosen, retains the principle that knowledge means actual knowledge; however, it allows the imputing of knowledge to a person who did not have actual knowledge on the ground that that person knew of facts or circumstances which, but for his wilful or deliberate disregard of them, would have given him actual knowledge of the fact at issue. Such cases where a person wilfully closes his eyes may be illustrated by the following:

*Example:* Various bills and notes are stolen from Payee (P). P informs among others A about the theft and requests him to compare the signature on any instrument that may be offered to him with the specimen signature of P which A has in his hands. Later, A takes a bill, on which the endorsement of P is forged, without examining the signature, although he remembers P's earlier warning. He deliberately closes his eyes because of an overwhelming interest in acquiring this bill, for example, because he does not want to endanger the conclusion of an advantageous deal. In such a case it seems justified to treat A as if he had actual knowledge.

15. It should be noted that the suggested modification of article 5 would not cover any instance of negligence or carelessness which does not amount to wilful disregard. However, this restriction is irrelevant in the context of those provisions of the draft Convention where lack of knowledge is qualified by words such as “provided that such absence of knowledge was not due to his negligence” (see articles 23(2), (3) and 23 bis (2), (3) as adopted by the Working Group, A/CN.9/261, paras. 38, 47; articles 25(1)(d) and 26(1)(c)).

**C. Limit of liability in articles 23(4) and 23 bis (4) (A/CN.9/261, paras. 39 and 48)**

16. The following modification of article 23(4) is suggested:

“(4) Except as against the forger, the damages recoverable under paragraph (1) may not exceed *the amount*

*of the instrument, plus interest calculated at the rate of ..., and any reimbursement [actually paid] for expenses of protest and notices, and any interest or cost incidental to the giving of security under article 74.”*

17. The above text is intended to avoid the reference to articles 66 and 67, which was viewed as questionable by some representatives and observers at the last session of the Working Group. If this proposed wording is accepted, it should also be used in the new article 23 bis (4).<sup>5</sup>

**D. Liability of transferor, article 41 (A/CN.9/261, paras. 49–63)**

1. *Nature of liability of transferor by mere delivery (or by endorsement “without recourse”)*

18. Article 29 of the draft Convention sets forth the general principle that a person is not liable on an instrument unless he signs it. Accordingly, a person who transfers an instrument by mere delivery, without endorsement, incurs no liability on the instrument to his transferee and other subsequent holders.

19. However, most, if not all, legal systems recognize some kind of liability of a transferor by mere delivery, which is based on the assumption that a person, in transferring an instrument, makes certain implied representations or warranties. In common law systems such liability is expressly regulated in the statutory enactments of negotiable instruments law. In civil law systems such liability derives from the general law of obligations or contract, in particular the law of sale. Under all systems, a transferor by mere delivery, unlike an endorser, does not guarantee payment of the instrument. His liability is not on the instrument but rests on other grounds.

(a) *Common law*

20. Under section 58(3) of the English Bills of Exchange Act, 1882 (BEA), and those enactments that are directly derived from it,<sup>6</sup> the transferor of a bearer bill is liable to reimburse his immediate transferee who gave value to him if:

(a) the bill is not what it purports to be (i.e. if it is a forgery);

(b) he has no right to transfer it (i.e. he has a defective title);

(c) he is at the time of transfer aware of any fact which renders it valueless (i.e. he knows that the bill will not be paid).

Section 58 (3) of the BEA also applies where a party endorses a bill “without recourse”.

<sup>5</sup>A/CN.9/261, para. 48.

<sup>6</sup>E.g. Australian Bills of Exchange Acts (1909–1936) section 63; New Zealand Bills of Exchange Act, 15 of 1908, section 58; Sri Lanka Bills of Exchange Ordinance, Chapter 18 of the Revised Statutes (1938), section 58; Canadian Bills of Exchange Act, Chapter 16 of the Revised Statutes (1927), sections 137, 138.

21. Under section 3-417(2) of the Uniform Commercial Code of the United States of America (UCC), the transferor whether by endorsement or by mere delivery who receives consideration warrants to his transferee who takes the instrument in good faith:<sup>7</sup>

- (a) that he has good title to the instrument;
- (b) that all signatures are genuine or authorized;
- (c) that the instrument has not been materially altered;
- (d) that no defence of any party is good against him; and
- (e) that he has no knowledge of any insolvency proceeding instituted with respect to the maker or acceptor or the drawer of an unaccepted instrument.

Where a party endorses "without recourse", the warranty stated under (d) above is limited to a warranty that the transferor has no knowledge of such a defence.

22. The liability of the transferor by mere delivery under the above mentioned enactments is not, as is the liability of an endorser on the instrument, conditioned by presentment, dishonour and any necessary notice of dishonour or protest of the instrument, but arises at the time of the transfer. The transferee has an action for breach of warranty immediately upon his discovery of a fact constituting such breach, irrespective of whether the instrument has matured.

23. The type and nature of liability incurred by the transferor by mere delivery may be illustrated by the following:

*Example:* X forges on a note the signature of Maker (M) and issues it to Payee (P). P endorses the note in blank and delivers it to A. A delivers the note to B. Upon presentment at maturity, M refuses to pay. B would have a recourse action against P, based on P's endorsement, but would not have any action on the instrument against A since A has not signed it. B, however, would have a special statutory right to proceed against A on the ground that A transferred an instrument in breach of a representation he impliedly made, namely in the case at issue that the note is what it purports to be (BEA) or that all signatures are genuine or authorized (UCC).

24. As mentioned, an important distinction between an action on the instrument by way of recourse and an action off the instrument is that the action off the instrument is not conditioned upon presentment, dishonour and notice of dishonour or protest. In the above example, B, upon discovering that the maker's signature was forged, need not wait till the day of maturity and non-payment of the note before suing A.

<sup>7</sup>Where a transfer is by endorsement, the warranties are given in favour of all subsequent transferees.

(b) *Civil law*

25. Unlike the common law statutes, the negotiable instruments laws of civil law countries do not set forth provisions regarding the liability of the transferor by mere delivery.<sup>8</sup> Doctrinal writings in these countries give little or no discussion of such liability and, at most, treat the matter in a cursory fashion.

26. In civil law countries, the question whether a transferor by delivery and, for that matter, an endorser who endorses without recourse make implied representations<sup>9</sup> is to be answered by reference to the general law, more particularly by reference to the provisions in the civil code governing the sale of claims and other incorporeal rights.<sup>10</sup> Under these provisions, the transferor by delivery guarantees the existence of the rights embodied in the instrument at the time of transfer; exceptions to this rule relate to instances which hardly ever occur in international commercial practice. The remedy for breach of the representation or guarantee thus made is a civil action for damages.

(c) *Tentative conclusion*

27. It would appear that most, if not all, legal systems recognize that a transferor by mere delivery or an endorser who endorses without recourse may be liable where the instrument transferred is not what he impliedly represented it to be. Whereas the common law statutes on negotiable instruments set forth specific provisions in this respect, the negotiable instruments laws of civil law countries are silent on the point and regard must be had to general provisions of the civil code. The dearth of judicial decisions and writings on this issue in civil law countries causes considerable difficulty in ascertaining, and reporting here, in respect of which defects or infirmities the transferor by delivery makes an implied guarantee and whether an action on the ground of breach of such guarantee is available to the transferee before maturity of the instrument, i.e. upon his discovery of the infirmity.

28. In view of the above, it may be thought unsatisfactory if the proposed Convention were to remain silent on the point and the issue were to be left to the applicable national law. Before drawing a final conclusion, consider-

<sup>8</sup>An exception is provided by Colombia and Panama whose negotiable instruments law is inspired by the Uniform Negotiable Instruments Law (1896) of the United States. Articles 67 and 68 of the Colombian Law 46 of 1923 and article 65 of the Panamanian Law 52 of 1917, following section 65 of the Uniform Negotiable Instruments Law, provide that a person negotiating an instrument by delivery or by qualified endorsement, warrants:

(a) That the instrument is genuine and in all respects what it purports to be;

(b) That he has good title to it;

(c) That he has no knowledge of any fact which would impair the validity of the instrument or render it valueless.

Where the negotiation is by delivery alone, the warranty extends only in favour of the immediate transferee.

<sup>9</sup>The basis for liability may be somewhat differently described.

<sup>10</sup>E.g. French Civil Code, art. 1693; German Civil Code, art. 437; Italian Civil Code, art. 1266; Mexican Commercial Code, art. 39 and Civil Code, art. 2043; Netherlands Civil Code, arts. 1570-1571.

ation should be given to the question whether liability for the infirmities listed in article 41(1) should also be imposed on a transferor by endorsement and delivery.

## 2. Extension of article 41 to endorsers

### (a) General considerations

29. All negotiable instruments laws recognize that an endorser, unless he has stipulated otherwise, undertakes to pay the instrument if it is dishonoured by non-acceptance or non-payment. Depending on the law which is applicable, the conditions precedent to such liability are due presentment, protest or the giving of notice of dishonour.

30. As noted above (para. 21), under at least one negotiable instruments law (UCC) the endorser also represents that he has good title to the instrument, that all signatures are genuine or authorized, that the instrument has not been materially altered, that no defence of any party is good against him and that he has no knowledge of any insolvency proceeding instituted with respect to the maker or acceptor or the drawer of an unaccepted instrument. This liability of the endorser is available to the holder before the maturity of the instrument.

31. Under systems other than the UCC the holder's remedies may only be derived from the general law of contract or the law of sale. Within these systems, different positions are taken as to whether in fact liability of an endorser off the instrument is recognized. One position is that there is no need for such liability on the grounds that the liability of an endorser on his endorsement is sufficient to compensate the transferee. Sometimes this result is explained by means of an *e contrario* argument where there is in the negotiable instruments law a specific rule imposing such liability only upon a transferor by mere delivery.

32. The opposite position is that the existence of liability on the endorsement does not exclude liability off the instrument under the general law as a result of the fact of delivery which, after all, takes place both in the case of a mere delivery and in the case where the transferor endorses the instrument. The practical relevance of liability off the instrument is that the endorsee would not have to wait for the dishonour of the instrument, as he has in respect of his rights under the endorsement, but has an immediate right of action without there being a dishonour. This liability is of particular importance in those cases where the transferor endorses the instrument without recourse. Another situation where such liability gains practical relevance is where, within one and the same transaction, endorser and transferor are not identical (e.g. agent liable on endorsement and principal liable as transferor) and one of them is insolvent.

### (b) Conclusion

33. As has been observed by some Governments in their comments on article 41 of the draft Convention, if

the draft Convention were to impose a liability off the instrument on a transferor by mere delivery but not on a transferor by endorsement and delivery, a more extensive liability would then be imposed on a transferor by mere delivery in that his liability would not be conditioned upon presentment, dishonour and the making of protest and, furthermore, could be invoked by his transferee before maturity of the instrument. Moreover, it would appear that the considerations set forth in paras. 18 to 28 supporting the imposition of liability on a transferor by mere delivery would apply with similar force to the question whether such liability should also be imposed on an endorser.

34. It would, therefore, seem appropriate and desirable to treat these two situations alike. Consequently, the draft Convention should either include a regime in respect of such liability for both the transferor by mere delivery and the transferor by endorsement and delivery or not deal with this liability off the instrument at all.

35. If it were decided that the draft Convention should include provisions in this respect, the Working Group may wish to consider the revised draft of article 41, as set forth and explained below (paras. 43-53).

36. If it were, however, decided that the draft Convention should not deal with such liability, the Working Group may wish to consider, as regards the liability of an endorser off the instrument, whether

- (a) the matter should be left to the applicable national law, or
- (b) the draft Convention should expressly exclude the application of national law.

37. As to the approach under (a), it is questionable whether the draft Convention could satisfactorily achieve its objectives or accommodate the relevant rules of an applicable national law. Various fact patterns could be envisaged which might lead one to conclude that this approach is perhaps not the most commendable.

*Example:* Seller, on 1 September, draws a bill, subject to the Convention, on Buyer in favour of himself. The bill is drawn payable on 1 December. On 5 September Seller endorses and delivers the bill to A. On 6 September A learns that the goods delivered by Seller to Buyer were defective and that Buyer thus has a defence to his liability on the bill to Seller.

38. If the draft Convention were to leave room for the application of a national law, in order to determine whether Seller, in addition to his liability under the Convention as an endorser, may also be liable to A off the instrument, one would obviously first have to determine which law was applicable. Such a determination may not be free from difficulties. But assuming that the applicable law could be determined and that it did not recognise a liability off the instrument in respect of a transferor by endorsement and delivery, A, in the above example, would have an action against Seller, by way of

recourse, only if Buyer dishonoured the bill. A different result would obtain if the applicable law made available to A an action for breach by Seller of the warranty he gives as transferor that no defence of any party is good against him (cf. UCC, S. 3-417(2)(d)). In such event A may bring an action for damages against Seller or rescind the transaction between him and Seller already on 6 September.

39. It may be asked whether it would be acceptable for such different results to occur under a Convention setting forth uniform rules in respect of international negotiable instruments.

40. More problematic is the question whether a national law which makes a breach of warranty action available to the transferee where, say, an endorsement is forged, such as the UCC, can properly be accommodated within the system of the draft Convention. Under the UCC, the breach of warranty action may be justified by the fact that the transferee of an instrument containing a forged endorsement is not a holder and, consequently, has no right to payment of the instrument. Under the draft Convention, however, a forged endorsement does not prevent the transferee from being a holder, and thus from being entitled to payment, though he may incur liability under article 23.

41. The approach under (b) above would expressly exclude the application of national law. Its advantages are that there would be no need to ascertain the applicable national law and that the regime regarding the liability of a transferor by endorsement would be uniform. However, the express exclusion of national law should not prevent the matter from being governed by private contract. In many countries, special provisions, often in the form of general banking conditions or contained in the contract of deposit between customer and bank, may apply where a bill of exchange is endorsed to a bank for collection or is discounted. By virtue of such provisions banks usually are entitled, in case of dishonour, to charge back the amount credited to the account of the endorser/transferor. By virtue of applicable general conditions, a bank may also be authorized to charge back, under certain circumstances, the amount credited even before maturity.

42. Therefore, it may be thought that, given the vagueness of national laws, the legal regime for international negotiable instruments which the draft Convention seeks to establish would gain in clarity and certainty if it set forth basic provisions establishing liability off the instrument in respect of an endorser. Obviously, this solution would make sense only if it were decided that the draft Convention should contain provisions regarding the liability of the transferor by mere delivery.

3. *Proposed redraft of article 41 (A/CN.9/261, paras. 56-59)*

43. The following revised draft of article 41 is suggested:

*"Article 41*

"(1) Unless otherwise agreed, a person who transfers an instrument [by mere delivery] represents to the holder to whom he transfers the instrument that:

- (a) The instrument does not bear any forged or unauthorized signature;
- (b) The instrument has not been materially altered;
- (c) No party has a valid claim to the instrument or a defence against him;
- (d) The instrument has not been dishonoured by non-acceptance or non-payment.

"(2) Liability on account of any defect referred to in paragraph (1) of this article is incurred only to a holder who took the instrument without knowledge of such defect and, as regards a defect referred to in paragraph (1)(d), only if the transferor had knowledge of the defect.

"(3) The amount recoverable under paragraph (1) of this article may not exceed

*Variant A:* the value received by the transferor for the instrument, plus interest calculated at the rate of ...

*Variant B:* the amount of the instrument, plus interest calculated at the rate of ..."

44. The above suggested revised draft of article 41 follows in substance the draft prepared by the representative of France and adopted by the Working Group, subject to improvement of its drafting and modification of paragraph (3). However, the following amendments are proposed and explanations submitted for consideration by the Working Group.

45. Following a request by the Working Group,<sup>11</sup> no reference is made to the notion of "warranty", and the term "represents" is used instead. Also the term "damages" is no longer used in the proposed text.

46. As regards the opening words of paragraph (1), the words "by mere delivery" are placed between square brackets, pending decision on the question whether liability would be incurred only by a transferor by mere delivery or by any transferor, whether or not he endorsed the instrument.

47. The secretariat has considered whether subparagraph (c) of paragraph (1) should be deleted in view of the decision by the Working Group, as reflected in the new paragraph (2 *bis*) of article 25, that claims and defences that are listed in article 25(1)(b) and (2) may be set up against a holder who is not a protected holder only if the holder had knowledge of them when he took the instrument.<sup>12</sup> Since thus a holder without knowledge of such a claim or defence is not subject to it, it would

<sup>11</sup>A/CN.9/261, para. 59.

<sup>12</sup>A/CN.9/261, para. 18.

appear that the reference in article 41(1)(c) loses its justification in respect of those claims and defences covered by the new paragraph (2 *bis*).

48. However, article 41(1)(c) remains relevant as regards other defences, which include those listed in article 25(1)(a), (c) and (d). Since these remaining defences essentially relate to discharge or absence of liability, there does not appear to be any reason why, if knowledge on the part of the transferor is not required in respect of the defects listed in article 41(1)(a) and (b), knowledge should be required in respect of the defects under subparagraph (c). Consequently, the above redraft of article 41(2) retains the requirement of knowledge merely in respect of the defects listed in subparagraph (d).

49. Subparagraph (d) has been retained even though dishonour by non-acceptance or non-payment may give rise to discharge of liability under article 59 and would thus fall under article 41(1)(c). However, liability under article 41 should also exist in cases where protest has been made upon dishonour and liability on the instrument is thus not discharged. In the latter case, the value of the instrument would be affected and therefore only a transferor who knew about the dishonour should be held liable in this respect.

50. Paragraph (3) fixes a limit of the liability incurred under paragraph (1) by establishing a ceiling for the amount recoverable by the transferee. Variant A implements the decision of the Working Group that the amount which the holder may recover from a transferor by mere delivery should be limited to the amount he paid, or the value he gave, for the instrument plus interest which, in a given case, may be less than the amount of the instrument.<sup>13</sup>

<sup>13</sup>A/CN.9/261, para. 57.

51. Variant B has been added by the secretariat for consideration by the Working Group for the following reasons. The amount of the instrument provides a clear-cut ceiling, while the value received by the transferor may be less easily determined when goods or services were given to him by the holder. This ceiling would also better accord with the basis of the liability, namely, that the holder received an instrument which was not what the transferor represented it to be.

52. It may be noted that paragraph (3) merely regulates the limit of liability, without specifying which particular remedies may be available and how the recoverable amount would be assessed. While thus recovery of damages could be accommodated as well as rescission of contract, these two methods should be taken into account when selecting the most acceptable variant of paragraph (3). In particular, if variant B were chosen it should be considered whether this ceiling would apply only to recovery of damages or also to rescission of contract, i.e. limit the amount or value to be returned by the transferor to the holder to the amount of the instrument.

53. As regards assessment of damages, it is submitted that this is to be done in accordance with the applicable national law which, in most likelihood, will provide that the recoverable loss consists of the difference between what the holder justifiably expected to receive and what he in fact received. The assessment is easily made after maturity when the holder can clearly see the extent to which the defect affects his right to obtain payment. As regards assessment of damages before maturity or dishonour, a practical way of determining the loss due to the defect or infirmity under article 41(1) would be to ascertain the actual or probable market price which a buyer, who knows about the defect, would pay for the instrument.

#### 4. Draft Convention on International Bills of Exchange and International Promissory

Notes: response to requests of the Working Group on International Negotiable Instruments: note by the secretariat: (A/CN.9/285)

[Original: English]

1. At its fourteenth session, the Working Group on International Negotiable Instruments requested the secretariat to undertake certain enquiries or to prepare certain draft provisions in implementation of decisions made by it in respect of the draft Convention on International Bills of Exchange and International Promissory Notes and to present its conclusions to the Commission for consideration. This note conveys the conclusions of the secretariat in these matters.

##### I. Definition of money or currency, article 4(11)

2. The definition of money or currency in article 4(11) as found in document A/CN.9/211 was as follows:

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

The Working group adopted a revised text as follows:

"(11) 'Money' or 'currency' includes a monetary unit of account which is established by an intergovernmental institution or by agreement between two or more States."

In doing so, the Working Group noted that there might be implications to its decision of which it was unaware.

Accordingly, it requested the secretariat to consult with the International Monetary Fund and to report to the Commission (A/CN.9/273, para. 90).

3. The International Monetary Fund has informed the secretariat that it sees no problems arising out of the new definition for drawing or making instruments under the Convention in SDRs or similar units of account established by an intergovernmental institution.

4. Two considerations in respect of monetary units of account established by agreement between two or more States have been noted and are brought to the attention of the Commission:

— The definition would include the units of account denominated in specified quantities of gold found in several important liability conventions. These do not appear to be among the units of account contemplated by the Working Group.

— Units of account created by agreement of two or more States for specific purposes may be terminated when that purpose is fulfilled. It is possible that no means of converting those units into replacement currencies or units of account would be devised, especially if the States concerned were unaware that private obligations had been created in that unit of account.

## II. Floating interest rates

### *Provision permitting floating interest rates*

5. The Working Group at its fourteenth session requested the secretariat to prepare in consultation with the UNCITRAL Study Group on International Payments a text permitting the issuance of instruments under the Convention with floating interest rates (A/CN.9/273, para. 97). In this respect, the following text is suggested as a new paragraph (5) of article 7.

“(5) A rate at which interest is to be paid may be expressed either as a definite rate or as a variable rate. For a variable rate to qualify for this purpose, it must vary in accordance with provisions stipulated in the instrument and those provisions must refer to one or more other rates of interest [that are both publicly available and not subject to the control of the payee].”

6. Proposed article 7(5) states two definite requirements for a variable or floating interest rate provision to qualify as a permissible interest provision: the means of calculating the rate must be stipulated in the instrument and the rate must vary in accordance with one or more other interest rates. The first of these requirements is in conformity with general concepts of negotiable instruments law that the rights of the parties must be determined or determinable from the face of the instrument. The second requirement, that the interest rate must vary in accordance with one or more other interest rates, is in conformity with the idea that a floating interest rate should reflect changes in the cost of funds in a relevant

financial market. If the interest rate provision did not meet either requirement, article 7(4) would apply and the instrument would bear no interest.

7. The Working Group suggested two additional requirements: any adjustments to the original stated rate should relate directly to the movement of an index which is publicly disclosed and the index should not be subject to the control of interested persons, in particular, the payee (A/CN.9/273, para. 93). Those two requirements are found in proposed article 7(5) in square brackets. Although those proposed requirements should be followed in practice, stating them as requirements for validity of a floating interest rate provision may create potential difficulties. Many floating interest rate provisions refer to particular rates offered by named banks or to the average of several such rates. If these rates are not published but are available upon enquiry, as is common, it may be questioned whether they are publicly disclosed. Similarly, if the payee is a large bank in the same city as other banks whose rates are the reference rates, the argument might be subsequently raised that the payee had sufficient influence over those rates to have exercised “control”. As pointed out above, if a floating interest rate provision did not meet the stated requirements, under article 7(4) the instrument would bear no interest.

### *Alternative consequences of invalidity of floating interest rate provision*

8. The consequences arising out of the invalidity of the floating interest rate provision could be reduced by providing that interest would be payable at the rate specified in article 66(2). This solution could also be used to solve the problem arising when the numerical value of the rate of interest cannot be calculated for any reason, either at the time of issue of the instrument or later. This can occur because the provision as drafted, although adequate on its face, cannot be applied or because the referenced interest rate or rates are no longer available. Although the floating interest rate provision in the instrument may provide for alternative means of calculating the interest rate if the first method cannot be applied, the alternative means of calculating the interest rate may also be impossible to apply. The suggested reference to article 66(2) could appear in article 7(6) as follows:

“(6) If a variable rate does not qualify under the preceding paragraph or for any reason it is not possible to determine the numerical value of the variable rate for any period, interest shall be payable for the relevant period at the rate specified in article 66(2).”

9. Even if this suggestion was followed, there would be a difference between the interest payable for one or more periods as envisaged under the floating interest rate provision in the instrument and the interest payable under article 66(2). That difference could be to the benefit of either party. Therefore, it may be thought that where proposed article 7(6) was to be applied, either the holder or the person liable on the instrument should have the right to declare the instrument immediately due and payable by notice to the other party. This latter sugges-

tion would seem to be even more appropriate if the consequence following from the invalidity of the floating interest rate provision was that no interest was payable by application of article 7(4).

#### Other matters

10. The secretariat was also requested by the Working Group to consider the need for redrafting other provisions (e.g. articles 1(2)(b), 1(3)(b) and 7(4)) with a view to clarifying the applicability of the Convention to instruments with floating interest rates (A/CN.9/273, para. 97). There seems to be no need to redraft articles 1(2)(b) and 1(3)(b) since the instrument would be for a definite sum as intended by those provisions when the interest rate was determined or determinable as described above. Article 7(4) need not be redrafted as a result of the proposed articles 7(5) and 7(6). Nevertheless, the possibility that interest might be payable at the rate specified in article 66(2) when the variable interest rate provision in the instrument could not be applied for some reason, raises the question whether interest should also be payable at the rate specified in article 66(2) in the cases currently covered by article 7(4), i.e. when payment of interest has been stipulated in the instrument but no rate, whether fixed or not, has been indicated. However, it should be noted that parties who did not indicate an interest rate when the stipulation for interest was part of a printed form may have intended that there be no interest applicable to the instrument.

11. During discussions of article 66(2) it was noted that, while in some countries there was no official rate (bank-rate), in others there were two or more. In order to solve the latter problem, the last sentence of article 66(2) might read "In the absence of any such rate or in the presence of more than one such rate, ...".

### III. Model forms

12. In order to aid users in designing forms that would satisfy the requirements of the Convention, the Working Group requested the secretariat to submit to the Commission at its nineteenth session model forms of instruments to be included in an annex to the Convention (A/CN.9/273, para. 67). These model forms were not to be mandatory.

13. In the context of the discussion in the Working Group, the purpose of the model forms was to aid in distinguishing instruments that were to be governed by the Convention from those instruments that would be governed by other legal rules. This involves, in particular, the requirement that the words "international bill of exchange (Convention of ...)" or "international promissory note (Convention of ...)" appear in both the heading and the text of the instrument. The model forms were not expected to provide guidance for other matters that might be found in an instrument. As a result, the model forms suggested by the secretariat are limited to the essential elements of these instruments.

International bill of exchange (Convention of ...)

place where drawn

date

Pay against this international bill of exchange (Convention of ...) [*specify on demand or definite time*] the sum of

in words

in figures

to [the order of] \_\_\_\_\_ of

place of payee

Payable at

To \_\_\_\_\_  
name of drawee

\_\_\_\_\_   
place of drawee

signature of drawer

place of drawer

International promissory note (Convention of ...)

place where made

date

[*specify on demand or definite time*] I/we promise to pay against this international promissory note (Convention of ...) to [the order of]

name of payee

place of payee

the sum of

in words

in figures

[with interest payable ....]

Payable at

signature of maker

place of maker



## B. Electronic funds transfers

### Report of the Secretary-General (A/CN.9/278) [Original: English]

#### INTRODUCTION

1. The Commission, at its fifteenth session in 1982, had before it a report of the Secretary-General which considered several legal problems arising out of electronic funds transfers (A/CN.9/221). In the light of those problems, the report suggested that, as a first step, the Commission should prepare a legal guide on the problems arising out of electronic funds transfers. The guide, it was suggested, should be oriented towards providing guidance for legislators or lawyers preparing the rules governing particular systems for such transfers.

2. The Commission accepted that recommendation and requested the secretariat to begin the preparation of a legal guide on electronic funds transfers in co-operation with the UNCITRAL Study Group on International Payments.<sup>1</sup> Several chapters of the draft legal guide were submitted to the Commission at its seventeenth session in 1984 (A/CN.9/250 and Add.1 to 4) and the remaining draft chapters were submitted to the Commission at its eighteenth session in 1985 (A/CN.9/266 and Add.1 and 2).

3. At its eighteenth session, the Commission requested the Secretary-General to send the draft Legal guide on electronic funds transfers to Governments and interested international organizations for comment.<sup>2</sup> It also requested the secretariat, in co-operation with the UNCITRAL Study Group on International Payments, to revise the draft in the light of the comments received for submission to the nineteenth session of the Commission for consideration and possible adoption.

#### A. Draft Legal guide on electronic funds transfers

4. Replies have been received from eight Governments<sup>3</sup> and seven international intergovernmental or non-governmental organizations.<sup>4</sup> The unanimous response was that the draft Legal guide was a useful tool for legislators

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17 (A/37/17)*, para. 73.

<sup>2</sup>Report of the United Nations Commission on International Trade Law on the work of its eighteenth session, *Official Records of the General Assembly, Fortieth Session, Supplement No. 17 (A/40/17)*, para. 342.

<sup>3</sup>Australia, Germany, Federal Republic of, Hungary, Japan, Mexico, Netherlands, Tonga, United Kingdom of Great Britain and Northern Ireland. In addition to the replies from Governments, the secretariat has received a reply from the French Association of Banks and a report on "Electronic Funds Transfers in Belgium", prepared by the National Bank of Belgium, which bases its discussion of possible improvements in the rules governing electronic funds transfers on the Legal guide.

<sup>4</sup>Economic Commission for Africa, Economic Commission for Europe, Economic Commission for Western Asia, Commission of the European Communities, Organization for Economic Co-operation and Development, International Chamber of Commerce, Latin-American Federation of Banks.

and lawyers preparing the rules governing particular funds transfer systems. The replies from several Governments show that the list of legal issues contained in the final chapter (A/CN.9/266/Add.2) serves as a useful basis for consideration of the issues involved in preparing new legislation or the adaptation of existing legislation. Requests for copies of the final text of the Legal guide have been received from governmental and non-governmental sources in a number of countries.

5. The replies of Australia, Federal Republic of Germany and the United Kingdom contained suggestions for clarification of certain points in the draft chapters. These suggestions form the basis of the proposed modifications to the draft chapters as contained in the annex to this report. In addition to the modifications set forth in the annex, the annex to the chapter on Finality of Funds Transfer, entitled "National experience in reducing system risk", will be modified when the final text is prepared to reflect the current status of developments in the countries considered. Review of the draft chapters has also revealed several corrections of an editorial nature to be made to the final text.

6. The Commission may wish to consider adopting the Legal guide on electronic funds transfers and requesting that it be published in an appropriate manner.

#### B. Preparation of model rules

7. During the discussions leading to the decision to prepare the Legal guide on electronic funds transfers at the fifteenth session of the Commission in 1982, "several representatives expressed the view that the Guide might show areas in which the Commission could in the future prepare uniform rules. It was suggested that such uniform rules might be in the nature of a model law, which would be of particular value to developing countries, or might concentrate on certain aspects of international electronic funds transfers".<sup>5</sup> The Commission may wish to consider whether it would now be appropriate to begin the preparation of uniform rules and, if so, the nature of those rules.

8. Preparation of the Legal guide has confirmed the general conclusions found in the report of the Secretary-General to the fifteenth session of the Commission that electronic funds transfers have developed in a partial legal vacuum (A/CN.9/221, para. 82). Although basic banking procedures are the same whether a funds transfer is made by paper-based means or electronically, and as a

<sup>5</sup>Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17 (A/37/17)*, para. 70.

result many of the rules governing paper-based funds transfers can be applied to electronic funds transfers with appropriate results, many other rules should be reconsidered in the light of the new banking and legal environment. Decisions should be made as to such matters as the legal value to be given to the authentication of an electronic funds transfer instruction, the right of a bank to debit an account when the customer denies having issued an electronic funds transfer instruction and there is no independent paper record, and the frequency at which and the means by which a bank must inform a customer of debits or credits to his account and the obligation of the customer to inform the bank of errors.

9. To the extent that the use of electronics has led to changes in banking procedures, new legal rules are needed. It has been noted, for example, that rules as to the finality of a funds transfer have usually assumed a procedure whereby amounts were debited and credited to the customers' accounts throughout the banking day as funds transfer instructions were received by the bank, a process that is not followed in regard to most electronic funds transfers at the present time.<sup>6</sup> More strikingly, in those countries that in the past have relied on cheques (a form of debit transfer) for all or most non-cash funds transfers, there may be no body of law currently available to govern credit transfers, which are the most important form of electronic funds transfers.

10. These developments have led several countries to consider whether and to what extent the existing law should be modified.<sup>7</sup> It could be expected that in the near future other countries will embark on a similar review of the adequacy of the existing law in this area. Co-ordination of these national efforts would reduce the likelihood of incompatible legal regimes.

11. The vast increase in volume and in value of international electronic funds transfers has also increased the desirability of considering the adoption of a new legal regime to govern such transfers. The Commission is eminently well placed to undertake the task.<sup>8</sup>

12. The nature of the payment system is such that a legal regime governing international electronic funds transfers must either be restricted to limited aspects of the inter-bank relationship, similar to the coverage of the S.W.I.F.T. rules,<sup>9</sup> or it must create a substantially complete legal regime governing the rights and obligations of

the banks' customers as well as of the banks. The undertaking of the latter task would be similar in scope to the preparation of the draft Convention on International Bills of Exchange and International Promissory Notes.

13. Another possible approach, and one that might be thought to be preferable, would be to undertake the harmonization of rules in national legal systems governing both domestic and international electronic funds transfers. Such an approach can aim at the same result for electronic funds transfers on a world-wide scale that was achieved 50 years ago by the Geneva system for negotiable instruments within countries of the civil law tradition, i.e. reduction of legal problems arising in international funds transfers by harmonizing and modernizing domestic law.

14. Such a goal is ambitious. It might also be thought that the proposal to prepare model rules for electronic funds transfers is both premature and too late. The proposal might be thought to be premature because the technology and the resulting banking practices are still in a state of rapid flux.<sup>10</sup> It might be too late because, even though electronic funds transfers are a relatively new phenomenon in themselves, in countries where electronic funds transfer systems have already been implemented, they reflect the banking and legal environment already in place. Rules governing electronic funds transfers must be in conformity with that banking and legal environment. As a consequence, a legal regime designed especially for electronic funds transfers may be accepted most easily by countries which do not have a highly developed electronic funds transfer system already in place.

15. These difficulties could be overcome by preparing model rules that were flexible. Solutions could be drafted in such a way that they did not depend upon specific technology. Where two or more solutions seemed desirable because of the differences in banking systems, the model rules could present those solutions as alternative texts. While this would reduce the degree of harmonization that might be achieved by preparation of the rules, the number of points on which alternatives would be necessary might not be excessively large since there appears to be common agreement on many important issues. Where there is no common agreement, presenting alternative solutions might serve to enhance the utility of the model rules as a guide to national legislation in this field.

16. If the Commission accepts the suggestion that it undertake the preparation of model rules on electronic funds transfers, it may wish to assign the task to the Working Group on International Negotiable Instruments. It might wish to decide that the Working Group should begin its work by considering the legal issues set forth in the last chapter of the Legal guide as well as any other issues the secretariat might believe to be appropriate to place before the Working Group at that time.

<sup>6</sup>Chapter on "Finality of funds transfer", A/CN.9/266/Add.1, paras. 31-47.

<sup>7</sup>In addition to the report of the National Bank of Belgium, note 3, above, see the report from Australia of the Working Group Examining Consumer Protection Aspects of Electronic Funds Transfer Systems, which considers many basic aspects of the law governing funds transfers from the viewpoint of their impact on consumers. The preparation of a new law for large-value electronic funds transfers has been undertaken in the United States of America.

<sup>8</sup>The comments submitted by Hungary, Mexico and the United Kingdom anticipate the receipt of suggestions as to possible further steps that the Commission might take following preparation of the Legal Guide.

<sup>9</sup>The draft inter-bank compensation rules currently being prepared by the Commission on Banking Technique and Practice of the International Chamber of Commerce are of this nature.

<sup>10</sup>The comments of the Federal Republic of Germany state that for these reasons the preparation of rules by the Commission would not be desirable at this time.

## ANNEX

**Proposed modifications to the draft chapters of the legal guide on electronic funds transfers as contained in A/CN.9/250/Add.1 to 4 and A/CN.9/266/Add.1 and 2***A/CN.9/250/Add.1: "Terminology used in this guide"*

1. Paragraph 3, last sentence: delete the words "and will include the terms defined in this guide".

2. Paragraph 5, last sentence should read as follows:

"BIS has also published a monograph entitled 'Security and Reliability in Electronic Systems for Payments' (3rd ed., 1985)."

*A/CN.9/250/Add.2: "Electronic funds transfer systems in general"*

3. Paragraph 23, last sentence should read as follows:

"Even when a clearing-house established net balances for the participating banks, it does not affect the relationship between sending and receiving banks except as to the means of settlement and the consequences of a failure to settle."

4. Add a new paragraph 28a immediately following figure 4.

"28a. In a second commonly used pattern the inter-bank relationships are in the form of a triangle. The transferor bank instructs the transferee bank to credit the transferee's account and informs the transferee bank that it will be reimbursed by credit to its account with intermediary bank. By a second message, transferor bank instructs intermediary bank to debit its account and to credit transferee bank's account. The inter-bank messages are completed by a credit advice from intermediary bank to transferee bank, with appropriate references to the prior messages permitting reconciliation of the accounts."

5. Add a new section D as follows:

*"Credit cards and debit cards"*

"39a. The origins of credit cards and debit cards lay outside the banking system. As a result, they took on certain special characteristics which continue to apply today. The most evident of these characteristics are the names given to the two types of cards, the confusion over the proper distinction between them and the fact that the clearing channels are distinct from the clearing channels for other payment mechanisms.

"39b. Credit cards evolved from the credit tokens or cards issued by certain merchants to identify customers who were authorized to purchase on credit. The distinguishing feature of the travel and entertainment cards, which first appeared in the 1950's, and the bank-issued credit cards, which first appeared in the 1960's, was that the cards could be used with a large number of merchants. However, those cards retained the impor-

tant characteristic that they gave access to a line of credit and the debit was not made to the customer's current account in a bank. Therefore, in order for the customer to discharge his obligation arising out of use of the card, a separate funds transfer in favour of the card issuer had to be made.

"39c. If the debit arising out of use of the card is made to a current account in a bank, rather than to a separate credit card account, the transaction is usually referred to as a debit card transaction. Since the use of some cards can give rise to a debit to either type of account depending on varying circumstances, it can be difficult at times to distinguish between a debit card and a credit card. The legal significance of distinguishing between them normally lies in that credit card transactions may be subject to provisions of consumer credit legislation whereas debit card transactions are usually treated as funds transfers. In those countries where this distinction is made, a statutory definition of the two terms can be expected.

"39d. When first developed, credit cards were used to create paper-based debit transfer instructions, and this use is still common for both credit cards and debit cards. These paper-based debit transfer instructions are usually transmitted between banks and other financial institutions by special clearing channels. It is common for them to be truncated early in the clearing process and for only the essential data to be sent forward to the institution holding the customer's account. The addition of magnetic stripes to the back of cards, and more recently the addition of micro-circuit chips, has permitted them to be used as access devices to various forms of electronic funds transfers."

6. Paragraph 49, last sentence should read as follows:

"The category of customer-activated electronic funds transfers might also be considered to include the preparation by the customer of computer memory devices containing debit or credit transfer instructions and the lodgement of those devices with the bank or, where permitted, directly with the automated clearing house."

*A/CN.9/250/Add.3: "Agreements to transfer funds and funds transfer instructions"*

7. Paragraph 13, last sentence should be deleted and replaced by the following:

"It is also followed in respect of cheques in an increasing number of countries including Belgium, Denmark, the Federal Republic of Germany and Sweden, while other countries such as Australia, France and Switzerland are planning to introduce this procedure."

8. Paragraph 32, add the following to the end of the paragraph:

"More advanced telecommunication networks record the calling line identity as part of their normal opera-

tion and this information can be made available to the called terminal. Not only would an intruder on the system have to simulate the authentication procedures, but he would have to do so on a line normally used by an authorized user."

9. Paragraph 46, second sentence should read as follows:

"Where the transfer is identified only by account number, [...] the bank can identify the account to be debited only by reference to that number and it is believed that in most States this practice is legally justified either under general principles of law or as a result of contract between the bank and the customer."

10. Paragraph 49, last sentence: the words "(with the current exception of France and the United Kingdom)" should be deleted.

11. Paragraph 53, last sentence should read as follows:

"The incompatibility of formats may preclude the clearing [...] or limit the access [...]"

12. Paragraph 56, third sentence: delete the words "(e.g. S.W.I.F.T. and, in a different sense, CHIPS)".

13. Paragraph 69 should read as follows:

"In many parts of continental Europe it is common practice in an inter-bank transfer to credit the transferee's account with an interest date one or two banking days subsequent to the entry date. The time can stretch to four calendar days over an ordinary weekend. This period of one or two banking days is intended to allow the transferee bank to receive settlement from the transferor bank prior to the date on which the transferee would begin to earn interest. The funds can be withdrawn or transferred to another account immediately. However, they do not draw interest until the indicated interest date. Moreover, if they are withdrawn before that date, the customer is charged for the relevant period. This practice assures the banks a minimum period during which neither bank is paying interest on the amount transferred in addition to any period of time necessary to make the transfer."

*A/CN.9/250/Add.4: "Fraud, errors, improper handling of transfer instruction and related liability"*

14. Paragraph 17, third sentence should be deleted and replaced by the following:

"In some proposed home banking systems it would not be feasible to use a plastic card for authorization purposes; therefore the authorization procedure may depend on the use of a PIN or password alone. In other systems the PIN or password, which the customer uses over a period of time, may be combined with a transaction number which is unique to that transaction."

15. Paragraph 24, sixth sentence should read as follows:

"However, an encryption standard which is highly secure today may be rendered insecure within a few years by the development of more powerful computers allowing exhaustive search for encryption keys or, in the case of public key cryptosystems, by the development of new techniques for factoring the large numbers on which they are based."

16. Paragraph 36, last two sentences should be deleted and the following inserted:

"However, errors in a fully automatic system are much harder to prove, especially where only one transaction has been affected. Accordingly, the question of allocation of responsibility for any losses arising is itself a serious problem for the customer. Other types of error may affect many customers because of the extremely large numbers of transactions processed by computer. Furthermore, because of the increasing complexity of computer systems now in use or planned for the future, it is virtually impossible to validate them completely. As a result, there is a possibility of massive failure out of all proportion to prior experience and it is essential that fallback positions be prepared by banks for this eventuality."

17. Paragraph 61, add a new sentence at the end as follows:

"Such disclaimer provisions should be drafted in clear and unambiguous terms so that customers can know precisely for which circumstances and types of loss the bank or other party will, or will not, accept liability."

## II. NEW INTERNATIONAL ECONOMIC ORDER

### A. Report of the Working Group on the New International Economic Order on the work of its eighth session

(Vienna, 17–27 March 1986) (A/CN.9/276) [Original: English]

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#### INTRODUCTION

1. At its eleventh session (1978), the United Nations Commission on International Trade Law decided to include in its work programme a topic entitled "The legal implications of the new international economic order" and established a Working Group to deal with this subject.<sup>1</sup> At its twelfth session (1979), the Commission designated member States of the Working Group.<sup>2</sup> At its thirteenth session (1980), the Commission decided that the Working Group should be composed of all States members of the Commission.<sup>3</sup> The Working Group consists, therefore, of the following States: Algeria, Australia, Austria, Brazil, Central African Republic, China, Cuba, Cyprus, Czechoslovakia, Egypt, France, German Democratic Republic, Germany, Federal Republic of, Guatemala, Hungary, India, Iraq, Italy, Japan, Kenya, Mexico, Nigeria, Peru, Philippines,

Senegal, Sierra Leone, Singapore, Spain, Sweden, Trinidad and Tobago, Uganda, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland, United Republic of Tanzania, United States of America and Yugoslavia.

2. At its first session (1980), the Working Group recommended to the Commission for possible inclusion in its programme of work, the harmonization, unification and review of contractual provisions commonly occurring in international contracts in the field of industrial development.<sup>4</sup> The Commission, at its thirteenth session, agreed to accord priority to work related to those contracts and requested the Secretary-General to undertake a study concerning contracts on the supply and construction of large industrial works.<sup>5</sup>

3. The study prepared by the secretariat<sup>6</sup> was examined by the Working Group at its second (1981) and third (1982) sessions.<sup>7</sup> At its third session, the Working Group requested the secretariat, pursuant to a decision of the

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its eleventh session, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17 (A/33/17)*, para. 71.

<sup>2</sup>Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17 (A/34/17)*, para. 100.

<sup>3</sup>Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 143.

<sup>4</sup>A/CN.9/176, para. 31.

<sup>5</sup>See footnote 3, above.

<sup>6</sup>A/CN.9/WG.V/WP.4 and Add.1–8, and A/CN.9/WG.V/WP.7 and Add.1–6.

<sup>7</sup>A/CN.9/198 and A/CN.9/217.

Commission at its fourteenth session,<sup>8</sup> to commence the drafting of a legal guide on contractual provisions relating to contracts for the supply and construction of large industrial works.<sup>9</sup> The Legal Guide is to identify the legal issues involved in such contracts and to suggest possible solutions to assist parties, in particular from developing countries, in their negotiations.<sup>10</sup>

4. At its fourth session (1983), the Working Group examined a draft outline of the structure of the Legal Guide and some sample draft chapters prepared by the secretariat<sup>11</sup> and requested the secretariat to proceed expeditiously with the preparation of the Guide.<sup>12</sup> At its fifth (1984), sixth (1984) and seventh (1985) sessions,<sup>13</sup> the Working Group discussed a note on the format of the Guide<sup>14</sup> and additional draft chapters.<sup>15</sup>

5. The Working Group held its eighth session at Vienna from 17 to 27 March 1986. All members of the Working Group were represented with the exception of Algeria, Central African Republic, Cyprus, Hungary, Iraq, Peru, Philippines, Sierra Leone, Singapore, Trinidad and Tobago, Uganda and United Republic of Tanzania.

6. The session was attended by observers from the following States: Argentina, Bulgaria, Cameroon, Canada, Colombia, Côte d'Ivoire, Dominican Republic, Ecuador, Finland, Holy See, Indonesia, Kuwait, Netherlands, Panama, Republic of Korea, Saudi Arabia, Switzerland, Thailand and Uruguay.

7. The session was also attended by observers from the following international organizations:

- (a) *United Nations specialized agency*  
United Nations Industrial Development Organization (UNIDO)
- (b) *Intergovernmental organizations*  
Asian-African Legal Consultative Committee (AALCC)  
Organization of African Unity (OAU)
- (c) *International non-governmental organizations*  
European International Contractors  
International Bar Association  
International Chamber of Commerce (ICC)  
International Federation of Consulting Engineers  
International Law Association  
International Progress Organization

8. The Working Group elected the following officers:

*Chairman:* Mr. Leif SEVON (Finland)<sup>a</sup>

*Rapporteur:* Mrs. Jelena VILUS (Yugoslavia)

<sup>a</sup>The Chairman was elected in his personal capacity.

<sup>8</sup>Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17 (A/36/17)*, para. 84.

<sup>9</sup>A/CN.9/217, para. 130.

<sup>10</sup>See footnote 8, above.

<sup>11</sup>A/CN.9/WG.V/WP.9 and Add.1-4.

<sup>12</sup>A/CN.9/234, paras. 51 and 52.

<sup>13</sup>A/CN.9/247, A/CN.9/259 and A/CN.9/262.

<sup>14</sup>A/CN.9/WG.V/WP.9/Add.5.

<sup>15</sup>A/CN.9/WG.V/WP.11 and Add.1-9, A/CN.9/WG.V/WP.13 and Add.1-6 and A/CN.9/WG.V/WP.15 and Add.1-10.

9. The Working Group had before it for examination the "Introduction" to the draft Legal Guide on drawing up international contracts for the construction of industrial works (A/CN.9/WG.V/WP.17/Add.1) and draft chapters on "Pre-investment studies" together with proposed additions to the draft chapters on "Procedure for concluding contract" and "Delay, defects and other failures to perform" (A/CN.9/WG.V/WP.17/Add.2), "General remarks on drafting" (A/CN.9/WG.V/WP.17/Add.3), "Supply of equipment and materials" (A/CN.9/WG.V/WP.17/Add.4), "Supply of spare parts and services after construction" (A/CN.9/WG.V/WP.17/Add.5) and "Settlement of disputes" (A/CN.9/WG.V/WP.17/Add.6), as well as revised draft chapters on "Choice of contracting approach" (A/CN.9/WG.V/WP.17/Add.7), "Transfer of technology" (A/CN.9/WG.V/WP.17/Add.8) and "Termination of contract" (A/CN.9/WG.V/WP.17/Add.9).

10. The Working Group adopted the following agenda:

- (a) Election of officers
- (b) Adoption of the agenda
- (c) Consideration of draft Legal Guide on drawing up international contracts for the construction of industrial works
- (d) Other business
- (e) Adoption of the report

11. The Working Group proceeded to discuss the documents before it in the order presented below.

#### INTRODUCTION TO THE GUIDE<sup>16</sup>

12. It was noted that in deciding to publish a Legal Guide on Drawing Up International Contracts for the Construction of Industrial Works the Commission sought to contribute to the advancement of the objectives of the new international economic order. It was generally agreed that a reference to that fact should appear at the beginning of the "Introduction" to the Guide, and that the substance of paragraphs 5 and 6 of the draft "Introduction", insofar as they discussed the context of the new international economic order, should be set forth in paragraph 1. A view was expressed that in connection with the resolutions of the General Assembly on the new international economic order reference should be made to the Charter of Economic Rights and Duties of States. Various additional suggestions were made for improving the drafting of paragraph 1.

13. It was noted that the Guide was intended to identify issues to be taken into consideration by the parties in negotiating and drafting their contract, and, where appropriate, to set forth possible ways in which the parties might, by agreement, deal with those issues. In that connection, it was generally agreed that the "Introduction" should stress that the Guide was not intended to

<sup>16</sup>A/CN.9/WG.V/WP.17/Add.1.

have an independent juridical status, to be used, for example, for interpreting contracts that had been entered into before or after the issuance of the Guide.

14. There was general agreement with the suggestion of the secretariat that a three-tiered approach should be adopted in putting forward recommendations or suggestions in the Guide. The highest level, indicated by a statement that the parties "should" take a particular course of action, would be used only when the course of action was logically required or legally mandated. This could be simply a recommendation that the parties should include in their contract a provision dealing with a particular issue, or a recommendation that in the provision the parties should adopt a particular approach or solution to the issue. An intermediate level would be used when it was "advisable", but not logically or legally required, that the parties adopt a particular course of action. A formulation such as "the parties may wish to consider" or "the parties may find it desirable" would be used for the lowest level of recommendation or suggestion. It was generally agreed that this three-tiered approach should be clearly set forth in paragraph 15 of the Introduction to the Guide. A suggestion was made that the reference in the second sentence of paragraph 2 to "solutions recommended" should be clarified in the light of the three-tiered approach. According to another view, however, that reference was satisfactory in its present form.

15. With respect to paragraph 3, it was generally agreed that the relationship of a "works contract" to other types of contracts for the construction of industrial works should be clarified. A view was expressed that the examples given at the end of the last sentence of the paragraph were insufficient, in that they excluded other important obligations sometimes undertaken by a contractor, such as the training of manpower. It was suggested that either the examples should be deleted, or additional ones should be added.

16. A view was expressed that section B of the "Introduction" ("Intended audience") should be combined with section D ("How to use the Guide"). According to a further view, the title "How to use the Guide" was not necessary.

17. It was generally agreed that the material in paragraphs 7 to 9, dealing with the history of the Guide, was not of great importance to the user of the Guide; it should be removed from the "Introduction" and possibly placed in a "Foreword", perhaps in a shortened form.

18. With respect to certain terminology used in the Guide to describe the obligations of the contractor, a view was expressed that the Guide should refer to the construction of works, erection of buildings and installation of machinery. It was generally agreed that whatever terminology was finally settled upon, it should be used consistently throughout the Guide.

19. Various views were expressed with respect to the list of definitions in paragraph 17. According to one view, it was in principle desirable to define as many terms used in the Guide as possible, in order to assist, in particular, readers from developing countries. Disagreement was expressed with respect to the appropriateness of certain of the definitions given in paragraph 17. According to other views, paragraph 17 should be deleted for the following reasons. The meanings of most of the terms defined in that paragraph were given in the chapters of the Guide dealing with the subject-matter of the terms. The reader of the Guide would be assisted in locating those meanings by the detailed table of contents and the alphabetical index, which were to be included in the Guide. Moreover, it was difficult to reduce the meanings of some terms to concise definitions, and the meanings of some terms varied among legal systems. In those cases it was preferable for the reader to be referred to the substantive chapters of the Guide where the terms were discussed.

20. A suggestion was made that terms which were not defined in other chapters of the Guide, such as "contractor", "purchaser" and "works contract", should be defined in paragraph 17 of the "Introduction". According to other suggestions, those terms should be defined in the chapter on "General remarks on drafting", or in the index.

21. After discussion, the Working Group agreed that paragraph 17 should be deleted, and the table of contents and the alphabetical index should be structured so as to enable the reader to locate the meanings of terms used in the Guide in the chapters of the Guide in which the terms were discussed. The index should incorporate an analytical approach. Thus, systematic sub-divisions should be set forth for each term contained in the index (e.g. giving references to places in the Guide where meanings of the terms were given, and references to related terms and concepts). The index should also contain a separate entry, perhaps entitled "meanings of terms", which would list particular terms and indicate where in the Guide their meanings were discussed. Section D of the "Introduction" to the Guide should inform the reader about the index and its use in locating the meanings of terms. As for terms which were not defined elsewhere in the Guide, it was generally agreed that the meanings of the terms "contractor" and "purchaser" should be made clear in the opening paragraphs of the "Introduction" to the Guide by, for example, referring to the nature of the obligations undertaken by those parties. Similarly, the meaning of the term "works contract" should be made clear in paragraph 3.

#### PRE-INVESTMENT STUDIES<sup>17</sup>

22. It was generally agreed that the title of this chapter should be changed to "Pre-contract studies".

23. It was generally agreed that the first sentence of paragraph 3 should be deleted. It was also agreed that the

<sup>17</sup>A/CN.9/WG.V/WP.17/Add.2.

paragraph should refer to responsibility for the accuracy and sufficiency of information given to the purchaser by a contractor who performed pre-contract studies as well as to information given to the contractor by the purchaser.

24. With respect to paragraph 5, a suggestion was made that the paragraph should be deleted, since the substance of the advice given in that paragraph would already be known to the purchaser. The prevailing view, however, was that the paragraph should be retained, but be re-drafted in order to reflect the intended meaning, i.e. that the purchaser should not necessarily choose the least expensive pre-contract studies, or restrict the scope of the studies to save money, since that course of action could result in inadequate studies and ultimately result in greater cost to him. It was agreed that the word "improper" should be replaced by the word "unwise".

25. A view was expressed that the chapter should stress the value to the purchaser of opportunity studies, and that reference should be made to the fact that there existed international organizations, and in some countries national agencies, which performed those studies.

26. It was generally agreed that the last two sentences of paragraph 7 should be deleted, as they were repetitions of the preceding sentences. With respect to paragraph 10, it was agreed that, in addition to the items to be dealt with by feasibility studies enumerated in that paragraph, the studies should also consider the kinds of manpower which would be needed to construct the works. Moreover, the words "and climatic conditions" should be added to the end of the last sentence of that paragraph.

27. It was generally agreed that paragraph 11 should not refer to the allocation of the risks of inadequacies or errors in feasibility studies, and that the paragraph should be re-drafted as follows:

"Feasibility studies typically assume the existence of certain situations or facts, and therefore incorporate an element of uncertainty. The purchaser should be able to ascertain from the study the assumptions which have been made and the extent of the uncertainty. Sometimes feasibility studies include 'sensitivity studies', which vary some of the assumptions on which the feasibility study is based to determine the effect of those changes in assumptions on the feasibility of the project."

28. It was generally agreed that, in paragraph 12, the purpose of detailed studies should be clarified, i.e. by indicating that once the feasibility of the project had been confirmed, the detailed studies would provide more refined and detailed information needed for the design of the works and to settle other aspects of the particular project. It was also agreed that the secretariat should consider whether the substance of paragraph 12 should be placed before or after the present section F of the chapter.

29. With respect to paragraph 13, it was generally agreed that the tenor of the paragraph should not be to

describe current practice; rather, the paragraph should indicate possible approaches to the issues discussed which the parties might wish to consider. It was agreed that the same change should be made with respect to paragraphs 14 and 15. It was agreed, however, that paragraphs 13 and 14 should not make any recommendation that one particular approach should be adopted in preference to another.

30. The question of the selection of consultants to perform feasibility studies was discussed. It was observed that, in order to promote competition, consultants were sometimes chosen by the use of selection procedures, but even in those cases the procedures were usually less formal and extensive than tendering procedures used for the selection of contractors. It was generally agreed that with respect to the performance of pre-contract studies, the purchaser should be advised to consider whether he was able to perform the studies himself. If not, he should consider having them performed by an outside firm in which he had confidence. In choosing such a firm, the purchaser should consider not only the price charged by it (bearing in mind that the least expensive one was not always the best choice), but also such other factors as its reputation and expertise. The purchaser should also be advised that if he could not find a suitable firm, he may obtain assistance in doing so from sources such as lending institutions, international organizations and professional bodies.

31. The Working Group discussed the possible conflict of interest which could arise if the consultant engaged to perform the pre-contract studies might also be later engaged to supply the design for the works or serve as the consulting engineer in connection with the construction of the works (paragraph 14), or if the studies were to be performed by a firm which might later be engaged as the contractor under the works contract (paragraph 15). A view was expressed that the extent of the problem in the two cases was different. The performance of the studies by a firm which might be later engaged as the contractor could present more serious difficulties for the purchaser than the performance of the studies by a consultant who might later be engaged to supply the design of the works or serve as the consulting engineer. Therefore, the two cases should not be linked, and the third sentence of paragraph 15 should be reconsidered in that connection.

32. A view was expressed that it was not necessarily undesirable from the purchaser's point of view for the consultant who performed the pre-contract studies to be engaged to supply the design for the works or to serve as the consulting engineer in connection with the construction of the works. Some lending institutions allowed that to occur, and the practice of those which did not (referred to in the last sentence of paragraph 14) should not be supported in the Guide. Therefore, it was generally agreed that paragraph 14 should advise the purchaser that he might wish to consider engaging the consultant who performed the pre-contract studies to supply the design or act as the consulting engineer under the works contract, but that he should pay attention to the possibility of a conflict of interest in such a case.



33. With respect to engaging the firm which performed the pre-contract studies as the contractor under the works contract, a view was expressed that this was undesirable for the purchaser, although it might be acceptable for the firm merely to supervise the construction of the works by others. It was noted, however, that in some highly specialized areas it was necessary for the pre-contract studies to be performed by the contractor, since there existed no independent consultants with expertise in those areas. It was generally agreed that paragraph 15 should stress the risks to the purchaser of a conflict of interest when the contractor also performed the pre-contract studies, and the strongest level of recommendation should be used against that practice. However, the paragraph should also note that in some cases there might be no alternative to the studies being performed by the contractor.

#### DELAY, DEFECTS AND OTHER FAILURES TO PERFORM (continued)<sup>18</sup>

34. The Working Group took note of the statement by the secretariat that, although this material had been designated as an addition to chapter XVIII, "Delay, defects and other failures to perform", it might be appropriately included in some other chapter, in view of a previous decision of the Working Group to restrict chapter XVIII to a discussion of remedies. The Working Group requested the secretariat to determine the most appropriate location for the material.

35. A view was expressed that this material should commence with a discussion of the background to the issue addressed (i.e. responsibility for information needed by the contractor for the construction of the works); the possible approaches for dealing with the issue should then be discussed separately. It was also suggested that the parties should be advised to take into account mandatory rules of applicable law imposing liability for insufficient or erroneous information.

36. A suggestion was made that a reference to information concerning climatic and soil conditions should be added to the first sentence of paragraph 1. With respect to paragraph 2, a view was expressed that the phrase in the fourth sentence, "and to the extent that the contractor is able to rely on that information", implied that the contractor should always be able to rely on information provided to him by the purchaser. It was therefore suggested that the phrase be deleted. It was further suggested that the last sentence of paragraph 2 should be reformulated so as to recommend that each party be responsible for the accuracy of information given by him to the other party.

37. In connection with the first approach to the allocation of responsibility for the sufficiency and accuracy of information, discussed in paragraph 3, a view was expressed that the paragraph should indicate the kinds of information for which each party might be made respons-

ible in the contract. It was suggested that data relating to boring should be added to the examples given in the last sentence of the paragraph. According to a further suggestion, it should be pointed out that site conditions were sometimes an element of the design of the works.

38. A view was expressed that the variation of the first approach, described in paragraph 4, was similar to the second approach, described in paragraph 5, and that the two should be consolidated. It was also suggested that the reference to the cost ceiling in the second sentence of paragraph 4 should be elaborated, and that a reference should be given to the chapter in the Guide where the cost ceiling was discussed. With respect to the last sentence of paragraph 4, it was suggested that the obligation of the contractor to discover errors in information should depend upon his own level of experience. Furthermore, it was suggested that the sentence should clarify who was to bear the risk of errors discovered after the contract had been entered into.

39. In connection with paragraph 5, a view was expressed that the costs resulting from the existence of information or situations which were not discoverable or foreseeable should be shared on an equal basis between the two parties, instead of being totally assumed by the purchaser.

#### PROCEDURE FOR CONCLUDING CONTRACT (continued)<sup>19</sup>

40. The Working Group noted that the subject matter covered by this section of the chapter was extensive and complex. It was therefore not possible to treat it comprehensively and in detail in the context of and within the present scope of the Guide. In the light of those considerations, the Working Group considered whether the subject-matter should be discussed in the Guide, and, if so, how it should be treated.

41. The prevailing view was that because of the complexity of the issues connected with the contracting arrangements discussed in the material, a discussion of them would be of particular benefit to purchasers in developing countries, who might need information and advice concerning those arrangements.

42. A view was expressed that the contracting arrangements referred to in the chapter should not be discussed in detail. Rather, the Guide should merely refer to the fact that the purchaser might consider entering into one of the contracting arrangements referred to. The Guide should also refer the reader to sources of further information on those arrangements, including relevant work done by other international organizations. According to another view, the present discussion should be expanded in order to assist purchasers in developing countries. After discussion, the Working Group generally agreed that the scope of the discussion should be as set forth in paragraphs 46 and 60, below.

<sup>18</sup>Ibid.

<sup>19</sup>Ibid.

43. It was observed that the arrangements in section A (contracting by the purchaser with a group of firms which would perform the obligations of the contractor) were of a fundamentally different character from those discussed in section B (formation by the purchaser and the contractor of a joint venture for the operation of the works and marketing of its output, and perhaps also for the construction of the works). It was agreed that the discussion of the two types of arrangements should be separated; the discussion of the subject-matter of section A should be retained in the chapter entitled "Procedure for concluding contract", and the possibility of adopting the kind of arrangement discussed in section B, as an alternative to a works contract, should be mentioned instead in the chapter entitled "Choice of contracting approach".

44. It was observed that the term "joint venture" was used in sections A and B with different meanings, which could result in confusion for the reader. It was suggested that terminology should be chosen to describe the arrangements dealt with in sections A and B so as to avoid that confusion. It was also observed that the terminology used in practice to describe those arrangements was not settled or uniform. The view was expressed that it would be desirable if the Guide contributed to uniformity with respect to terminology. It was generally agreed that the Guide should advise the parties that in using particular terminology in their contract they should consider what legal consequences might flow from the terminology chosen.

45. Views were expressed that the Guide should advise purchasers contemplating entering into arrangements described in sections A and B to obtain expert legal advice in that regard. In addition, it was observed that in many legal systems various aspects of those arrangements were governed by legal rules, some of which might be mandatory. It was suggested that the Guide should advise the parties to take such legal rules into consideration.

#### *Contracting with group of firms*

46. It was generally agreed that the Guide should point out various issues which the purchaser should consider when entering into a contract with a group of firms. The discussion should not, however, engage in a detailed analysis of those issues, or recommend particular approaches to dealing with them. The Guide should direct the reader to sources of detailed information and advice on the subject. It was also generally agreed that the Guide should advise the purchaser that when he contracted with a group of firms which was not organized as an independent legal entity, every member of the group should become a party to the contract.

47. Various suggestions were made with respect to issues which the Guide should point out with respect to contracting by the purchaser with a group of firms. Those included, for example, the problem of obtaining jurisdiction over several separate firms, often from different countries, in connection with dispute settlement proceedings (in that regard a suggestion was made that one

solution might be for the group to form an independent legal entity in the country of the site); the nature of the liability of the members of the group to the purchaser in respect of the performance of the obligations of the contractor (e.g. joint and several liability of all members of the group for the performance of those obligations, or liability of each member only for the performance of particular obligations); guarantees to be given in respect of the performance by the members of the group (in that regard a suggestion was made that each member of the group might guarantee the performance by all members); financial arrangements between the group and the purchaser; taxation questions; and ancillary agreements which would have to be entered into by the purchaser.

48. A view was expressed that contracting by the purchaser with a group of firms which was to perform the obligations of the contractor should be differentiated from the situation where the purchaser entered into separate contracts with two or more contractors (referred to elsewhere in the Guide as the "separate contracts approach"). Such a clarification should be made in particular in paragraph 3. Moreover, the "silent" contract referred to in paragraph 3 should be more clearly differentiated from subcontracting by the contractor. A view was expressed that the contract should require the consent of the purchaser to any arrangement by the contractor with other contractors in respect of the construction of the works, especially in cases where the contractor was chosen because of his purported capability of doing all the work.

49. A suggestion was made that the discussion should only deal with the case where the purchaser entered into a contract with a group of firms which was not organized as an independent legal entity. Where the group was organized as an independent legal entity, that entity alone would be the contractor under the contract, and the problems faced by a purchaser entering into a contract with several firms which were to perform the obligations of the contractor would not arise. According to another view, the discussion should differentiate an "integrated" arrangement (where the members of the group set up a separate entity to construct the works) from a "non-integrated" one (where the various obligations in respect of the construction of the works were allocated among the members of the group).

50. It was pointed out that the possible problems for the purchaser arising from his contracting with an independent legal entity with minimum capitalization organized by a group of firms, referred to in paragraph 5, were not limited to the case of the organization of the independent entity by a group of firms, but arose in any case where the contractor was organized with minimum capitalization. A view was expressed that the reference in paragraph 5 to performance guarantees should make it clear that the guarantees should not be obtained from the independent entity itself; rather, they might be obtained from the individual members of the entity, or from a third person.

51. It was suggested that the fourth sentence of paragraph 5 should clarify that a claim against an independent

legal entity for failure to perform its contractual obligations could be governed by law other than that of the place where the entity was established, e.g. the law of the place where the works was being constructed.

52. A view was expressed that the discussion placed excessive emphasis on the desirability that members of a group which undertook the obligations of a contractor be jointly and severally liable to the purchaser for a failure by a member to perform. According to that view, there existed other methods of protecting the purchaser (e.g. guarantees). In connection with paragraph 6, it was observed that members of a group might in some cases be unwilling to accept joint and several liability.

53. With respect to paragraph 7, a view was expressed that the authority of a member of a group to serve as spokesman for the group should be differentiated from his authority to act for the group. It was suggested that the paragraph should point out that the designation by members of a group of one member to serve as the spokesman of the group and to act for it could be beneficial not only for the purchaser, but also for the group.

#### *Joint ventures between contractor and purchaser*

54. It was suggested that the importance of joint ventures between the contractor and the purchaser as a form of transfer of technology should be emphasized. However, it was agreed that the Guide could not deal comprehensively with such arrangements. While some parts of the Guide could be relevant to those arrangements, most of the Guide would not be.

55. It was suggested that the Guide should concentrate only upon joint ventures whose purposes included operating the works and marketing of its output, since only joint ventures formed for those purposes were of practical importance. Joint ventures were usually not formed only for the purpose of constructing the works. A view was expressed that the essence of joint ventures formed by the parties was equity participation by the parties in the joint ventures, and that therefore they should be referred to in the Guide as "equity contracts". It was suggested that the Guide should refer to the various possible ways in which a joint venture could be organized, without, however, recommending any particular approach.

56. A view was expressed that section B attempted to deal in summary form with some very complex issues, and could be misleading, and that the Guide should therefore do no more than indicate possible arrangements.

57. With respect to paragraph 9, a view was expressed that the Guide should point out that the formation by the contractor and the purchaser of a joint venture could create difficulties for the purchaser as a result of having to share some managerial control with the contractor. Pursuant to that view it was suggested that a clause be incorporated in the contract creating the joint venture providing for a revision of the arrangement if such difficulties arose. According to another view, the sharing

by the purchaser of some managerial control with the contractor was not necessarily disadvantageous for the purchaser.

58. Concerning paragraph 11, it was suggested that the second sentence should avoid the implication that the works contract was entered into after the formation of the joint venture by the contractor and the purchaser to operate the works and market its output, since that sequence of events did not reflect usual practice. A view was expressed that the third sentence of paragraph 11 should be reformulated in order to clarify the situations in which a group of entities without independent legal personality might enter into a works contract. A suggestion was made that the last two sentences of paragraph 11 should be deleted.

59. With respect to the terminology used in section B, a suggestion was made that the terms "corporate" or "contractual" joint ventures should be used in preference to entities with or without independent legal personality.

60. After discussion of the treatment in the Guide of the formation by the purchaser and the contractor of a joint venture, it was generally agreed that the Guide should inform the purchaser that he might wish to consider the possibility of forming a joint venture characterized by a relatively high level of integration, or one with a looser arrangement. The Guide should point out possible types of arrangements within that range, without, however, discussing them in detail or recommending any particular type. The Guide should direct the reader to sources of detailed information and advice on the subject.

#### GENERAL REMARKS ON DRAFTING<sup>20</sup>

61. The view was expressed that the chapter as presently drafted was too detailed, and contained some advice of an elementary nature which might be deleted. The prevailing view, however, was that an extended treatment of the problems which might arise in drafting was useful, in particular if, as was sometimes the case, drafting of works contracts was undertaken by persons who were not lawyers. A detailed treatment would also have the advantage of bringing to the attention of the parties issues which they might overlook. It was noted that particular attention should be given in the chapter to drafting problems which were of special importance in relation to works contracts (e.g. inconsistencies between contract documents).

62. The view was expressed that the Guide should mention the possibility of each party establishing for himself a procedure containing steps to be taken during the negotiation and drafting of works contracts. Such a procedure, based on suggestions contained in the chapter, would reduce the possibility of omissions or mistakes in drafting. It was also noted that the Guide should mention the desirability of the purchaser obtaining legal or technical advice to assist him in drafting the contract when he

<sup>20</sup>A/CN.9/WG.V/WP.17/Add.3.

did not himself possess the necessary expertise. It was noted that legal advice might be needed not merely on liability for taxation (as mentioned in paragraph 4) but on other issues as well.

63. Different views were expressed concerning the advantages to the purchaser of preparing a first draft of the contract. It was agreed that the Guide should not make a recommendation to this effect, but only mention the possible advantages and disadvantages of his doing so. It was noted that, if tendering procedures were adopted by the purchaser, he would be obliged to prepare a first draft of the contract so that tenders might be submitted on the basis of that draft.

64. It was suggested that paragraphs 3 and 4, dealing with the need to take account of applicable laws when drafting the contract, might be reconsidered and simplified. It was noted that paragraph 3 suggested that, after agreement had been reached between the parties on the main technical and commercial issues relating to the proposed contract, it would be useful for the parties to agree upon the law applicable to the contract and to review the documents reflecting their agreement in the light of the chosen law. The view was expressed that the Guide should also note the possibility of the parties agreeing upon the law applicable to the contract at the commencement of their negotiations, thus enabling them to keep in mind the requirements of that law in the future negotiations. Such initial agreement on the law applicable to the contract would eliminate the need to review at a later stage the terms of documents which had already been agreed upon.

65. It was noted that, in addition to the reasons stated in paragraph 3 for taking into account the law applicable to the contract when drafting the contract, it was important to take that law into account because it might provide for terms to be implied in the contract when an issue was not regulated by express terms. It was also noted that, besides the mandatory legal rules of an administrative, fiscal or other public nature in the country of each party, such rules in other countries (e.g. in the country of a supplier of technology) might also need to be taken into account in drafting the contract.

66. The view was expressed that paragraph 5 should be modified to refer to the potential usefulness of standard forms of contract or general conditions as aids to drafting. Standard forms or general conditions might provide examples of issues to be addressed, and might also help in determining how such issues might be resolved.

67. Different views were expressed as to whether it was advisable to draw up the contract in only one language, or in the languages of the two parties where those languages differed. It was agreed that the Guide should not make a recommendation on that issue, but should mention both approaches and state the respective advantages and disadvantages of each approach. In accordance with that decision, the fifth sentence in paragraph 2, which implied that only one language was to be used, should be deleted.

Several other observations were made with regard to the language in which the contract might be drafted. It was noted that the third sentence of paragraph 6 should be clarified so as to avoid an inference that the contract must be drafted in a third language and not in the language of either of the parties. If the language of one of the parties was generally used in international commerce, it might be advisable to draft the contract in that language. It was suggested that, if the contract were to be drafted in a language or languages which were not languages of the country of the applicable law, an agreed translation of the contract might be made into the language of that country. It was noted that where a contract was drafted in two languages, and a contract provision in one language version was unclear, the contract might provide that the other language version might be examined to remedy the lack of clarity.

68. The view was expressed that the reference in paragraph 7 to a contract document coming first in logical sequence among all of the contract documents and controlling the other documents pre-supposed a complex works contract consisting of many documents. It was suggested that the Guide should also envisage and deal with the organization of documents in a simpler works contract. It was also suggested that in paragraph 7 the parties should be advised to set forth in the contract not only the date on which it was signed, but also the date on which it was to enter into force. It was proposed that paragraph 8 should be less categorical about the need for a party to require proof from the other party of his capacity to enter into a works contract, or about the need to require proof that an official of a corporation which was to be a party to a contract had the authority to bind the corporation. In some cases the previous trade relations between the parties would already have furnished sufficient proof of those matters. It was noted that the documents which might form a works contract were somewhat differently described in paragraph 9 and the first sentence of paragraph 12, and that the descriptions should be harmonized.

69. It was observed that the law applicable to the contract might provide rules of interpretation to resolve an inconsistency between contract documents or within the same document. Paragraph 10 should bring the possible existence of such rules, which might even be of a mandatory character, to the attention of the parties. It was also observed that, while this paragraph noted the possibility of inconsistency within the same document, it did not suggest a solution for resolving the inconsistency.

70. It was observed that paragraph 11 set forth two approaches which might be adopted with respect to the relationship between the contract documents, on the one hand, and the oral exchanges, correspondence and draft documents which emanated during the negotiations, on the other. It was suggested that it would be sufficient to describe the two approaches, without indicating that one approach might lead to a fairer result. It was also noted that oral exchanges, correspondence and draft documents might emanate subsequent to entry into force of the

contract. It was observed that the parties should be advised to clarify the relationship between the contract documents, on the one hand, and these oral exchanges, correspondence and draft documents, on the other. Where a draft document was intended to form part of the contract, the parties should clearly so provide.

71. A suggestion was made that paragraph 12 should discourage the inclusion of introductory recitals in a works contract, since the extent to which recitals might influence the interpretation of a contract was uncertain. The view was expressed that, in addition to indicating that separate contracts might include a description of the interrelationship of the time-schedules for performance under related contracts, paragraph 14 should also indicate the desirability of including descriptions of the interrelationship of aspects of infra-structural work to be executed under the separate contracts.

72. In regard to the time when notifications were to be effective, it was suggested that paragraph 16 might mention the possibility of a notification being effective after the lapse of a specified period of time following the dispatch of the notification. The Guide should mention the advantages of selecting a means of giving notification under which proof of dispatch or receipt of a notification could be obtained. It was noted that the example given in paragraph 17 of an exception to a general rule that a notification was effective upon dispatch was sufficient, and that it was unnecessary to justify the exception on the basis of fairness.

73. It was observed that, with regard to notifications which were not of a routine character, paragraph 18 only noted the possibility of such notifications being given by the purchaser to the head office of the contractor. The paragraph should also refer to the possibility of non-routine notifications being given by the contractor to the head office of the purchaser.

74. Some proposals were made for modifying paragraph 19 dealing with the legal consequences of a failure to notify. It was observed that the description contained in the paragraph was too simple. The consequences of a failure to notify could not be set forth in a generalized manner, but would depend upon the purpose for which the notice was given. A suggestion was made that this difficulty might be resolved in part by adding cross-references to other chapters where the effects of a failure to notify were dealt with. There was wide agreement that the paragraph should be revised and expanded.

75. While there was general agreement that a works contract needed to contain definitions of certain key concepts, there was disagreement as to whether the Guide should provide examples of definitions. Under one view, such definitions should not be provided. The definitions might be used by parties in contracts where they were inappropriate. It was also difficult to formulate definitions which would be acceptable in all business circles, since different drafting techniques and traditions prevailed in different regions. Under another view, a few

examples of definitions would help users of the Guide to draft definitions appropriate to their own contract. A suggestion was made that, instead of presenting its own definitions, the Guide might reproduce a few selected definitions taken from some well-known model contracts. The prevailing view, however, was that the Guide should not include provisions contained in standard contracts drafted by other bodies, since those definitions might conflict with the terminology used in the Guide. Furthermore, the definitions contained in those standard contracts might be subsequently revised.

76. After deliberation, it was agreed that paragraph 22 should be modified to include a statement that the parties might find it useful to define certain key concepts which were frequently used in the contract. The concepts which the parties might find it advisable to define might be mentioned, without, however, providing definitions for those concepts. In addition, the paragraph could set forth a few selected definitions which might command wide acceptance. It was suggested, for example, that definitions of "the contract", "writing", "dispatch" and "receipt" might be included. The paragraph could also indicate that descriptions of other concepts were contained in the various chapters of the Guide, and that those descriptions could be located by the use of the index to the Guide.

#### SUPPLY OF EQUIPMENT AND MATERIALS<sup>21</sup>

77. A view was expressed that the quality of equipment and materials, and the inspection of equipment during manufacture, were important issues. Therefore, they should be mentioned in the present chapter, and reference should be given to the other chapters of the Guide where those issues were discussed.

78. A suggestion was made that the concepts of supply, take-over and receipt as used in the chapter should be clarified. Additional suggestions were made with respect to the terminology used in the chapter. The secretariat was requested to reconsider the use of the terms "plant" and "equipment". It was suggested that instead of the term "take-over", it might be advisable to use the expression "take into possession". According to a further suggestion, the term "specification", rather than "quality", should be used in connection with the description of the equipment and materials to be supplied.

79. With respect to the suggestion in the chapter that the parties might include in the contract a particular trade term in order to establish which party was to pay the costs of shipping equipment and materials, and refer to INCOTERMS to define that term, it was suggested that the chapter should also warn the parties that INCOTERMS regulated other matters in addition to who bears the shipping costs (e.g. passing of risk). In incorporating INCOTERMS, therefore, the parties should be sure they wished to settle all such issues in the manner settled by INCOTERMS. A further suggestion was made

<sup>21</sup>A/CN.9/WG.V/WP.17/Add.4.

that the parties might wish to consider settling in their contract various issues referred to in the present chapter simply by referring to INCOTERMS, rather by elaborating the settlement of those issues in contractual provisions. Therefore, it might be advisable to discuss the applicability of INCOTERMS in the "General remarks" section of the chapter.

80. It was suggested to stress in paragraph 3 that the supply of equipment and materials might not necessarily result in the passing of risk or the transfer of ownership in respect of the equipment and materials. It was agreed to delete the last sentence of paragraph 4 and to deal with the issue covered by that sentence either in the chapter on "Passing of risk" or in the chapter on "Delay, defects and other failures to perform", giving a reference to those chapters in the present chapter.

81. A view was expressed that the Guide should note that some equipment and materials might be obtained in the country of the site, rather than from abroad, and advise the parties also to consider solutions to issues discussed in the chapter which were suitable for the former cases. It was further suggested that the concept of bailment which existed in some legal systems should be referred to in connection with the storage of equipment and materials. It was suggested that paragraphs 3, 22 and 25 might need to be harmonized.

82. With respect to paragraph 5, a suggestion was made to delete the expression "as a general matter" in the first sentence and to replace the word "risk" in the fourth sentence by another suitable expression. A view was expressed that the Guide should strongly recommend that the parties adequately describe in the contract the equipment and materials to be incorporated in the works. It was suggested that paragraph 6 should not imply that the contractor should in all cases be obligated to supply all equipment and materials needed for his construction, even if they were not specified in the contract.

83. A view was expressed that the contractor should not be able to avoid liability for defects in equipment and materials by obtaining them from third persons. It was suggested that this point be discussed in the chapters on "Subcontractors" or "Delay, defects and other failures to perform".

84. With respect to the question of whether the contract should permit the contractor to supply equipment and materials earlier than the date stipulated in the contract, a view was expressed that the contract should not imply that whether or not the purchaser had funds to pay for the equipment and materials was always relevant to that question. It was suggested to clarify in what situations it might not be possible to stipulate in the contract a date for the supply of equipment and materials.

85. A view was expressed that it was desirable to delete the second part of the first sentence and the fourth sentence in paragraph 9. According to another view they should be retained.

86. A view was expressed that the contractor under a turnkey lump sum contract should not in all cases be obligated to bear the costs connected with the transport of equipment and materials, and the second sentence in paragraph 10 should be re-drafted to reflect that point. According to another view, the contractor in a turnkey lump sum contract should always be obligated to pay those costs. It was noted that costs connected with transport might include insurance costs, and a reference to the chapter on "Insurance" would therefore be advisable. In connection with paragraph 12, it was suggested to delete the expression in the first sentence "in all cases", since in some exceptional cases the purchaser might be responsible for packing the equipment and materials and protecting them during transport.

87. A view was expressed that in the heading of subsection B.4, the term "restriction" should be replaced by another term which would take into account the contents of paragraph 17. It was suggested that the last two sentences in paragraph 16 be redrafted to include the possibility that the contractor might in some cases be responsible for payment of import customs duties. It was noted that the issues concerning customs duties might need to be expressly settled in the contract if INCOTERMS were not incorporated in the contract.

88. It was suggested to expand paragraph 17 in order to explain the different kinds of restrictions which might apply with respect to the supply of equipment and materials. In that connection, a view was expressed that the Guide should mention import and export prohibitions, and import and export licence requirements. In addition, it would be advisable to distinguish between prohibitions and licence requirements existing at the time of conclusion of the contract, and those arising after that time. If the former restrictions could affect the availability of items essential to the completion of the contract, the parties might wish to consider deferring entry into force of the contract until after the relevant permits had been obtained. The contract should establish which party was to procure licences, and that party should give to the other party timely notice of steps which had been taken and of the results achieved. It was suggested to include in the last sentence in paragraph 17 a reference to the chapter on "Termination of contract", and to redraft that sentence.

89. A suggestion was made to clarify in the last sentence of paragraph 18 the situations in which the purchaser or another contractor might incorporate into the works the equipment supplied by one contractor. It was further suggested to delete the term "loss" in the last sentence of paragraph 19. In addition, it was suggested to limit the effects mentioned in that sentence to a specified period of time.

90. A view was expressed that the issue of liability for defects in equipment and materials should be discussed in the chapter on "Delay, defects and other failures to perform". A suggestion was made that the contractor should in some cases entitle the purchaser to establish a time-schedule for the repair of defects by the contractor.

91. A view was expressed that the third sentence of paragraph 20 should be redrafted, and there should be no obligation to take over defective equipment and materials by the purchaser.

92. It was suggested that the contractor should be liable for damages not only in the case of defects in equipment and materials, but also in case of delay in supplying equipment and materials. It was also suggested to include a cross reference to the chapter in which the contractor's obligation to demonstrate that the equipment complied with the specifications was discussed.

93. A view was expressed that even if the purchaser was to bear the risk of loss of and damage to equipment and materials stored by him, in certain situations he should not be obligated to hand them over to the contractor in the same condition in which he received them for storage (e.g. in cases of damage due to natural causes or damage caused by the contractor). A view was expressed that, if necessary, the purchaser would carry out the conservation of equipment which was being stored by him.

94. Suggestions were made to delete the two last sentences in paragraph 30, and to harmonize the terminology used in paragraphs 20 and 29.

#### SUPPLIES OF SPARE PARTS AND SERVICES AFTER CONSTRUCTION<sup>22</sup>

95. There was wide agreement that section A of the chapter ("General remarks") should include a paragraph describing possible connections between the subjects dealt with in the chapter and the policy of developing countries with regard to industrialization. It was suggested that the Guide should stress the importance to developing countries that the purchaser himself, or other enterprises from his country, achieve as early as possible the capability to manufacture spare parts and to maintain, repair and operate the works, so that the dependency of the purchaser on the contractor would be reduced. The achievement of this capability would often depend on adequate training being given to the personnel of the purchaser, and the paragraph should stress the importance of contractual arrangements providing for training. The importance of training should also be stressed at appropriate points within the chapter.

96. It was noted that a distinction might be drawn between the supply of spare parts and repair of the works by the contractor, on the one hand, and maintenance and operation by him, on the other. As regards the supply of spare parts and repair, it was probable that purchasers from many developing countries would need assistance from the contractor for the operational lifetime of the works. As regards maintenance and operation, however, it was probable that, within a certain period of time after the commencement of operation of the works, the purchaser's personnel would be able to perform those functions. That distinction would be relevant to the

duration of the obligations to be imposed on the contractor and should be taken into account in sections H and I of the chapter ("Commencement and duration of obligations of parties" and "Termination").

97. It was observed that legal regulations, which might be mandatory, regulating the obligations of the parties in regard to the subject-matters dealt with in the chapter, in particular maintenance and operation, existed in some countries. The parties should be advised to take those regulations into account when drafting the contract.

98. It was noted that the time when the post-construction obligations dealt with in the chapter became relevant and were to be imposed on the contractor was not accurately described in paragraph 1. Those obligations did not become relevant immediately after the works were ready to operate, but subsequently, after the works had been taken over by the purchaser. A cross-reference to chapter XIV, "Completion, take-over and acceptance" was desirable.

99. It was observed that the subjects dealt with in the present chapter were often interlinked (e.g. spare parts might be needed for repair, and maintenance might include the repair of certain elements). The subjects themselves should be carefully described, and the linkages noted.

#### *Contractual arrangements*

100. The view was expressed that parties would often find it difficult at the time of the conclusion of the contract to determine the nature and extent of the rights and obligations to be created between them in regard to the subjects dealt with in the chapter (e.g. the quantity of spare parts to be delivered, the personnel to be supplied by the contractor to assist in operating the works). The chapter, possibly in paragraph 4, should set forth a procedure to be followed where the parties had decided that certain contractual terms were to be agreed in the future, but were unable to reach agreement at a later stage. It was also noted that paragraph 5 should stress that the conclusion of contracts for the supply of spare parts and post-construction services separate from the works contract was a common method of dealing with that difficulty, in particular in regard to the provision of maintenance needed after the expiry of the guarantee period.

#### *Spare parts*

101. There was wide agreement that the continued availability of spare parts for the operational lifetime of the works was of great importance to purchasers. Such availability was of particular importance in developing countries where works were often expected to have a longer lifespan than in developed countries.

102. It was noted that the amount of the spare parts needed might vary at different stages: i.e. at the stage of completion of construction, during the guarantee period, and during the subsequent lifetime of the works.

<sup>22</sup>A/CN.9/WG.V/WP.17/Add.5.

103. The view was expressed that the contractor could not at the time of the conclusion of the contract predict with certainty the kinds or quantity of spare parts that might be needed at different stages, and that the first sentence of paragraph 6 should be amended to reflect that fact. It followed that where the contractor had given an estimate of the quantities needed, but the estimate turned out to be incorrect (paragraph 12), it might be unreasonable to obligate the contractor to supply additional spare parts at the prices at which they were originally supplied. The vital interest of the purchaser which needed to be protected was the continued availability of the spare parts, more than the price at which he could obtain them.

104. It was noted that, apart from the distinction between standard and non-standard spare parts noted in paragraph 7, a distinction could be drawn between parts which were routinely subject to wear and tear and therefore had to be periodically replaced, and parts which only had to be replaced for exceptional causes (e.g. breakage due to accidents or faulty use of equipment). While fairly accurate estimates could be made of the quantities of spare parts needed in the first category, it was difficult to make an estimate of needs in regard to parts in the second category. It was also noted that while paragraph 7 stated that non-standard spare parts were obtainable only from the contractor, paragraphs 10 and 11 indicated that they might be obtainable from other sources as well; those paragraphs should therefore be harmonized.

105. It was proposed that paragraph 8 should be amended to state that non-standard spare parts "may normally" be obtainable more cheaply from sources other than the contractor, since the uncertainty of market forces made it impossible to be certain about the cheapest source of supply. In paragraph 9, it was proposed that the purchaser should be advised to obtain by the time the construction was completed an "adequate", rather than a "large", stock of spare parts. A large stock of certain very durable parts (e.g. generators) might be unnecessary. It would also be inadvisable to obtain a large stock of spare parts with a short shelf life.

106. It was observed that where certain spare parts had been manufactured for the contractor by suppliers (paragraph 10) it might nevertheless be preferable from the point of view of the purchaser to enter into a contract with the contractor obligating him to supply spare parts, rather than to arrange with him to procure them as an agent. Under the former arrangement, the contractor could be held personally liable if the spare parts were defective.

107. Several observations were made with regard to paragraph 11, dealing with the possible manufacture by the purchaser of non-standard spare parts. It was observed that while some developing countries which were technologically advanced might have this capability, a great many developing countries would always have to rely on outside sources of supply. It was noted that while paragraph 11 referred to the relevant technological capa-

bility as being that of the purchaser himself, the more relevant consideration was the capability in the country of the purchaser. It was also noted that paragraph 11 should refer to the possibility that if the purchaser used spare parts manufactured by him, performance or other guarantees given by the contractor might cease to be operative, depending on the terms of the contract. It was further suggested that the last sentence of the paragraph dealing with possible difficulties of the contractor in supplying to the purchaser drawings and specifications of spare parts manufactured by a supplier because the supplier had industrial property rights in regard to the items should be deleted or amplified. If amplified, the sentence might note the possibility of the purchaser obtaining a licence from the supplier, and also note that the difficulty would not arise if the industrial property rights of the supplier were not enforceable in the country of the purchaser.

108. Views were exchanged on the situation where the contractor was obligated to supply spare parts manufactured by him over a long period of time, and within that period of time the contractor changed his production facilities, with the result that the manufacture of the spare parts had to be discontinued, or the cost of manufacture was greatly increased. It was agreed that the Guide should stress that the continued availability to the purchaser of spare parts for the operational lifetime of the works was a key issue. With that in mind, the Guide could note that different solutions might be considered. A continuing obligation of supply for the lifetime of the works might be imposed on the contractor, which might be regarded as the primary solution. As a second possibility, continuing obligations might be imposed on suppliers from whom the contractor obtained the spare parts. As a further possibility, drawings or specifications might be supplied to the purchaser, or licences granted to him, in order to enable him to manufacture the spare parts or have them manufactured by a third party. It was observed, however, that the last possibility might not be appropriate in those developing countries where neither the purchaser nor other enterprises in his country had the capability to manufacture the spare parts.

109. The view was expressed that the scheme suggested in paragraph 14 for two different guarantee periods in respect of the quality of the spare parts supplied was not often encountered in practice, and that a simpler scheme, involving a single period, might be suggested. Under another view, however, the scheme suggested was appropriate, in particular because it took into account the fact that certain spare parts had a short shelf life. In that connection it was suggested that spare parts were usually described not by reference to their "quality", but by reference to technical standards.

110. It was noted that the contract should provide that the instruction manuals to be supplied by the contractor (paragraph 16) should be drafted in a manner (e.g. format, language) which would make them readily understandable to the personnel of the purchaser. In addition to manuals, "as built" drawings should be supplied,



explaining how the various pieces of equipment were interconnected, and the facilities available for repair or maintenance work at the place where the equipment was located.

### *Maintenance*

111. The view was expressed that the appropriate stage at which a contractor might be obligated to supply a maintenance programme was some time prior to the completion of the works, and not (as suggested in paragraph 11) at the time of the conclusion of the contract. The paragraph should also indicate that the maintenance manuals to be provided by the contractor should be readily understandable by the personnel of the purchaser. Reference might also be made to model forms of agreement for maintenance.

112. It was noted that, while the sixth sentence of paragraph 18 suggested that the purchaser might find it preferable to enter into independent maintenance contracts with suppliers, it would be difficult for the purchaser to identify and contact suppliers at times when maintenance was needed if at those times their identity was unknown. It was suggested that the contractor should be obligated to disclose the identity of suppliers at the time that the contract was entered into, so as to give the purchaser the option of concluding maintenance contracts with suppliers at a time when he wished to do so.

113. Several observations were made to the effect that the term "workmanlike manner" referred to in paragraph 19 as a method of defining the standards to be observed during maintenance might not have a clear meaning in certain regions. Alternative terms which might be used (e.g. "professional manner") were suggested. It was also observed that the approach to maintenance discussed in the last two sentences of the paragraph, under which the contractor was obligated to ensure that the works operated in accordance with the contract for a specified percentage of its normal operating time, needed clarification.

114. It was observed that the first sentence of paragraph 21 was too sweeping, and therefore needed to be restructured.

115. It was observed that paragraph 22 should suggest that payment was to be made, not merely after the submission of an invoice by the contractor, but after the submission of an invoice accompanied by maintenance reports.

### *Repairs*

116. With regard to the possible difficulty faced by the purchaser in using persons other than the contractor to effect repairs because that might violate secrecy obligations binding on the purchaser (paragraph 23), the view was expressed that the contract might permit the use of certain enterprises whose assurances with regard to the maintenance of secrecy the contractor was prepared to

accept. Where the purchaser himself had the capability to effect certain repairs (paragraph 24), he might nevertheless not have the capability to start up the works after the repairs had been effected. Paragraph 23 might suggest the inclusion of a contract provision providing for assistance by the contractor in the start-up.

117. It was suggested that paragraph 25 might indicate that, pending the effecting of repairs, the purchaser could continue to use the works or the equipment to the extent possible. It was also noted that the contract might specify the period of time after notification when repairs must be commenced by the contractor.

118. With regard to paragraph 26, it was observed that an agreement to effect repairs should always be reduced to writing, whether or not the repairs were extensive. It was also observed that the suggestion in the paragraph that a technical expert might be employed to settle the time-schedule for effecting repairs when the parties failed to agree on the time-schedule might not always be appropriate. The failure of agreement might not depend on a technical issue, but might be caused by such reasons as the contractor not having qualified personnel immediately available, or the contractor deploying his personnel on other work.

119. Different views were expressed about whether it was appropriate to suggest (paragraph 27) that the purchaser might have to pay a fee to cover the contractor's costs in having personnel in readiness for an inspection. It was agreed that the paragraph should only state that the parties should reach agreement on which party was to bear the costs involved.

120. With regard to the report to be submitted by the contractor describing the repairs carried out by him (paragraph 29), it was suggested that the report should also describe the materials used during repair. It was also noted that a description of repair work which might be needed in the future raised separate issues from a description of the repair itself, and might more appropriately be treated in a document separate from the report of the repairs. It was further noted that if a new piece of equipment was installed in the course of a repair, a quality guarantee might be required by the purchaser in respect of that piece of equipment.

121. It should be stressed that, where an item had to be transported to the contractor's country for the purposes of repair (paragraph 30), the parties should co-operate in regard to the various incidents of transportation (e.g. customs clearance), both during the transportation of the item to the contractor's country and its return after repair to the purchaser's country.

### *Operation*

122. It was noted that the term "division of control" used in the fourth sentence of paragraph 32 was unclear, and should be re-considered. The paragraph might suggest that where directions on technical questions were

given by the purchaser's personnel to personnel of the contractor engaged to assist in operation, the latter contractor might be given some form of right of appeal against those directions. It was suggested that where the purchaser required the contractor to replace one of his employees even in the absence of a proved complaint against that employee, the Guide should not suggest that the expenses of replacement (e.g. travel and recruitment costs) were to be borne by the purchaser; the Guide might only suggest that parties should agree on this issue. It was noted that the suggestion in the fifth sentence of paragraph 33 that an incentive fee might be paid to the contractor depending on the productivity and profitability of the works should be either deleted or expanded to indicate that such a fee might also be paid to the contractor if it was paid to local employees of the purchaser.

*Facilitation by purchaser of services to be provided by contractor*

123. It was suggested that the language of the second sentence of paragraph 34 should be amended to clarify that both the contractor and the purchaser were bound to comply with safety regulations applicable to the works. It was also suggested that the paragraph should only mention the possibility of the purchaser supplying locally available equipment and materials, or facilities such as accommodation and transport for the contractor's personnel, without indicating any need for the purchaser to do so.

*Commencement and duration of obligations of parties, and termination*

124. The view was expressed that the statement in the penultimate sentence of paragraph 35 that repair obligations might commence from the date of expiry of the quality guarantee assumed by the contractor in respect of the works needed modification. Even during the period of the quality guarantee defects might occur needing repair which were not covered by the guarantee. It was suggested that the obligation of maintenance extending over the normal maintenance period should be provided for in a separate agreement.

125. It was suggested that it might be inadvisable to suggest (paragraph 36) that the time when the contractor's obligations as to the supply of spare parts, maintenance, repair and operation were to end might be determined by reference to the point of time when the purchaser had developed the capacity to supply the spare parts and services himself; that point of time might be uncertain. With regard to delimiting the duration of the contractor's obligations in that regard, it was noted that two approaches might be mentioned and distinguished in the paragraph. Under one approach, the obligations might be created for a relatively short period. If the purchaser wished the obligations to continue after the expiry of that period the parties might negotiate for their extension for a further period. Under another approach, the contractor's obligations might be created for a relatively long period, with the purchaser having the right to

terminate those obligations by giving a specified period of notice. The suggestions in paragraph 39 as to termination of obligations of the parties should be harmonized with those approaches. It was suggested that the term "specified failures of performance" (paragraph 39, last sentence) needed to be clarified, possibly by giving examples of failures of performance which might be specified in the contract. A suggestion was made to include in the last sentence of paragraph 39 unsatisfactory work as a ground for termination of the contract.

*Remedies other than termination*

126. It was observed that this section should be amended to make clear that it suggested the creation of a special system of remedies for failures to perform the post-construction obligations dealt with in the chapter. Appropriate remedies might be selected out of those described in other chapters dealing with the failure to perform construction obligations. It should be clarified that the section did not suggest the automatic application to post-construction obligations of remedies for failures to perform construction obligations.

*Summary*

127. It was generally agreed that the summary should be shortened. It should also be written in a style which could be readily comprehensible to non-lawyers.

*Drafting suggestions*

128. Several suggestions were made for improving the drafting of this chapter.

## SETTLEMENT OF DISPUTES<sup>23</sup>

129. It was noted that States or state-owned enterprises might be parties to works contracts, and the view was expressed that it would not be in accordance with the principle of state sovereignty for the courts of another State to exercise jurisdiction to settle disputes involving such parties. According to that view, the Guide should suggest negotiation, conciliation and arbitration as means of settling those disputes. According to another view, the issue of state sovereignty should not be mentioned in the Guide. It was agreed that the Guide should, however, indicate that the fact that one party to the contract was a State could influence the choice of a means of settling disputes arising from the contract.

130. A view was expressed that the principal means of settling disputes arising from works contracts should be judicial proceedings, and that the chapter as presently drafted over-emphasized the settlement of disputes by arbitral proceedings and by the use of experts. According to another view, however, arbitral proceedings were the most practical means of settling disputes arising from works contracts. It was generally agreed that the section of the chapter entitled "General remarks" should list the

<sup>23</sup>A/CN.9/WG.V/WP.17/Add.6.

various possible means of settling disputes, and the interrelation among those means, as well as kinds of disputes which might appropriately be settled by each means. In that connection it was noted that fact finding by experts might be mentioned.

131. A suggestion was made that the Guide should clearly point out that the supplementation and adaptation of a contract by a court, arbitral tribunal or expert, or the substitution of their consent for that of a party wrongfully refusing his consent, were not known in some legal systems, in order to avoid misleading readers who might not be familiar with those procedures. With respect to the refusal of a consent by a party, it was suggested that that situation could be dealt with by permitting a party to refuse consent only upon reasonable grounds. The question of whether the refusal of consent was reasonable would then be a question for resolution in dispute settlement proceedings, and the substitution of consent would not be involved. It was generally agreed that the Guide should stress that in drafting contractual clauses on the settlement of disputes the parties should carefully consider the law which would govern the various types of proceedings, and also consider in particular the scope of authority of a court, arbitral tribunal or expert, as the case may be.

132. It was suggested that the secretariat should reconsider the terminology used in the draft chapter. A question was raised as to whether the term "referee" instead of "expert" should be used in section F.

133. It was suggested that the Guide should differentiate between the resolution of routine problems or misunderstandings on the site, and the settlement of disputes. According to that view, the contract should provide that disputes to be settled by dispute settlement proceedings were to be formally notified by one party to another.

134. It was suggested that the first sentence of paragraph 1 should be reformulated so as to avoid the suggestion that disputes arising from works contracts always needed treatment different from the treatment of disputes arising from other types of contracts.

135. It was generally agreed that the last sentence in paragraph 4 should be deleted, since a court, arbitral tribunal or expert should not be able to order the construction to proceed notwithstanding the termination or suspension of the contract.

136. It was suggested that the Guide should mention the Convention on the Settlement of Investment Disputes between States and Nationals of other States of 18 March 1965, and indicate the scope of that Convention. According to another suggestion, in addition to the UNCITRAL Arbitration and Conciliation Rules, the Guide should refer to rules prepared by other international bodies. The prevailing view, however, was that the policy of the Working Group to refer explicitly only to texts prepared under the auspices of United Nations organs should not

be departed from. It was suggested that the references to the UNCITRAL Arbitration Rules and the UNCITRAL Conciliation Rules in paragraphs 17 and 11, respectively, should be removed to footnotes. Another view was that the reference should be kept in those paragraphs.

137. There was general agreement that the summary should be shortened. Various suggestions were made for improving the drafting of the chapter.

#### *Negotiation and conciliation*

138. It was generally agreed that the importance of negotiation as a means of settling disputes should be stressed in the Guide. It was suggested that the Guide should mention that the settlement of disputes by negotiation could avoid the disruption of the business relationship between the parties; moreover, dispute settlement by negotiation would avoid problems connected with enforcement of arbitral awards or judicial decisions. A suggestion was made that the phrase "broadly acceptable" in paragraph 5 should be replaced by a more appropriate one.

139. There was little support for suggesting in the Guide that the parties should be obligated to attempt to reach a settlement by negotiation before referring their dispute for settlement by other means. In that connection, a view was expressed that paragraph 6 should be deleted. According to another view, however, the concept behind paragraph 6 should be retained, but the parties should be warned of the problems which could arise if a long period of negotiation had to precede reference to settlement by other means.

140. It was suggested that paragraph 7 be redrafted so as to clarify that the settlement agreed to by the parties should be reduced to writing. Another suggestion was that paragraph 7 be deleted.

141. A suggestion was made to distinguish between the settlement of disputes by negotiation and conciliation, on the one hand, from settlement by arbitral and judicial proceedings, on the other. A view was expressed that the settlement of disputes by negotiation and by conciliation should be discussed in the same section, since those forms were interlinked. The prevailing view, however, was that they should be discussed in separate sections, since they reflected different methods of settling disputes. A view was expressed that the Guide should point out that negotiation or conciliation might be used in parallel with other means of settling disputes.

142. It was generally agreed that the Guide should mention a practice which existed whereby, before the construction commenced, the parties established a body which was to meet periodically on the site and suggest to the parties how disputes which arose in the course of the construction might be settled. The parties were free to accept or reject those suggestions, and to initiate legal proceedings at any time.

### Arbitration

143. Different views were expressed with respect to the advantages and disadvantages of arbitration as a means of settling disputes. It was suggested that, in addition to the advantages of arbitration mentioned in the draft chapter, the Guide should point out the following advantages: that arbitral proceedings might avoid the disruption of business relations between the parties which could result from judicial proceedings; that with arbitration neither party was forced to accept the jurisdiction of a court in the country of the other party; and that the parties could choose the language to be used in arbitral proceedings, and could possibly avoid the need to translate relevant documents. It was suggested that the Guide should mention as a disadvantage of arbitral proceedings that a party might have recourse to a court to set aside an arbitral award, which would result in prolonged dispute settlement proceedings.

144. Due to the different views expressed concerning the advantages and disadvantages of arbitration, it was generally agreed that the Guide should include only a brief listing of factors which the parties might wish to take into consideration in determining which means of dispute settlement to choose. It was suggested to include in the Guide a short characterization of arbitration as a method of dispute settlement.

145. With respect to the second sentence of paragraph 14, it was suggested to limit the point made in that sentence to cases where the arbitration agreement was recognized as valid by the court. A view was expressed that in the third sentence of that paragraph the word "usually" should be deleted, and that the sentence should indicate only that the courts "might" have the authority mentioned in that sentence.

146. It was suggested that paragraph 17 should be shortened. It was further suggested that the Guide should use the terms ad-hoc arbitration and institutional arbitration in paragraph 16, since those terms were commonly used in the practice. A view was expressed that paragraph 20 should discuss the procedure to be followed if the parties failed to appoint arbitrators. The paragraph should also refer to the possible relevance of the nationality of arbitrators in their selection. In the second sentence of paragraph 19 it was suggested that the term "works contract" be replaced by the term "arbitration agreements", as the latter was more appropriate.

147. A view was expressed that even greater emphasis should be placed on the importance of the place of arbitration. It was suggested that the discussion on the so-called mixed arbitration clause (paragraph 25) be deleted. The prevailing view, however, was that that type of clause was used in practice, and should be dealt with. It was noted that paragraph 25 covered two situations, i.e. where the parties agreed to two places of arbitration (the country of each party) and where they agreed upon two arbitration institutions, one located in the country of each party. While the disadvantages indicated in the latter part of the paragraph related to both those situations, the

present text might be interpreted as indicating that the disadvantages related only to the latter situation. The text should therefore be clarified. It was also suggested to indicate that an advantage of that clause was to enable the parties to compromise if the parties could not agree upon a single arbitration institution. The suggestion was also made to clarify that arbitration proceedings might be conducted at a different place from the location of the seat of the arbitration institution chosen by the parties. Under one view the last sentence in paragraph 23 might be deleted. Under another view that sentence was useful and should be retained. It was suggested that the parties might wish to specify in the contract that the arbitral award was to be issued at a place chosen by the parties, since issuance of the arbitral award at that place might facilitate its enforcement. It was suggested that the parties might be advised in the contract to choose the place where the site was situated as the place of arbitration, since very often relevant evidence would be available at the site.

148. It was suggested that the second sentence of paragraph 25 should be clarified, or deleted as superfluous. It was noted that under the legislation of some countries parties from those countries were only permitted to agree on a place of arbitration located in their countries, to agree upon arbitrators who were nationals of their countries, and to agree to the use of the official language of their countries in arbitral proceedings. The suggestion was made that paragraph 26 should explain the meaning of arbitrators being authorized to decide *ex aequo et bono*.

149. Under one view the first sentence of paragraph 27 should be deleted. The paragraph might indicate that any limitation in the arbitration clause in respect of the issues which might be settled in arbitration proceedings might lead to difficulties. Under another view the sentence should be retained. However, different views were expressed in respect of the issues which might be excluded from the arbitration. Under one view the list indicated in the paragraph 27 should be expanded (e.g. by the addition of a reference to liability for damages). Under another view some of the issues in the list should be deleted.

### Judicial proceedings

150. Differing views were expressed in respect of the section on judicial proceedings. Under one view that section should be expanded. It was suggested that the section might mention that under some legislation summary judicial proceedings might be initiated and that some issues could not be excluded from the competence of a court. Under another view, that section should be shortened. It was agreed to include in the section on "General remarks" a paragraph explaining that disputes would be settled in judicial proceedings if the parties did not agree upon an arbitration agreement. It was also agreed that a comparison should be made of the enforceability of a judicial decision and of an arbitral award, and the concept of enforceability stressed in choosing between judicial and arbitral proceedings.

151. It was suggested that paragraph 30 should mention that judicial proceedings might not always be an acceptable method for the settlement of disputes if a State or state-owned enterprise was a party to a works contract, and that the parties should consider whether such an issue existed and how to deal with it. Another suggestion was to indicate only that in those cases there might be in various countries different approaches to the settlement of disputes, including settlement in judicial proceedings.

152. It was agreed that the advantages and disadvantages of using an exclusive jurisdiction clause in the contract should be indicated. In addition to the disadvantages mentioned in the section, some other disadvantages (e.g. costs connected with judicial proceedings conducted abroad) might also be mentioned. It was noted that an exclusive jurisdiction clause might create great hardship to a party if the judicial decisions were not enforceable abroad, and the jurisdiction of other courts were excluded. However, a view was expressed that an exclusive jurisdiction clause might be useful since the courts which would have competence to decide disputes between the parties would be known from the time the contract was concluded.

153. It was suggested that only the first two sentences in paragraph 31 should be retained, and that paragraph 32 should be deleted as superfluous. It was noted that, in drafting the exclusive jurisdiction clause, the parties should take into consideration whether the selected court would be able to exercise the competence conferred by the parties. It was noted that the choice of the courts of a State other than the State of a party was not practical, and paragraph 31 should not include a reference to such a choice. Under one view paragraphs 33 and 34 did not convey significant information and might be deleted. Under another view those paragraphs were useful since they contained a warning against the possible consequences of an exclusive jurisdiction clause agreed upon by the parties without proper consideration. It was also noted that the applicable law might restrict the choice of a court by the parties.

#### *Experts*

154. It was noted that the settlement of disputes by experts was not regulated under any legal system. A view was expressed that the section on settlement of disputes by an expert should be deleted. The prevailing view, however, was that the use of experts in settling disputes was very important in practice, and, due to the absence of legal regulation, if the parties decided to engage an expert for settling their disputes they should be guided on how the issues which arose might be settled in the contract. If an expert was engaged, it would be advisable to determine in the contract what disputes he could settle, the extent of his authority, and the effects of his decision. It was stressed, however, that the parties should be cautious in engaging experts for the settlement of disputes, due to the absence of legal safeguards applicable to this method of settling disputes. It was agreed that the parties should be advised to limit the authority of experts to the

settlement of disputes of a technical nature which required rapid decisions. A view was expressed that the authority might be limited to the finding and verification of facts. It was noted that the decision of an expert would not have the binding effect of an arbitral award. The view was expressed that the respective functions of the expert and the consulting engineer should be clearly determined in the Guide.

155. It was pointed out that the potential authority of an expert to adapt or supplement the contract might be limited by the law applicable to the contract. It was agreed to place the section on the settlement of disputes by experts before the sections on settlement of disputes in arbitral and judicial proceedings. There was general agreement that the discussion in the chapter of the settlement of disputes by experts should be confined to general issues connected with the engagement of experts in the settlement of disputes and to delete paragraphs 40 to 46. Some of the issues discussed in those paragraphs might be mentioned, if needed, in connection with general issues.

#### *Disputes concerning failure of agreement or consent*

156. It was agreed to delete the section on disputes concerning failure of agreement or consent. It was suggested to include in the section entitled "General remarks" a paragraph which would recommend to the parties to consider to what extent, if at all, an arbitration clause should apply to cases of a failure of the parties to reach agreement, or a failure of a party to grant a consent if the agreement or consent was required by the contract. In addition, the way in which disputes concerning failure to agree on the adaptation of contractual terms to a new situation should be settled might be discussed in the chapters dealing with cases where such an agreement was required (e.g. in chapter XXII, "Hardship clauses" or chapter XXIII, "Variation clauses"). The way in which disputes concerning a failure to give a consent should be settled might be discussed in the chapters dealing with cases where such a consent was required (e.g. in chapter XI, "Subcontracting"). Cross-references to those chapters might be included in the section entitled "General remarks".

#### *Multi-party settlement of disputes*

157. It was agreed to delete the section on multi-party settlement of disputes. It was suggested that in the section entitled "General remarks" the attention of the parties should be drawn to issues which might arise in connection with the settlement of disputes when several parties participated in the construction of the works, and that some practical approaches to the resolution of the issues (e.g. the appointment of the same arbitrators to settle all disputes) be suggested.

#### *Illustrative provisions*

158. It was agreed to delete all the illustrative provisions at present set forth in the draft chapter, with the exception of paragraphs 1 and 7 of the illustrative arbitration clause set forth in footnote 7.

CHOICE OF CONTRACTING APPROACH<sup>24</sup>

159. There was wide agreement to organize the chapter into three sections, entitled "General remarks", "Single contract approach" and "Several contracts approach". It was generally agreed that all sub-headings in the chapter should be deleted, and that within the two latter sections the various contracting approaches dealt with in the chapter should be placed and discussed in the order of the comprehensiveness of the obligations undertaken by the contractor. Moreover, it was generally agreed not to use the terms "semi-turnkey contract" and "comprehensive contract" in the Guide, except when references were made to other texts or documents in which those terms were used.

160. A suggestion was made to remove paragraphs 11 and 12 from section C ("Engagement of more than one entity") to section B ("Engagement of single contractor"). According to another suggestion, however, those paragraphs properly belonged to section C.

161. A suggestion was made to expand upon the discussion of factors relevant to the choice of a contracting approach (paragraph 2), and to identify situations in which a particular contracting approach might be preferable.

162. It was suggested that the enumeration of the performances needed for the completion of the works should be deleted from the first sentence of paragraph 1, since the performances were set forth in paragraph 4. It was observed that the second sentence of paragraph 2 might be redrafted to eliminate a possible misinterpretation that in all cases other than the one mentioned in the sentence the purchaser should engage several contractors. A view was expressed that the single contract approach might be used by the purchaser even in cases where mandatory rules in his country required that local enterprises be engaged for certain aspects of the construction, since those enterprises might be engaged as subcontractors by the single contractor.

163. A view was expressed that the term "all performances" in the first sentence of paragraph 4 should be replaced by another term, such as "major tasks". Another view was that the former term should be retained, since the performance by the contractor was the relevant factor. It was suggested to redraft paragraph 4 so as to clarify that the obligation of the turnkey contractor was to render all performances needed for completion of the works, and not merely to co-ordinate the construction. It was also suggested to include training among the performances to be effected by the turnkey contractor. According to a further suggestion, paragraph 4 should advise that the turnkey contractor should complete the construction on a specified date and that the works should be capable of operating during a test period. It was suggested to add the words "in principle" before the word "liable" in the last sentence of paragraph 4.

164. It was suggested to substitute in the third sentence of paragraph 5 the word "supply" for the word "manufacture", and the word "specification" for the word "design". A question was raised as to whether tendering could be conducted on the basis of different designs (paragraph 5, last sentence).

165. In respect of paragraph 6, a suggestion was made to substitute in the second sentence the expression "at the same time" for the expression "on the other hand", and in the first sentence to substitute for the word "design" another expression to make clear that the design was not determined by unilateral decision of the contractor.

166. A view was expressed that, in connection with the characterization of the product-in-hand contract approach in paragraph 7, the contractor should not be obligated to ensure that his training was successful, but that he should only be obligated to use his best efforts to achieve that objective. According to another view, however, the characteristic feature of that contracting approach was the contractor's responsibility to achieve a specified result through training. It was suggested to substitute in the penultimate sentence of paragraph 7 the expression "assumes greater responsibility" for the expression "responsibility would be greater".

167. A suggestion was made to reflect in paragraph 8 that the capability of the purchaser in the field of the construction of the works was relevant to the choice of a contracting approach. In connection with the penultimate sentence of that paragraph, it was suggested to clarify that the total cost under the several contracts approach would be lower than under other approaches because under the several contracts approach the purchaser himself would perform some of the functions which would be performed by the contractor under other approaches. In that connection, it was suggested to indicate at the beginning of section C that in considering whether to adopt the several contracts approach the purchaser should consider whether he was capable of performing the co-ordination and other functions in relation to the construction which he would normally have to undertake under that approach. A view was expressed that under the several contracts approach, when the purchaser provided the design, the contractor might be obligated under the contract to notify the purchaser of evident defects in the design.

168. A view was expressed that paragraph 15 should be reformulated so as to provide a detailed clarification of the consequences of a failure of a contractor to perform with respect to the liability of the purchaser to other contractors. It was suggested that the purchaser might protect himself to some degree against those consequences by stipulating in each separate works contract that he would be liable to the contractor only for liquidated damages or penalties in the case where delay by other contractors prevented the contractor from commencing his performance. It was suggested to substitute in paragraph 16 the term "installation of equipment" for the term "erection of equipment".

<sup>24</sup>A/CN.9/WG.V/WP.17/Add.7.

169. In respect of paragraph 17 it was noted that the purchaser might wish to engage a construction manager in addition to a consulting engineer. It was also noted that the purchaser might engage a consulting engineer even under a single contract approach.

170. It was noted that the situation described in paragraph 18 was exceptional, and that a single contract approach would be preferable to that situation as a means of reducing the risks of co-ordination. It was suggested that a cross-reference to chapter X, "Consulting engineer", might be advisable with respect to the responsibility of the consulting engineer.

171. It was generally agreed that paragraph 20 should be deleted. Several suggestions were made for improving the drafting of the chapter.

#### TRANSFER OF TECHNOLOGY<sup>25</sup>

172. There was general agreement that the overall balance achieved by the draft chapter was satisfactory. It was proposed that section A ("General remarks") should refer to certain cases of transfer of technology which were at present not reflected in the section and which might occur when a works contract was concluded. Thus, the technology required to construct a portion of the works might be transferred to a purchaser by the contractor if it was agreed that the purchaser was to construct that portion. Technology might also be transferred to the purchaser with regard to the processing of the products of the works, in particular when those products were to be internationally marketed.

173. With regard to the description of the legal rules applicable to the grant of a patent, it was noted that a person who invented a product or process might apply for the grant of a patent not only to a government (paragraph 3, fifth sentence), but also to a governmental institution, such as a patent office. Furthermore, an inventor might apply not only in his own country, but also in other countries for the grant of a patent.

174. It was agreed that the description of national legal regulations, and the relevance of those regulations to the drafting of contract provisions, (paragraph 7) should be amplified. Reference should be made to legal regulations which might exist in the purchaser's country which might encourage the transfer of certain kinds of technology (e.g. technology which might increase productivity) or discourage the transfer of other kinds of technology (e.g. where similar indigenous technology was already available). Reference should also be made to the technology policy of a country which might be implemented by governmental agencies, and which might determine what provisions on transfer of technology might be included in a contract. It was also noted that the Guide should emphasize the importance of regulating the transfer of technology through contract provisions when no legal

regulations governing the transfer of technology existed in the purchaser's country.

175. A suggestion was made that the technology should be not only up to date, but also appropriate to local needs, and there should be no restrictions on exports by the transferor.

176. In regard to the description of the technology (subsection B.1), it was suggested that the contractor might be required to provide the description of the technology in the contract, since he had special knowledge of the technology. The Guide should also advise the purchaser to determine the level of the technology he required. In some cases, he might wish to obtain the most up-to-date technology, while in others he might prefer to obtain a technology which, while not being the most up to date, was the most appropriate for him. It was suggested that the Guide should note that the level of technology required could influence the price to be paid.

177. Views were exchanged on subsection B.2 ("Conditions restricting purchaser in use of technology"). Under one view, the present treatment of those conditions in the section was appropriate and should be retained. Under another view, the section emphasized too strongly the disadvantages which purchasers may suffer through those conditions, since in practice conditions which produced undue disadvantages for purchasers were not often imposed. It was agreed that, while the description of possible advantages and disadvantages to each party of such conditions should be retained, paragraphs 10 to 13 should be expanded by the addition of examples suggesting how the competing interests of the purchaser and contractor might be reconciled in a balanced manner. In regard to paragraph 11, it was proposed that the paragraph might suggest that, while the contractor should under the contract be given the right to control whether modifications to the technology might be effected by the purchaser, the contract should also provide that the contractor's consent to a request by the purchaser to make modifications should not be unreasonably withheld. In regard to paragraph 12, it was proposed that the paragraph might suggest that each party might be required to inform the other of improvements which he made to the technology, or that the contractor should be required against payment of an agreed remuneration to inform the purchaser of improvements that the contractor had made. Yet another possibility was that provision might be made for joint research and development of the technology. In regard to paragraph 13, it was proposed that the paragraph might note that, while export restrictions might be imposed on the purchaser in respect of certain markets, other export markets might be reserved for the purchaser.

178. It was proposed that the opening phrase, "For these reasons", should be deleted from the fourth sentence of paragraph 9, since the statement made in that sentence did not result from reasons stated in preceding sentences. It was also proposed that a further footnote be appended at an appropriate place to that paragraph

<sup>25</sup>A/CN.9/WG.V/WP.17/Add.8.

referring to the UNCTAD Draft Model Law on Restrictive Business Practices.

179. It was proposed that the guarantee to be given by a turnkey contractor suggested in the second sentence of paragraph 14 should be operative only if the works were operated by the purchaser in accordance with operation manuals and training provided by the contractor. The view was expressed that the substance of paragraph 15 was better presented in its original drafting (i.e. in paragraph 12 of A/CN.9/WG.V/WP.15/Add.3) than in the present drafting. The present drafting should therefore be reconsidered, retaining, however, changes to the original drafting proposed by the Working Group at its seventh session (i.e. in A/CN.9/262).

180. In regard to paragraph 16, the view was expressed that the second sentence of that paragraph, in addition to mentioning the cases presently set forth therein where infringement of industrial property rights of a third party might occur, should also mention that such infringement might occur through the construction of the works itself. In regard to the third sentence of paragraph 17, it was proposed that the supplier of technology should be obligated to assist the transferee of the technology when legal proceedings were brought against the latter only to the extent that the legal proceedings resulted from the supply of the technology by the supplier. In regard to the suggestion contained in the last sentence of paragraph 17 that royalty payments were to cease in the event of successful legal proceedings being brought against the purchaser by a third party, it was proposed that the payments should cease only if the contractor was liable to the purchaser for the infringement of the rights of the third party.

181. With regard to section C ("Issue special to know-how provisions: confidentiality"), the view was expressed that, while that section treated the issue of confidentiality as being special to know-how provisions, this was not always the case; confidentiality might also relate to certain information conveyed when industrial property rights were licensed. Under another view, however, information which was protected by industrial property legislation was not kept confidential, but merely protected from unauthorized use by the legislation. It was observed that the section contemplated only the imposition of obligations of confidentiality on the purchaser. However, in some situations (e.g. when improvements to the technology made by him were communicated by the purchaser to the contractor) it might be appropriate to obligate the contractor to maintain confidentiality. The section should be expanded to include a mention of those cases.

182. It was suggested that the Guide should note that even when a legal system contained obligations as to the observance of good faith during negotiations (paragraph 18, last sentence), it might nevertheless be advisable for the contractor to conclude an agreement as to confidentiality. It was also suggested that the term "public domain" (paragraph 19, third sentence) was not suffi-

ciently precise to be used to delimit the point of time at which obligations of confidentiality ended.

183. With regard to section D ("Communication of technical information and skills"), it was noted that documentation supplied at the time equipment was supplied might be relevant to the communication of technical information and skills. It was proposed that cross-references should be given to other chapters which referred to the need to supply documentation communicating technical information and skills. It was suggested that the words "and required under the contract to be delivered prior to the completion" be inserted in the second sentence of paragraph 22 between the words "works" and "has", as that would clarify the meaning. Divided views were expressed on the advisability of amending the last sentence of paragraph 22 to suggest that, where loss was caused to the purchaser through errors or omissions in the documentation, a liability to pay liquidated damages might be imposed on the contractor as an alternative to the liability of the contractor to pay damages referred to in that sentence.

184. In view of its importance, it was decided that the training of personnel (subsection D.2) should be dealt with in an independent section. It was proposed that paragraph 24 should indicate that the purchaser should be obligated not to remove trainees during the period of training without good reason.

#### TERMINATION OF CONTRACT<sup>26</sup>

185. A view was expressed that the contract need not contain provisions entitling a party to terminate the contract in certain cases (e.g. in the case of the bankruptcy of the other party, or in the case of abandonment of construction by the contractor), since the contract would be terminable under the applicable law. According to that view, the rules on termination under applicable law were adequate; consequently, the last sentence of paragraph 3 should be deleted. According to another view, however, even if termination were permitted under the applicable law, it would still be advisable for the contract to contain provisions dealing with termination, since the scope of or conditions to the right of termination under that law might be ill-suited to a works contract, or might lead to results different from those which the parties might wish to achieve. With respect to the last sentence of paragraph 3, it was suggested that the paragraph should elaborate upon the ways in which legal rules on termination under the applicable law might be ill-suited to works contracts.

186. A view was expressed that it was too categorical to suggest (paragraph 6) that the contract should be terminated only in respect of the construction which had not yet been performed because the purchaser could not return to the contractor the portion of the works which had already been constructed. It was noted that, in some cases, the purchaser might be able to dismantle and

<sup>26</sup>A/CN.9/WG.V/WP.17/Add.9.



return construction which had been effected by the contractor. In addition, if the contractor had not yet begun construction on site, but had supplied certain equipment or materials, the purchaser might be able to return to the contractor what had been supplied. The entire contract might be terminable by the purchaser in cases such as those. It was therefore generally agreed that paragraph 6 should be reformulated so as to be more flexible with respect to the extent to which the contract should be terminable. It was also agreed that the paragraph should be kept in a separate section, as it presently appeared in the draft chapter, rather than including it in the section on "General remarks".

187. A suggestion was made to replace the words "to be obligated" in the last sentence of paragraph 2 with "he may be required".

188. It was generally agreed that the word "unilateral" should be removed from the headings of subsections 1 and 2 of section C.

189. A suggestion was made to shorten the discussion in paragraphs 8 through 14. The prevailing view, however, was that the discussion should not be shortened.

190. With regard to the suggestion set forth in the draft chapter that before terminating the contract for certain grounds a party be required to give notice of the existence of those grounds to the other party, and then to give notice of termination if the grounds had not been remedied within a specified period of time, a view was expressed that the requirement of two notices was unnecessary. It was observed, however, that the requirement was in furtherance of the policy that termination should be resorted to only as a last resort, since it gave the party against whom the right of termination was being invoked an opportunity to remedy the grounds before the termination was effected. It was generally agreed to retain the two-notice system. It was also agreed to add at the end of the last sentence of paragraph 2 a reference to the requirement that the contractor remedy the grounds for termination within a specified period of time.

191. With respect to abandonment of the construction by the contractor, a view was expressed that the term "abandonment" was unclear, and involved the intent of the contractor. It could, therefore, give rise to questions in particular cases as to whether the contractor had abandoned the construction. According to a further view, a remedy of the purchaser in the case of abandonment of construction by the contractor might be to compel performance by the contractor. It was generally agreed that the Guide should clarify cases in which abandonment might be considered to occur (e.g. if the contractor notified the purchaser that he would not continue with the construction of all or part of the works, or if the contractor vacated the site before the completion of construction). It was also agreed that the Guide should recommend that, before terminating the contract, the purchaser should be required to deliver to the contractor a notice requiring him to continue with the construction,

and that the purchaser should be entitled to terminate if the contractor did not do so within a specified period of time. With respect to the illustrative provision in footnote 1, it was agreed that the provision concerning abandonment should be deleted, as the discussion in the text should give adequate guidance to the drafting of a provision on abandonment.

192. A suggestion was made to reconsider the words "may entitle" in paragraph 9.

193. It was generally agreed that the second sentence of paragraph 11 should be reformulated so as to clarify the idea that the contract might provide for the payment by a contractor in delay of liquidated damages up to a specified limit; when that limit had been reached, the contract should be terminable by the purchaser.

194. It was generally agreed that paragraph 14 should clarify that the purchaser might agree to subcontracting by the contractor which was otherwise in violation of contractual restrictions on subcontracting, in which case there should be no ground for termination of the contract by the purchaser.

195. With respect to termination by a party on the ground of bankruptcy of the other party, a view was expressed that a distinction should be drawn between the institution of involuntary bankruptcy proceedings against the party, and the adjudication of bankruptcy. The mere institution of bankruptcy proceedings should not constitute ground for termination of the contract by the other party, since the alleged bankrupt might successfully defend against an adjudication of bankruptcy. In the case of voluntary bankruptcy proceedings instituted by the party himself, an adjudication of bankruptcy would normally be issued within a short period of time, and the other party would not be prejudiced by waiting until the adjudication before terminating the contract. According to another view, however, the institution of voluntary or involuntary bankruptcy proceedings by or against a party could affect the performance of the contract by the party and should constitute a ground entitling the other party to terminate the contract. It was generally agreed that the Guide should stress the necessity that the contractual provisions in respect of bankruptcy be in accord with the applicable national laws on bankruptcy.

196. It was generally agreed that the term "performance guarantee" in paragraph 18 should be reconsidered, and that a reference to the chapter entitled "Security for performance" should be included in paragraph 18.

197. With respect to termination by the purchaser for convenience, it was noted that under many legal systems it was possible for either party to terminate a contract, so long as he fully compensated the other party for his losses resulting from the termination. A view was expressed that the second sentence of paragraph 19 should be deleted, since the right of termination for convenience should not be restricted to governments or government entities. According to that view, the exercise of the right would be

very expensive for a party, which inhibited the exercise of the right. On the other hand, it was observed that for policy reasons a Government or government entity might seek the right to terminate for convenience, and that the contract might restrict the amount of compensation to be paid to the other party upon termination for convenience. It was generally agreed that the second sentence of paragraph 19 should be changed to read "A purchaser, e.g. a Government or government entity, may wish to be entitled by the contract to terminate the contract for convenience". It was also agreed that paragraph 38 should refer to the possibility of restricting the amount of compensation payable upon the exercise of that right to, for example, a specified percentage of the contract price in respect of the terminated portion of the contract.

198. A suggestion was made to refer to termination for convenience in the section of the chapter entitled "General remarks". According to an additional suggestion, the third sentence of paragraph 19 should be deleted.

199. It was generally agreed that the language contained within brackets in paragraph 21 should be deleted. Also, the word "purchaser" as it first appeared in the last sentence of that paragraph should be changed to "contractor".

200. With respect to paragraph 28, it was generally agreed that the Guide should advise the parties that if they agreed that the contractor should be obligated to take the measures referred to in the paragraph, the contract should contain an express provision to that effect.

201. A suggestion was made in connection with paragraph 29 that the right of the purchaser or of a new contractor to use the contractor's equipment and materials should be subject to the rights of third persons (e.g. lessors) in those items. According to another view, however, such a condition should not be included in the contract, since in agreeing to a provision entitling the purchaser or a new contractor to use those items, the contractor should satisfy himself that such use would not infringe the rights of third persons, and the contractor should bear the risk of such infringement.

202. It was generally agreed that the contractor should have the obligations referred to in paragraph 33 only if the contract was terminated for reasons other than ones attributable to the purchaser. A view was expressed that the contractor should not be obligated to create drawings and documents which had not yet been created. It was generally agreed that, rather than referring to an obligation of the contractor to "create" those items, the fifth sentence of paragraph 33 should refer to an obligation to "obtain" them, since the contractor might obtain them from other sources.

203. A suggestion was made to delete the reference in paragraph 36 to the costs of repatriating the contractor's personnel. It was generally agreed, however, that the reference should be retained.

204. A view was expressed that paragraphs 36 and 38 should also refer to the loss of profit by the contractor as a result of termination of the contract. It was generally agreed, however, that it was sufficient for the paragraphs to refer to the chapter of the Guide dealing with damages.

205. Various other changes were suggested for paragraph 38. It was generally agreed, however, that the paragraph should remain unchanged, with the exception of the inclusion of a reference to a possibility of restricting the amount of compensation payable by a purchaser terminating for convenience (see paragraph 199, above).

## TERMINOLOGY AND FUTURE WORK

### *Terminology*

206. The Working Group considered the question whether the term "purchaser", or a different term, should be used in the Guide to indicate the party for whom the works was to be constructed.<sup>27</sup> After deliberation, the Working Group decided that for the English version of the Guide the term "purchaser" was preferable to other terms such as "owner", "employer" and "client", and should be used. It was agreed that the term "purchaser" was appropriate both for the case where the party for whom the works was to be constructed was a private enterprise, and for the case where the party was a government or governmental entity.

207. As regards the French version, the prevailing view was that the term "*acquéreur*" should be used as the equivalent of "purchaser". However, the French version of the Guide should explain at its commencement that the term "*acquéreur*" was used as an equivalent of the term "*maître d'ouvrage*", which was used in some legal systems.

208. It was noted during the deliberations that some passages of the Guide in language versions other than English did not correspond to the original English version, or were deficient in other respects. The secretariat was requested to make greater efforts to eliminate such deficiencies. In that connection, it was agreed that it would be helpful if members of the Working Group who might note deficiencies at any future time transmitted a record of those deficiencies to the secretariat.

### *Future work*

209. A statement was made by the Secretary of the Commission on the future course of the work as envisaged by the secretariat. It was proposed that the secretariat would revise the "Introduction" and all draft chapters of the Guide, and submit them to a further session of the Working Group. The Working Group could then determine whether the secretariat had fulfilled its mandate.

<sup>27</sup>A/CN.9/WG.V/WP.17, para. 4.

210. The Working Group agreed with that course of action. It was generally felt that during the next session the Working Group would restrict itself to determining whether decisions taken by it during its previous sessions had been reflected in the revised draft chapters before it.

The Working Group also discussed the possible duration and date of its ninth session. After deliberation, it was decided to recommend to the Commission that the session be held for a period of three weeks, during March-April 1987.

**B. Working paper submitted to the Working Group on the New International Economic order at its eighth session – Draft Legal Guide on Drawing Up International Contracts for the Construction of Industrial Works: report of the Secretary-General (A/CN.9/WG.V/WP.17 and Add. 1 to 9)**

**[Original: English]**

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<sup>a</sup>This draft chapter is a revised version of draft chapter II, "Choice of contracting approach" (A/CN.9/WG.V/WP.15/Add.8).

<sup>b</sup>This draft chapter is a revised version of draft chapter XXII, "Transfer of technology" (A/CN.9/WG.V/WP.15/Add.3).

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**[A/CN.9/WG.V/WP.17]****Draft legal guide on drawing up international contracts for the construction of industrial works: report of the Secretary-General**

1. The present report contains in its addenda a draft "Introduction" to the legal guide on drawing up international contracts for construction of industrial works (Add.1) and the following new draft chapters prepared by the secretariat: "Pre-investment studies" and proposed additions to the chapters "Procedure for concluding contract" and "Delay, defects and other failures to perform", Add.2; "General remarks on drafting", Add.3; "Supply of equipment and materials", Add.4; "Supply of spare parts and services after construction", Add.5; and "Settlement of disputes", Add.6.

2. The chapters have the titles and numbers assigned to them in the revised structure of the legal guide as approved by the Working Group at its seventh session.<sup>1</sup> However, in the exercise of the discretion given to the secretariat<sup>2</sup> it was considered advisable to change the title of chapter I to "Pre-investment studies" and to place the discussion of the issues concerning the selection of parties, in particular contracting with consortia and joint ventures in the chapter, "Procedure for concluding contract". It was also considered advisable to place the issues connected with the relevance of information based on pre-investment studies for the liability of parties in the chapter, "Delay, defects and other failures to perform".

3. In addition to the new draft chapters, the report contains revised draft chapters on "Choice of contracting approach", Add.7; "Transfer of technology", Add.8; and "Termination of contract", Add.9. These draft chapters are revisions of documents A/CN.9/WG.V/WP.15/Add.8 and Add.4, and A/CN.9/WG.V/WP.9/Add.5, respectively.

4. At a previous session of the Working Group the question was raised whether the term "purchaser", or another term, should be used in the legal guide to indicate the party for whom the works is to be erected. The term "purchaser" has been used in the draft chapters for the following reasons. First, the term is sometimes used in practice, including, for example, in other United Nations documents concerning the construction of industrial works.<sup>3</sup> Second, the term seemed preferable to other terms sometimes used in practice, such as "owner", "employer" or "client", since these terms connoted legal relationships between the parties which differ from the legal relationship between parties to a works contract. The term "purchaser" should create no implication that a works contract is in the nature of a sales contract, in which the relevant party is more often referred to as the

"buyer" (e.g. in the United Nations Convention on Contracts for the International Sale of Goods, Vienna, 1980), in particular because the term "contractor" is used in the legal guide to indicate the other party to the works contract.

**[A/CN.9/WG.V/WP.17/Add.1]****Introduction****A. Purpose and approach of Guide**

1. The purpose of this Guide is to assist persons involved in the negotiation and drawing up of international contracts for the construction of industrial works. These contracts are typically of great complexity, both with respect to the technical aspects of the construction and the legal relationships between the parties. The obligations to be performed by contractors under these contracts will normally extend over a relatively long period of time – often several years. Contracts for the construction of industrial works therefore differ in important respects from traditional contracts for the sale of goods or the supply of services in ways that may be unfamiliar to many persons. Consequently, rules of law drafted to govern sales or services contracts cannot settle in an appropriate manner issues arising in contracts for the construction of industrial works. These issues should therefore be settled by the parties through contract provisions. The preparation of this Guide was largely motivated by an awareness that the complexities and technical nature of this field often made it difficult for purchasers of industrial works, particularly those from developing countries, to acquire the necessary information and expertise required to draw up appropriate contracts. The Guide has therefore been designed to be of particular benefit to those purchasers, while seeking at the same time to take account of the legitimate interests of contractors.

2. The Guide seeks to assist parties in negotiating and drawing up international contracts for the construction of industrial works by identifying the legal issues involved in those contracts, discussing possible approaches to the solution of the issues, and, where appropriate, suggesting solutions which the parties may wish to incorporate in their contract. The discussion in the Guide and the solutions recommended are written in the light of the differences between the various legal systems in the world. It is hoped that one result of the Guide will be to promote the development of an international common understanding as to the identification and resolution of issues arising in connection with those contracts.

3. The Guide deals with contracts in which the contractor assumes the obligation to supply equipment and materials to be incorporated in the works, and either to erect the works or to supervise such erection by others. For brevity, these contracts are referred to in the Guide as "works contracts". In addition to the obligations just

<sup>1</sup>A/CN.9/262, paras. 95–99.

<sup>2</sup>A/CN.9/234, para. 13.

<sup>3</sup>For example, in the "General conditions for the supply and erection of plant and machinery for import and export", Nos. 188A and 574A, of the United Nations Economic Commission for Europe, and in the "UNIDO model form of turnkey lump-sum contract for the construction of a fertilizer plant" (UNIDO/PC.25).

mentioned, which are the essence of a works contract, a contractor often assumes other important obligations, such as the design of the works, and the transfer of technology.

### B. *Intended audience*

4. The Guide has been designed to be of use to persons involved at various levels in negotiating and drawing up works contracts. It is intended for use by lawyers representing the parties, as well as non-legal staff of and advisers to the parties (e.g. engineers) who participate in the negotiation and drawing up of the contracts. The Guide is also intended to be of assistance to persons who have overall managerial responsibility for the conclusion of works contracts, and who require a broad awareness of the structure of those contracts and the principal legal issues to be covered by them. Such persons may include, for example, high level officials of a government ministry under the auspices of which the works is being constructed. It is emphasized, however, that the Guide should not be regarded by the parties as a substitute for obtaining legal and technical advice and services from competent professional advisers.

### C. *Background to Guide*

5. In 1974 and 1975, the United Nations General Assembly, at its sixth and seventh special sessions, adopted certain resolutions dealing with economic development and the establishment of a new international economic order. As one of the organs of the United Nations, the United Nations Commission on International Trade Law (UNCITRAL) was called upon by the General Assembly to take account of the relevant provisions of those resolutions. It responded by including in its programme of work the topic of the legal implications of the new international economic order,<sup>1</sup> and considered how, having regard to its special expertise, and within the context of its mandate, it could most effectively advance the objectives set forth in the General Assembly resolutions. In doing so it also took into account a recommendation of the Asian-African Legal Consultative Committee (AALCC) that the Commission should deal with this topic.<sup>2</sup>

6. To assist it in defining the nature and scope of possible work in this area, the Commission in 1978 established a Working Group on the New International Economic Order, and charged it with the task of making recommendations as to specific topics which could appropriately form part of the programme of work of the

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its eleventh session, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17 (A/33/17)*, paras. 67(c)(vi), 68, 69.

<sup>2</sup>This recommendation is set forth in Recommendations of the Asian-African Legal Consultative Committee: note by the Secretary-General, A/CN.9/155, Annex (Ibid., Volume IX: 1978, Part Two, IV, B); see, also, Legal implications of the new international economic order: note by the secretariat, A/CN.9/194.

Commission.<sup>3</sup> The Working Group, aided by studies prepared by the Secretary-General, submitted to the Commission a list of several possible topics and reported that its discussions had revealed that, of this list, a study of contractual provisions commonly occurring in international industrial development contracts would be of special importance to developing countries, in view of the role of industrialization in the process of economic development.<sup>4</sup> Based upon the discussions and conclusions of the Working Group, the Commission in 1980 decided to accord priority to work related to contracts in the field of industrial development. It assigned this work to the Working Group, and enlarged the composition of the Working Group to consist of all 36 States members of the Commission.<sup>5</sup> In 1981 the Commission instructed the Working Group to prepare a Legal Guide on Drawing Up International Contracts for the Construction of Industrial Works.<sup>6</sup>

7. Work leading to the preparation of the Guide progressed in two stages. In the first stage, which was carried out in 1981 and 1982, the secretariat prepared for the Working Group a study of clauses commonly found in international contracts for the construction of industrial works. At sessions of the Working Group views were expressed regarding the various issues presented in the study, and possible solutions to these issues were discussed. The purpose of this discussion was to provide guidance to the secretariat when it commenced the drafting of the Guide.

8. Once this stage of the work had been completed, the Working Group in 1982 instructed the secretariat to begin work on the second stage, namely, the drafting of chapters of the Guide.<sup>7</sup> The secretariat prepared initial draft chapters of the Guide in consultation with experts in the field of industrial works contracts, and submitted these drafts to the Working Group. The draft chapters were revised by the secretariat in the light of the views expressed and decisions taken by the Working Group. After all the draft chapters of the Guide had been examined by the Working Group, revised by the secretariat, and examined by the Working Group a second time, the draft Guide was submitted to the Commission for adoption. The Legal Guide was adopted by the Commission at its ..... session in .....

9. In the preparation of the Guide numerous materials, including books, articles and other textual materials, as

<sup>3</sup>Report of the United Nations Commission on International Trade Law on the work of its eleventh session, fn. 1, above, para. 71; Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17 (A/34/17)*, para. 100.

<sup>4</sup>Report of the Working Group on the New International Economic Order on the work of its session, A/CN.9/176, paras. 31 and 32.

<sup>5</sup>Report of the United Nations Commission on International Trade Law on the work of its thirteenth session *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 143.

<sup>6</sup>Report of the United Nations Commission on International Trade Law on the work of its fourteenth session *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17 (A/36/17)*, para. 84.

<sup>7</sup>Report of the Working Group on the New International Economic Order on the work of its third session, A/CN.9/217, para. 130.

<sup>8</sup>Report of the United Nations Commission on International Trade Law on the work of its ... session, *Official Records of the General Assembly, ..... Session, Supplement No. 17 (A/.../17)*, para. ...



well as model forms of contract, general conditions of contract and contracts actually entered into have been consulted. Such materials are too numerous to be able to acknowledge them individually; however, recognition is hereby given to the contributions made by this growing body of literature to the area of international works contracts.

#### D. How to use Guide

##### 1. Arrangement of Guide

10. The Guide is arranged in two parts. Part One deals with certain matters arising prior to the time when the contract is drawn up. These include the identification of the project and its parameters through feasibility studies, and the possible legal character of the parties (chapter I); the various contracting approaches which the parties may adopt (e.g. turnkey, comprehensive, product-in-hand, semi-turnkey or separate contracts approaches) (chapter II); the possible procedures for concluding the contract (i.e. tendering, or negotiation without prior tendering), and the form and validity of the contract (chapter III). The discussion of these subjects has two aims: to direct the attention of the parties to important matters which they should consider prior to commencing to negotiate and draw up a works contract, and to provide a setting for the discussion of the legal issues involved in the contract.

11. Particular notice may be taken of the discussion in chapter II of the various possible approaches to contracting. The settlement of certain issues in the contract may depend upon the contracting approach which is adopted by the parties; and throughout the Guide, whenever appropriate, the discussion points out the different situations or solutions which may apply under different contracting approaches.

12. Part Two of the Guide deals with the drawing up of specific provisions of a works contract. It discusses the issues to be addressed in such provisions and in many cases proposes approaches to the treatment of those issues. Part Two is thus the core of the Guide. Each chapter in Part Two deals with a particular issue which is usually addressed in a works contract. To the extent possible, the chapters have been arranged in the order in which the issues dealt with in those chapters are frequently addressed in a works contract.

##### 2. Chapter summaries

13. Each chapter of the Guide is preceded by a summary of the chapter. The summaries are designed to serve the needs of management or other non-legal personnel who need to be aware of the principal issues covered by a particular type of contract clause, but who do not require a discussion of the issues in the depth or detail contained in the main text of a chapter. Such readers might obtain information which they require about the settlement of issues arising in the contract as a whole or in particular types of clauses by reading the summaries alone. To assist such readers who find that they would like further

information on particular points, cross-references are provided to paragraphs in the main text of the chapter where points referred to in the summary are discussed. Persons directly involved in drawing up works contracts, for whom the main text of each chapter is principally designed, might find reading the summaries to provide a useful overview of the subject-matter and issues covered by each chapter. They might also use the summaries as a check-list of issues to be addressed in negotiating and drawing up contractual provisions.

##### 3. "General remarks"

14. The main text of each chapter begins with a section entitled "General remarks". This is intended to serve as an introduction to the subject-matter of the chapter, and to cover certain matters which are applicable to the chapter as a whole so as to avoid repeating them in each section of the chapter where they are relevant. In some cases the section also deals with points which do not easily fit elsewhere within the structure of the chapter. The section often refers readers to other chapters where matters related to the chapter in which the section appears are discussed.

##### 4. Recommendations made in Guide

15. Where appropriate, the Guide contains recommendations as to ways in which certain issues in a works contract might be settled. These are simply suggestions which the parties may wish to take into consideration in the light of their particular contract and their respective needs and objectives. Such recommendations, including those that advise that the parties "should" take a particular course of action, are not intended to indicate that a particular approach is legally required, or is the only possible course of action. Any recommendation made in the Guide will of course have effect only to the extent that the recommendation is incorporated by the parties in their contract.

##### 5. Illustrative provisions

16. Some chapters contain one or more "illustrative provisions" set forth in footnotes. They are included in order to make issues discussed in the text of a chapter easier to understand. They also serve to illustrate how certain solutions discussed in the text, particularly those that are complex or may otherwise present difficulties in drafting, might be structured. *It is emphasized, however, that illustrative provisions should not necessarily be regarded as models of provisions which should be included in particular contracts.* The precise content and language to be used in a clause may vary with each contract. In addition, there is usually more than one possible solution to an issue, even though only one of those alternatives is presented in an illustrative provision. The illustrative provisions have been designed to fit within the overall scheme followed and approaches taken in the Guide. It is therefore important that parties who draft a provision for their contract based upon an illustrative provision should carefully consider whether the provision as drafted fits

harmoniously within their own contract. In general, illustrative provisions have not been included where an understanding of an issue and guidance to drafting is clearly obtainable from the text of the chapter.

#### 6. Terminology used in Guide

17. Certain terms used in the Guide have been used with particular meanings. The definitions given below are intended to assist in the understanding of those terms. Chapter IV, "General remarks on drafting", contains a list of terms and their definitions which the parties might use in the contract. Other terms (e.g. "hardship" or "variation") are defined in the chapters where the subject-matter covered by those terms is dealt with. The detailed alphabetical index located at the end of the Guide may also assist the reader in understanding terminology used in the Guide by referring to paragraphs where the particular terms are used and discussed.

#### *Applicable law*

"Applicable law" includes not only the legal rules which govern the mutual contractual rights and obligations of the parties (referred to in this Guide as the "law applicable to the contract": see chapter XXVIII, "Applicable law"), but other legal rules, of whatever nature, relevant to the legal relationship between the parties (e.g. procedural rules, administrative rules, or rules relating to the settlement of disputes).

#### *Clause*

"Clause" is a collection of provisions which deals with a certain major topic in the contract (e.g. a clause dealing with variations, or with the settlement of disputes).

#### *Time of conclusion of the contract*

"Time of conclusion of the contract" is the time when the contract becomes binding upon the parties (as distinct from the time when the parties are obligated to commence performance of the contract).

#### *Construction of the works*

"Construction of the works" may include supply of the design of the works, supply of equipment and materials to be incorporated in the works, and construction on site (i.e. civil engineering, building or erection of equipment).

#### *Contractor*

"Contractor" is the party to the contract who is to supply equipment and materials and erect the works or supervise such erection by others.

#### *Mandatory rules of law*

"Mandatory rules of law" are legal rules in force within a legal system, whether by virtue of statute, administrative regulation or otherwise, from which the parties may not by agreement derogate.

#### *Provision*

"Provision" is a portion or section of a contract clause which deals with a particular issue in the clause.

#### *Purchaser*

"Purchaser" is the party to the contract for whom the works is to be erected.

### [A/CN.9/WG.V/WP.17/Add.2]

## Chapter I. Pre-investment studies

### *Summary*

Pre-investment studies enable the purchaser to decide whether to proceed with investment in an industrial works and to determine the nature and scope of the works. They are usually carried out by the purchaser, or by a consultant engaged by him (paragraphs 1 and 2).

Pre-investment studies may include opportunity studies (paragraph 6), preliminary feasibility studies (paragraphs 7 and 8), feasibility studies (paragraphs 9 to 11) and detailed studies (paragraph 12).

The consultant to perform pre-investment studies may be selected through pre-qualification and competitive tendering or by negotiation without prior tendering (paragraph 13). The purchaser should consider whether it is desirable for the consultant who makes the pre-investment studies to be engaged subsequently to supply the design for the works or to serve as the consulting engineer, or for a potential contractor who makes the studies to be engaged as the contractor under a works contract (paragraphs 14 and 15).

\* \* \*

### A. General remarks

1. A purchaser contemplating investment in an industrial works will have to acquire and analyse a large amount of technical, commercial, financial and other information in order to be able to decide whether to proceed with the investment, and to determine the nature and scope of the works. That information is acquired and analysed in the context of one or more studies, referred to in this Guide as "pre-investment studies".<sup>1</sup> Pre-investment studies are in most cases carried out by or on behalf of the purchaser. Sometimes, however, they are carried out by the contractor (see paragraph 15, below). In some countries, particularly those in the process of industrialization, pre-invest-

<sup>1</sup>For a discussion of the content and methodology of pre-investment studies, see *Manual for the Preparation of Industrial Feasibility Studies* (United Nations publication, Sales No. E.78.II.B.5).

ment studies may also constitute an element of the country's overall planning process by enabling the country to compare and evaluate various potential industrial projects in order to determine its investment priorities.

2. Pre-investment studies are not only essential decision-making tools for the purchaser, they are often required by lending institutions which provide financing for the construction of industrial works. Those institutions sometimes even participate in or carry out pre-investment studies themselves.

3. The works contract will not require pre-investment studies to be made since they will have already been made by the time the purchaser is ready to conclude the contract. However, since the studies may contain information which might be made available by the purchaser to the contractor, the works contract may deal with the responsibility of the parties for the accuracy and sufficiency of that information. Contractual provisions in this regard are discussed in chapter XVIII, "Delay, defects and other failures to perform".

4. Pre-investment studies are often carried out in stages, the results of the study in one stage providing the basis for a decision whether to proceed to the study in the next stage and serving as the foundation for that study. The nature and sequence of those studies are typically as set forth in the following paragraphs.

5. Purchasers should be aware that an attempt to economize through studies which are inadequate could result in false savings, since this may result in the making of an improper investment decision, or having to vary the design of the works or construction methods during construction in order to conform to circumstances which were not known or were erroneously forecast as a result of the feasibility study.

### **B. Opportunity studies**

6. These studies are often carried out by countries in the process of industrialization. They are designed to identify potential investment opportunities within the country to be pursued either by the government itself or to be proposed to potential independent investors in investment promotion programmes. The studies may explore, for example, various possibilities for constructing works to manufacture a particular product which the government is interested in producing locally, and the potential market for the product. They may explore possibilities for constructing works to make use of locally available resources or to promote industrialization in a particular region. Opportunity studies usually deal only with the principal economic and technical aspects of various potential investment opportunities, without attempting to define the parameters of a particular project in detail.

### **C. Preliminary feasibility studies**

7. When the purchaser has begun to focus upon a particular project, he will engage in studies aimed at

ascertaining the technical and financial viability of the project. Full-scale feasibility studies (discussed in paragraph 9 to 11, below) are often costly; in some cases, therefore, the purchaser may wish to engage in a preliminary feasibility study in order to determine whether a full-scale feasibility study is warranted. In other cases, the purchaser may wish to by-pass the preliminary study and proceed directly with the feasibility study. This might be the case, for example, when the purchaser can conclude on the basis of an opportunity study that the feasibility study is justified.

8. The preliminary feasibility study should enable the purchaser to determine on a general basis the viability of the project. It will often investigate many of the same matters and address many of the same issues as does the feasibility study (see paragraph 10, below), although in less detail. The preliminary feasibility study will often enable the purchaser to evaluate various options concerning the scope and the manner of execution of the project. It may also point out particular matters requiring more detailed investigation and help to determine the nature of investigations and tests to be conducted in the context of the feasibility study. On the basis of the preliminary feasibility study the purchaser might approach potential sources of financing for the project. The purchaser may wish to do so prior to the full-scale feasibility study in particular because some lenders wish to have their terms of reference incorporated in the feasibility study, and sometimes to have their own experts involved in the study.

### **D. Feasibility studies**

9. The feasibility study should be designed so as to provide the purchaser with the information which he needs in order to decide whether to invest in the project and, if he decides to do so, to settle upon the parameters of the works to be constructed (e.g. its size, location, cost, production capacity, and perhaps the possible technologies which may be used), the source and method of financing, the contracting approach to be used (e.g. product-in-hand contract, turnkey contract, comprehensive contract, semi-turnkey contract or separate contracts approach: see chapter II, "Choice of contracting approach"), and the method of obtaining offers from contractors (e.g. by tender or by negotiation: see chapter III, "Procedure for concluding contract"). The lending institution which is to finance the construction of the works may collaborate in the making of these decisions on the basis of the feasibility study.

10. The exact scope and contents of the feasibility study will depend on the project concerned. However, feasibility studies typically cover the following matters and issues: the potential market size and potential market price for the product to be produced by the works; the capacity of the works; raw materials, power and other inputs for the manufacturing process; the location and site of the works; transport and other elements of infrastructure; civil, mechanical and electrical engineering; technology; organization of the works and overhead

costs; manpower requirements; and legal constraints (e.g. land-use requirements and environmental controls). The feasibility study should contain an analysis of the financial viability of the works, including the total investment required, possibilities concerning the financing of construction and the commercial profitability of the works. It may also evaluate the project in relation to the national economy. The feasibility study will usually also include an investigation of the site to determine its topography and geological characteristics.

11. Feasibility studies typically assume the existence of certain situations or facts, such as the availability or cost of construction materials. The purchaser should be able to ascertain from the study the assumptions which have been made and the risk that the real situations or facts are different from those assumed. The purchaser should determine which of these risks he might require the contractor to undertake, bearing in mind the cost to him of the contractor undertaking the risks. Sometimes feasibility studies include "sensitivity studies", which vary some of the assumptions on which the feasibility study is based to determine the effect of those changes in assumptions on the feasibility of the project.

#### **E. Detailed studies**

12. A detailed study is sometimes conducted prior to entering into the works contract or to soliciting offers in order to settle final details of the works and of construction methods, as well as the nature and number of contracts to be entered into.

#### **F. Specialists performing pre-investment studies**

13. Pre-investment studies are usually made by a team composed of specialists in various relevant disciplines, e.g. economists, financial experts, geologists, engineers and industrial management experts. Since purchasers often do not possess all of the required expertise within their own staff, it is common for consulting firms to be engaged to conduct the studies. These consultants may be selected through pre-qualification and competitive tendering procedures or by negotiation without prior tendering. Some international lending institutions require the consultant to be chosen by pre-qualification and tendering. Consultants are often engaged under contracts which define in detail the rights and obligations of the parties and which address many of the same issues as those addressed in the contract for the construction of the works.<sup>2</sup>

14. The purchaser should consider whether the consultant who conducts the pre-investment studies should subsequently be engaged to supply the design for the works or to serve as the consulting engineer (see chapter X, "Consulting engineer"). On the one hand, if the consultant who makes the studies believes that he might

be engaged to perform such additional functions, he might be tempted to produce studies which are more encouraging to the purchaser to proceed with the project than is justified. On the other hand, when the consultant who supplies the design for the works is different from the consultant who did the pre-investment studies, he may have to spend time examining the studies in detail, and perhaps even duplicate some investigations made for the studies, resulting in higher cost to the purchaser. This would not be the case if the design were produced by the same consultant who made the studies. Some international lending institutions will not allow the consultant who made the pre-investment studies to serve as the supplier of the design or as the consulting engineer.

15. Sometimes, and in particular when a turnkey contract is contemplated, feasibility studies and other pre-investment studies are made by a potential contractor. In some cases the contractor takes the initiative in proposing the studies to the purchaser with a view towards showing that the works is feasible and profitable so that the purchaser will contract with him for the construction of the works. The advantages and disadvantages of having the pre-investment studies made by the contractor are the same as when the studies are made by a consultant who supplies the design for the works or serves as the consulting engineer. If the studies are made by the contractor, the purchaser may wish him to accept full responsibility for the results of the studies and the conclusions appearing in them as to the feasibility of the project including, for example, the availability of raw materials and the marketability of projected levels of output of the works. If the studies are made by a consultant, on the other hand, he may assume responsibility only for making the studies competently, without guaranteeing their results. If the pre-investment studies are made by a contractor, the purchaser may wish to have the studies reviewed by an independent specialist. Some lending institutions will not allow the entity who made the pre-investment studies to serve as the contractor.

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### **Chapter XVIII. Delay, defects and other failures to perform (continued)<sup>3</sup>**

#### *Responsibility for information needed for construction of the works*

1. When the purchaser solicits offers for the construction of the works (see chapter III, "Procedure for concluding contract") he may communicate certain information to potential contractors concerning conditions at the site or other information which will affect the construction of the works. Some of this information may

<sup>3</sup>The following material is included in this addendum because of its relationship with the material on pre-investment studies, although its scope is not limited to that subject. It will be incorporated in chapter XVIII, "Delay, defects and other failures to perform" (see A/CN.9/WG.V/WP.11/Add.2 and Add.3), with appropriate headings and numbering.

<sup>2</sup>See *Manual on the Use of Consultants in Developing Countries* (United Nations publication, Sales No. E.72.II.B.10).

have been obtained by the purchaser in the pre-investment studies (see chapter I, "Pre-investment studies"). In some cases, the contract might presuppose that the purchaser has provided particular types of information, such as information concerning conditions at the site.

2. Contractors, in preparing their offers, will perform certain investigations in order to obtain information concerning matters affecting the performance to be required under the works contract, and which they will therefore need as a basis for their offers. However, such investigations are often limited, since contractors cannot incur the expense of extensive investigations when they are not assured of being engaged by the purchaser. In addition, contractors may have only a relatively short period of time within which to prepare and submit their offers to construct the works (see chapter III, "Procedure for concluding contract"). To the extent that the purchaser provides information to the contractor, and to the extent that the contractor is able to rely on that information, the contractor may be freed from having to perform the investigations necessary to acquire it himself. This could result in financial savings to the purchaser if the purchaser could acquire the information at a lesser cost than could the contractor or if the contractor could offer to construct the works at a lower price by virtue of having more precise information as to conditions affecting the construction. The works contract should allocate between the parties responsibility for information upon which the contractor's offer is based, and responsibility for the discovery after the conclusion of the contract of conditions which were not known or taken into account when the contract was concluded.

3. The parties should consider the most appropriate way to allocate responsibility for the sufficiency and accuracy of the information. Under one approach, various types of information would be considered individually in order to determine the most appropriate allocation of that responsibility. In making that determination the parties might consider such factors as which party can more easily and at least cost obtain the information and bear the risk of any inadequacy or error in the information, and which party can more easily control the sufficiency and accuracy of the information. Information for which one party or the other might be specifically allocated responsibility might include, for example, conditions at the site (e.g. topography, climate), the nature of the technology that might be used in the works, and environmental and other legal regulations which might affect the construction of the works.

4. A lump-sum contract (see chapter II, "Choice of contracting approach") would provide that the purchaser was to bear the costs of any additional work required to be performed by the contractor as a result of insufficiency of or errors in the information for which the purchaser is responsible. In a cost-reimbursable or unit-price contract, those costs would be borne automatically by the purchaser; however, such contracts might provide that those costs were not to be taken into account in determining whether a cost ceiling had been reached. A variation of

that approach, irrespective of the method of pricing used in the contract, might require the contractor to examine the information provided by the purchaser for any apparent inconsistencies or other errors prior to the conclusion of the contract, and to notify the purchaser of any errors at that time. The contract might also provide that the contractor was to bear the costs of additional or unnecessary work occasioned by any errors in the information which he had failed to notify to the purchaser.

5. Under a second approach, the contractor would be required to make himself aware of any information or situations which were reasonably discoverable or foreseeable by him, and to bear the costs of additional work required as a result of a failure to discover such information or situations, with the purchaser assuming the costs resulting from the existence of information or situations which were not reasonably discoverable or foreseeable. The provision of information by the purchaser to the contractor would not free the contractor from his responsibility to obtain all necessary discoverable or foreseeable information, even if that required duplicating investigations performed by the purchaser. The provision of information by the purchaser could make certain information or situations foreseeable which would not otherwise be foreseeable. Under a third approach, the contractor would be responsible for all information which he needed in order to perform the contract, and would bear the cost of any additional work required due to the insufficiency or inaccuracy of any information or the existence of conditions not foreseen at the time the contract was entered into.

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### Chapter III. Procedure for concluding contract (continued)<sup>4</sup>

1. A purchaser may contemplate entering into a contract with a group of firms, rather than with a single firm. He may also contemplate entering into a joint venture with the contractor. This Guide does not deal in depth with the legal issues connected with arrangements of these types.<sup>5</sup> The purpose of the discussion of these

<sup>4</sup>The following material had been proposed to be incorporated in chapter I of the Guide together with the material on pre-investment studies (see "Revised draft outline of the Guide", A/CN.9/WG.V/WP.15/Add.7). Since the relationship of this material with the material on pre-investment studies is slight, it is now proposed to separate them, and incorporate the following material in chapter III, "Procedure for concluding contract" (see A/CN.9/WG.V/WP.15/Add.10), with appropriate headings and numbering.

<sup>5</sup>Issues relating to groups of firms acting as contractors are discussed in *Guide for Drawing up International Contracts between Parties Associated for the Purpose of Executing a Specific Project* (United Nations publication, Sales No. E.79.II.E.22) and in *Guide on Drawing up Contracts for Large Industrial Works* (United Nations publication, Sales No. E.73.II.E.13). Joint ventures between contractors and purchasers are discussed in *Manual on the Establishment of Industrial Joint-Venture Agreements in Developing Countries* (United Nations publication, Sales No. E.71.II.B.23).

arrangements in the present chapter is to bring them to the attention of the parties and to point out some of the principal issues associated with them which the parties may wish to consider.

#### A. Contracting with groups of firms

2. The construction of a complex and large-scale industrial works is often beyond the technical or financial means or the experience of a single contractor. This may be the case in particular where all or a substantial part of the works is to be constructed under a single contract, as in the product-in-hand contract, comprehensive contract, and turnkey contract approaches (see chapter II, "Choice of contracting approach"). In such a case one possibility may be for a single firm to enter into the contract as the contractor, and to engage subcontractors in order to perform those obligations which he cannot himself perform (see chapter XI, "Subcontracting"). Another possibility may be for a group of firms to combine and with their collective expertise and resources to perform the obligations of the contractor. In addition, groups of firms may be created for the purpose of constructing the works in order to satisfy eligibility requirements (e.g. those concerning the nationality of the contractor) which may be imposed by law, by the purchaser or by an international lending institution, or in order to take advantage of financial benefits available to contractors meeting certain nationality requirements.

3. The terminology used to refer to a group of firms acting as the contractor is not settled. In practice, the terms "consortium" and "joint venture" are often used. Sometimes, "consortium" is used to refer to a group in which the various elements of the construction of the works are specifically allocated among separate firms which are members of the group by an agreement among the members, and in which under the agreement and under the works contract with the purchaser each member is responsible only for the performance of the obligations allocated to him. The term "joint venture" is often used to refer to an arrangement by which two or more separate firms combine to form a business unit, and the obligations of the contractor under the works contract are performed by the unit, it being agreed among the firms which are members of the unit and in the works contract with the purchaser that each member is jointly and severally responsible for the full performance of those obligations. Units of that nature may be organized as independent legal entities, but usually are not. An arrangement sometimes known as a "silent" consortium or joint venture may exist when only one firm enters into a contract with the purchaser but has an arrangement with other firms concerning the allocation of the various obligations of the contractor. The purchaser may or may not be aware of the arrangement. In such a case the purchaser may claim performance only by the firm which entered into the contract.

4. The organization and management of the group and the division of responsibility among members of the group is determined principally by the agreement among the members and by the law governing the agreement. However, various aspects of the agreement will have consequences with respect to the performance of the contract for the construction of the works. The purchaser should take these aspects into consideration in connection with the works contract.

5. The purchaser may enter into a contract with a group of contractors in various ways. If the group is organized as an independent legal entity, the purchaser will enter into the contract with the entity itself, and the entity will function under the works contract as a single party. The legal relationship of the purchaser will be with that entity, and not with the individual members of the entity. In the event of a failure by the entity to perform its contractual obligations, the purchaser may be restricted by the law pursuant to which the entity was established to pursuing its claim against the entity, rather than against the individual members. This point may be of particular concern to the purchaser, since some legal systems permit these entities to be organized with minimal capitalization, and limit the responsibility of their members to the amount of their respective capital contributions. In such a case it may be important for the purchaser to obtain performance guarantees in order to provide sufficient financial security for the performance by the contractor (see chapter XVII, "Security for performance"). In some legal systems, however, the members of entities of certain types may have some liability for a failure of the entity to perform.

6. If, as is normally the case, a group acting as a contractor is organized without independent legal personality, it would be advantageous to the purchaser if each of the members became a party to the contract, since responsibility for performance would be spread among several firms instead of being concentrated in only one firm. The purchaser would be best protected if all of the members of the group were to assume joint and several liability for the performance of the obligations incumbent upon the contractor, instead of each member assuming liability only for obligations to be performed by him. With all members being jointly and severally liable, the purchaser would be able to claim performance against any one or combination of the members without having to attribute the failure to a particular member, and each member would be personally liable for any failure to perform. In the event of such a failure the purchaser would be able to reach the combined assets of all the members.

7. It would be advisable for the purchaser not to have to deal with each member of a group which has no independent legal personality in connection with matters arising during the course of the performance of the contract. The members may designate one of the members to serve as spokesperson for the group and to act on behalf of all members in their dealings with the purchaser.

### B. Joint venture between contractor and purchaser

8. An alternative to the conventional contract, in which each party has certain rights and assumes certain obligations, including assumption of the costs and risks associated with the performance of his own obligations, is the joint venture between the contractor and the purchaser. Joint ventures of this nature involve, to varying degrees, the combining of resources of the contractor and the purchaser in order to accomplish the objectives of the venture, and the sharing by the parties of the profits and losses of the venture as well as the risks associated with it. The objectives of the joint venture usually include not only the construction of the works, but also the subsequent operation of the works and the production and marketing of the output of the works.

9. A joint venture between the contractor and the purchaser could in some cases offer certain advantages to the purchaser as compared with a conventional contract. The joint venture might facilitate the obtaining of technology, managerial skills and access to world markets (e.g. markets to which the contractor has access) by the purchaser. The sharing of the costs and risks associated with the venture means that those factors are less burdensome to the purchaser than under a conventional contract. A joint venture involving the production and marketing of the output of the works could give the contractor a greater interest in the proper functioning of the works. That factor sometimes prompts international lending institutions to require the contractor to enter into a joint venture with the purchaser. The cost to the purchaser of those advantages, however, is the loss of some degree of managerial control and the necessity of sharing the profits of the venture with the contractor.

10. To the contractor, a joint venture with the purchaser may present the advantages of, for example, facilitating access to markets in the country or region of the purchaser, or to markets which favour purchasing from the country of the purchaser, and the opportunity to participate in the profits of the venture. Furthermore, some developing countries offer financial incentives to encourage foreign enterprises to form joint ventures with local enterprises. The costs to the contractor of these advantages arise principally from his sharing of the risks associated with the venture.

11. When a joint venture is formed between the contractor and the purchaser, the joint venture entity usually enters into a contract for the construction of the works which is separate from the agreement establishing the joint venture. If the joint venture entity has independent legal personality, it might enter into a works contract with the contractor who is a member of the joint venture, or it might enter into a works contract with a second contractor who is not a member of the joint venture. If the joint venture entity does not have independent legal personality, it may enter into a works contract with a contractor who is not a member of the joint venture. In some cases the purchaser may enter into a works contract with the

contractor, and enter into a joint venture with the contractor only with respect to the production and marketing of the output of the works. In any of these cases the discussion in part two of this Guide is relevant to the issues arising in the context of the works contracts.

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[A/CN.9/WG.V/WP.17/Add.3]

## Chapter IV. General remarks on drafting

### Summary

A purchaser may find it advantageous to prepare the first draft of a works contract, as this will enable him to clarify what he wishes to achieve through the contract. The contract terms as reduced to writing should be unambiguous, and the relationship between the various documents comprising the contract should be clearly established. After the parties have reached agreement on the main technical and commercial issues, it would be useful to review the documents in the light of the law applicable to the contract (paragraphs 1 to 3). The parties should also take account of mandatory legal rules of a public nature relevant to the contract (paragraph 4). If the parties use precedents (e.g. standard forms of contract) to facilitate their drafting, they should carefully examine the provisions of those precedents to see if the precedents accurately reflect their own agreement (paragraph 5).

It would be preferable to conclude the contract in a single language version understood by the senior personnel of each party who will be implementing the contract. If the contract is concluded in more than one language version, the contract should provide which version is to prevail in the event of a conflict between them (paragraph 6).

The parties to the contract should be identified in a controlling document which comes first in logical sequence among the contract documents. This document should set forth the names of the parties, their addresses, the subject-matter of the contract, and also record the date on which and the place at which the contract was signed. Evidence should be obtained of the capacity of a party to enter into the contract, and the authority of a representative or agent to represent or contract on behalf of a party (paragraphs 7 and 8).

The parties should clearly identify which documents constitute the contract, and provide rules for resolving inconsistencies between contract documents (paragraphs 9 and 10). The parties should also determine the extent to which oral exchanges, correspondence and draft documents which emanated during the negotiations may be used to interpret the contract documents (paragraph 11). The parties may wish to provide that headings and marginal notes used in the contract to facilitate its reading

are not to be regarded as affecting the rights and obligations of the parties. If considered desirable, recitals may be included in the controlling contract document to describe the object of the contract, or the context in which it was concluded (paragraphs 12 and 13).

Notifications by one party to the other are frequently required under works contracts for certain purposes. It would be desirable to provide that all such notifications are to be given in writing. What may qualify as writing should be defined. The contract should specify the time when a notification is to be effective: either upon despatch by the party giving the notification, or upon receipt by the party to whom the notification is given (paragraphs 15 to 17). The contract should also determine in which cases a notification may be given by the purchaser to a representative of the contractor in the country where the works are being constructed, in which cases it must be given to the head office of the contractor, and the consequences of a failure to notify (paragraphs 18 and 19).

Works contracts often define key words used in the contract to ensure that the words defined are understood in the same sense wherever they are used in the contract. What words need to be defined, and the meaning to be assigned to a particular word, will depend on the language used in a particular contract and the intention of the parties. Parties may find the definitions set forth in this chapter useful for the purpose of formulating definitions relevant to their contract (paragraphs 20 to 22).

\* \* \*

#### A. *General remarks*

1. A works contract is usually the end product of extensive negotiations between the parties, including oral exchanges, correspondence and the consideration of draft documents prepared by each party. A first draft of the contract is often prepared by one of the parties, usually the purchaser. This draft may be provided to prospective tenderers, or to persons with whom the purchaser proposes to negotiate a contract, as the basis on which a contract is to be concluded. The purchaser may find it advantageous to prepare a first draft, as the process of preparing the draft will generally clarify what he wishes to achieve through the contract and enable him to determine his negotiating position. During negotiations between the prospective parties to the contract, this first draft will be refined and elaborated resulting in a preliminary set of contract documents which, after final review, will become the contract between the parties.

2. The contract may need to be administered by persons who have not participated in the negotiations leading to the conclusion of the contract, and at a time long after the negotiations have taken place. Accordingly, the parties should take particular care to ensure that the contract terms as reduced to writing are unambiguous and will not

give rise to disputes, and that the relationship between the various documents comprising the contract is clearly established. To this end, each party may find it useful to designate one person, either on his staff or specially retained for this purpose, to be primarily responsible for the drafting. Such a person should be a skilled draftsman familiar with international works contracts and have a mastery of the language in which the contract is to be drafted. To the extent possible, this person should be present during important negotiations. Each party may find it useful to have the final contract documents scrutinized by a team having expertise in the areas of knowledge reflected in the documents in order to ensure accuracy and consistency of style and content.

3. After the parties have reached agreement on the main technical and commercial issues, it would be useful if the parties agreed upon the law applicable to the contract (see chapter XXVIII, "Choice of law") and reviewed the documents reflecting their agreement in the light of the applicable law. This law will contain rules on the interpretation of contracts and may contain presumptions as to the meaning of certain words or phrases. It may also contain mandatory rules regulating, in particular, the form or validity of contracts, which the parties should take into account in drafting their contract. In particular, it is desirable that the legal terminology of the contract should, wherever possible, be in conformity with the terminology of the applicable law.

4. In addition to the law applicable to the contract, the different types of relevant mandatory legal rules of an administrative, fiscal or other public nature in the country of each party should be taken into account before the contract is finalized. Certain rules may concern the technical aspects of the works or the manner of its construction (e.g. rules relating to environmental protection, or safety standards to be observed during construction). The terms of the contract should not conflict with such rules. Other rules may concern export, import and foreign exchange restrictions, and should be taken into account when formulating the rights and obligations of the parties on issues such as the export and import of equipment and materials, the supply of services, the transfer of technology and payment of the price. Yet other rules relating to taxation may be a factor influencing the contracting approach to be chosen (see chapter II, "Choice of contracting approach") and may determine whether provisions should be included in the contract dealing with liability for tax. Furthermore, the parties should take into consideration treaties on the avoidance of double taxation which may have been concluded between their countries. The parties may find it desirable to consult expert advisers on the various aspects of liability for taxation when drafting their contract.

5. If the parties find it useful to examine standard forms of contract, general conditions, standard clauses, or previously concluded contracts as precedents to facilitate the preparation of contract documents, the provisions of such precedents should be adopted only after critical examination. A precedent may as a whole reflect a



balance of interests which is not desired, or the various terms of the precedent may not accurately reflect the terms agreed to by the parties to that contract. Or, while a provision regarded as a precedent may be acceptable in isolation, it may not be consistent with other provisions agreed upon by the parties. The parties may find it useful to refer to the illustrative provisions set forth in the various chapters of this guide as aids to drafting (see also "Introduction").

### **B. Language of contract**

6. The contract may be concluded in only one language version, or in more than one language version. Concluding the contract in only one language version will reduce conflicts of interpretation in regard to contractual provisions. The language chosen should be one understood by the senior personnel of each party who will be implementing the contract, and may even be a language other than that of either the purchaser or contractor. The language should also contain the technical terms necessary to reflect the agreement of the parties on technical issues. If the language of the country of the applicable law is one understood by both parties, dispute settlement may be facilitated by a choice of that language. Where the parties cannot agree to confine the contract to a single language version, the parties should specify in the contract which language version is to prevail in the event of a conflict between the various versions. For example, if the contract is concluded in two languages, but the negotiations were conducted in one of the two languages, they may wish to provide that the version in the language of the negotiations is to prevail. A provision that one of the language versions is to prevail would induce both parties to clarify as far as possible the prevailing language version. The parties may wish one language version to prevail in respect of certain contract documents (e.g. technical documents) and another language version in respect of the remainder of the documents. Alternatively, the parties may provide that all language versions are to have equal status. In such a case, however, the parties should attempt to provide guidelines for the settlement of disputes if conflicts are later shown to exist between the language versions (e.g. that the rights and obligations of the parties should be determined in accordance with their true intention, regard being had to the contract in both its language versions).

### **C. Parties to and execution of contract**

7. The parties to the contract are normally identified in a document which comes first in logical sequence among the contract documents, and which usually performs a controlling role over the other documents. This document should set forth in a legally accurate form the names of the parties, indicate their addresses, record the fact that the parties have entered into a contract, briefly describe the subject-matter of the contract, and be signed by the parties. It should also set forth the date on which, and the place where, the contract was signed. Further reference

in the contract to the parties would be facilitated if the phrases "hereinafter referred to as the purchaser" and "hereinafter referred to as the contractor" are added after the names of the purchaser and contractor respectively. The construction is sometimes undertaken by two or more enterprises acting in collaboration (sometimes referred to as a consortium: see chapter I, "Pre-investment studies". In such cases, the names and addresses of each enterprise should be set forth. A party may have several addresses (the address of its head office, the address of a branch through which the contract was negotiated) and it may be preferable to include an address to which notifications directed to a party may appropriately be sent (e.g. the head office, see paragraph 18, below).

8. Parties to works contracts are usually corporate bodies. In such cases the source of their corporate status (e.g. incorporation under the laws of a particular country) should be set forth. Corporate bodies often have limitations on their capacity to enter into contracts. Each party should therefore require from the other documentary proof of capacity to enter into the works contract. If a party to the contract is a corporate body and the contract is signed by an official of the corporate body (e.g. the managing director), evidence that the official can bind the corporation should be annexed. If the contract is entered into by an agent on behalf of a principal, the name, address, and status of the agent and principal should be identified, and evidence of authority from the principal enabling the agent to enter into the contract on his behalf may be annexed (unless sufficient evidence of authority has already been provided with the tender documents, see chapter III, "Procedure for concluding contract").

### **D. Contract documents and interpretation**

9. It is desirable to avoid uncertainty as to what constitutes the works contract. To achieve this, the parties should in the first place reduce to writing the terms agreed upon between them. It may in addition be desirable for the contract to provide that any modification to such terms should also be effected in writing. A works contract usually consists of several documents (e.g. documents setting out contract terms, drawings and specifications). These documents may be attached as annexes to the controlling document (see paragraph 7, above), with the controlling document making clear through a definition of "the contract" (see paragraph 22, below) or otherwise, that the controlling document and the annexes constitute the contract. Where for reasons of convenience a single contract document is physically separated into parts, the parts should be identified as together constituting a single document.

10. Despite the best efforts of the parties to achieve consistency between the documents, it may be discovered during the performance of a contract that the provisions in two documents, or even within the same document, appear to be inconsistent. The parties may wish to provide that in the first instance the entirety of the

contract documents should be examined to discover the intention of the parties on the relevant issue, and an attempt made to resolve the inconsistency in the light of that intention. The parties may also wish to provide for instances where this approach fails to resolve the inconsistency. They may wish to provide in the contract that in respect of certain types of contract documents one is to prevail over the other in the event of inconsistency (e.g. that the controlling contract document prevails over all others, that a contract document is to prevail over an appendix thereto, or that a contract document is to prevail over general conditions incorporated therein by reference). The imposition of such rules as to priority often acts as an inducement to the parties to scrutinize with care the documents subject to the rules. In respect of other types of contract documents, however, it may be difficult to lay down rules in the contract that certain documents are to prevail over others. Several factors may have to be taken into account in determining which document is to prevail, such as which document embodied the later negotiations between the parties, the nature of the conflict between the documents, and which document was principally focused on the issue in question. The parties may wish to lay down criteria for determining which document is to prevail (e.g. that the document which enables the contract to be implemented more efficiently should prevail).

11. With regard to the relationship between the contract documents, and the oral exchanges, correspondence and draft documents which emanated during the negotiations, one of two approaches may be adopted. The parties may wish expressly to provide that such communications and documents cannot be used to interpret the contract. An alternative approach is to provide that such communications and documents may be used to interpret the contract to the extent permitted by the applicable law. The former approach may reduce uncertainty as to the parties' rights and obligations, while the latter approach may lead to a fairer result if a dispute arises as to the meaning of contract language. In any event the contract should provide that such communications and documents shall not modify the agreement of the parties as set forth in the contract.

12. The various parts of a contract, the parts of a contract document, or a group of contract provisions are often introduced by headings. Short marginal notes are also sometimes placed by the side of contract provisions describing the substance of those provisions. Since headings and side notes are generally inserted only to facilitate the reading of the contract, the parties may wish to provide that they are not to be regarded as setting forth or affecting the contractual rights or obligations of the parties.

13. The parties may wish to consider whether the controlling contract document should set forth introductory recitals. One purpose of the recitals may be to set forth representations which induced the conclusion of the contract. Other purposes may be to set forth the object of the contract, or to describe the context in which it was

concluded. The extent to which the recitals are used in the interpretation of a contract may vary under different legal systems. If the contents of the introductory recitals are intended to be significant in the interpretation or implementation of the contract, it may be preferable to include the contents of the recitals in contract provisions.

14. When the separate contracts approach is adopted, the time-schedules for the performances of two or more contractors are often interdependent. Thus delay by one contractor may result in a second contractor being unable to commence his part of the construction on the appointed date. The second contractor may be entitled to recover compensation for loss arising out of the delay from the purchaser, and the purchaser will wish in turn to be indemnified by the contractor in delay. In order to bring to the knowledge of a contractor the possible consequences of his delay, it may be advisable for each contract to mention the relationship of its time-schedule to related time-schedules of other contracts. If a time-schedule integrating the performances of the various separate contracts has been prepared, it may be sufficient to annex this integrated time-schedule to the contract.

#### **E. Notifications**

15. Works contracts frequently require a party in defined cases to notify the other party of certain events or situations. Such notifications may be required for one or more of the following purposes: to enable co-operation in the performance of the contract (e.g. a notification by the contractor that performance tests will be held on a specified date), to enable a party to take action (e.g. a notification by the purchaser of defects discovered by him in the works, in order to enable the contractor to remedy the defects) or as the prerequisite to the exercise of a right (e.g. notification by a party to the other of the existence of an exempting impediment, such notification being under the contract a prerequisite to his ability to rely on the exempting impediment). The parties should address and resolve certain issues which arise in connection with such notifications.

16. In the interests of certainty, it would be desirable to require that all notifications referred to in the contract be given in writing. The parties may also wish to define "writing" (see paragraph 22, below) and to specify what means of conveying notifications (surface mail, airmail, telex, telegraph, electronic data transmissions) are acceptable. They may also wish to specify the language in which the notifications are to be given. With regard to the time when a notification is to be effective, two approaches are available to the parties: to provide that a notification is effective upon despatch of the notification by a party, or that it is effective only upon receipt of the notification by the other party (see paragraph 22, below). Under the former approach the risk of a failure to transmit or an error by the transmitting agency in transmission of the notification rests on the party to whom the notification is sent, while under the latter approach it rests on the party despatching the notification. The parties may find it

advisable to select means of conveying notifications under which (depending on the approach adopted) proof of despatch or receipt, and the time of despatch or receipt, may be readily obtained.

17. It may be convenient for the contract to provide that, unless otherwise specified, one or the other approach with respect to when a notification becomes effective is to apply to notifications referred to in the contract. Exceptions to the general approach adopted may be appropriate for certain notifications. Thus, when a general rule is provided that a notification is to be effective upon despatch, it may nevertheless be provided that notifications to be given by a party who has failed to perform should be effective upon receipt, since it is fair that such a party should bear the risk of a failure or error in communication. When a general rule is provided that a notification is to be effective upon receipt, it may nevertheless be provided, for instance, that if a purchaser is obligated to notify the contractor of the existence of defects in the works and the purchaser loses his remedies in respect of the defects if he fails to notify, such a notification is effective upon despatch.

18. Since the contractor will sometimes have a representative in the country where the works is being constructed, the contract may provide that notifications by the purchaser to the contractor may be given to such representative, and also that the representative is authorized to give notifications on behalf of the contractor. The uncertainties of foreign transmission of notifications may thereby be reduced. All notifications of a routine character required in the course of the performance of the contract may be given to the representative. If the representative is present on site, a written record of the notifications (e.g. a correspondence log) may be jointly maintained on site by the representatives of the purchaser and the contractor. The contract may also provide that notifications which are not of a routine character (e.g. notifications of suspension of construction, or termination of the contract) are to be given only to the head office of the contractor.

19. The parties should also determine the legal consequences of a failure to notify. Where there is a contractual obligation to notify, failure to notify will normally result in a liability to pay damages. In exceptional cases, the parties may also wish to provide that a party who fails to notify loses a right which he possesses (e.g. to rely on an exempting impediment: see chapter XXI, "Exemption clauses"). In some cases a party to whom a notification is given may be required to give a response to that notice. The parties may wish to specify the consequences of a failure to respond. For example, they may provide that a party to whom drawings or specifications are sent for approval and who does not respond within a specified period of time is deemed to approve them.

## F. Definitions

20. Works contracts often contain definitions of key words used in the contract. A definition ensures that the

word defined is understood in the same sense whenever it is used in the contract, and dispenses with the need to clarify the intended meaning of the word on each occasion that it is used. A definition is advisable if a word which needs to be used in the contract is ambiguous. Definitions contained in a contract are frequently made subject to the qualification that the words defined bear the meanings assigned to them, "unless the context otherwise requires". Such a qualification deals with the possibility that a word which has been defined has inadvertently been used in a context in which it cannot bear the meaning assigned to it in the definition. The preferable course is for the parties to scrutinize carefully the contract to ensure that the words defined bear the meanings assigned to them wherever they occur, thereby eliminating the need for such a qualification.

21. Since a definition is usually intended to apply throughout a contract, a list of definitions may be included in the controlling contract document. Where, however, a word which needs definition is used only in a particular provision or a particular section of the contract, it may be more convenient to include a definition in the provision or section in question.

22. What words need to be defined, and the meaning to be assigned to a particular word, will depend on the language used in a particular contract and the intention of the parties. The following words are often used in works contracts, and the parties may find the definitions set forth below to be useful guides for the purpose of formulating definitions relevant to their own contract:

### *The contract*

"The contract" consists of the following documents, and has that meaning in all the said documents:

- (a) This document
- (b) .....
- (c) .....

etc.

### *Site*

"Site" means the area of land as described in [identify contract document] on which the works is to be constructed.

### *Contractor's machinery and tools*

"Contractor's machinery and tools" means any appliances, equipment, sheds, stores, or other things brought on the site by or on behalf of the contractor for the performance of the contract, but not for incorporation in the works.

### *Writing*

"Writing" includes statements contained in a telex, telegram or other means of telecommunication which provides a record of such statements.

*Despatch*

"Despatch" by a party of a notification occurs when it is properly addressed and conveyed for transmission by a mode authorized under the contract to the appropriate authority for such transmission.

*Receipt*

"Receipt" by a party of a notification occurs when it is handed over to that party, or when it is delivered at an address of that party to which, under the contract, the notification may be delivered.

*Subcontractor*

"Subcontractor" means any person engaged by the contractor to perform any of his obligations under the works contract in regard to the construction of the works.

*Legal proceedings*

"Legal proceedings" means judicial proceedings or arbitral proceedings.

**[A/CN.9/WG.V/WP.17/Add.4]****Chapter VIII: Supply of equipment and materials***Summary:*

The supply of equipment and materials to be incorporated in the works is connected with issues such as the passing of risk of loss or damage to the equipment and materials from the contractor to the purchaser, the transfer of ownership of the equipment and materials, insurance of the equipment and materials and the supply of spare parts for the equipment after construction. Those connected issues are dealt with in other chapters (paragraphs 1 and 2). Since the equipment and materials are usually to be incorporated in the works by the contractor, the supply, unlike the delivery of equipment and materials under a sales contract, is only a partial performance of the contractor's obligations (paragraph 3).

It is desirable for the contract to describe the equipment and materials to be supplied. The nature of the description will depend upon the contracting approach chosen by the purchaser and the extent of the contractor's obligations (paragraphs 5 and 6).

The contract should specify the time when and the place to which equipment and materials are to be supplied. The contract may, depending on the nature of the time-schedule for the contract, express the time for supply as a specified date, or as a period of time. A specification of the time of supply is important in cases where the performances of several contractors have to be co-ordinated. In such cases the time of supply may be specified in the time-schedule as obligatory (paragraphs 7 and 8). Specification of the place to which equipment and

materials are to be supplied may be important to enable the purchaser to determine where he is to take over the equipment and materials, or where risk of loss of or damage to the equipment and materials may pass to him (paragraph 9).

The contract should specify which party is obligated to arrange for the transport of equipment and materials to the site, and bear the costs connected with that transport. The contract should deal with such issues as the packing of the equipment and materials, permits required for the transport, marking of the equipment and materials, and despatch of the transport documents (paragraphs 10 to 14).

The contract should determine which party is to be responsible for customs clearance of equipment and materials, and for the payment of customs duties. There may be legal rules in the country where the works are to be constructed which restrict the import of equipment and materials, and rules in the contractor's country which restrict the export of equipment and materials. The contract should allocate responsibility for obtaining necessary import or export licences (paragraphs 15 to 17).

Equipment and materials supplied by the contractor may need to be taken over by the purchaser prior to storing them, or prior to their incorporation in the works by the purchaser or by a contractor other than the one supplying the equipment and materials. Disputes may arise as to whether loss or damage to, or defects in, the equipment and materials arise before or after the take-over. Such disputes may be reduced if the purchaser is obligated to check the apparent condition of the equipment and materials at the time of take-over, and notify the contractor of any loss, damage or defects which he discovers. The contractor should be obligated to cure the defects (paragraphs 18 to 20).

If equipment and materials are to be stored on site, the contract should determine which party is to assume responsibility for storage and is to provide storage facilities. If the purchaser stores the equipment and materials, the contract should provide that the contractor is to check the equipment and materials at the time that they are handed back to him (paragraphs 21 to 26).

If the purchaser is to supply certain equipment and materials for use by the contractor, the contract should specify the quantity and quality of the equipment and materials to be so supplied. The parties may wish to specify the legal consequences of delay in supply by the purchaser and of defects in the equipment and materials supplied (paragraphs 27 to 30).

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**A. General remarks**

1. This chapter deals with the supply of equipment and materials which are to be incorporated in the works. The contractor's machinery and tools which are to be used for

effecting the construction without becoming part of the works are discussed in chapter IX, "Construction on site".

2. Certain aspects of the supply of equipment and materials to be incorporated in the works are discussed in other chapters. The time of the passing of risk of loss of or damage to equipment and materials from the contractor to the purchaser, and the consequences of the passing of risk, are discussed in chapter XIV, "Passing of risk". The time of the transfer of ownership of equipment and materials from the contractor to the purchaser is discussed in chapter XV, "Transfer of ownership of property". Insurance of equipment and materials is discussed in chapter XVI, "Insurance". Spare parts for equipment incorporated in the works to be supplied by the contractor after completion of construction are discussed in chapter XXVI, "Supplies of spare parts and services after construction".

3. Since equipment and materials supplied by the contractor are usually also to be incorporated in the works by him, the mere supply of the equipment and materials is only a partial performance of the contractor's obligations. Supply under a works contract is therefore to be distinguished from the delivery of equipment and materials under a sales contract. In some cases (in particular if only a single contractor is engaged to construct the whole works) the equipment and materials may remain in the hands of the contractor after arrival at the site until their incorporation in the works. In other cases they may be taken over by the purchaser for storage purposes, and later handed back to the contractor for incorporation in the works.

4. The time of supply to the site of equipment and materials by the contractor may have certain legal consequences. The time of supply may be relevant for checking the progress of construction under a time-schedule (see chapter IX, "Construction on site"). If the purchaser fails to take over equipment and materials at the place of supply, risk may pass to the purchaser in respect of the equipment and materials (see chapter XIV, "Passing of risk").

## **B. Supply of equipment and materials by contractor**

### *1. Description of equipment and materials to be supplied*

5. As a general matter, it is desirable for the contract to describe the equipment and materials which are to be supplied by the contractor. However, the nature of the description will depend upon the contracting approach chosen by the purchaser and upon the extent of the contractor's obligations. In some cases, for example, the contractor may be one of several engaged to construct the works, and his principal obligation may be to supply a certain type of equipment. Since under that contracting approach the purchaser assumes the risks associated with co-ordinating the performances to be effected by the

contractors (see chapter II, "Choice of contracting approach"), he must ensure that all equipment and materials required for the construction of the entire works are included and clearly described in the various contracts.

6. When a single contractor is obligated to construct the entire works (e.g. under a turnkey contract) or a particular portion of the works (e.g. a power station), the contractor is obligated to supply all equipment and materials needed to effect the required construction, even if all items of the equipment and materials are not specifically described in the contract. Nevertheless, it is often desirable for the contract to describe the important items of equipment and materials to be supplied, since such a description may provide an assurance of the quality of construction (see chapter V, "Description of works" and chapter XII, "Inspection").

### *2. Time and place of supply*

7. The contract should specify the time when and the place to which the equipment and materials are to be supplied. The contract may express the time for supply as a specified date, or a period of time. A specified date is appropriate when a rigid time-schedule has been established for the construction, with the contractor possibly not even being permitted to supply earlier than the specified date (e.g. because storage facilities or funds to pay for the supply would not be available earlier). In certain circumstances, it may not be possible to specify a date for supply, for example, when the time of supply has to be linked to prior performance by another contractor, and the time of that performance is uncertain. It may then be appropriate to provide for supply during a period of time commencing to run from the completion of that performance by the other contractor. If a period of time is provided, the contract may stipulate that the contractor is entitled to supply the equipment and materials at any time within the period, or may stipulate that the purchaser is entitled to require the equipment and materials to be supplied at a particular time within the period (e.g. in the light of progress in construction by other contractors).

8. When equipment and materials are to be incorporated in the works by other contractors under the supervision of the contractor supplying the equipment and materials, a specification of the time when the equipment and materials must be supplied is important in order to ensure that the other contractors know when they can commence their performances. In those cases it is usually desirable to specify in the time-schedule for construction that the time of supply is obligatory. Even in cases where the equipment and materials are to be used only by the contractor supplying them, specification of the time and place of supply may be important to enable the purchaser to determine whether a time-schedule for construction is being observed by the contractor (see chapter IX, "Construction on site"). A failure of the contractor to supply equipment and materials on time at the place of supply will result in the contractor being in delay in cases where the time of supply under the time-

schedule is obligatory. Furthermore, the payment of a portion of the price may be linked to the time of supply of equipment and materials.

9. If equipment and materials are to remain in the hands of the contractor to be incorporated by him in the works, the specified place of supply should normally be the site, and the contract should provide that the supply is to take place upon the arrival of the equipment and materials at the site. If the equipment and materials are to be taken over by the purchaser (see paragraph 18, below) the contractor should be obligated to supply the equipment and materials by placing them at the disposal of the purchaser on the site or at another specified place. In cases where the purchaser is to arrange for the transport of the equipment and materials to the site, the contractor may be obligated to hand over the equipment and materials at a specified place of supply to the first carrier engaged by the purchaser for the transport. The costs of supplying the equipment and materials at the specified place of supply should be borne by the contractor, unless the cost reimbursable method of pricing is used. Furthermore, the place of supply may be important in some cases for the passing of risk from the contractor to the purchaser. For example, the contract may provide that equipment and materials are to be supplied to a specified place, and that the risk of loss of or damage to the equipment and materials passes to the purchaser if he fails to take over the equipment and materials within a specified period of time after they are placed at his disposal.

### 3. *Transport of equipment and materials*

10. The contract should specify which party is obligated to arrange for the transport of equipment and materials to the site, and to bear the costs connected with that transport. In a turnkey lump-sum contract the contractor is frequently responsible for arranging transport, and the costs connected therewith are usually considered to be included in the lump-sum price. Under other contracting approaches either the contractor or the purchaser might be obligated to arrange the transport.

11. The contract might obligate the contractor to arrange and pay for transport to the place where the equipment and materials are to be supplied. The contract may refer to an appropriate trade term (e.g. C.I.F.) as interpreted under the International Rules for the Interpretation of Trade Terms (INCOTERMS)<sup>1</sup>. If the purchaser is to arrange for the transport, the contractor should be obligated under the contract to notify the purchaser of the date when the transport is needed sufficiently in advance of that date.

12. The contractor should in all cases be responsible for the packing and protection of the equipment and materials in a manner adequate for transport to the site by the means of transport envisaged. The packing of equipment

may be governed by legal rules applicable to international transport or to transport in the countries through which the equipment is to be transported (e.g. in respect of the dimensions of a package and the method of packing certain items such as dangerous goods). Under the lump-sum method of pricing the costs incurred in connection with the packing of equipment and materials are normally considered to be included in the agreed price.

13. The transport of the equipment may require road, rail or other transport permits, and the contract should specify which party is to be responsible for obtaining them. The party not responsible for obtaining them should be obligated to render any assistance necessary to obtain them (e.g. by providing information about the dimensions of the equipment, the kind of packaging used, or the formalities to be satisfied for obtaining the permits under applicable regulations).

14. If equipment and materials are to be taken over by the purchaser at the place of destination, it would be desirable for the contractor to be obligated to mark the packages containing the equipment and materials in a suitable manner so that they can be identified by the purchaser. In addition, the contractor should be obligated to mark the equipment and materials in accordance with the rules applicable to the mode of transport envisaged (e.g. to use the appropriate marking to indicate that the equipment is fragile or that the materials are dangerous). The contractor should be obligated to send the purchaser the relevant documents (such as invoices or transport documents); some of these documents may be required by the purchaser to receive the shipment (e.g. a bill of lading) or the receipt of the documents by the purchaser may be a precondition to payment of the price for the equipment and materials (see chapter VII, "Price"). Documents required by the purchaser to receive the shipment should be sent to the purchaser a reasonable time before the equipment and materials arrive at the place of destination.

### 4. *Customs duties and restrictions applicable to supply*

#### (a) *Customs duties*

15. The contract should specify which party is to arrange customs clearance of the equipment and materials and is to pay the customs duties. Customs duties are normally imposed on imported equipment and materials. However, in exceptional cases customs duties may be imposed on exported equipment and materials, or on equipment and materials during transit. It may be advisable to provide that customs clearance of equipment and materials for export, and the payment of export customs duties, are to be the responsibility of the contractor, and that customs clearance during transit, and the payment of transit customs duties, are to be the responsibility of the party making arrangements for the transport.

16. The contract should provide which party is responsible for customs clearance of equipment and materials for import, and the payment of import customs duties. If

<sup>1</sup>The International Rules for the Interpretation of Trade Terms (INCOTERMS) prepared by the International Chamber of Commerce (ICC) are contained in ICC publication No. 350, 1980.

equipment and materials are to be taken over by the purchaser (see paragraph 18, below), he may be responsible for the import customs clearance. If equipment and materials are to remain in the hands of the contractor after import, import customs clearance may be the responsibility either of the contractor or the purchaser, depending on which party would find it easier to satisfy the customs regulations applicable to the clearance. The party not responsible for the clearance should be obligated to assist in the clearance procedure, in particular by providing documents which may be needed therefor (e.g. the contractor by providing invoices and certificates of origin, and the purchaser by providing import licences or other required permits issued in the country of the purchaser). With regard to the payment of import customs duties, it may be advisable to provide that it is to be the responsibility of the purchaser. If such payment is to be the responsibility of the contractor, a change in the rates of import customs duties from those existing at the time of the conclusion of the contract may require a revision of the price (see chapter VII, "Price").

(b) *Restrictions applicable to supply*

17. There may be legal rules in the country where the works is to be constructed which restrict the import of equipment and materials, or rules in the contractor's country or another country from which equipment and materials are to be exported, which restrict the export of equipment and materials. The parties should take such rules into account when negotiating the contract. If import licences are required for the import of equipment and materials into the country where the works is to be constructed, the purchaser should be obligated to obtain the required licences. The contractor should be obligated to obtain any required export licences. The contract may provide that its entry into force will depend upon the granting of import and export licences (see chapter III, "Procedure for concluding contract"). If the licences needed for the import and export of the equipment and materials are not all obtainable within a short period of time after the conclusion of the contract, it may be provided that the contract enters into force even prior to the grant of the licences. The contract should however specify the consequences of a failure to obtain the licences (see chapter XXI, "Exemption clauses").

5. *Take-over of equipment and materials by purchaser*

18. In certain circumstances, equipment and materials supplied by the contractor may need to be taken over by the purchaser. Thus the purchaser may need to take over the equipment and materials prior to storing them (see section 6, "Storage on site", below). He may also need to take them over prior to their incorporation in the works when the incorporation is to be done either by himself or another contractor.

19. In some cases the contract may provide that the take-over of the equipment and materials by the purch-

aser is to result in the risk of loss of or damage to the equipment and materials passing to the purchaser from the time of take-over (see chapter XIV, "Passing of risk"). Where risk so passes, disputes may arise as to whether loss or damage occurred before or after take-over. Disputes may also arise as to whether defects were caused prior to take-over, e.g. by faulty manufacture or inadequate packing by the contractor, or after take-over, e.g. by improper storage by the purchaser. Such disputes may be reduced if the purchaser is obligated to check the apparent condition of the equipment and materials at the time of take-over, and to notify the contractor promptly of any loss, damage or defects which the purchaser discovers. However, the purchaser may not be familiar with the expected quality of the equipment and materials (e.g. because he does not have the technical knowledge to evaluate such quality). In addition, some defects may be discoverable only after the incorporation of the equipment and materials in the works and the completion of construction. Accordingly, even in cases where the purchaser fails to notify loss, damage or defects in respect of the equipment and materials, the contract may provide that the purchaser does not lose his rights in respect of the loss, damage or defects, provided however that he proves that the contractor is liable for the loss, damage or defects.

20. If the equipment and materials have defects for which the contractor is responsible, he should be obligated to cure the defects, though he should normally be free as to the manner in which the cure is to be effected. In addition, the purchaser may be entitled to prohibit the use of the defective equipment and materials by the contractor, and may be entitled to refuse to pay the price for the equipment and materials. To enable the contractor to repair the defects, the purchaser should be obligated to take over the defective equipment and materials, since in most cases the repair may be effected on the site (see chapter XVIII, "Delay, defects and other failures to perform"). The purchaser should, however, be entitled to compensation from the contractor for loss suffered by reason of the fact that the equipment and materials were defective (e.g. additional costs of storage until the cure of defects, or, where the purchaser himself was to use the equipment and materials, losses resulting from the purchaser's inability to use the equipment and materials until the cure of defects). The contract may provide that, if the defects in the equipment and materials are cured by the contractor, the time the cure is effected is deemed to be the time of supply. If the purchaser fails to take over equipment and materials, the contract may provide that the equipment and materials are deemed to be supplied at the time that they are placed at the disposal of the purchaser.

6. *Storage on site*

21. Equipment and materials must normally be available on the site at the time when the time-schedule calls for their incorporation in the works. They must, therefore, usually be supplied to the site and stored there prior to the time when they will be used. The contract should

determine the responsibilities of the parties in connection with such storage.

22. Who is to assume responsibility for storage should depend upon the contracting approach chosen by the purchaser. If only one contractor is engaged to construct the works, he should normally assume responsibility for storage. If more than one contractor is engaged to construct the works, the responsibility for storage of the equipment and materials supplied by each of the contractors may be assumed by him. If, however, the personnel of the contractor supplying the equipment and materials are not present on site at the time of supply or the contractor does not have suitable storage facilities, the purchaser may assume responsibility for storage. The contractor may be obligated to advise the purchaser on the appropriate manner in which the equipment and materials should be stored.

23. The responsibility for storage is distinct from the responsibility to provide storage facilities. If the contractor assumes responsibility for storage, but is unable to obtain suitable storage facilities, the purchaser may be obligated to provide storage facilities at a time to be determined in the time-schedule for construction (see chapter IX, "Construction on site"). When the contractor is obligated to provide storage facilities, the purchaser is usually obligated to provide the land on which the facilities are to be located.

24. The contract should clearly define the scope of the responsibility of a party for storage, and harmonize the provisions on such responsibility with the provisions on the passing of the risk of loss of or damage to equipment and materials supplied by the contractor. Thus, if the equipment and materials are, after having been supplied to the site, to remain in the hands of the contractor and be stored by him and the contractor bears the risk of loss of or damage to the equipment and materials, it may not be necessary to define his responsibility for storage. In such cases the contractor's responsibility for defects in the works, or the portion of the works in which the stored equipment and materials are to be incorporated, will be a sufficient incentive to exercise proper care in storage.

25. If the equipment and materials are to be stored by the purchaser, and the risk of loss of or damage to the equipment and materials is to be borne by him, the purchaser may be obligated to hand over the equipment and materials to the contractor in the same quantity and condition in which the purchaser took them over for storage. In cases where storage is to be effected by the purchaser but the risk is to be borne by the contractor, the purchaser may be obligated to take all reasonable precautions to prevent or minimize any loss or damage to the stored equipment and materials. In all cases where he stores the goods, the purchaser should be obligated to notify the contractor without delay of any loss of or damage to the stored equipment and materials.

26. The contract, or an agreement subsequently concluded between the parties, may determine the time and

manner in which equipment and materials are to be handed back by the purchaser from his stores to the contractor to be used for construction. The contractor may be obligated to check the equipment and materials at the time they are handed back to him by the purchaser, and to notify the purchaser of defects. Whether the purchaser is liable for the defects will depend on the nature of the purchaser's responsibility for storage. However, the contract may provide that, if the contractor does not notify the purchaser of defects for which the purchaser is liable and describe their nature within a specified period of time after he has discovered or ought to have discovered them, the contractor loses his right to hold the purchaser liable for those defects.

### *C. Supply of equipment and materials by purchaser*

27. Under some works contracts the purchaser may assume the obligation to supply certain equipment and materials needed for the construction of the works by the contractor. This should be distinguished from the situation where the purchaser has decided to construct a portion of the works himself, for which construction the purchaser is to be solely responsible (see chapter II, "Choice of contracting approach"). The supply by the purchaser of equipment and materials needed for the construction of the works by the contractor may in particular be advisable where the equipment and materials can be obtained in the purchaser's country at lesser cost than abroad, or where it is important for the purchaser to conserve foreign exchange.

28. The quantity and quality of the equipment and materials to be supplied by the purchaser should be specified in the contract. It may be the responsibility of the contractor to specify the quantity and quality of equipment and materials appropriate for the construction to be effected by him. The time of supply by the purchaser to the site should be identified in the time-schedule (see chapter IX, "Construction on site") by reference to dates or periods of time in a manner similar to the identification of the time of supply by the contractor (see paragraph 7, above).

29. The supply to be effected by the purchaser would affect the performance of the construction obligations of the contractor. The parties may, therefore, wish to specify in the contract the legal consequences of delay by the purchaser in supplying the equipment and materials, or of supplying equipment and materials of a quality inferior to that specified in the contract. The contractor should not be considered to be in delay if the construction of the works or a portion thereof is not completed by him in time due to the purchaser's delay in supplying equipment and materials. In addition, the contractor should not be responsible for defects in the works if they were caused by defects in equipment and materials supplied by the purchaser (see chapter XVIII, "Delay, defects and other failures to perform"). Furthermore, the contractor



may be entitled to damages for loss caused to him by delay or defects (see chapter XX, "Damages" and chapter XXI, "Exemption clauses"). The contractor should, however, be obligated to inspect with reasonable care the equipment and materials promptly after their supply. The contract may also provide that, if the contractor does not notify the purchaser of defects which he has discovered or could have discovered through a reasonable inspection, within a specified period of time after the supply, the contractor loses his right to rely on those defects as an excuse for responsibility for defects in the works, or to recover damages for loss caused to him by those defects.

30. The parties may usually wish to agree that the contractor is not to pay for the supply of equipment and materials by the purchaser as a separate item, but that the value of the supply by the purchaser is to be accounted for in determining the price to be paid by the purchaser for construction of the works. Exceptionally, however, the parties may wish to agree that the contractor is to pay the purchaser for the supply of some or all of the equipment and materials as a separate item. The payment conditions would usually be similar to those used in an international sales contract.

#### [A/CN.9/WG.V/WP.17/Add.5]

### Chapter XXVI. Supplies of spare parts and services after construction

#### *Summary*

Even after the works are ready to operate, the purchaser may need assistance which the contractor is able to supply. Spare parts will be needed to replace equipment which is worn out. The works will need to be maintained. If breakdowns occur, the works will need to be repaired. If the purchaser does not have all the skilled personnel necessary for the technical operation of the works, he may need assistance from the contractor to operate it. The planning of the parties in regard to the supply of spare parts and services would be facilitated if the parties could provide for the supply in the works contract (paragraphs 1 to 4).

A person offering to construct the works may be required to indicate the spare parts which will be needed over a specified period of operation, and the prices at which and the period of time during which he can supply them. In regard to spare parts obtainable only from the contractor, the purchaser may find it advisable to obligate the contractor to supply a large stock of such spare parts by the time the construction is completed (paragraphs 6 to 9). If spare parts are manufactured not by the contractor but for the contractor by suppliers, the purchaser may enter into contracts with those suppliers (paragraph 10).

If the estimate of spare parts needed over a given period furnished by the contractor is discovered to be incorrect, the contractor should be obligated to supply such additional spare parts as are needed. The parties should address the modalities of ordering and delivery of spare parts. The contract should determine the quality of the spare parts to be supplied, and provide for a quality guarantee in respect of them (paragraphs 12 to 14).

The contractor should be obligated to inform the purchaser if he re-designs or improves spare parts which he has undertaken to supply. He should also be obligated to supply instruction manuals, tools and equipment necessary for the installation of spare parts (paragraphs 15 and 16).

A person offering to construct the works may be required to indicate whether he is prepared to supply the maintenance services required by the works and the duration for which he is prepared to supply those services. The contractor may be required to submit a maintenance programme designed to ensure the proper operation of the works, and the maintenance obligations of the contractor may be defined on the basis of that programme (paragraphs 17 and 18).

The standards to be observed by the contractor when performing maintenance work may be specified. The contractor should be obligated to furnish a report on each maintenance operation (paragraphs 19 and 20). The contract should specify how the price is to be determined (e.g. a lump-sum price, unit rates, or a cost-reimbursable basis). The payment conditions applicable (e.g. relating to the currency, place and time of payment) should also be specified (paragraphs 21 and 22).

The contract should define the extent of the contractor's repair obligations (paragraphs 23 and 24). The procedure for notifying the contractor of the need for repairs should be settled. The contractor may be required to submit an estimate of the cost of repair and the time-schedule for effecting them, and thereafter the terms of repair may be agreed by the parties. The payment conditions applicable should be specified (paragraphs 25 to 27).

The standards to be observed by the contractor when effecting repairs may be specified. The contractor should be obligated to furnish a report on each repair operation which he performs. The contractor should be required to give a guarantee under which he assumes responsibility for defects in repairs (paragraphs 28 and 29).

If the contract imposes obligations on the contractor with regard to the technical operation of the works, the scope of these obligations should be carefully defined. In order to define the obligations of the contractor with regard to the operation of the works, an organizational chart may be prepared showing the functions allotted to the personnel of the contractor. The division of control between the purchaser and contractor during the operation of the works should be clearly described. The

contract should also provide a procedure for resolving complaints by one party against the other (paragraphs 31 and 32).

The contract should provide how the price is to be determined (e.g. a lump-sum price, or fixed amounts combined with the cost reimbursable method). The payment conditions applicable should also be specified (paragraph 33).

The purchaser may be obligated to facilitate the maintenance, repair and operation by the contractor (e.g. by obtaining visas or work permits for the contractor's staff). The purchaser may wish to supply locally available equipment and materials needed for maintenance and repairs (paragraph 34).

The contract should specify when the obligations undertaken by the contractor as to the supply of spare parts, maintenance, repair and operation are to commence and also determine the duration of the obligations undertaken by the contractor. The duration may be the expected lifetime of the works, or a shorter period which is to be automatically renewed (paragraph 35 and 36). Where the contract imposes obligations on the contractor over a long duration, it may be desirable to include mechanisms (e.g. a periodic review) to modify the scope of obligations imposed on the contractor and the price payable by the purchaser. Even in cases where the scope of the contractor's obligations is not modified, a revision of the price payable may be required because the costs of the goods and services required to discharge those obligations have changed (paragraphs 37 and 38).

The contract may entitle the purchaser to terminate the contractor's obligations as to supply upon the giving of a specified period of notice. The purchaser may additionally be given the right to terminate for convenience at any time, subject to the payment of compensation if loss is suffered by the contractor through the termination (paragraph 39).

The parties may wish to provide for remedies other than termination which are to be available upon failure of performance by a party (e.g. damages, or liquidated damages and penalties) (paragraph 40).

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#### A. General remarks

1. Even after the construction is completed and the works are ready to operate, the purchaser may need assistance which the contractor is able to supply. The normal operation of the works will entail the replacement by spare parts of equipment, components and machinery as they wear out. The purchaser will need to ensure that the works are properly maintained. Maintenance has primarily a preventive function: in the short-term, it prevents costly breakdowns, while in the long-term it

prevents the works from ceasing to operate in good order before the expiry of its expected lifetime. Despite regular maintenance, however, portions of the works may from time to time break down and need repair. Breakdowns may cause considerable loss to the purchaser, and he has a vital interest in seeing that repairs are carried out expeditiously. Repair therefore has primarily a curative function. Spare parts will have to be available to effect both maintenance and repairs.

2. At the time the construction is completed, the personnel of the purchaser may not have all the skills necessary for the technical operation of the works, and the purchaser may therefore wish the contractor to assist in its operation. The degree of the assistance can vary. The contractor may in some cases provide the personnel to man many of the technical posts in the works, while in other cases he may provide technical experts to collaborate with the personnel of the purchaser in a few highly specialized operations.

3. Operation of the works should be distinguished from training obligations which may also be undertaken by a contractor. For example, under a product-in-hand contract, the contractor is obligated to train the personnel of the purchaser, and to show during a test period specified in the contract that the works can be operated and agreed production targets achieved by the personnel using the raw materials and other inputs that the purchaser would use (see chapter II, "Choice of contracting approach"). Under other contracting approaches the contractor may be obligated to instruct the purchaser's personnel in operating specified items of equipment (see chapter VI, "Transfer of technology"). It may be essential for the purchaser that the contractor is obligated to supply spare parts and maintenance, repair and operation services after construction. Spare parts and repair services in particular may not be obtainable from any other source.

#### B. Contractual arrangements

4. The planning of the parties in regard to the supply of spare parts and services after construction would be greatly facilitated if at the time of the conclusion of the contract the parties could anticipate and provide in the works contract for the needs of the purchaser in respect of spare parts and services. Agreement between the parties on the extent of the spare parts and services to be supplied, the duration of the supply, and the price to be paid therefor, may be reached more easily at the time of the conclusion of the contract than at a later time. In some cases, however, the extent of the spare parts and services that will be needed by the purchaser may be uncertain at the time of the conclusion of the contract (e.g. the skilled personnel which will be locally available at the time of the completion of construction may not be predictable). In such cases, a possible approach is for the contract to identify the types of assistance the need for

which is uncertain (e.g. maintenance) and to provide that, if so requested by the purchaser before the completion of the construction, the contractor is obligated to provide such assistance as is required by the purchaser to the extent that the contractor has the capacity to supply it. The parties should agree on the basis for determining the price payable by the purchaser (see paragraphs 13, 21, 26 and 33, below). They should also include in the contract provisions on all issues on which agreement can be reached at the time of the conclusion of the contract (e.g. quality of spare parts or services, and conditions of payment).

5. An alternative approach towards meeting the difficulty that the purchaser's needs may be uncertain at the time of the conclusion of the works contract is to set forth the obligations of the parties in a separate contract. Such a contract may be concluded closer in time to the completion of construction, at which time the purchaser may have a clearer estimate of his needs.<sup>1</sup>

### C. Spare parts

6. The contractor is in the best position to ascertain the kinds, quantity, and quality of spare parts which will be needed during the operation of the works. Accordingly, a tenderer or a person with whom a contract is being negotiated may be required to supply prior to the conclusion of the contract (e.g. together with his offer to construct the works) a list of the spare parts and the quantities of spare parts which will be needed over a specified period (e.g. during the course of two years' operation of the works), the period of time after the commencement of operation of the works during which he is prepared to supply the spare parts, the prices at which he is prepared to supply those spare parts and the period of time for which he is prepared to maintain those prices. He may also be required to identify in the list which of the spare parts he will manufacture himself, and which spare parts he will obtain from suppliers.

7. The spare parts needed for the works usually fall into two categories. The first category consists of standard parts which are obtainable both from the contractor and from several other sources. The second category consists of non-standard parts which are obtainable only from the contractor.

8. As regards spare parts in the first category, they would normally be obtainable more cheaply and conveniently from sources other than the contractor than from the contractor. However, the contractor may be obligated to supply at the time of the completion of construction a limited stock to cover the time period elapsing between the commencement of operation of the works, and the

establishment by the purchaser of his own sources of supply. The contractor may also be obligated to indicate sources from which the spare parts may be obtained by the purchaser.

9. As regards spare parts in the second category, the purchaser has to obtain them from the contractor. The purchaser may find it advisable for the contractor to be obligated to supply by the time the construction is completed a large stock of such spare parts (e.g. sufficient for two year's operation of the works). The spare parts can then be produced at the same time that the equipment to be incorporated in the works is produced, and transported to the site together with the equipment, thus usually resulting in savings in production and transport costs. The purchaser may obtain an even larger stock if the contractor's prices are likely to be much higher in respect of spare parts supplied at a later stage.

10. Where non-standard spare parts are manufactured not by the contractor but for the contractor by suppliers, the purchaser may either obligate the contractor to supply the spare parts (it being the responsibility of the contractor to obtain them from suppliers) or the purchaser may himself enter into independent contracts with the suppliers. Where the purchaser wishes to contract with the suppliers, he may wish to engage the contractor as his agent in procuring the spare parts. The services to be supplied by the contractor should be agreed between the parties and might include contacting possible suppliers, obtaining competitive offers, determining the required quantities of spare parts, evaluating the offers, making recommendations as to purchase, and arranging for delivery.

11. In exceptional cases, the purchaser may have the technical capability to manufacture certain non-standard spare parts, and may wish to manufacture them (e.g. to conserve foreign exchange). In such cases the contract should obligate the contractor to supply the drawings and specifications necessary for their manufacture where it is feasible for him to do so. It may not be feasible if a spare parts item comes from a supplier, in particular if the supplier has industrial property rights in regard to that item.

12. Where the contractor has supplied an estimate of the quantity of spare parts needed over a given period of operation of the works, and the purchaser has purchased that quantity from the contractor, it may be discovered during actual operation that the estimate was incorrect, and that the purchaser needs an additional quantity. The contractor should be obligated in such circumstances to supply the additional spare parts at the prices at which they were previously supplied if the purchaser so requests within a specified period after the commencement of operation.

13. The parties should address issues connected with the ordering and delivery of spare parts. They should determine when delivery is to take place (e.g. some spare parts may be delivered automatically at specified intervals,

<sup>1</sup>The Economic Commission for Europe has under preparation a guide on drawing up international contracts for services relating to maintenance, repair and operation of industrial and other works which will assist parties in drafting a separate contract or contracts dealing with maintenance, repair and operation.

while others may be delivered upon order by the purchaser). They should also determine the manner in which orders are to be communicated, and the period following the order when delivery has to be made (e.g. within one month of delivery of the order). The purchaser may wish to stipulate that liquidated damages or penalties are payable for delay in delivery (see chapter XX, "Liquidated damages and penalty clauses"). With regard to the passing of risk, packaging, payment of customs duties and taxes, and other incidents of the delivery of the spare parts, the parties may wish to provide that such issues are to be settled in accordance with a well-recognized trade term (e.g. F.O.B., C.I.F.).<sup>2</sup> The prices for the spare parts should be agreed upon on the basis of the prices quoted by the contractor (see paragraph 6, above). The parties should also agree upon the payment conditions applicable (e.g. the currency, time and place of payment).

14. The contract should determine the quality of the spare parts to be supplied. The contract may provide, for example, that they are to be of the same quality as the parts originally incorporated in the works, or provide that the quality must be in accordance with technical specifications set out in the contract. In addition, the contract should include a quality guarantee in respect of the spare parts under which the contractor assumes responsibility for defects discovered and notified before the expiry of a guarantee period (see chapter XVIII, "Delay, defects and other failures to perform"). Since spare parts supplied on a particular date may be put to use only at a later date, the determination of the length of the guarantee period and the time when the period commences to run may present difficulties. A possible approach may be to provide for a relatively short guarantee period commencing to run from the date the spare parts are put to use, and to provide further that, whether or not the spare parts are put to use, the guarantee expires at the end of a longer period commencing to run from the date of delivery of the spare parts.

15. After the works are constructed, the contractor may improve or re-design some of the items which he manufactures and which he has undertaken to supply as spare parts. Each party may have an interest in substituting the improved or re-designed items for the ones originally supplied. The contractor should therefore be obligated to inform the purchaser whenever improvements or re-designing takes place, so that, if the purchaser so wishes, negotiations may take place for the supply of the improved or re-designed spare parts instead of the spare parts originally agreed to be supplied.

16. It is desirable for the purchaser's personnel to develop the technical capability to install the spare parts. For this purpose, the contractor may be obligated to supply necessary instruction manuals, tools and equipment. If necessary, he should also be obligated to train the purchaser's personnel in installing the spare parts.

<sup>2</sup>The trade term may be identified by reference to the *International Rules for the Interpretation of Trade Terms* (INCOTERMS) prepared by the International Chamber of Commerce (ICC) (ICC publication No. 350, 1980).

#### D. Maintenance

17. Certain operations are a necessary component of the maintenance of industrial works, e.g. periodic inspection of the works; lubrication, cleaning and adjustment; replacement of defective or worn out parts. Maintenance may also include such operations of an organizational character as establishing a maintenance schedule or a record of maintenance. A tenderer or a person with whom a contract is being negotiated may be required to indicate whether he is prepared to supply the maintenance services required by the works, and the duration for which he is prepared to supply them.

18. In order to assist the purchaser in maintaining the works, the contractor may be required to submit at the time of the conclusion of the contract a maintenance programme designed to keep the works operating at the efficiency required by the purchaser over the lifetime of the works. The contractor may also be required to supply maintenance manuals setting forth appropriate maintenance procedures. The purchaser may wish to engage a consulting engineer to review the maintenance programme and procedures submitted by the contractor. The purchaser would then be in a position to determine what part of the maintenance he may be able to undertake himself (e.g. depending on the skilled personnel he has available, the training obligations assumed by the contractor (see chapter VI, "Transfer of technology"), or the maintenance equipment the purchaser possesses). The contract should specify the items to be maintained (e.g. the entire works, or certain items of equipment) and define the maintenance obligations which the parties wish the contractor to undertake. If major items of equipment have been manufactured for the contractor by suppliers, the purchaser may find it preferable to enter into independent maintenance contracts with the suppliers, as they may be better qualified to maintain those items. Proof of proper maintenance may be facilitated by providing that the personnel of the purchaser are to be associated with the personnel of the contractor conducting the maintenance operations. This may also serve as an effective means of training the purchaser's personnel in maintenance operations.

19. The parties may wish to specify the standards to be observed by the contractor when performing maintenance work. If maintenance norms or standards established by professional bodies are available, the contractor's obligations may be described by reference to those norms or standards. Where such norms or standards are not available, the contract may specify that the maintenance is to be effected in a workmanlike manner. Another approach may be for the contractor to undertake that the standards of maintenance will be such that, over a specified period (e.g. one year), the portion of the works being maintained will operate in accordance with the contract for a specified percentage of its normal operating time over that period. Failure of the works to operate due to causes for which the contractor is not responsible (e.g. faulty operation by the purchaser's personnel) should be excluded from the scope of the undertaking.

20. The contractor should be obligated to furnish a report on each maintenance operation immediately following the operation. The report should describe the maintenance activities undertaken. It should also set forth any defects discovered in the works, any repair work needed, or any maintenance work needed which is outside the scope of the contractor's obligations, together with an estimate of costs for carrying out the repair or maintenance work if it can be carried out by the contractor.

21. The main obligation of the purchaser will be the payment of the price. The price may be determined as a lump sum payable for all the obligations undertaken and costs thereby incurred by the contractor in respect of a maintenance operation. This approach may be appropriate when the maintenance operations are of a standard and routine character. Another approach may be to agree on unit rates for units of time expended on the various work processes involved in the maintenance. Yet another approach may be to provide that the contractor is to be paid a fee to cover his overhead and profit, while he is to be paid for his direct expenses on a cost reimbursable basis. The direct expenses for which the contractor is to be reimbursed should be clearly specified (see chapter VII, "Price").

22. The parties should also agree upon the payment conditions applicable. Thus such issues as the currency, place and time of payment should be settled in the contract (see chapter XV, "Price"). With regard to the time of payment, the contract may provide that payment is to be made within a specified period of time after the submission of an invoice by the contractor following the completion of each maintenance operation.

### E. Repairs

23. The purchaser should enter into contractual arrangements which ensure a speedy repair of the works in the event of a breakdown. In many cases the contractor is better qualified than a third party to effect repairs. In addition, the use of third parties to effect repairs may result in the violation of obligations of secrecy binding on the purchaser in regard to the technology supplied by the contractor. If, however, major items of equipment have been manufactured for the contractor by suppliers, the purchaser may find it preferable to enter into independent contracts for repair with the suppliers, as they may be better qualified to repair those items. It should be noted that in defining the repair obligations imposed on the contractor, those obligations should be carefully distinguished from obligations assumed by the contractor under guarantees of quality to make good defects in the works which are notified to the contractor during the guarantee period (see chapter XVIII, "Delay, defects and other failures to perform").

24. The contractor's repair obligations should be clearly defined. The extent of the obligations to be imposed on

the contractor may depend on the repair capabilities of the contractor, and on whether the purchaser wishes to undertake certain repair operations himself (e.g. replacement of minor items of defective equipment). However, the obligation of the contractor cannot be described in terms of specific repair operations, since the repair operations needed will depend on the nature of a particular breakdown.

25. Because repairs may have to be undertaken speedily, the contract should clearly settle the procedures for calling on the contractor to effect repairs. The contract should specify the modes by which the contractor can be notified of a breakdown (e.g. telex, telephone), and the period of time after notification within which the contractor must inspect the breakdown.

26. The contract may also specify that, where repairs do not have to be undertaken immediately, the contractor must submit to the purchaser within a specified period of time a report describing the repairs needed, an estimate of costs, and a time-schedule for effecting the repairs. Once the report has been submitted by the contractor, the parties may thereafter agree on the terms for effecting the repairs. If the repairs are extensive, it would be advisable for the agreement to be reduced to writing. The contract may provide that, if the parties fail to reach agreement on the time-schedule, it is to be determined by a technical expert nominated under the contract (see chapter XXIX, "Settlement of disputes"). If the parties fail to reach agreement on the price payable for effecting the repairs, the contract may provide for payment on a cost reimbursable basis (with the contractor being paid reasonable costs incurred by him in effecting the repairs, and a fixed amount as a fee). However, in cases where the purchaser needs to make the works operational in the shortest possible time, he may dispense with the submission by the contractor of cost estimates and a time-schedule for effecting repairs, and the parties may agree that the repairs are to be effected on a cost reimbursable basis.

27. The parties should agree upon the payment conditions applicable. Thus, such issues as the currency, place and time of payment should be settled in the contract. With regard to the time of payment, the contract may provide that payment is to be made within a specified period of time after the submission of an invoice by the contractor following the completion of a repair operation. If the contractor is to be obligated to inspect a breakdown within a short period after notification of a breakdown, the purchaser may have to pay a fee to cover the contractor's costs in always having personnel in readiness for an inspection.

28. The parties may wish to specify the standards to be observed by the contractor when effecting repairs, either by reference to established norms and standards, or by specifying that the repairs are to be effected in a workmanlike manner (see paragraph 19, above).

29. The purchaser will wish to have proof that the repairs have been duly carried out, and the parties should

agree on how such proof is to be furnished. After the completion of repairs, the contractor should be obligated to furnish a report describing the repair work effected, any repair work which may be needed in the future, and the causes of the breakdown. The report may be supported by records evidencing the time expended by various categories of personnel, and the work processes used. In some cases, proper repair may be proved through a joint inspection by the parties of the repairs, while in others the contractor may furnish such proof through the successful operation of the works. Proof of proper repair may be facilitated by providing that the personnel of the purchaser are to be associated with the personnel of the contractor undertaking the repair operations. This may also serve as an effective means of training the purchaser's personnel in the techniques associated with repair operations. If the parties fail to agree on whether there has been proper repair, the issue may be referred for settlement to a technical expert nominated under the contract (see chapter XXIX, "Settlement of disputes"). The contractor should also be required to give a guarantee under which he assumes responsibility for defects in the repair discovered and notified to him before the expiry of a specified guarantee period.

30. While repairs would normally be carried out at the site, or elsewhere in the country where the works are situated, in some cases it may be necessary to send an item to the contractor's country for repair. The purchaser may be obligated to arrange for the transport of the item to the contractor's country, and for any necessary insurance of the item up to the time of delivery to the contractor. The contractor may be obligated to assist the purchaser to make such arrangements (e.g. advise on proper packing, obtain import permits which may be necessary in his country). The contractor may be obligated to arrange for the transport of the item after repair to the purchaser's country, and for any necessary insurance. The contract should determine who is to bear the expenses involved.

#### **F. Operation**

31. If the contract imposes obligations on the contractor with regard to the technical operation of the works, the scope of these obligations should be carefully defined. For this purpose the purchaser and contractor in consultation should prepare an organizational chart showing the personnel required for the technical operation, and the functions to be discharged by each person. The positions to be occupied by personnel who are employees of the contractor may then be identified, and the qualifications and experience of those persons may be specified. The functions allotted to posts to be filled by employees of the contractor should be defined with particular care. In determining what personnel are to be supplied by the contractor, the parties should take account of any mandatory regulations which may exist in the country of the purchaser regarding employment of foreign personnel.

32. The contract should determine the nature of the division of control between the purchaser and contractor during the operation of the works. It may, for example, be necessary for the general manager employed by the purchaser to give certain directives to engineers who are employees of the contractor based on policy decisions taken by the general manager. Conversely, the engineer supplied by the contractor may have to issue directions to subordinate engineers employed by the purchaser. In order to avoid friction and inefficiency, the division of control should be described as clearly as possible. In particular, the parties may wish to provide a procedure for dealing with complaints by one party against the other (e.g. incompetence, inefficiency, failure to follow directions). They may, for example, agree that such complaints are to be investigated by a panel composed of a senior executive officer of each party. The contract may provide that, if specified serious complaints against employees are held to be proved, those employees must be replaced by the party who engaged them at his own expense within a specified period of time. However, the purchaser should be entitled to require the contractor to replace at the purchaser's expense any employee of the contractor, even in the absence of a proved complaint against that employee.

33. The main obligation of the purchaser is the payment of the price. Where a reasonable estimate can be made of the costs to be incurred by the contractor, the price may be determined as a lump sum payable for all the obligations undertaken by the contractor over a specified period. Another approach may be to combine the payment of fixed amounts with the cost reimbursable method (i.e. the reimbursement of costs incurred by the contractor together with the payment of a fee). Thus, fixed amounts may be provided in respect of items for which reasonable cost estimates can be made (e.g. the salaries of the personnel to operate the works, the cost of their accommodation and travel) and the cost reimbursable method provided for the remaining items of expenditure. In cases where the operational functions performed by the contractor are closely linked to the productivity and profitability of the works, the purchaser may wish to consider the additional payment of an incentive fee (e.g. a specified percentage of the value of the yearly turnover). The parties should also agree on the payment conditions applicable. Thus such issues as the currency, place and time of payment should be settled in the contract.

#### **G. Facilitation by purchaser of services to be provided by contractor**

34. The purchaser may be obligated to facilitate in specified ways the maintenance, repair and operation by the contractor. Thus the purchaser may be obligated to assist the contractor to obtain visas or work permits for the contractor's staff, to give safe access to the works to the contractor, to inform the contractor of alterations to

the original construction of the works which may influence the maintenance, repair, and operation, to comply with safety regulations applicable to the works, and to inform the contractor of mandatory safety regulations to be observed during the conduct of maintenance, repair and operation. The purchaser may wish to assume the obligation of supplying locally available equipment and materials needed for maintenance and repairs, as such supply may reduce costs. The contractor may be obligated to state his requirements as to such equipment and materials. In addition, the purchaser may be obligated to provide other facilities such as accommodation and transport to the contractor's personnel. If he is so obligated, the contract should determine which party is to bear the costs of providing such facilities.

#### **H. Commencement and duration of obligations of parties**

35. The contract should specify when the obligations undertaken by the contractor as to the supply of spare parts, maintenance, repair and operation are to commence. The supply of spare parts may commence from the estimated date that the purchaser will need them, taking into account the initial stock supplied by the contractor (see paragraph 9, above). The date of commencement of the maintenance obligations may depend on other obligations undertaken by the contractor. Thus, if the contractor has undertaken complete responsibility for the operation of the works for a specified period of time after acceptance of the works by the purchaser, maintenance obligations might commence after the expiry of that period. Repair obligations may commence from the date of expiry of the quality guarantee assumed by the contractor in respect of the works. The date of commencement of the obligations of the contractor in regard to operation may be fixed having regard to the other conditions which have to be satisfied before the works can commence to operate (e.g. availability of the staff to be employed by the purchaser).

36. The contract should determine the duration of the obligations undertaken by the contractor as to the supply of spare parts, maintenance, repair and operation. The duration of the obligations may be the expected lifetime of the works. Alternatively, the duration may be shorter. For example, it may be determined by reference to the training programme for the personnel of the purchaser, the contract providing that the contractor's obligations are to end when the purchaser has developed the capability to provide the services himself. Obligations as to training which may be imposed on the contractor are dealt with in chapter VI, "Transfer of technology". Where a shorter duration for the contractor's obligations is agreed but the purchaser is not certain that he will be self-sufficient at the expiry of that period, the contract may provide that, unless the renewal is prevented, the contractor's obligations are to be renewed automatically for further periods of the same duration, subject to changes in the scope of services to be provided by the

contractor and the price to be paid by the purchaser (see paragraphs 37 and 39, below).

37. Where the contract imposes obligations on the contractor over a long duration, it may be desirable to include mechanisms to modify the contract terms, in particular as to the scope of obligations imposed on the contractor, and the price payable by the purchaser. The purchaser may increase his own capabilities, and with such increase wish to assume certain services originally provided by the contractor. Conversely, it may transpire during the operation of the works that the purchaser cannot provide certain services which he had assumed he could provide, and he may wish the contractor to provide those services. Any change of the scope of obligations undertaken by the contractor would usually require an adjustment of the price. Accordingly, the contract may provide that the scope of obligations and the price are to be periodically reviewed and agreed upon by the parties (e.g. every two years, or at each renewal of the contract) and that the purchaser is entitled at the review to request a reduction or increase in the scope of obligations. The contract may provide that the contractor is not obligated to comply with a request for increased services if he does not have the capacity to provide them.

38. Even in cases where the scope of the contractor's obligations are not changed at a periodic review, a revision in the price payable may be required because the cost of the goods and services required to discharge these obligations has changed. The parties may wish to provide that at each periodic review changes in cost are to be taken into account, and a new price agreed upon if necessary. Alternatively, the parties may link the price payable to an appropriate price index, if one is available. The price may then automatically be revised in accordance with changes in the index (see chapter VII, "Price"). The index should be structured in accordance with the particular circumstances of the obligation, the price of which is to be revised. Therefore, it is usually not suitable to adopt the same index used for revision of the price for the construction of the works in respect of the obligations of the contractor dealt with in this chapter.

#### **I. Termination**

39. The parties may also wish to regulate the termination of the obligations as to the supply of spare parts, maintenance, repair, and operation. Where the duration of the obligations is a single specified period, the contract may permit the purchaser to terminate the obligations prior to the end of that period upon giving the contractor a specified period of notice. The specified period of notice should be sufficiently long to enable the contractor to phase out without suffering loss the arrangements he has made to fulfil his obligations. As a further protection to the contractor, it may be provided that the notice may be given only after the supply has continued for a specified length of time. Where the duration of the

obligations consists of a period which is subject to renewal (see paragraph 36, above), the purchaser can prevent the renewal by the giving of a specified period of notice of non-renewal, such period of notice to expire at the end of the initial or of a renewed period of the contractor's obligations. Whether the duration consists of a single specified period or of periods which are successively renewed, the purchaser may in addition be given the right to terminate for convenience at any time, subject to the payment of compensation if loss is suffered through the termination by the contractor (see chapter XXV, "Termination of contract"). The purchaser may wish to have such a right to deal with a situation where he is unexpectedly able to obtain from other sources at lesser cost the spare parts and services provided by the contractor. The contract may also provide for termination by either party for specified failures of performance by the other party, for bankruptcy or insolvency of the other party, or where performance by the other party is prevented for a specified period by exempting impediments (see chapter XXV, "Termination of contract").

#### **J. Remedies other than termination**

40. The parties may wish to provide for remedies other than termination which are to be available upon failure of performance by a party. They may wish to select such remedies as are appropriate out of those which they have provided for failures of performance during construction (see chapter XVIII, "Delay, defects and other failures to perform", chapter XIX, "Liquidated damages and penalty clauses" and chapter XX, "Damages"). Alternatively, they may leave the remedies to be determined by the applicable law.

[A/CN.9/WG.V/WP.17/Add.6]

### **Chapter XXIX. Settlement of disputes**

#### *Summary*

Disputes arising in connection with works contracts may require treatment which differs from the treatment of disputes arising under other types of contracts. This may be due, for example, to the complexity and comprehensiveness of works contracts and the fact that a number of entities may participate in the construction. Disputes may relate to technical matters and require a rapid settlement (paragraph 1). Decisions to be made concerning disputes arising in connection with a works contract may relate not only to failures of performance, but also to failures of agreement or consent (section G). Interim measures may also have to be taken pending the final settlement of a dispute (paragraph 2).

The mechanisms for the settlement of disputes provided in the contract might include negotiation (section

B), conciliation (section C), arbitration (section D) and judicial proceedings (section E). An independent expert may also be authorized to settle disputes (section F). The contract might also provide for the multiparty settlement of disputes (section H) (paragraph 3).

A settlement of a dispute reached through negotiation between the parties could be expected to be broadly acceptable to both parties, and save the cost and delay which normally occur in the settlement of disputes by other means (paragraph 5). The contract may require negotiation between the parties and provide for the relationship of settlement through negotiation to settlement of the dispute in arbitral or judicial proceedings (hereinafter collectively referred to as legal proceedings) (paragraph 6). A negotiated settlement of a dispute may be reduced to writing and signed by both parties (paragraph 7).

If the parties fail to settle their disputes through negotiation, they may wish to resort to conciliation, in which a third party conciliator suggests possible solutions to the disputes (paragraphs 8 and 9). Conciliation may enable a good business relationship to be preserved, and is usually less costly and time-consuming than legal proceedings (paragraph 10). The parties may wish to provide for conciliation under the UNCITRAL Conciliation Rules (paragraph 11).

Disputes arising from works contracts are frequently settled through arbitration. Arbitration may offer certain advantages over judicial proceedings. For example, the parties can appoint as arbitrators persons of their choice who have expert knowledge of the subject-matter of the dispute, and they can choose the place where the arbitral proceedings are to be conducted (paragraph 12). Arbitration may be conducted only on the basis of an agreement by the parties to arbitrate. Such agreement may take the form of an arbitration clause included in the contract. If proceedings are instituted in a court on a matter which is covered by the arbitration clause, the court will normally refer the dispute to arbitration (paragraphs 13 and 14).

It may be advisable for the parties to agree that the arbitral proceedings are to be regulated by a set of arbitration rules of their choice.

The parties frequently select an arbitration institution to administer the arbitral proceedings and agree that the proceedings are to be regulated by the rules of that institution (paragraphs 15 and 16). As another possibility, they may agree that a set of arbitration rules prepared by an international organization (e.g. the UNCITRAL Arbitration Rules) are to apply. The parties may find it advisable to agree on certain issues related to the arbitration (paragraphs 17 and 18).

The parties may wish in particular to agree in the arbitration clause on the number of arbitrators who are to comprise the arbitral tribunal, and to designate an appointing authority to appoint the arbitrators in the event that they do not agree on the appointment (para-



graphs 19 and 20). They should also designate the language to be used in the arbitral proceedings (paragraph 21). They may also wish to specify the place where the arbitration is to take place. Selection of the place of arbitration may be significant for several reasons (paragraphs 22 to 24).

In some cases the parties may wish to agree that the place of arbitration is to be in the country of the party against whom a claim is brought (paragraph 25). It is advisable for the parties to be cautious in authorizing the arbitral tribunal to decide *ex aequo et bono*, since such an authorization may be interpreted in different ways (paragraph 26).

The parties should decide what disputes they wish to have settled by arbitration, and reflect their decision in the arbitration clause (paragraph 27). They may wish to authorize the arbitral tribunal to order interim measures of protection (paragraph 28). It may be advisable to stipulate in the arbitration clause that the parties are obligated to comply with arbitral decisions (paragraph 29).

Where the parties wish their disputes to be settled in judicial proceedings, it would be advisable for the contract to include an exclusive jurisdiction clause which reduces uncertainty in respect of court jurisdiction (paragraphs 30 to 32). The validity and effect of the contemplated exclusive jurisdiction clause should be considered in the light of the law of the country of the selected court, as well as the law of the countries of the two parties (paragraph 33). The parties should consider to what extent decisions of the selected court might be enforceable in the countries of the two parties (paragraph 34). It is advisable to provide that a particular court in the place where the judicial proceedings are to be instituted is to have jurisdiction (paragraph 35).

The use of an expert may be advisable when disputes of a technical nature require a rapid settlement (e.g. the procedure to be followed can be informal and structured to suit the kinds of disputes to be settled). On the other hand, there are only limited legal safeguards to ensure that proceedings before an expert are conducted carefully and impartially, and the decision of an expert cannot be directly enforced if a party fails to comply with it. It may therefore be preferable to request an expert to act as a sole arbitrator unless there are good reasons why he should not act in that capacity (paragraphs 36 and 37).

The parties may designate an expert in the contract, or provide in the contract for a procedure for the appointment of an expert after a dispute has arisen (paragraphs 40 to 43).

The contract may provide that a party has the right to initiate legal proceedings without being obligated first to propose that the dispute be settled by an expert, or may provide that legal proceedings cannot be initiated before the expiry of a specified period from the time that one party proposes to the other that the dispute be settled by

an expert (paragraph 44). The contract may also determine in what circumstances an expert is to cease to act when legal proceedings are initiated in respect of the dispute being settled by him (paragraph 45).

The contract should describe the nature of the issues with which the expert is authorized to deal (paragraph 46). The action to be taken by the expert in dealing with such issues may take various forms. He may be empowered to make findings of fact, to decide on the taking of interim measures, to decide on failures of performance, and to make decisions where there has been a failure of agreement or consent. The contract may contain provisions on the extent to which the decisions of the expert are to be reviewable in legal proceedings (paragraphs 47 to 49). The parties should be obligated under the contract to comply with the decisions of the expert (paragraph 50).

The parties may provide that the contract is to be supplemented after its conclusion by provisions agreed to by the parties. It may also provide that the contract is to be adapted by agreement if certain changes of circumstance occur during its performance. The parties may fail to agree on the required supplementation and adaptation. A party may also fail to give a consent required to be given under the contract. However, failures of agreement or consent may occur. The resolution of disputes concerning supplementation or adaptation requires the creation of new contractual rights and duties. The resolution of disputes concerning the failure to give a consent requires the making of a decision by a third party which has the effect of the required consent (paragraph 51).

Under some legal systems a court or arbitral tribunal is not entitled to create new contractual rights and obligations, or to make a decision which takes the place of a required consent. However, under many legal systems an expert may be so authorized (paragraph 52). Where the applicable legal system so permits, a court, arbitral tribunal or expert may be empowered to create new contractual rights and obligations or to make a decision which takes the place of a required consent (paragraph 53).

The clause on the settlement of disputes should determine the legal consequences of decisions dealing with the types of disputes referred to in the immediately preceding paragraph. The parties may wish to indicate in the contract the criteria to be taken into consideration in reaching such decisions (paragraphs 54 and 55).

A problem arising in connection with the construction of the works may involve several entities participating in the construction. It may be desirable for the rights and obligations of all entities involved in a dispute or related disputes to be resolved in the same proceedings, referred to in this Guide as "multi-party proceedings" (paragraph 58).

Many States have laws which provide for and regulate multi-party judicial proceedings. However, few States at present have a legal framework regulating multi-party

arbitral proceedings. The conduct of those proceedings therefore depends entirely upon the agreement of the entities participating in the proceedings (paragraphs 59 and 60).

Notwithstanding the absence of a legal framework to support the structuring of multi-party arbitral proceedings, the parties may wish to endeavour to provide for such proceedings by agreement. The agreement of entities to participate in multi-party arbitral proceedings may be in the form of harmonized arbitration clauses in their different contracts, or a single separate arbitration agreement among all entities. In the latter case, it would be preferable for each entity to become a party to the separate agreement contemporaneously with his entering into a works contract, or a contract linked to a works contract, rather than to attempt to conclude a multi-party arbitration agreement after a dispute actually arises (paragraphs 61 and 62).

The arbitration clauses or separate arbitration agreement should provide a mechanism whereby arbitral proceedings involving all entities relevant to a dispute or related disputes are conducted before the same arbitral tribunal (paragraph 63). They should also define the scope of the multi-party proceedings (paragraph 64). The parties should give careful consideration to the choice of rules which are to govern the multi-party proceedings (paragraph 65).

If it is found not to be possible to structure an arrangement for multi-party proceedings, the parties may wish to attempt in other ways to reduce the possibilities of inconsistencies in decisions in two-party arbitrations involving related disputes (paragraph 66).

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#### **A. General remarks**

1. Disputes arising in connection with works contracts may require treatment which differs from the treatment of disputes arising under other types of contracts. The complexity and comprehensiveness of works contracts, the fact that they are to be performed over a relatively long period of time (sometimes several years), and the fact that a number of entities may participate in the construction of the works require special mechanisms for the settlement of disputes and the making of various types of decisions (see paragraph 2, below). Disputes may concern highly technical matters connected with the construction process (e.g. those relating to standards for equipment and materials to be incorporated in the works) or purely legal matters (e.g. the legal consequences of a failure to perform). In addition, disputes often arise during construction, which must be resolved without an interruption of the construction.

2. The decisions to be made and measures taken in connection with a works contract cover a broad spectrum.

For example, it may have to be decided whether or not one party has failed to perform his obligations and, if so, what are the consequences of the failure. The contract may provide that some of its terms are to be adapted by the parties to meet a change in the circumstances existing at the time of its conclusion. In addition, the contract may provide that some of its terms are to be agreed upon after its conclusion, and the contract thereby supplemented. The contract may also require the consent of a party to be given in certain situations. Disputes concerning a failure of the parties to agree upon the adaptation or supplementation of the contract, or concerning a failure to give the consent, may require that a dispute settlement procedure be used in which the decision has the effect of an agreement of the parties or the consent of a party (see section G, "Disputes concerning failure of agreement or consent", below). In addition, interim measures may have to be taken in order to protect certain rights of a party to a dispute pending a final settlement of the dispute.

3. The parties should provide in the works contract mechanisms to deal in the most appropriate and expeditious manner with the various types of disputes. The contract might include provisions concerning the settlement of disputes by the parties through negotiation (see section B, "Negotiation", below) or by conciliation (see section C, "Conciliation", below). It might also provide for arbitration (see section D, "Arbitration", below), or contain provisions dealing with judicial proceedings (see section E, "Judicial proceedings", below). The contract might also provide in some cases for an independent expert to settle disputes (see section F, "Settlement of disputes by experts", below). The contract might provide for the multi-party settlement of disputes (see section H, "Multiparty settlement of disputes", below).

4. If a dispute of any kind arises between the parties, each party should be obligated under the contract to proceed with the performance of his obligations despite the dispute, unless the contract has been terminated or the performance suspended in accordance with contractual provisions or the law applicable to the contract. Even in cases where a party has terminated a contract or suspended performance, and the termination or suspension is in dispute, the arbitral tribunal or a court or an expert may be empowered to decide that the contractor is to proceed with his construction obligations pending the settlement of the dispute.

#### **B. Negotiation**

5. The settlement of a dispute by the parties themselves through negotiation is usually the most satisfactory method of dealing with the dispute. A settlement reached through negotiation could be expected to be broadly acceptable to both parties. In addition, the parties may be saved the considerable cost and delay which normally occur in the settlement of disputes by other means. In order to facilitate the settlement of future disputes by

negotiation, the contract may contain certain provisions dealing with the procedure to be followed.

6. The contract sometimes provides that in the event of a dispute arising from the contract a party can initiate arbitral or judicial proceedings (hereinafter collectively referred to as legal proceedings) for settlement of the dispute only if the parties have previously failed to agree upon a settlement by negotiation within a specified period of time. This period may commence to run when a written proposal as to how the dispute may be settled has been delivered by one party to the other. The period of time specified by the parties should not be long, as otherwise an early settlement of the dispute in legal proceedings may not be possible. Either party may be permitted under the contract to initiate legal proceedings before the expiry of the specified period of time if the party receiving a proposed settlement refuses it and states that he is not prepared to negotiate further. In addition, either party may be permitted to initiate legal proceedings before the expiry of the specified period of time if the initiation is needed to prevent the loss of a right, or the expiry of a prescription period.

7. It is advisable for the contract to require an agreement between the parties settling a dispute to be reduced to writing and signed by both parties. If the agreement involves the interpretation of the contract, or adaptation or supplementation of contractual terms, the contract may require the parties to indicate that the agreement forms an integral part of the contract.

### C. Conciliation

8. If the parties fail to settle their disputes through negotiation, they might not wish to resort immediately to legal proceedings. The contract may therefore contain provisions for the settlement of disputes by conciliation.

9. The purpose of conciliation is to achieve an amicable settlement of the dispute with the assistance of an independent third-party conciliator respected by both parties. The settlement of the dispute remains in the hands of the parties. In contrast to an arbitrator or judge, the conciliator does not adjudicate, but assists the parties in reaching a settlement by suggesting possible solutions to the parties in an impartial manner.

10. The main advantage of conciliation over legal proceedings is that the non-adversary character of conciliation may enable a good business relationship between the parties to be preserved, while legal proceedings could adversely affect the relationship. In addition, conciliation proceedings are usually less costly and time-consuming than legal proceedings. On the other hand, a potential disadvantage of conciliation is that, if the attempt at conciliation were to fail, the money and time spent on it may have been wasted. This disadvantage might be mitigated if the contract did not require the parties to engage in conciliation proceedings before they initiated

legal proceedings. The parties would then initiate conciliation proceedings only in cases where they considered that a real likelihood of an amicable settlement existed.

11. Many legal systems contain no special rules governing conciliation proceedings. Accordingly, a number of issues arising in the proceedings need to be settled by the parties in order to make the proceedings effective. It is not feasible to settle all these issues in the body of the contract, and the use of a set of rules on conciliation prepared by an international organization is advisable. The parties may wish to incorporate by reference in the contract the UNCITRAL Conciliation Rules,<sup>1</sup> a comprehensive set of rules the use of which has been recommended by the United Nations General Assembly in its resolution 35/52 of 4 December 1980.

### D. Arbitration

12. Disputes arising from works contracts are frequently settled through arbitration. International commercial arbitration may offer certain advantages over judicial proceedings. The parties can appoint as arbitrators persons of their choice who have expert knowledge of the subject-matter of the dispute. They can also choose the place where the arbitral proceedings are to be conducted. In addition, arbitral proceedings could be structured by the parties so as to be less formal than judicial proceedings and better suited to the specific features of the subject-matter of the dispute and the needs of the parties. The choice by the parties of the law applicable to the contract will almost always be respected by an arbitral tribunal, while this might not be the case in some judicial proceedings. Arbitral proceedings and awards can be kept confidential, while judicial proceedings and decisions usually cannot. Furthermore, arbitral proceedings tend to be more expeditious and in some cases less costly than judicial proceedings. Finally, as a result of international conventions which assist in the recognition and enforcement of foreign arbitral awards, these awards are frequently recognized and enforced more easily than are foreign judicial decisions.<sup>2</sup> However, while under some legal systems multi-party proceedings may be initiated in a court, it is difficult to arrange for those proceedings in arbitration (see section H, "Multi-party settlement of disputes", below).

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 106. The UNCITRAL Conciliation Rules have also been reproduced in booklet form (United Nations publication, Sales No. E.81.V.6). Accompanying the Rules is a model conciliation clause, which reads: "Where, in the event of a dispute arising out of or relating to this contract, the parties wish to seek an amicable settlement of that dispute by conciliation, the conciliation shall take place in accordance with the UNCITRAL Conciliation Rules as at present in force".

<sup>2</sup>A broad enforceability of arbitral awards is established under the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, adopted in New York on 10 June 1958 (*Register of Texts of Conventions and other Instruments concerning International Trade Law*, vol. II, p. 24 (United Nations publication, Sales No. E.73.V.3) or United Nations, *Treaty Series*, vol. 330, No. 4739, p. 38).

13. In general, arbitral proceedings may be conducted only on the basis of an agreement by the parties to arbitrate. Their agreement may be reflected either in an arbitration clause included in the contract, or in a separate arbitration agreement concluded by the parties before or after a dispute has arisen. Since it may be more difficult to reach an agreement to arbitrate after a dispute has arisen, it is advisable either to include an arbitration clause in the contract, or to enter into a separate arbitration agreement at the time that the contract is concluded. However, under some legal systems, an agreement to arbitrate is valid only if it is concluded after a dispute has arisen.

14. The arbitration clause should indicate the disputes which are to be settled by arbitration (see paragraph 27, below). If proceedings are instituted in a court on a matter which is covered by the arbitration clause, the court will normally, upon the request of a party within a time period specified in its law, refer the dispute to arbitration. Notwithstanding an arbitration clause, the competent court usually has authority to order interim measures of protection, to control certain aspects of arbitral proceedings (e.g. to decide on a challenge to arbitrators) and to set aside arbitral awards on grounds determined by the law applicable to the arbitration.

#### 1. *Arbitral proceedings*

15. The law applicable to the arbitration, which is usually the arbitration law in force at the place where the arbitration is conducted, will regulate many issues arising in the arbitral proceedings. The law applicable to the arbitration usually gives wide autonomy to the parties to agree upon the procedure to be followed in the arbitration. Since this law may not regulate some issues arising in the arbitral proceedings, or may not regulate them in a satisfactory manner, it may be advisable for the parties to agree that the arbitral proceedings are to be regulated by a set of arbitration rules of their choice.

#### (a) *Rules to regulate arbitral proceedings*

16. Arbitration institutions offer services ranging from merely appointing arbitrators to full administration of the arbitral proceedings. The parties may wish to consider the extent to which they wish to make use of those services. Parties which have selected an arbitration institution to administer the arbitral proceedings frequently agree that the proceedings are to be regulated by the rules of that institution, if they consider the content of the rules to be acceptable. Some arbitration institutions are ready to administer the arbitral proceedings only when the parties agree that the arbitration rules of the institution are to apply. A number of arbitration institutions apply the UNCITRAL Arbitration Rules (see immediately following paragraph) as their own rules, in some cases with certain supplementations needed to conform to the statutes of or administrative services offered by those institutions.

17. Several international organizations have prepared arbitration rules<sup>3</sup> which can be made applicable by agreement of the parties in cases where no arbitration institution has been selected to administer the arbitral proceedings. The UNCITRAL Arbitration Rules,<sup>4</sup> the use of which was recommended by the United Nations General Assembly in its resolution 31/98 of 15 December 1976, are widely used in these cases. Certain institutions, while having their own arbitration rules, are prepared to apply the UNCITRAL Arbitration Rules to arbitration proceedings administered by them if the parties so desire. Certain other institutions which offer less comprehensive services than full administration of arbitration proceedings have declared their willingness to act as an appointing authority for the appointment of arbitrators (see paragraph 20, below) and to provide other administrative services in arbitrations under the UNCITRAL Arbitration Rules if the parties so desire.

18. Arbitration rules prepared by international organizations usually give the parties autonomy to adapt the rules to their particular needs. However, some limitation to the autonomy is usually imposed in the rules of arbitration institutions in regard to services offered by those institutions. The solutions provided by the arbitration rules to certain issues normally apply only if the parties have not agreed on those issues. The parties may find it advisable to agree, in particular, on the number of arbitrators, the place of arbitration, and the language to be used in the arbitration proceedings (see footnote 7, below, paragraph (7)(a), (b) and (c)).

#### (b) *Appointment of arbitrators*

19. The parties may wish to specify in the arbitration clause the number of arbitrators who are to comprise the arbitral tribunal. Works contracts often provide for three arbitrators. Three arbitrators might bring to the proceedings a broad range of legal and technical expertise. However, the parties might wish to consider the possibility of providing for only one arbitrator. Proceedings before a single arbitrator are less costly than before three arbitrators, and it is easier to schedule proceedings before one arbitrator. Since it may be impossible at the time of the conclusion of the contract to envisage the complexity and nature of a potential dispute, another possibility may be for the parties to agree on the number of arbitrators after a dispute has arisen. If they fail to reach agreement, the rules which govern the arbitral proceedings will determine the number of arbitrators.

<sup>3</sup>Arbitration Rules of the United Nations Economic Commission for Europe (*Register of Texts of Conventions and other Instruments concerning International Trade Law* (United Nations publication, Sales No. E.73.V.3), vol. II, p. 100 or *Arbitration Rules of the United Nations Economic Commission for Europe* (United Nations publication, Sales No. E.70.II.E/Mim.14)); Rules for International Commercial Arbitration and Standards for Conciliation of the United Nations Commission for Asia and the Far East (*Register of Texts of Conventions and other Instruments concerning International Trade Law*, (United Nations publication, Sales No. E.73.V.3), vol. II, p. 95).

<sup>4</sup>Report of the United Nations Commission on International Trade Law on the work of its ninth session, *Official Records of the General Assembly, Thirty-first Session, Supplement No. 17 (A/31/17)*, para. 57. The UNCITRAL Arbitration Rules have also been reproduced in booklet form (United Nations publication, Sales No. E.77.V.6).

20. Arbitrators are normally appointed by agreement of the parties. When the arbitration is not to be administered by an arbitration institution, the parties should designate in the arbitration clause an appointing authority to appoint the arbitrators in the event that they do not agree as provided for under the arbitration clause (see footnote 7, below, paragraph (7)(d)). The appointing authority may be an institution or a person (e.g. the president of a specified chamber of commerce). The parties should make sure that the chosen institution or person is willing and will be available to appoint the arbitrator. The UNCITRAL Arbitration Rules provide a procedure for designating an appointing authority where no appointing authority is agreed upon by the parties, or where the appointing authority agreed upon fails to appoint arbitrators.<sup>5</sup>

(c) *Language to be used in arbitral proceedings*

21. The parties may also wish to designate in the arbitration clause the language to be used in the arbitral proceedings. The choice of the language may influence the expeditious conduct and the cost of the arbitral proceedings. Whenever possible, the parties should designate a single language. When more than one language is designated, the costs of translation and interpretation between one designated language and the other are usually considered to be part of the costs of arbitration and are apportioned in the same way as the other costs of arbitration. In many cases, it would be desirable for the designated language to be the language in which the contract is written. The written pleadings, testimony at a hearing, the award, and other decisions or communications by the arbitrators may be required to be in or be translated into the designated language. The arbitrators may be empowered to admit documents as evidence in their original language.

(d) *Place of arbitration*

22. The arbitration clause may specify the place where the arbitration is to take place. In selecting the place, the parties should note that the arbitration law in that place will often determine what disputes are arbitrable, and also resolve certain other issues arising in arbitral proceedings (see paragraph 15, above). An international treaty resolving certain issues arising in arbitral proceedings may also apply in the country where the arbitration is to take place. A number of states, including several states outside Europe, are contracting parties to the European Convention on International Commercial Arbitration prepared by the United Nations Economic Commission for Europe.<sup>6</sup>

23. In deciding the place of arbitration, the parties should anticipate the need to enforce the award. For

instance, in deciding upon the country where the proceedings are to take place, the parties should consider whether awards made in that country would be enforceable in the country of each party on the basis of international conventions or the applicable municipal laws. Or, they may wish to provide that arbitral proceedings are to take place in a country where both parties have assets against which execution of an award may be made.

24. If the parties have chosen an arbitration institution to administer the arbitration, they should specify a location for the arbitration where that institution is able to perform its functions. Whether or not they have chosen an arbitration institution to administer the arbitration, in choosing the place of arbitration the parties should in any event take into consideration such factors as the convenience of the parties, the availability of communications and other support services, the arbitration law in force and, in particular, what disputes are arbitrable under that law, and the cost of conducting an arbitration at that place.

25. In some cases, the parties may wish to agree that the place of arbitration is to be in the country of the party against whom a claim is brought. This may facilitate the enforcement of the award against that party in his country, since the award would not be considered a foreign award in that country. They may so agree when the arbitration is to be regulated by arbitration rules prepared by an international organization. Alternatively, they may agree upon two arbitration institutions, one located in the country of each party, and provide that the arbitration is to be administered by the institution in the country of the party against whom a claim is brought (the so-called mixed arbitration clause). The parties may wish to adopt this approach if they cannot agree upon a single arbitration institution to administer the arbitration. This approach may, however, give rise to some difficulties. The legal rules applied to arbitration in the two countries are likely to differ, and could be more burdensome or otherwise less satisfactory to a party in one country than in the other. In addition, if arbitral proceedings involving disputes arising out of the same works contract are conducted in both countries, the proceedings will be controlled by different courts, and different degrees of control may be exercised (see paragraph 14, above).

(e) *Decision ex aequo et bono*

26. It is advisable for the parties to be cautious in authorizing the arbitral tribunal to decide disputes *ex aequo et bono*, since such an authorization may be interpreted in different ways, and in some cases might lead to results which depart from the legal framework agreed upon by the parties in the contract. Under some legal systems an arbitral tribunal is not permitted to decide *ex aequo et bono*. If the parties do wish to authorize the arbitral tribunal to decide *ex aequo et bono*, they should also obligate it to decide the dispute in accordance with the terms of the contract and taking into account the usages applicable to the transaction.

<sup>5</sup>In such cases either party may request the Secretary-General of the Permanent Court of Arbitration at The Hague, Netherlands, to designate an appointing authority.

<sup>6</sup>See *Register of Texts of Conventions and other Instruments concerning International Trade Law* (United Nations publication, Sales No. E.73.V.3), vol. II., p.34 or United Nations, *Treaty Series*, vol. 484, No. 7041, p. 364.

## 2. Disputes to be settled by arbitration

27. The parties should indicate what disputes they wish to have settled by arbitration. An approach often adopted to drafting the arbitration clause is to stipulate that all disputes arising out of or relating to the contract are to be settled by arbitration (see footnote 7, below, paragraph (1)). In some cases the parties may wish to exclude from the wide jurisdiction thus conferred on the arbitrators some disputes they do not wish to be settled by arbitration. Alternatively, in exceptional cases the parties may wish to specify in the arbitration clause the kinds of disputes which are to be settled by arbitration (for example, disputes concerning some of the following issues: determination of the rights and duties of the parties; whether or not the contract has been breached, and if so the consequences of the breach; whether or not the contract or some of its provisions are invalid, and if so the consequences of the invalidity; whether or not performance of the contract is or may be suspended, and if so the consequences of the suspension; whether or not the contract is to be terminated, and if so the consequences of the termination). Under many legal systems an arbitration clause is considered to be an independent agreement which may be valid and remain in force even if the contract in which it was included is invalid or terminated. Under those legal systems therefore the arbitrators have the competence to decide that the contract in which the arbitration clause was included is invalid or terminated without at the same time destroying their authority to arbitrate. The parties may also wish to authorize the arbitrators to settle certain specified disputes concerning a failure of agreement or consent (see section G, "Disputes concerning failure of agreement or consent", below, and illustrative provisions in footnote 7, below, paragraphs (2) and (3)).

28. The parties may wish to authorize the arbitral tribunal to order interim measures of protection. Under some legal systems, however, interim measures ordered by an arbitral tribunal cannot be enforced. In such cases it may be preferable for the parties to rely on a court to order interim measures. Under most legal systems a court may order interim measures even if the dispute is to be or has been submitted to arbitration. In cases where the arbitration clause may be interpreted as excluding the power of a court to order interim measures, it is advisable to provide in the contract that the agreement to settle disputes by arbitration does not prevent either of the parties from requesting a court to order interim measures of protection (see footnote 7, below, paragraph (4)(a), (b) and (c)).

29. It may be advisable to stipulate in the arbitration clause that the parties are obligated to comply with arbitral decisions, including interim measures. Where an arbitral award is not directly enforceable, a failure to comply with the arbitral decision may be regarded in judicial proceedings as a breach of a contractual obligation.<sup>7</sup>

<sup>7</sup>Illustrative provisions (arbitration clause)

"(1) Any dispute, controversy or claim arising out of or relating to this contract, or the breach, termination or invalidity [or suspension

## E. Judicial proceedings

30. If the parties do not agree on the settlement of their disputes by arbitration, disputes between the parties will be decided by the courts which have jurisdiction to decide those disputes. The scope of court jurisdiction is not the same in all countries, and the courts of two or more countries may be competent to decide the same disputes between the parties. A court in principle applies only the rules of private international law of its country, and even

of performance] thereof shall be settled by arbitration in accordance with ... (identify arbitration rules) as at present in force."

"(2) Where the parties fail to reach agreement on adapting or supplementing the contract as required under articles ... of this contract, the arbitral tribunal is entitled to adapt or supplement the contract. The decision of the arbitral tribunal shall be deemed to be an agreement of the parties which is incorporated in the contract from the date specified in the award."

(This paragraph may be included in the arbitration clause if the contract is to be adapted or supplemented, and the law applicable to the arbitration permits the arbitral tribunal to adapt or supplement the contract.)

"(3) If [a party] [the purchaser] wrongfully fails to give his consent as required under articles ... of this contract, the arbitral tribunal is entitled to make a decision which has the effect of a consent given by [the party] [the purchaser]."

(This paragraph may be included in the arbitration clause if the contract requires that the consent of a party (frequently the purchaser) be given in certain situations, and the law applicable to the arbitration permits the arbitral tribunal to make a decision which has the effect of a consent required to be given by a party.)

"(4) (a) The arbitral tribunal is entitled during the arbitral proceedings, upon the request of a party made in writing, to order any interim measures of protection

- necessary for the establishment or preservation of evidence to be used in arbitral proceedings, or
- which are urgently needed to safeguard the rights of a party, or to prevent or mitigate serious loss which may be caused to a party by an act or omission to act by the other party in connection with a dispute in respect of which arbitral proceedings have been initiated.

"(b) Interim measures ordered by the arbitral tribunal shall cease to have effect when the dispute to which the interim measures relate is settled in arbitral proceedings, unless the order for interim measures specifies that they are to cease to have effect at an earlier time.

"(c) The authority given to the arbitral tribunal under subparagraph (a) of this paragraph to order interim measures does not exclude the right of either party to request a court to order interim measures of protection."

(This paragraph may be included in the arbitration clause if no provision for taking interim measures is contained in the arbitration rules which are to be incorporated by reference under paragraph (1) of this clause.)

"(5) The arbitral tribunal is entitled to review decisions made by the expert under articles ... of this contract and to set aside or modify his decisions in accordance with the provisions of those articles."

(This paragraph may be included in the arbitration clause if an expert is authorized to settle specified disputes in respect of the contract, and the law applicable to the arbitration permits the review. The articles to be enumerated are those conferring powers on the expert in regard to the settlement of disputes: see footnotes 11, 12, 13 and 14, below).

"(6) The parties are obligated to comply with arbitral decisions made by the arbitral tribunal.

"(7) (a) The number of arbitrators shall be ... (one or three).

"(b) The place of arbitration shall be ... (town or country).

"(c) The language[s] to be used in the arbitral proceedings shall be ....

"(d) The appointing authority shall be ... (name and address of institution or person)."

(Subparagraph (d) should be included in the arbitration clause if the rules which are to be incorporated by reference under paragraph (1) of this clause are not the rules of an arbitration institution.)

the validity and effect of a choice by the parties of the law applicable to the contract is determined by a court by reference to laws identified in accordance with those rules (see chapter XXVIII, "Choice of law"). Accordingly, the legal position of the parties in the event of a dispute depends to some extent upon which court decides the dispute.

31. Uncertainty in respect of court jurisdiction is reduced if the parties include an exclusive jurisdiction clause in the contract. Under such a clause, the parties are obligated to submit disputes which arise between them in connection with the contract to a court at a specified place in a specified country (see footnote 8, below, paragraph (1)). An exclusive jurisdiction clause would usually designate a court in the country of one of the parties. However, the courts of other countries are also often designated. The law of many countries gives effect to these clauses in international trade contracts, though under varying conditions (e.g. some laws may require a link between the contract and the country of the selected court). The law of many countries requires an exclusive jurisdiction clause to be in writing.

32. If the parties wish the selected court to have exclusive jurisdiction, they should so specify. If they fail to specify exclusivity, the clause may be interpreted as giving the selected court a jurisdiction which is only concurrent with that of other courts which have jurisdiction under the laws determining their jurisdiction.

33. The validity and effect of the contemplated exclusive jurisdiction clause should be considered in the light of the law of the country of the selected court, as well as the law of the countries of the two parties. If the clause is valid under the law of the countries of each of the two parties but invalid under the law of the country of the selected court, difficulties may arise in initiating judicial proceedings in any of the countries. If the clause is considered valid under the law of the country of the selected court but invalid under the law of the countries of the two parties, the jurisdiction of the selected court would not be exclusive and its decisions may not be enforceable in the countries of either of the two parties.

34. The parties should consider to what extent decisions of the selected court might be enforceable in the countries of the two parties. In this regard, they should take into account any international treaty concluded between the country of the selected court and their own countries which establishes conditions under which decisions of the selected court are enforceable in their countries. In the absence of such a treaty, they should take into account the conditions under which such decisions are enforceable under the laws of their countries. Under many legal systems reciprocity may be a condition for enforceability.

35. It is advisable to provide in the exclusive jurisdiction clause that a particular court in the place where the judicial proceedings are to be instituted is to have jurisdiction. If the clause only refers to the courts of a place in the selected country without identifying a par-

ticular court, there may be difficulty in determining which court in that place is to decide the disputes. An exclusive jurisdiction clause is normally valid under the law of the country of the selected court only if the selected court is competent under its jurisdictional laws to decide upon the kind of disputes which that court is intended to decide under the clause. The parties should therefore ascertain that the court contemplated by them has the competence to decide the types of disputes which they wish to submit to it. The clause may specify the disputes to be decided by the selected court in a manner similar to the specification of the disputes under an arbitration clause (see paragraph 27, above).<sup>8</sup>

#### F. Settlement of disputes by experts

36. The use of an expert may be advisable when disputes of a technical nature require a rapid settlement. It may be possible to commence proceedings before an expert much more quickly than to commence legal proceedings. The procedure to be followed by the expert can be quite informal and expeditious, and it can be structured by the parties so as to suit the kind of disputes to be settled by the expert. Under some legal systems an expert may be competent to create new contractual rights and obligations, or to make decisions which have the effect of a consent required to be given by a party under the contract, while a court or arbitral tribunal may not have that competence.

##### <sup>8</sup>*Illustrative provisions (exclusive jurisdiction clause)*

"(1) Any dispute, controversy or claim arising out of or relating to this contract, or the breach, termination or invalidity [or suspension of performance] thereof shall be settled exclusively by ... (specify court) at ... (specify town and country).

"(2) Where the parties fail to reach agreement on adapting or supplementing the contract as required under articles ... of this contract, the court is entitled to adapt or supplement the contract. The decision of the court shall be deemed to be an agreement of the parties which is incorporated in the contract from the date specified in the decision."

(This paragraph may be included in the exclusive jurisdiction clause if the contract is to be adapted or supplemented, and the law applicable to the judicial proceedings permits the court selected by the parties to adapt or supplement a contract when the parties have authorized it to do so.)

"(3) If [a party] [the purchaser] wrongfully fails to give his consent as required under articles ... of this contract, the court is entitled to make a decision which has the effect of a consent given by [the party] [the purchaser]."

(This paragraph may be included in the exclusive jurisdiction clause if the contract requires that the consent of a party (frequently the purchaser) be given in certain situations, and the law applicable to the judicial proceedings permits the court selected by the parties to make a decision which has the effect of a consent required to be given by a party when the parties have authorized the court to do so.)

"(4) Notwithstanding the provisions of paragraph (1) of this clause, a party may request a court other than the court specified in paragraph (1) to order any interim measures of protection.

"(5) The court is entitled to review decisions made by the expert under articles ... of this contract and to set aside or modify his decisions in accordance with the provisions of those articles."

(This paragraph may be included in the exclusive jurisdiction clause if an expert is authorized to settle specified disputes in respect of the contract, and the law applicable to the judicial proceedings permits the court selected by the parties to review the decisions of the expert when the parties have authorized it to do so. The articles to be enumerated are those conferring powers on the expert in regard to the settlement of disputes: see footnotes 11, 12, 13 and 14, below).

37. On the other hand, the procedure of dispute settlement by an expert is not regulated under many legal systems, and there are only limited legal safeguards to ensure that the proceedings are conducted carefully and impartially. In addition, the decision of an expert cannot be directly enforced if a party fails to carry it out and legal proceedings must be initiated in which the failure to comply with the expert's decision may be regarded as a breach of a contractual obligation (see paragraph 50, below). It may therefore be preferable to request the expert to act as a sole arbitrator unless there are good reasons why he should not act in that capacity. Such reasons would exist if arbitral proceedings would not be expeditious enough, or if the law applicable to the arbitration does not permit the dispute in question to be settled in arbitral proceedings. The authority given to the expert should be limited in the contract to the settlement of issues which are carefully delineated and whose major content is technical. The authority should not cover purely legal issues, since in many cases the expert will have no legal training, and legal proceedings are more appropriate for the settlement of those issues. It may be advisable to provide for a review of the expert's decision by a court or arbitral tribunal (see paragraphs 47-49, below).

38. The procedure of dispute settlement by an expert is not regulated under many legal systems, and must therefore be regulated by contractual provisions. This Guide therefore deals with these issues arising in connection with the settlement of disputes by an expert in some detail.

39. In some cases the parties may wish to agree in the contract that certain technical disputes are to be settled by a consulting engineer employed by the purchaser. The selection of a consulting engineer who is to have such authority, and the kinds of dispute which are to be settled by him, are discussed in chapter X, "Consulting engineer".

#### 1. *Appointment of expert*

40. The parties may decide to designate an expert in the contract (see footnote 9, below, alternative I). This may accelerate the settlement procedure, by making it possible for a party to request the expert to settle a dispute as soon as it has arisen. The other party should be notified of the request. It may be advisable to designate in the contract an alternate expert to settle disputes when the first expert designated is not immediately available. Alternatively, the parties may designate only one expert, but agree with him that he should be immediately available during a specified period for the settlement of disputes. It may be necessary to pay the expert a fee to secure such availability. However, where a complex industrial works is being constructed, different technical disputes may arise which require different specializations for their settlement. Since at the time the contract is concluded it will be impossible to predict the nature of the disputes which might arise, it may not be desirable to designate an expert in the contract, since his specializations would necessarily be limited.

41. The expert will be able to settle disputes more expeditiously if he is acquainted with the construction that has been completed, and the current situation on the site. The parties may therefore provide that he is to be kept informed of progress in the construction, and specify the form in which the necessary information is to be given to the expert.

42. Instead of designating the expert in the contract, an alternative approach is to provide in the contract for a procedure for the appointment of the expert after a dispute has arisen (see footnote 9, below, alternative II).

43. If the parties fail to agree upon an expert within a period of time to be specified in the contract after a notice calling for the designation of an expert has been delivered, the expert may be designated by an institution or person specified in the contract. The parties should make sure that the chosen institution or person is willing and will be available to appoint an expert. The parties may choose an institution which has issued rules expressing its willingness to designate technical experts if so requested by a party or parties to a contract on the basis of a contractual clause.<sup>9</sup>

#### 2. *Commencement and cessation of proceedings before expert*

44. The contract may provide that any party has the right to initiate legal proceedings without being obligated first to propose that a dispute be settled by an expert. If this approach is adopted a party can choose the dispute settlement procedure which he considers to be more appropriate for the dispute in question. An alternative approach may be to provide that legal proceedings cannot be initiated before the expiry of a specified period of time commencing to run from the time that one party proposes to the other party that the dispute be settled by an expert. The period of time specified by the parties should not be long, as otherwise an early settlement of the dispute in legal proceedings may not be possible. Furthermore, the contract should permit either party to initiate legal proceedings before the expiry of the specified period of time if the initiation is needed to prevent the loss of a right, or the expiry of a prescription period.

45. In general, the contract may provide that the expert is to cease to act when legal proceedings are initiated in respect of the dispute being settled by him. In certain cases, however, the contract may provide that the expert is to continue to act after legal proceedings are initiated,

##### <sup>9</sup>*Illustrative provisions*

###### *Alternative I*

"The parties designate ... (name, profession and address) as the expert for the settlement of disputes required to be settled by an expert under this contract."

###### *Alternative II*

"(1) The expert for the settlement of disputes required to be settled by an expert under this contract shall be designated by agreement of the parties.

"(2) If the parties fail to agree upon an expert before the expiry of ... days after a party has delivered to the other party a notice calling for the designation of an expert, the expert shall be designated by ... (name and address of institution or person)."



for example in cases where the expert's function is limited to making findings preserving or establishing evidence to be used in the legal proceedings, or to the taking of interim measures. The expert should, however, cease to act when the dispute is settled in the legal proceedings (see footnote 10, below, paragraph (1); footnote 11, below, paragraph (1); footnote 12, below, paragraph (2); footnote 13, below, paragraph (2); and footnote 14, below, paragraph (2)).

### 3. Mandate of expert

46. The expert may be authorized to deal with technical issues which require a rapid settlement, and whose legal content is minimal. For example, he may be authorized to deal with issues concerning the fixing of the time-schedule for construction (see chapter IX, "Construction on site"), the determination of the amount of an instalment of the price to be paid during construction (see chapter VII, "Price"), the validity of the contractor's objections to a variation ordered by the purchaser, the consequences of the variation on the time-schedule and the price (see chapter XXIII, "Variation clauses"), and the results of mechanical completion and performance tests (see chapter XIII, "Completion, take-over and acceptance"). In dealing with such issues, he may make findings of fact, order interim measures, decide on disputes concerning failures of performance, or make decisions when there has been a failure of agreement or consent.

47. The expert may be empowered to make findings of fact (see footnote 10, below, paragraph (1)). During the construction process, the condition of the uncompleted works changes rapidly, and partially completed construction is soon covered up by further construction. In the event of a dispute involving the condition of uncompleted works, it is thus important that evidence of the relevant condition of the works is secured as soon as possible, since it may be impossible at a later stage to obtain such evidence. The expert may be authorized upon request of either party to determine the condition of the works and to preserve or establish evidence to be used in possible legal proceedings. The contract may provide that his findings are to be regarded as expert evidence by a court or arbitral tribunal, and evaluated in the same manner as other expert evidence (see footnote 10, below, paragraph (2), alternative I). Another approach may be to provide in the contract that the parties are not permitted to question the correctness of the findings of fact in legal proceedings (see footnote 10, below, paragraph (2), alternative II).<sup>10</sup>

#### <sup>10</sup>Illustrative provisions

"(1) Upon the request of a party made in writing, the expert is authorized before the commencement of [and during] [arbitral] [judicial] proceedings to make findings of fact concerning ... (specify scope of fact-finding by the expert).

#### Alternative I

"(2) Findings of fact made by the expert and submitted to the [arbitral tribunal] [court] must be evaluated by the [arbitral tribunal] [court] as expert evidence.

#### Alternative II

"(2) The parties are not permitted to question in legal proceedings the correctness of findings of fact made by the expert."

48. Since the need to continue construction without interruption may sometimes require urgent interim measures to be taken in respect of a dispute between the parties before the dispute is settled in legal proceedings, the expert may be empowered to decide on the taking of interim measures in respect of specified kinds of disputes. For example, where the amount due to a contractor for a completed portion of the works is in dispute during the construction, an interim decision that some amount must be paid to the contractor for completed work may be needed in order to enable him to have the funds to proceed with the construction. The parties may wish to authorize the expert to take such interim measures.<sup>11</sup>

49. Disputes concerning failures of performance by a party often involve significant legal issues, and should normally be settled in legal proceedings. However, the expert may be authorized to decide on specified disputes concerning failures of performance (e.g. whether construction is defective, and the purchaser is entitled to order stoppage of the construction).<sup>12</sup> He may also be

#### <sup>11</sup>Illustrative provisions

"(1) Upon the request of a party made in writing, the expert is authorized before the commencement of [and during] [arbitral] [judicial] proceedings to order interim measures concerning ... (specify the matters concerning which interim measures may be ordered).

"(2) (a) The parties must comply with interim measures ordered by the expert under this clause unless the interim measures are outside the terms of reference given to the expert by the parties, or set aside or modified in accordance with subparagraphs (b) and (c) of this paragraph.

"(b) The interim measures may be reviewed in [arbitral] [judicial] proceedings, provided a party initiates those proceedings within ... days (specify period of time) after the decision on the interim measures.

"(c) At a review, the [arbitral tribunal] [court] may modify or set aside the interim measures [but only if it decides that the expert has violated the applicable law or a contractual provision]."

#### <sup>12</sup>Illustrative provisions

"(1) Upon the request of a party made in writing, the expert is authorized to settle disputes concerning .... (specify the disputes of a technical nature concerning failures of performance which the expert may settle).

#### Alternative I

"(2) (a) Either party is entitled to initiate [arbitral] [judicial] proceedings in respect of a dispute irrespective of whether or not the settlement of the dispute by an expert is proposed or has commenced.

"(b) The expert shall [cease to act in the settlement of any dispute when [arbitral] [judicial] proceedings are initiated in respect of that dispute] [continue to act in the settlement of any dispute after [arbitral] [judicial] proceedings are initiated in respect of that dispute]. The expert shall, however, cease to act in the settlement of the dispute when the dispute is settled in those proceedings].

#### Alternative II

"(2) (a) Neither party is entitled to initiate [arbitral] [judicial] proceedings relating to any dispute which the expert is authorized to settle before the expiry of ... days (specify a period of time) from the time when one party informs the other that he wishes that dispute to be settled by the expert.

"(b) Either party is however entitled to initiate [arbitral] [judicial] proceedings before the expiry of the period of time specified in subparagraph (a) of this paragraph if the initiation of the proceedings is needed to prevent the loss of a right or the expiry of a limitation period.

"(c) The expert shall cease to act in the settlement of any dispute when [arbitral] [judicial] proceedings are initiated in respect of that dispute.

empowered to decide on the adaptation or supplementation of the contract,<sup>13</sup> or to make a decision which has the effect of a consent required to be given by a party,<sup>14</sup> if the decision in either case involves the consideration of technical issues (see section G, "Disputes concerning failure of agreement or consent", below). The parties should consider whether a court or arbitral tribunal is entitled under the laws governing their proceedings to review decisions of an expert of the kind referred to in this paragraph. Under some legal systems a court or arbitral tribunal is entitled to make a review. Under other legal systems a court or arbitral tribunal is entitled to make a review if it is so authorized by the parties. Some legal systems which admit a review without authorization permit the parties to exclude it. Excluding or not authorizing a review has the advantage that a final decision on the dispute is reached rapidly. Permitting a review gives the parties greater assurance that they will obtain a fair and just decision. The advantages of both approaches may to some extent be combined by stipulating in the contract that the expert's decision is binding on the parties and cannot be reviewed in legal proceedings, unless a party initiates the proceedings within a short specified period of time after the expert's decision is delivered to him (see footnote 12, above, paragraph (3)(b)).

- "(3) (a) The parties must comply with the decision of the expert unless the decision is outside the terms of reference given to the expert by the parties, or set aside or modified in accordance with subparagraphs (b) and (c) of this paragraph. (b) The decision may be reviewed in [arbitral] [judicial] proceedings, provided a party initiates those proceedings within ... days (specify period of time) after the decision of the expert has been delivered to him. (c) At a review, the [arbitral tribunal] [court] may modify or set aside the decision."

<sup>13</sup>*Illustrative provisions*

"(1) Upon the request of a party made in writing, the expert is authorized to settle disputes concerning the [adaptation] [supplementation] of the contract if the parties fail to reach agreement under articles ... (specify articles) of this contract."

(Paragraph (2) of this provision is identical with paragraph (2) set forth in footnote 12.)

"(3) (a) The decision of the expert shall have the effect of an agreement of the parties incorporated in this contract from the date specified in the decision, unless the decision is outside the terms of reference given to the expert by the parties or set aside or modified in accordance with subparagraphs (b) and (c) of this paragraph. If a party fails to comply with the decision, the other party may in [arbitral] [judicial] proceedings claim performance of the obligations imposed by the decision."

(Subparagraphs (b) and (c) of this provision are identical with paragraph (3)(b),(c), set forth in footnote 12.)

<sup>14</sup>*Illustrative provisions*

"(1) Upon the request of a party, the expert is authorized to settle disputes relating to the failure of [a party] [the purchaser] to give a consent required to be given under articles ... (specify articles) of this contract."

(Paragraph (2) of this provision is identical with paragraph (2) set forth in footnote 12.)

"(3) (a) The decision of the expert shall have the effect of the consent of a party required under the articles of this contract enumerated in paragraph (1), above, unless the decision is outside the terms of reference given to the expert by the parties or set aside or modified in accordance with subparagraphs (b) and (c) of this paragraph."

(Subparagraphs (b) and (c) of this provision are identical with paragraph (3)(b),(c), set forth in footnote 12.)

50. Under many legal systems an expert's decision cannot be directly enforced if a party fails to perform it, since it does not have the status of an arbitral award or judicial decision. The parties should therefore be obligated under the contract to comply with the decisions of the expert.

**G. Disputes concerning failure of agreement or consent**

51. At the time of the conclusion of the contract the parties may not have sufficient information to agree how certain issues are to be resolved (e.g. to fix the time-schedule for the entire construction) and they may therefore in the contract provide that those issues are to be resolved at a later stage. Furthermore, during the performance of the contract a change of circumstances may occur which under the contract requires the parties to renegotiate the contract and adapt it to the new circumstances. In such cases the parties may at a later stage fail to agree how the postponed issues are to be resolved, or whether a change of circumstances requiring the adaptation of the contract has occurred and, if so, how the contract should be adapted. In addition, disputes may arise concerning the failure of a party to give a consent which he is required to give under the contract (e.g. for the employment of a subcontractor). The resolution of such disputes requires decisions creating new contractual rights and obligations, or the making of a decision by a third party which has the effect of a consent required to be given by a party to the contract. Such decisions are distinct from the adjudication of disputes relating to existing rights and obligations, and the consequences of a failure to perform an obligation (e.g. liability to pay damages).

52. Whether a court or arbitral tribunal is entitled to create new contractual rights and obligations, or to make a decision which takes the place of a consent required to be given under the contract by a party, depends on its competence under the law applicable to the legal proceedings. Under some legal systems, a court is not entitled to exercise such powers, and arbitrators are entitled to exercise only the powers which a court may exercise. Under other legal systems a court or arbitral tribunal is entitled to exercise such powers if the parties by agreement have expressly conferred such powers on them. Under many legal systems an expert is entitled to create new contractual rights and obligations or to make a decision which has the effect of the consent of a party, if he is authorized under the contract to do so.

53. Where the applicable law permits a court, an arbitral tribunal or an expert to create new contractual rights and obligations or to make a decision which has the effect of the consent of a party, it is advisable for the clause in the contract on the settlement of disputes expressly to authorize the arbitral tribunal, court or expert to exercise those powers (see footnote 7, above, paragraphs (2) and (3); footnote 8, above, paragraphs (2) and (3); footnote 13, above, paragraph (1); and footnote

14, above, paragraph (1)). In the absence of an express authorization, the clause may be interpreted as only conferring authority to adjudicate on disputes relating to existing rights and obligations and the consequences of a failure to perform an obligation. In addition, the parties should identify the disputes to be settled under the authority conferred by them, if possible by reference to contractual provisions calling for supplementation or adaptation of the contract or requiring the consent of a party (see footnote 13, above, paragraph (1), and footnote 14, above, paragraph (1)).

54. The clause on the settlement of disputes should determine the legal consequences of decisions in the types of disputes dealt with in this section. If the creation of new contractual rights and obligations is contemplated, the clause should provide that the decision is binding on the parties in the same manner as contractual terms agreed to by the parties. In contrast to a decision in a dispute concerning a failure to perform an obligation, a binding decision creating new contractual rights and obligations may not be directly enforceable. If, however, a party fails to perform an obligation created by the decision, it may be possible to initiate legal proceedings in which failure to comply with the decision may be regarded as a breach of a contractual obligation.

55. In many legal systems there is an absence of substantive rules determining the criteria which should be taken into consideration by a court or arbitral tribunal in deciding disputes concerning the creation of new contractual rights and obligations, or the making of a decision which has the effect of the consent of a party. As a result, such decisions may be given merely on a fair and discretionary assessment of all relevant circumstances.

56. In order to reduce the possible uncertainty connected with such decisions, the parties may wish to indicate in the contract the criteria to be taken into consideration in reaching a decision. Since different criteria may be relevant depending on the content of a particular contractual provision, it may be preferable to specify those criteria which are relevant to a particular contractual provision in that particular provision (e.g. see chapter XXIII, "Variation clauses").

57. The difficulties mentioned above which arise in connection with the adaptation of contractual rights and obligations by a court, an arbitral tribunal or an expert may be reduced if a mechanism is provided in the contract under which contractual terms are to be automatically modified by the application of a formula specified in the contract without the need for further agreement by the parties. Such an approach is practicable particularly in connection with the adjustment or revision of the price. The contractual mechanism may be based on a specified mathematical formula. Alternatively, the contract may provide for the payment of costs reasonably incurred by a party (see chapter VII, "Price"). Where such an approach is used by the parties, there will be no disputes involving failure of agreement, and potential disputes will relate only to the effect of the contractual provisions.

## H. *Multi-party settlement of disputes*

58. The construction of industrial works often involves the participation of a number of different entities, each under his own contract with the contractor or the purchaser. These may include, for example, contractors under separate works contracts with the purchaser, engineers, subcontractors and suppliers of equipment and materials. A problem arising in connection with the construction of the works may involve several of these entities. For example, one contractor may claim damages against the purchaser because the contractor was prevented from commencing construction on the date fixed for commencement in his contract with the purchaser. He may have been prevented from doing so due to a failure by another contractor engaged by the purchaser to complete a portion of the construction. The first contractor would have a claim against the purchaser and the purchaser would have a claim against the second contractor. It may be more efficient and satisfactory for the rights and obligations of all entities involved in a dispute or related disputes to be resolved in the same proceedings, with all of these entities participating, rather than in separate proceedings. In addition, the joinder of several contractors in a single proceeding would be advantageous to the purchaser when it is unclear which of the contractors is responsible for defects in the works. Proceedings involving more than two entities are referred to in this Guide as "multi-party proceedings". Multi-party proceedings would avoid inconsistent decisions being given due, for example, to the application of different procedural rules or different evaluations of the same evidence in separate proceedings. They could also facilitate the taking of evidence, and expedite and reduce the costs of the settlement of disputes.

59. Many States have laws which provide for and regulate multi-party proceedings in their courts. In some States entities may be compelled under certain circumstances to participate in multi-party judicial proceedings, and under other circumstances entities are permitted to intervene in proceedings between other entities, even without the prior agreement of the entities concerned. In other countries multi-party judicial proceedings are permitted only if the entities concerned agree to such proceedings. Where the law of the selected court where judicial proceedings are to be brought (see section E, "Judicial proceedings", above) permits multi-party judicial proceedings, entities who have agreed to the jurisdiction of the court may wish to include provisions in their contracts which enable those proceedings to be brought.

60. The conduct of multi-party arbitral proceedings is more difficult. The law of most States does not provide for or otherwise deal with such proceedings. The conduct of multi-party arbitral proceedings therefore depends entirely upon the agreement of the entities participating in the proceedings. Thus, an entity usually cannot be compelled to participate in proceedings involving other entities nor can an entity intervene in proceedings between other entities, without the agreement of those entities.

61. Notwithstanding the absence of a legal framework for the structuring of multi-party arbitral proceedings, the parties may wish to endeavour to provide for such proceedings by agreement.<sup>15</sup> The agreement to participate in multi-party arbitral proceedings may be expressed in ways similar to its reflection in agreements to participate in traditional two-party arbitral proceedings (see paragraph 13, above). The entities may enter into a multi-party arbitration agreement after a dispute arises, or they may do so when they enter into their contracts for or in connection with the construction of the works. In the latter case the agreement may be in the form of harmonized arbitration clauses in the different contracts, or a single separate arbitration agreement to which all entities become parties contemporaneously with entering into their contracts. For reasons noted in paragraph 13, above, it would be preferable for the agreement of the entities to participate in multi-party arbitral proceedings to be expressed when they enter into their contracts, rather than attempting to conclude a multi-party arbitration agreement after a dispute actually arises.

62. Much of the difficulty in providing for multi-party arbitral proceedings derives from the necessity, at a time when the nature and scope of possible disputes between them is not known, for the numerous participants in the construction of the works to agree to procedures that are consistent. To ensure this consistency, it may be preferable for all entities to become parties to a single separate arbitration agreement, rather than to attempt to provide for multi-party proceedings through arbitration clauses in individual contracts. The following are examples of issues which should be addressed in a multi-party arbitration clause or agreement.

63. The arbitration clauses or separate arbitration agreement should provide a mechanism whereby arbitral proceedings involving all entities concerned in a dispute or related disputes are conducted before the same arbitral tribunal. In some cases it may be possible for all envisaged participants in multi-party proceedings arising from the construction of the works to agree to the same arbitrator or arbitrators. However, it may be difficult to achieve such agreement on the part of the various participants at the time of entering into a separate arbitration agreement or a contract containing an arbitration clause. Therefore, it may be preferable for all of the entities in their arbitration clauses or in the separate

arbitration agreement to agree to the same appointing authority, and to authorize the appointing authority to decide upon the number of arbitrators to resolve a particular dispute and to appoint all arbitrators.

64. The arbitration clauses or separate arbitration agreement should define the scope of the multi-party proceedings, both as to the entities who may participate in particular proceedings as well as to what may be the subject-matter of the proceedings. With respect to the participants in the proceedings, the arbitration clauses or agreement should specify the criteria by which particular entities may be compelled, if at all, to participate in multi-party proceedings, and by which entities are entitled to intervene in proceedings between other entities. With respect to the subject-matter of multi-party proceedings, the arbitration clauses or agreement should specify the criteria by which related two-party proceedings may be consolidated into a single multi-party proceeding. They may also delimit the types of disputes which may be resolved in multi-party proceedings (see paragraph 27, above).

65. The parties should give careful consideration to the choice of rules which are to govern the multi-party arbitral proceedings (see paragraphs 15 to 18, above). Since existing established arbitration rules are designed to deal with two-party arbitral proceedings, the parties should examine the provisions of the rules to determine whether they are appropriate for multi-party proceedings, and should make necessary modifications to the rules, if possible.

66. Without a legal framework for multi-party proceedings or adequate models to follow, it may be difficult to structure a satisfactory arrangement for proceedings of that nature by agreement. If it is found not to be possible to do so, the parties may wish to attempt in other ways to reduce the possibility of inconsistencies in decisions in two-party arbitrations involving related disputes. They might, for example, require all relevant entities in their individual contracts to designate the same appointing authority for arbitral proceedings arising from those contracts. That authority would then be able to appoint the same arbitrators for related disputes. The entities might also provide in their individual contracts for co-operation among them by, for example, making evidence or information in the hands of one entity available to another entity when relevant to a dispute by the other entity with a third entity.

<sup>15</sup>This Guide does not attempt to deal in detail with the issues which might be addressed by the parties. It is only recently that attention has been devoted by practitioners and scholars to issues and problems in connection with multi-party arbitral proceedings. More analytical work in this field will have to be done before detailed recommendations of general applicability can be made in a guide such as this one. The establishment within national legal systems of a legal framework for multi-party arbitral proceedings, and the creation of a set of arbitration rules which take into account the particular features of multi-party proceedings (see paragraph 65, below), would greatly facilitate the creation by parties of arrangements for multi-party proceedings and the conduct of multi-party proceedings. For the present, bearing in mind the advantages of multi-party proceedings described above, and the advantages of arbitral over judicial proceedings, readers of this Guide are recommended to consider in the context of their own contracts possible solutions to issues such as those mentioned in this section.

## [A/CN.9/WG.V/WP.17/Add.7]

### Chapter II. Choice of contracting approach

#### Summary

A purchaser who intends to contract for the construction of industrial works has a choice between entering into a single contract with a single contractor who would be responsible for all performances needed for the

completion of the works, or dividing the performances needed among several entities (paragraph 1). Which technique he adopts may depend on several factors (e.g. whether the technology to be used in the works is the exclusive property of a single supplier, whether the purchaser has the capability to co-ordinate the performances of several entities, or whether mandatory legal regulations in the country of the purchaser require local enterprises to be engaged for certain aspects of the construction). Within these techniques, there are different possible approaches to contracting, and a particular terminology has been adopted in the Guide to describe these approaches (paragraphs 2 and 3).

The contractual approach whereby a single contractor is engaged to render all performances needed for the completion of the entire works is referred to as the "turnkey contract approach". The turnkey contractor is liable for any delay in construction or defects in the works (paragraph 4). Where offers are solicited from potential turnkey contractors, each offer will be based on an individual design, and the purchaser will be able to choose the design which is most responsive to his requirements, though in some cases comparison of the different designs may be difficult (paragraph 5). A turnkey contractor may sometimes be motivated more by a desire to offer an attractive price than by the need to ensure the durability, reliability and ease of maintenance of the works. On the other hand he usually has no incentive to over-design the works (paragraph 6).

In some cases a single contractor, in addition to assuming the obligations of a turnkey contractor, may undertake to ensure that after the works is completed, it can be operated and agreed production targets achieved by the purchaser's own staff, using raw materials and other inputs specified in the contract. This approach is referred to as the "product-in-hand contract approach" (paragraph 7).

Since a single contractor bears a high degree of risk in effecting all the performances needed for the completion of the works, and must incur costs to guard against this risk, the total cost of the works may be lower if several contractors are engaged than if a single contractor is engaged (paragraph 8).

If the purchaser engages more than one entity to effect the performances needed for the completion of the works, each entity will be responsible only for the performance of the obligations specified in his contract. If the works is defective, it may be difficult for the purchaser to discover which party is liable for the defects. The purchaser has a choice of several approaches when he contracts with several entities (paragraphs 9 and 10).

The purchaser may engage one contractor for the transfer of the technology, the supply of the design and the construction of a vital portion of the works, and also obligate this contractor to define the scope and quality of the construction to be effected by the other entities. This approach is referred to as the "semi-turnkey contract approach". The semi-turnkey contractor may be respon-

sible for handing over to the contractor at an agreed time complete works which is capable of operation as required by the contract, unless he is prevented from doing so by the failure of performance of another entity (paragraphs 11 and 12).

Another approach is to engage one or more entities other than the contractor to transfer the technology and supply the design of the works, and to conclude a works contract with a single contractor for the construction of the entire works in accordance with the design. This approach is referred to as the "comprehensive contract approach". The contractor must co-ordinate the construction process in the same way as a turnkey contractor, but is not liable for defects in the technology or design (paragraph 13).

A further approach available to the purchaser is to divide the construction of the works among two or more separate contractors, the transfer of technology and the supply of the design being also effected by one or more of these contractors, or by other entities. This approach is referred to as the "separate contracts approach". Under this approach the purchaser must co-ordinate the scope and the time of the performances under each separate contract so as to achieve his construction targets (paragraphs 14 and 15). The way in which the construction is to be apportioned among the various contractors will depend upon the nature and size of the works (paragraph 16).

The risks borne by the purchaser in connection with the co-ordination of the separate contracts would be considerably reduced by employing a consulting engineer to advise the purchaser on how to achieve a proper co-ordination. Alternatively, the purchaser may engage a construction manager with a wider scope of responsibility. Another technique is to have one of the separate contractors assume responsibility for some part of the co-ordination (paragraphs 17 and 18).

The separate contracts approach will facilitate the use by a purchaser of local contractors to construct portions of the works. This approach may also enable the purchaser to retain a certain degree of control over the construction (paragraph 19).

As an alternative to settling upon the entire design before the contractors are engaged, the purchaser may wish to consider the use of a method sometimes referred to as "fast track" contracting (paragraph 20).

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#### **A. General remarks**

1. A purchaser who intends to contract for the construction of industrial works has a choice between entering into a single contract with a single contractor, who would be responsible for all performances needed for the

completion of the works, e.g. the transfer of the technology to be used in the works, the supply of the design, and the construction of the works (see section B, "Engagement of single contractor", below), or dividing the performances needed among several entities, concluding an individual contract with each entity (see section C, "Engagement of more than one entity", below). Within these techniques there are different possible approaches to contracting, as discussed below. These approaches differ in important respects, for example, as to the extent of the responsibility of the contractor, the extent to which the purchaser must co-ordinate construction, and in many cases the total cost to the purchaser.

2. Whether the purchaser contracts with a single contractor or several entities for the construction of the works may depend upon the nature of the technology to be used in the works. Where the technology is highly specialized or is the exclusive property of a single supplier, the entire works may have to be designed and constructed by the supplier of the technology. In other cases it may be possible for the purchaser to enter into separate contracts for, e.g., the transfer of the technology, the supply of the design, and the construction. Other factors may be relevant to the choice of a contracting approach. For example, if several entities are engaged for the construction, the burden of co-ordinating the performances of the various entities rests on the purchaser, and he must have appropriate capabilities (see paragraph 15, below). Mandatory legal regulations in the country of the purchaser may require that local enterprises be engaged for certain aspects of the construction (e.g. civil engineering) in order to develop the technological capability of the country and to conserve foreign exchange. The extent of the contractor's liability to taxation may influence the contracting approach to be chosen by the parties. The parties may wish to obtain expert advice on the issue of taxation.

3. At present there is no uniformly accepted terminology to describe the various contractual approaches to the construction of works. However, in order to facilitate the discussion in the Guide of issues arising in connection with the different contracting approaches, a particular terminology has been adopted in this chapter. The terminology adopted reflects the terminology often used in practice.

## **B. Engagement of single contractor**

### *1. Turnkey contract approach*

4. The contractual approach whereby a single contractor is engaged to render all performances needed for the completion of the entire works, i.e. the transfer of the technology, the supply of the design, the supply of equipment and materials, the erection of the equipment and the performance of the other construction obligations (such as civil engineering and building) is referred to in the Guide as the "turnkey contract approach". Under this

approach the single contractor must co-ordinate the construction process, and is liable for any delay in construction or defects in the works.

5. Where the purchaser chooses the turnkey contract approach, and decides to solicit competitive offers from potential contractors (see chapter III, "Procedure for concluding contract"), each offer made by a potential turnkey contractor will be based on his individual design. The purchaser will thus be able to choose the design which is most responsive to his requirements. In addition, since the turnkey contractor is himself to manufacture equipment and effect construction pursuant to the design supplied by him, the design may reflect manufacturing and construction economies and techniques available to the contractor, and thus result in construction which is economical and efficient. On the other hand, it may sometimes be difficult for the purchaser to evaluate and compare the different designs and different combinations of construction elements and methods contained in offers by different potential turnkey contractors.

6. In taking his decisions on design, construction methods and selection of sub-contractors, a turnkey contractor having responsibility for all aspects of the construction may sometimes be motivated more by a desire to offer an attractive price than by the need to ensure the durability, reliability and ease of maintenance of the works. On the other hand, a turnkey contractor usually has no incentive to over-design the works (i.e. to include in the design unnecessary features and technical safeguards to ensure that the works perform as required by the contract). Over-designing would make a turnkey contractor's offer uncompetitive. If the design is supplied by a separate designer, there may exist some incentive to over-design.

### *2. Product-in-hand contract approach*

7. In some cases a single contractor, in addition to assuming the obligations mentioned in paragraph 4, above, may undertake to ensure that after the works is completed, it can be operated and agreed production targets achieved by the purchaser's own staff, using raw materials and other inputs specified in the contract. This approach is referred to in the Guide as the "product-in-hand contract approach". It may be used by the purchaser as a means of making the contractor responsible, not only for the completion of the entire works, but also for an effective transfer to the purchaser's personnel of the technical and managerial skills and knowledge required by the purchaser's personnel for the successful operation of the works. In contrast to the case where the contractor merely undertakes to train the purchaser's personnel in the operation of the works (see chapter VI, "Transfer of technology"), this approach requires the contractor to ensure that his training is successful. The contract should specify the results which the contractor is obligated to achieve through his training. The contract may provide that the training must enable the purchaser's personnel

during the agreed test period to operate the works under the guidance of the contractor's managerial personnel. However, the contractor's responsibility would be greater if the contract provided that the training must enable the purchaser's personnel to operate and manage the works independently. This contracting approach should be distinguished from cases where the contractor undertakes in the contract to assist with his own personnel in the operation of the works after its completion (see chapter XXVI, "Supplies of spare parts and services after construction").

### 3. Risk and price

8. A single contractor bears a high degree of risk in effecting all the performances needed for the completion of the works. He may insure against this risk, or provide some financial reserves to cover the risk. The cost of adopting these measures is usually reflected in the calculation of the price. If, therefore, the purchaser has the capability effectively to co-ordinate the construction process, the total cost of the works may be lower if several contractors are engaged than if a single contractor is engaged. Since under the product-in-hand contract approach the contractor not only assumes extensive training obligations but also bears the risk of failing to reach the agreed training results, the price charged by him under that approach is likely to be higher than under the turnkey contract approach.

### C. Engagement of more than one entity

9. An alternative to engaging a single contractor is to divide all the performances needed for the completion of the works among two or more entities. The purchaser may engage one or more entities other than the contractor to transfer the technology and to supply the design for the entire works and one or more contractors to construct the works. In contrast to the case where a single contractor is engaged, none of the entities will be totally responsible for the appropriate operation of the works; each entity will be responsible only for the performance of the obligations specified in its contract. If the works is defective it may be difficult for the purchaser to discover which party is liable for the defects.

10. The purchaser has a choice of several contracting approaches when he contracts with several entities for the completion of the works. The approach chosen will affect the extent of the risk to be borne by him.

#### 1. Semi-turnkey contract approach

11. In some cases the purchaser may reduce the risks connected with engaging more than one entity (see paragraph 15, below) by engaging one contractor for the

transfer of the technology, the supply of the design for the entire works and the construction of a vital portion of the works. This contractor may be obligated to provide to the purchaser at the time of the conclusion of the contract or within a specified period of time thereafter specifications defining the scope and quality of the construction to be effected by other entities under individual contracts with the purchaser, and the time-schedule for the construction by the other entities. This approach is referred to in the Guide as the "semi-turnkey contract approach".

12. The semi-turnkey contractor may be responsible under the contract for handing over to the purchaser at an agreed time completed works which are capable of operation as required by the contract, unless he is prevented from doing so by the failure of another entity to perform his construction obligations in accordance with the design, specifications or time-schedule provided by the semi-turnkey contractor to the purchaser. An advantage of the semi-turnkey contract approach for the purchaser is that the responsibility for the transfer of the technology, the supply of the design and the construction of a vital portion of the works is concentrated in one contractor.

#### 2. Comprehensive contract approach

13. Another approach available to the purchaser is to engage one or more entities other than the contractor to transfer the technology and supply the design for the works, and to conclude a works contract with a single contractor for the construction of the entire works in accordance with the design. The design is usually obtained by the purchaser before the tendering procedure or negotiations in respect of the works contract commence, in order that offers to construct may be solicited on the basis of the design. This contracting approach is referred to in the Guide as the "comprehensive contract approach". Since the contractor under this approach is responsible for the construction of the entire works, he must co-ordinate the construction process in the same way as a turnkey contractor. He will not, however, be liable for defects in the technology or design. Under this approach the purchaser does not have a choice among several designs. On the other hand he can more easily compare the offers to contract of the various potential contractors (see paragraph 5, above).

#### 3. Separate contracts approach

14. A further approach available to the purchaser is to divide the construction of the works among two or more separate contractors. The transfer of technology and the supply of the design may also be effected by one or more of these contractors, or may be effected by other entities. This approach is referred to in the Guide as the "separate contracts approach".

15. Under the separate contracts approach the purchaser must co-ordinate the scope and the time of the performances under each separate contract so as to

achieve his construction targets. The purchaser will bear the risk of delay in construction or defects in the works resulting from his failure to determine appropriately in each contract the equipment, materials and construction services to be supplied by each separate contractor, and the time-schedules to be observed by them. Moreover, if a failure to perform by one contractor has repercussions on the work of the others, the purchaser may be liable to compensate the others for losses suffered by them, provided that they have performed or were ready to perform their contractual obligations. In respect of such compensation paid by him, the purchaser may be entitled to liquidated damages or penalties or to indemnification from the contractor who is liable for the failure. However, the possibility of recourse by the purchaser against the contractor who failed to perform to recover the compensation paid by the purchaser to another contractor may be limited by the contract or the applicable law. As a result, the purchaser may have to bear some portion of the loss caused to him by the contractor who failed to perform.

16. Under the separate contracts approach, the supply and erection of equipment and the supply of materials in respect of a portion of or the entire works is often effected under one contract, and building and civil engineering under another one. The erection of equipment may in some cases be effected by the purchaser's personnel or by a local enterprise under the supervision of the contractor (see chapter IX, "Construction on site"). However, the way in which the construction is to be apportioned among the various contractors will depend upon the nature and the size of the works. In general, the less complex is the works, the fewer the number of contractors required, and the easier it will be for the purchaser to co-ordinate the scope and the time of the performances under the separate contracts. The risks connected with co-ordination increase when a large number of parties participate in the construction.

17. The risks borne by the purchaser in connection with the co-ordination of the scope and the time of the performances of separate contracts would be considerably reduced by employing a consulting engineer (see chapter X, "Consulting engineer") to advise the purchaser as to how to achieve a proper co-ordination. Alternatively, the purchaser may engage a construction manager (sometimes called managing contractor) with a wider scope of responsibility. The construction manager may be the designer of the works, or an expert with management capabilities. The responsibility of the construction manager need not be limited to giving advice, but may include integrated construction management (e.g. inviting tenders or negotiating and concluding separate contracts for the various portions of the works for and on behalf of the purchaser, co-ordinating all site activities and control of the construction process). If the construction manager is not the designer, he may be obligated to check the design and to assume responsibility for design defects which he could reasonably have discovered. He may also be obligated to advise the purchaser on the selection of contractors. The fee paid for the services of a construction

manager is usually higher than the fee of a consulting engineer because of the wider scope of the construction manager's responsibility. The parties may agree that the fee is to be reduced according to a specified formula if the works is completed late or if the cost of the construction is higher than a target cost, and increased if the works is completed early or the cost is less than the target cost (see chapter VII, "Price").

18. Another technique which the purchaser might wish to adopt in order to reduce his risks in co-ordination is to have one of the separate contractors assume responsibility for some part of the co-ordination. This contractor may, for example, be obligated to define the scope of the work to be effected by other contractors engaged by the purchaser, and to provide a time-schedule for that work. He may also be obligated to check the construction effected by the other contractors and to notify the purchaser of defects in the construction which he could reasonably have discovered.

19. In addition to making possible the obtaining of a lower price (see paragraph 8, above), the separate contracts approach will facilitate the use by purchasers from developing countries of local contractors to construct portions of the works, perhaps under the supervision of an experienced foreign contractor. This may save foreign exchange and facilitate the transfer of technical and managerial skills to enterprises in the purchaser's country. It may also enable the purchaser to retain a certain degree of control over the construction and the entities involved in it.

#### 4. "Fast track" contracting

20. As an alternative to settling upon the entire design before the contractors are engaged (as for example, under the comprehensive contract approach), the purchaser may wish to consider the use of a method sometimes referred to as "fast track" contracting. Under this approach the design is separately prepared for the various phases of the construction. After the design for a particular phase of the construction has been prepared, the purchaser invites contractors to tender or to enter into negotiations on the basis of this design. A design for the following phase is then prepared followed again by invitations to tender or negotiations. This method may reduce the total period of time needed for the completion of the construction. It may be used even if a single contractor is to complete the entire works. In such a case, several separate contracts, each for the completion of an individual phase, would be concluded with him. The "fast-track" method requires the purchaser to have the project carefully planned before commencing to conclude contracts. In addition, the purchaser may have difficulty in co-ordinating the construction through its several phases. The purchaser will have to make very rapid design decisions; and a high degree of co-operation between the designer and the contractor will be needed.



[A/CN.9/WG.V/WP.17/Add.8]

## Chapter VI. Transfer of technology

### *Summary*

The purchaser will require a knowledge of the technological processes necessary for production by the works, and require the technical information and skills necessary for its operation and maintenance. The communication to the purchaser of this knowledge, information and skills is often referred to as the transfer of technology (paragraph 1).

Differing contractual arrangements can be adopted for the transfer of technology and the performance of the other obligations necessary to construct the works (paragraph 2). The transfer of technology itself may occur in different ways. It may occur, for example, through the licensing of industrial property (paragraph 3) or the communication of confidential know-how (paragraph 4). The information and skills necessary for the operation and maintenance of the works may be communicated through documents, or through the training of the purchaser's personnel (paragraph 5).

This Guide does not attempt to deal comprehensively with the licensing of industrial property or the communication of know-how, and the present chapter merely notes certain issues which the parties should address when a works contract involves industrial property or know-how (paragraph 6). In drafting contract provisions relating to the transfer of technology, the parties should take account of mandatory legislation regulating such transfer which may be in force in the purchaser's and contractor's countries (paragraph 7).

Some issues which the parties should address are common both to licensing and know-how provisions, e.g. the description of the technology transferred, and conditions restricting the purchaser in the use of that technology. The extent to which the technology should be described may depend on the contractual arrangements which are adopted (paragraph 8). When deciding whether restrictions are to be imposed on the purchaser's use of the technology, the parties should take into account mandatory legislation which may regulate such restrictions and should attempt to negotiate provisions which are balanced and which impose only restrictions necessary to protect the legitimate interests of each party (paragraph 9). These considerations should apply, for example, to the following types of provisions which the contractor might seek to include: that the purchaser is obligated to purchase from him, or from sources designated by him, some of the materials needed for production by the works (paragraph 10); that the purchaser is prevented from adapting the technology or from introducing innovations to it (paragraph 11); that the purchaser is obligated to communicate to the contractor any improvements to the technology made by the purchaser in the course of using it (paragraph 12); that the purchaser is restricted from exporting products manufactured by the use of the technology to specified countries (paragraph 13).

The guarantees to be given by the contractor may depend on the contractual arrangements adopted, and may range from an unqualified guarantee that the works will operate in accordance with specified parameters, to a qualified guarantee that the works will operate in accordance with specified parameters provided certain conditions are satisfied (paragraphs 14 and 15).

The parties may wish to include in the contract an undertaking by the contractor that the use of the technology transferred will not result in claims by a third party whose industrial property rights may be infringed by the use (paragraph 16). They may wish to specify the procedure to be followed by them in the event of a claim by a third party that his industrial property rights have been infringed, and to determine their rights and obligations during the pendency of the legal proceedings, and in the event that the claim succeeds (paragraph 17).

An issue special to know-how provisions is confidentiality. The contractor will wish to obligate the purchaser to maintain confidentiality in respect of the know-how communicated. The extent to which confidentiality is imposed should be clearly defined in the contract. Furthermore, the contract should provide for situations in which the purchaser may reasonably need to disclose the know-how to third parties (paragraphs 18 and 19).

When technical information and skills are conveyed through documents, the contract may address several issues in regard to the documents. Such issues include the description of the documents to be supplied, demonstrations needed to explain the documents, and the times at which the documents are to be supplied (paragraphs 20 to 22).

A significant method of conveying technical information and skills is by the training of the personnel of the purchaser. The contractor should be obligated to supply the purchaser with an organizational chart showing the personnel requirements for the operation and maintenance of the works. This will aid the purchaser to determine his training requirements (paragraph 23). Issues to be dealt with in the contract may include the categories and numbers of trainees, their qualifications, the procedure for selecting the trainees, and the places at which they are to receive training (paragraphs 24 and 25).

The training obligations of the contractor should be clearly defined. The contractor may be obligated to supply to the purchaser a training programme which will permit the works to be operated by the purchaser's personnel. The programme may include a time-schedule for training, and describe the nature of the training to be given. The contractor should be obligated to engage trainers with qualifications and experience appropriate for the training (paragraphs 26 and 27). The contract should also fix the payment conditions relating to the training. However, for practical reasons, some issues relating to the training programme may need to be settled after the conclusion of the contract (paragraphs 28 and 29).

### A. General remarks

1. The works to be constructed will embody various technological processes necessary for production by the works. The purchaser will require a knowledge of the use and application of these various processes. The purchaser will also wish to acquire the technical information and skills necessary for the operation and maintenance of the works. The communication to the purchaser of this knowledge, information and skills is often referred to as the transfer of technology.

2. It may be noted that differing contractual arrangements can be adopted for the supply of technology and the performance of the other obligations necessary to construct the works (see chapter II, "Choice of contracting approach"). The purchaser may select a contractor who is able to supply the technology to be embodied in the works, as well as to construct the works or that portion of the works which embodies the technology. The purchaser may also enter into one contract for the supply of the technology, and into separate works contracts for the construction of the works embodying that technology.

3. The transfer of technology may occur in different ways. It may occur through the grant of licences to use products or processes which are the subject of patents or other forms of industrial property. Most legal systems provide for the registration, subject to certain conditions, of industrial products or processes which are thereby recognized and protected as industrial property within the territory of the country in which the registration takes place. The owner of the industrial property obtains the exclusive right to exploit the products or processes which are the subject of the industrial property. A common form of industrial property consists of patents. Under the legal systems of many countries, a person who invents a product or process can apply to the government for the grant to him of a patent protecting the invention. Once a patent is granted, for a limited period determined by the legal system the invention which is the subject-matter of the patent can be exploited (e.g. manufactured, used, sold) only with the consent of the patent holder. Most legal systems also recognize other forms of industrial property. For example, a distinctive sign used to identify goods and indicate their origin (e.g. as coming from a particular manufacturer) may be protected through registration as a trade mark. A protected trade mark cannot be used without the consent of the registered owner of the trade mark. A patent holder or the owner of a trade mark may license the patent or trade mark to the purchaser (i.e. permit the purchaser, subject to the conditions of the licence, to use the subject-matter of the patent, or the trade mark, in return for remuneration).

4. Certain industrial processes may be known only to one or a few entities. These entities may not have wished, or may have been unable, to protect the industrial processes through registration in accordance with the law relating to industrial property. They may, instead, keep this knowledge confidential. In such cases the transfer of technology may occur through the communication of this

knowledge (generally called know-how) to the purchaser.<sup>1</sup> Such communication is usually subject to conditions as to the maintenance of confidentiality by the purchaser (see paragraphs 18 and 19, below).

5. The information and skills necessary for the operation and maintenance of the works may be communicated by the contractor through documents, e.g. operating manuals (see paragraphs 21 and 22, below). They may also be communicated through the training of the personnel of the purchaser (see paragraphs 23 to 29, below). It may be noted that the different ways in which technology is transferred referred to in this and the previous paragraphs may be combined.

6. This Guide does not attempt to deal comprehensively with contract negotiation and drafting relating to the licensing of industrial property, or the communication of know-how, as this subject has already been dealt with in detail in publications issued by certain United Nations bodies.<sup>2</sup> The present chapter merely notes certain major issues which the parties may wish to address when a works contract contains provisions relating to the licensing of industrial property or the communication of know-how. Issues relating to the pricing of technology are dealt with in chapter VII, "Price".

7. In drafting their contract provisions relating to the transfer of technology, the parties should take account of mandatory legislation regulating such transfers which may be in force in the purchaser's and the contractor's countries.<sup>3</sup> The transfer may be regulated directly (i.e. through laws specifically directed at contracts involving the transfer of technology). Among those laws are legal regulations prohibiting or restricting the transfer of certain kinds of advanced technology. Contracts violating the prohibitions or restrictions may be void or unenforceable. Under some legal regulations contracts involving the transfer of technology require the approval of a governmental institution prior to their entry into force. Such an institution may have the power to require the deletion or modification of terms which are contrary to the national policy on technology transfer. Contracts or

<sup>1</sup>In some countries the term licensing is used to describe both the transfer of industrial property rights and the communication of know-how. In this chapter the term is used only with the first of these meanings.

<sup>2</sup>The drafting of agreements for the licensing of industrial property and the communication of know-how is dealt with in detail in World Intellectual Property Organization, *Licensing Guide for Developing Countries* (publication No. 620(E), hereinafter referred to as the *WIPO Guide*). The main issues to be considered in drafting such contracts are set forth in *Guidelines for Evaluation of Transfer of Technology Agreements*, Development and Transfer of Technology Series No. 12(ID/233), hereinafter referred to as the *UNIDO Guidelines* and in *Guide for Use in Drawing up Contracts Relating to the International Transfer of Know-how in the Engineering Industry* (United Nations publication, Sales No. 70.II.E.15). Another relevant publication is the *Handbook on the Acquisition of Technology by Developing Countries* (United Nations publication, Sales No. 78.II.D.15).

<sup>3</sup>See *WIPO Guide*, section U, "Approval of government authorities", and section O, 7, "Taxation". The legal regulations of several countries relating to the transfer of technology are contained in "Compilation of legal material dealing with transfer and development of technology" (TD/B/C.6/81), 1982.

contractual provisions which are not approved may be void or unenforceable. Furthermore, legal regulations often exist which make void or unenforceable contractual provisions in transfer of technology transactions which restrain competition between entities, or which hinder the technological development of a country (see paragraph 9, below). Legal regulations may also govern the pricing of technology. They may, for example, require each element of the technology transfer to be separately priced, or regulate the extent of the price payable, or the manner of payment (e.g. the manner in which royalties are to be calculated). Indirect regulation of transfer of technology may occur when export or import licences are not granted in respect of equipment which embodies certain kinds of technology, or when authority to make payment for technology is refused under exchange control regulations. Tax legislation may also affect the drafting of the contract (e.g. by requiring the parties to determine which party is responsible for the payment of tax on income arising from the transfer of technology).

## **B. Issues common both to licensing and to know-how provisions**

### 1. *Description of technology*<sup>4</sup>

8. In some cases a precise and comprehensive description of the technology is important, for example, when the purchaser enters into separate contracts with different entities for the supply of the technology and for the performance of the other obligations necessary to construct the works (e.g. supply of the design of the works, the supply of equipment and materials needed to enable the technology to be used in the works). Even if the turnkey contract approach is used, and a single contractor is to perform all the obligations necessary to construct the works, a precise and comprehensive description of the technology to be transferred may be needed to identify a particular technology which the contractor has agreed to supply. In some cases, however, the obligations of a turnkey contractor may be primarily defined in terms of constructing works which produce goods of a quantity and quality stipulated in the contract, and in those cases a general description of the technology to be supplied may be sufficient.

### 2. *Conditions restricting purchaser in use of technology*

9. The contractor may sometimes be prepared to transfer technology only if the purchaser accepts certain restrictions on the purchaser's use of the technology, or on his disposal of the products obtained by using the technology. Some of these restrictions are regulated by mandatory national legislation in many countries (e.g. declared void or unenforceable) not only because they create possible hardship to the purchaser, but also because they may conflict with public policy (for exam-

ple, the restrictions may restrain competition, or hinder the development of national technological capabilities). Some legislation at a regional level also exists regulating these restrictions on the basis of the public policy existing within the region.<sup>5</sup> Attempts are also being made at the global level to formulate norms which would be applicable to these restrictions where they are included in international transfer of technology transactions.<sup>6</sup> For these reasons, this chapter does not attempt to make normative recommendations as to the formulation of these restrictions, but merely describes a few restrictions of special importance in the context of works contracts, and the interests of the parties in regard to those restrictions. The parties should attempt to negotiate provisions which are balanced and which impose only those restrictions necessary to protect the legitimate interests of each party.

10. The contractor might seek to include a provision that the purchaser is obligated to purchase from him, or from sources designated by him, some or all of the materials needed by the works for production. The contractor might seek to include such a provision when, for example, the goods produced by the works can be associated with him by third parties (e.g. if they bear his trade mark), and the quality of the goods depends on the quality of the materials which he wishes to supply. He may also wish to prevent any lowering of the quality of the goods if the goods are to be bought by him, or to be supplied to his customers. Such a provision may, however, be disadvantageous to the purchaser (e.g. he may be able to obtain materials of the same quality as those which the contractor wishes to supply from other sources on more advantageous terms). These competing interests should be weighed in considering the inclusion of a provision on this issue.

11. The contractor might seek to include a provision that the purchaser is prevented from adapting the technology, or from introducing innovations to it. He might seek to include such a provision because he fears that adaptations or innovations by the purchaser may lower the quality of the products obtained by using the technology, and that such a lowering of quality may adversely affect him (see previous paragraph). The purchaser, however, might seek to adapt the technology to suit local conditions, or to introduce innovations which lower the cost of production, even if the adaptations or innovations lead to a slight loss of quality in the products. This loss of quality may not be significant in relation to the purchaser's requirements. Any provision on this issue should reconcile these interests of the parties in a reasonable manner.

<sup>5</sup>Articles 85, 86 and 87 of the Treaty establishing the European Economic Community, Rome, 25 March 1957 (United Nations, *Treaty Series*, No. 298, page 11) in relation to the countries of the European Economic Community.

<sup>6</sup>These norms are being negotiated at the sessions of the United Nations Conference on an International Code of Conduct on the Transfer of Technology. The latest (sixth) session of the Conference was held at Geneva from 13 to 31 May 1985, but ended without completing its work. The future course of the Conference will be decided by the General Assembly at its fortieth session.

<sup>4</sup>See *WIPO Guide*, section D, 1, "Identification and description of the basic technology".

12. The contractor might seek to include a provision that the purchaser is obligated to communicate to the contractor any improvements to the technology made by the purchaser in the course of using it. Such a provision could have certain disadvantages to the purchaser. It could prevent the purchaser from competing with the contractor in the field of technology in question, since the level of technological knowledge of the contractor will be maintained at a level not less than that of the purchaser. If, in addition to being obligated to communicate the improvements to the contractor, the purchaser is also obligated not to disclose them to third parties, the purchaser may be prevented from realizing their full commercial value. If the improvements are to be communicated without remuneration therefor being paid by the contractor, the contractor could benefit at the purchaser's expense. Since each party to a transfer of technology usually has an interest in obtaining improvements to that technology made by the other party, it may be advantageous to both parties that they negotiate a balanced provision for the communication of improvements.

13. The contractor might seek to include a provision restricting the purchaser from exporting products manufactured by the use of the technology to specified countries. He may previously have communicated confidential know-how to entities in those countries, and given undertakings to them that in the further communication of the know-how to others he would ensure that those others would not compete in the specified countries. Or, while not holding industrial property rights in the specified countries, he may have licensed his rights in other countries to entities in those countries who are exporting to the specified countries, and who are concerned that their markets in those countries should be protected. The purchaser may himself be interested in principle in export restrictions, since he might wish the contractor to restrict others from exporting to his own country competing products manufactured by using the same technology. On the other hand, the purchaser might seek to have export possibilities after the market capacity in his own country is exhausted. Mandatory legal rules relating to restrictive business practices and to the transfer of technology are of special relevance in the field of export restrictions, and the parties should agree upon an equitable provision, taking those rules into account.

### 3. *Guarantees*<sup>7</sup>

14. The guarantees to be given in regard to the performance of the technology supplied may depend on the nature of the contractual arrangements entered into by the parties. If the turnkey contract approach is adopted

<sup>7</sup>See *WIPO Guide*, section G, 4, "Guarantee of know-how", and *UNIDO Guidelines*, chapter III, "Performance of know-how - licensor's guarantee obligations". Issues relating to defects covered by a guarantee, the guarantee period, the effect on guarantees of termination for failure of performance by a contractor followed by the employment of a new contractor to complete the work (see paragraph 19, below), and a manufacturer's guarantee are dealt with in chapter XVIII, "Delays, defects and other failures to perform".

and the contractor, in addition to supplying the technology, is also to perform all the other obligations necessary to construct the works, he may be required to guarantee that the works will operate in accordance with specified parameters. The type of parameters used (e.g. product quality, production capacity, utilities consumption, catalyst consumption, or quantity of effluent) will depend on the nature of the works.<sup>8</sup> No separate guarantee concerning the technology may be necessary, as the guarantees concerning the quality and performance of the works would also cover the technology.

15. In some cases, however, the purchaser may enter into separate contracts with different entities for the supply of the technology and for the performance of the other obligations needed for the construction of the works. In such cases the supplier of technology may be unwilling to give an unqualified guarantee of performance similar to that noted in the previous paragraph. He may in such cases be required to give a guarantee that the use of the technology will result in the operation of the works in accordance with certain specified parameters, provided the technology is utilized and the works is constructed in accordance with conditions specified by him (e.g. use of certain construction methods, standards, components and raw materials; use of a certain design for layout of the works; provision of certain operating conditions, such as the temperature in certain areas of the works).

### 4. *Claims by third party*<sup>9</sup>

16. The parties might seek to include in their contract an undertaking by the contractor that the use of the technology transferred will not result in claims against the transferee by a third party whose industrial property rights may be infringed by the use. Infringement may occur through the use of the process transferred, or through the distribution of products manufactured by using the process. The parties may also wish to include an undertaking by the purchaser that, where the contractor has to manufacture machinery or equipment in accordance with designs supplied by the purchaser, such manufacture will not infringe the industrial property rights of a third party. Because of the difficulty of conducting a world-wide investigation as to whether third parties may have industrial property rights in the technology transferred, a supplier will normally undertake only that the use of the technology transferred will not infringe the rights of third parties in specified countries.

17. The parties might seek to specify the procedure to be followed by them in the event of a claim by a third party that his industrial property rights have been infringed, and that the industrial property rights held by the parties are invalid. Each party may be obligated to notify the other of any claim immediately after he learns of the claim. If legal proceedings are brought against the

<sup>8</sup>See chapter V, "Description of works".

<sup>9</sup>See *WIPO Guide*, section E, "Special aspects concerning patents", and section S, 2, d, "Warranty against third parties for infringement".

transferee of the technology, the supplier should be obligated to assist him in his defence by, for example, bearing the costs incurred in the defence, giving legal advice, or producing evidence as to the validity of the industrial property rights of the supplier. The parties might seek to determine their rights and obligations during the pendency of the legal proceedings, and in the event that the claim succeeds. The parties may provide, for example, for the suspension of royalty payments by the purchaser during the proceedings. They may further provide, for example, that if the claim succeeds, royalty payments are to cease, that royalties already paid are to be reimbursed, or that modified technology which does not infringe the rights of the third party but which does not adversely affect the capability of the works to operate in accordance with the contract is to be supplied.<sup>10</sup>

### C. *Issue special to know-how provisions: confidentiality*<sup>11</sup>

18. The contractor will usually require the know-how disclosed by him to be kept confidential (see paragraph 4, above). He may require such confidentiality at two stages. Firstly, he may disclose some know-how to the purchaser during negotiations in order to enable the purchaser to decide whether he wishes to enter into a contract, and to make proposals as to contract terms. He will wish the purchaser to keep this know-how confidential. Secondly, if a contract is concluded, the contractor will require the additional know-how disclosed thereafter to be kept confidential. To achieve these results, it may be necessary under some legal systems for the parties, prior to the commencement of negotiations, to conclude an agreement under which the purchaser undertakes to maintain confidentiality with regard to know-how disclosed during negotiations, and thereafter to include provisions on confidentiality in the works contract if the negotiations lead to the conclusion of a contract. Other legal systems, however, contain obligations as to the observance of good faith during negotiations which may make the conclusion of an agreement prior to negotiations unnecessary.

19. The extent to which obligations as to confidentiality can be imposed on the purchaser may be regulated by mandatory legal rules in the purchaser's country. Issues to be addressed by such contractual provisions on confidentiality may include clear identification of the know-how to be kept confidential, the duration of the confidentiality (e.g. a fixed period) and the extent of permissible disclosure (e.g. disclosure being permissible in specified

circumstances, or to specified persons). The parties might seek to provide that once the know-how to be kept confidential reaches the public domain, the obligation of confidentiality terminates, as does the obligation to pay royalties. The parties may also wish to provide, for example, that an engineer employed by the purchaser to supervise the construction should be allowed access to such of the know-how as is necessary for him to exercise effective supervision. They may further wish to provide that if the contract is terminated by the purchaser because of a failure of performance by the contractor, or because the contractor is prevented by an exempting impediment from completing the construction (e.g. regulations in the contractor's country prevent him from exporting certain equipment), and the purchaser wishes to complete the construction by engaging another contractor, the purchaser may disclose to the other contractor such part of the know-how as is necessary for completion of construction by the other contractor. The purchaser may, however, be obligated to obtain from the other contractor prior to the disclosure of the know-how to him an undertaking that the latter will not disclose the know-how to others.

### D. *Communication of technical information and skills*

20. The purchaser will usually wish to be provided by the contractor with the technical information and skills necessary for the proper operation and maintenance of the works. Such information and skills are normally conveyed through the supply of technical documentation and through the training of personnel.

#### 1. *Supply of documentation*

21. The documentation to be supplied may consist of plans, drawings, formulae, manuals of operation and maintenance, and safety instructions. It may be advisable to list in the contract the documents to be supplied. The contractor may be obligated to supply documents which are comprehensive and clearly drafted, and which are in a specified language. It may be advisable to obligate the contractor, at the request of the purchaser, to give demonstrations of procedures described in the documentation if the procedures cannot be understood without demonstrations.

22. The points of time at which the documentation is to be supplied may be specified. The supply of all documentation should usually be completed by the time fixed in the contract for completion of construction, and the parties might seek to provide that construction is not to be considered as completed unless all documentation relating to the operation of the works has been supplied. It may be advisable to provide that some documentation (e.g. operating manuals) is to be supplied during the course of construction, as such documentation may enable the purchaser's personnel or engineer to obtain an understanding of the working of machinery or equipment while it is being erected. It may also be advisable to

<sup>10</sup>The possible rights and obligations of the parties are discussed in *WIPO Guide*, section E, "Special aspects concerning patents", paras. 202-205.

<sup>11</sup>See *WIPO Guide*, section G, 2, "Legal means for preventing communication, disclosure or use of valuable information and expertise". In addition to confidentiality in respect of know-how, the contractor may require confidentiality in respect of documents describing the scope and quality of the works. This is dealt with in chapter V, "Description of works".

provide that the contractor is liable to pay damages for loss caused to the purchaser through any errors or omissions in the documentation.

## 2. *Training of personnel*

23. In order to enable him to decide on his training requirements, in the invitation to tender or during the contract negotiations the purchaser might request the contractor to supply him with an organizational chart showing the personnel requirements for the operation and maintenance of the works, including the basic technical and other qualifications which the personnel must possess (see also chapter XXVI, "Supplies of spare parts and services after construction"). This statement of requirements should be sufficiently detailed to enable the purchaser to determine the extent of training required in the light of the personnel available to him. The contractor will often have the capability to provide the training. In some cases, however, the training may be given more effectively by a consulting engineer, or through an institution specializing in training.

24. It would be advisable for the contract to fix the categories of employees in respect of which training is to be given (e.g. chief mechanical engineer, electrical engineer), and the numbers to be trained. It would also be advisable to fix the qualifications which trainees for a particular post must possess (e.g. educational background, linguistic abilities, technical skills, work experience). If these qualifications are not agreed in the contract, the contractor may have grounds for attributing the failure of the training to lack of relevant qualifications. The parties may also wish to provide that the selection of trainees is to be done jointly by the parties. Despite these procedures, the contractor may find during training that it is not feasible to train a particular trainee. The contractor may in those cases be obligated to inform the purchaser of, and provide supporting evidence for, his finding as soon as he makes it. The parties should thereafter be obligated to consult with a view to reaching an appropriate solution.

25. Training will often be required both on site and at places abroad. The places abroad at which training is to be given may be specified. While these would normally be the contractor's places of manufacture, in some cases the appropriate training might be available only at works or factories of third parties (e.g. equipment suppliers). In such cases, the contractor may be obligated to obtain placement of the trainees at those places. It may be advisable to provide that the operational conditions at the places of training are to be similar to those which the trainees will later encounter in the works. The contractor may also be obligated to assist in obtaining necessary visas, entry permits or work permits when training is to be given abroad.

26. The training obligations of the contractor in relation to each category of trainee should be clearly defined. In this connection, the contract may obligate the contractor

to supply to the purchaser a training programme which will enable the trainees to obtain the information and skills necessary for the proper discharge of their duties in the operation and maintenance of the works. The programme may include a time-schedule for training which is harmonized with the time-schedule for construction. The parties may provide that the training is to be completed by the time agreed for the completion of construction. The programme should also describe the nature of the training to be given. The contract may provide that this programme is to be approved by an engineer engaged by the purchaser.

27. The contract should also obligate the contractor to engage trainers with qualifications and experience appropriate for the training and to notify the purchaser before the commencement of training of the qualifications and experience of the trainers to be used. In formulating training obligations, the parties may wish to take into account legal regulations governing the employment of the personnel to be trained, which may regulate the manner in which personnel may be trained. Where the parties enter into a product-in-hand contract (see chapter II, "Choice of contracting approach"), the contractor is obligated to prove during a test period that the works can be successfully operated by the purchaser's staff. While in such a case the training obligations of the contractor may not be separately defined, he must give the purchaser's staff the training required by them for operating the works.

28. In some cases, only minimal training of the personnel of the purchaser may be necessary, e.g. making them acquainted on site with the procedures for operating and maintaining the plant. The parties might seek to agree that no price is to be paid for such training, as it would be ancillary to the obligations of the contractor to supply and construct the works. Where more extensive training is required, the price for the training might be included in the overall price charged for the construction, or it might be charged separately. The purchaser is better able to assess the costs of training when the price is charged separately. The price may be payable in instalments (e.g. a percentage as an advance payment, a further percentage during the performance of the training programme, and the balance after proof of completion of the programme). The training programme may involve other costs (e.g. the living expenses of the trainees in the contractor's country, or the living expenses of the contractor's trainers in the purchaser's country), and the allocation of those costs should be settled. The contract may provide that the portion of the price for the training which covers costs incurred in the purchaser's country should be paid in the currency of that country.

29. For practical reasons, at the time of the conclusion of the contract it may not be possible to settle some issues which arise in regard to training (e.g. the date for commencement of training, or the duration of training). The parties should agree that such issues should be settled by the parties within a specified period of time after the conclusion of the contract.

[A/CN.9/WG.V/WP.17/Add.9]

**Chapter XXV. Termination of contract***Summary*

It is desirable for the contract to include a termination clause in order to provide for an orderly and equitable termination in the event of circumstances which make it prudent or necessary to terminate the contract. Termination should be regarded as a remedy of last resort. Parties should attempt to use other measures or remedies provided by the contract in order to deal with a situation before resorting to termination. In addition, it may be desirable for a party intending to terminate the contract to notify the other party in order to give the other party an opportunity to remedy the situation asserted as justifying termination (paragraphs 1 to 5).

A party should be able to terminate the contract only in respect of the portion of the construction which has not yet been performed, and not also in respect of construction which has already been effected (paragraph 6).

The parties may wish to entitle the purchaser to terminate the contract in the event of a failure to perform by the contractor which has serious consequences. For example, the purchaser may be entitled to terminate if the contractor abandons construction (paragraphs 7 and 8). In some cases the parties may wish to entitle the purchaser to terminate if the contractor is in delay (paragraphs 9 to 11), if the contractor fails to remedy defects in construction or design (paragraph 12), and if the contractor assigns the contract or certain contractual rights and obligations, or sub-contracts, in violation of restrictions on assignment or sub-contracting (paragraphs 13 and 14).

The contract might entitle the purchaser to terminate if bankruptcy or similar or related proceedings are instituted in respect of the contractor (paragraphs 15 to 17). The purchaser might also be entitled to terminate if bankruptcy or similar or related proceedings are instituted in respect of a guarantor under a performance guarantee supplied by the contractor and the contractor fails to arrange for the provision of a performance guarantee by a guarantor acceptable to the purchaser (paragraph 18).

The parties may wish to consider whether the purchaser should be entitled to terminate the contract at his convenience (paragraph 19).

The parties may wish to entitle the contractor to terminate the contract in the event of non-payment by the purchaser, and perhaps if the purchaser interferes with the contractor's right to payment by, for example, failing to provide a letter of credit or failing to accept a completed stage of construction (paragraph 21).

The contract might also entitle the contractor to terminate if the purchaser interferes with or obstructs the contractor's work, or in the event of bankruptcy or similar or related proceedings being instituted in respect of the purchaser (paragraphs 22 and 23).

If the performance of obligations under the contract is prevented by the occurrence of an exempting impediment, the parties may wish to entitle either party to terminate if because of the impediment performance is suspended for a specified period of time, or if the cumulative duration of two or more suspensions exceeds a specified period of time (paragraphs 24 and 25).

The parties should consider whether the contract should require that the existence of any grounds asserted by a party as justifying termination are to be certified by a third party (paragraph 26).

The contract should specify the rights and obligations of the parties upon termination. The contractor should be obligated to cease construction and to cease incurring obligations to third parties. It is advisable for the contractor to be obligated to take measures to protect or secure various elements of the partially completed works (paragraphs 27 and 28).

The contract might permit the purchaser to use equipment and materials of a contractor who has been terminated by the purchaser due to grounds attributed to the contractor. If the equipment and materials are not used by the purchaser, the contract should obligate the contractor to remove them (paragraphs 29 and 30).

The parties should consider obligating the contractor to assign his sub-contracts to the purchaser, or to terminate those contracts, if requested by the purchaser, in cases where the contract is terminated for grounds attributable to the contractor. The contract should authorize the purchaser to make payment of sums owed by the contractor to sub-contractors and entitle the purchaser to recover them from the contractor (paragraphs 31 and 32).

In some cases where the contract is terminated by the purchaser the contract should obligate the contractor upon termination to deliver to the purchaser drawings, descriptive documents and similar items relating to the works, and to create and deliver items which have not yet been created (paragraph 33).

The contract should specify the payments which are to be made by one party to the other in the event of termination. Whether payments are to be made, and the extent of the payments, may depend on the cause for the termination (paragraphs 34 to 40).

The contract should specify those provisions which are to survive the termination and continue to bind the parties (paragraph 41).

\* \* \*

**A. General remarks**

1. Circumstances may arise which make it prudent or necessary to terminate the contract before it has been completely performed. It is desirable for the contract to include a termination clause in order to provide for an

orderly and equitable termination in the event such circumstances arise. This chapter deals with possible provisions of a termination clause in the contract. It does not deal with situations in which a contract may be void or voidable under the law applicable to the contract.

### C. Grounds for termination

#### 1. Unilateral termination by purchaser

##### (a) Failure to perform

7. In the construction of a works there frequently occur departures by the contractor from certain of his contractual obligations which are technically failures to perform, but which are either trivial or can be easily remedied. Other failures by the contractor to perform may have serious consequences, for example by interfering with the time-schedule for construction or affecting the quality of the completed works. The parties may wish to restrict the right of the purchaser to terminate the contract in the event of a failure to perform by the contractor to failures which have serious consequences. An approach which the parties may wish to consider in this regard is to specify in the termination clause certain serious types of failures to perform by the contractor which would entitle the purchaser to terminate the contract.<sup>1</sup> Examples of failures of this type are discussed in paragraphs 8 to 14, below.

##### (i) Abandonment of construction

8. The purchaser may be permitted to terminate the contract if the contractor abandons the construction.

##### (ii) Delay in construction

9. If the contractor fails to commence construction at the time stipulated in the contract, the contract may entitle the purchaser to notify the contractor that he is required to commence. If the contractor does not do so within a reasonable or specified period of time after the notice, the contract may permit the purchaser to terminate.

10. Works contracts often contain or provide for a construction time-schedule which, when several contractors are involved, serves to co-ordinate various phases of the construction and the work of the various contractors (such as the supply of equipment and materials and the

##### <sup>1</sup>Illustrative provisions

"The purchaser may, without the authorization of a court or any other authorization, terminate the contract in respect of the construction which has not yet been performed in accordance with the following provisions:

"(a) If the contractor abandons the construction, the purchaser may terminate the contract by delivering to the contractor a written notice of termination;

"(b) If the contractor fails to commence construction at the time set forth in article ... of this contract, the purchaser may deliver to the contractor written notice requiring him to commence. If the contractor fails to do so within [a reasonable time] [x days] after delivery of such notice, the purchaser may terminate this contract by delivering to the contractor a written notice of termination;

"(c) If the contractor fails to complete a portion of the construction by an obligatory milestone date set forth in article ... of this contract, the purchaser may deliver to the contractor written notice requiring him to complete that portion of the construction. If the contractor fails to do so within [a reasonable time] [x days] after delivery of such notice, the purchaser may terminate this contract by delivering to the contractor a written notice of termination;

"(d) [further grounds may be specified, e.g. those discussed in paragraphs 12 to 14]."

### B. Extent of termination

6. A party should be able to terminate the contract only in respect of the construction which has not yet been performed. He should not be able to terminate the contract in respect of construction which has already been performed, since this would require each party to return what he has received from the other. This would be difficult or impossible in the case of an industrial works; for example, the purchaser would not be able to return to the contractor the portion of the works which has been constructed on the purchaser's land. In addition, the parties may wish certain contractual rights and obligations to remain in effect even after termination of the contract (see paragraph 41, below).



erection of the works, see chapter IX, "Construction on site"). A failure by a contractor to meet an obligatory milestone on the date specified in the time-schedule may not prevent the final completion date from being met, since the contractor might be able to hire extra labour or take other measures to accelerate the performance of the balance of his work, and make up the time lost during the delay. However, a failure to meet an obligatory milestone on the date specified may result in the liability of the purchaser to other contractors who suffer financial loss because of an inability to commence their work on time due to the failure in co-ordination, and the purchaser would normally be able to claim damages for that liability from the contractor in delay. The contract may entitle the purchaser to notify the contractor that he is required to complete the portion of the construction to which the milestone relates, and, if the contractor fails to complete that portion within a reasonable or specified period of time after the notice, to terminate the obligation of the contract in relation to that portion. Alternatively, the contract might entitle the purchaser to terminate the entire contract (see chapter XVIII, "Delay, defects and other failures to perform").

11. Under another approach, the termination clause could provide that the purchaser may terminate the contract after the accumulation of a specified amount of unexcused delay by the contractor (see chapter XXI, "Exemption clauses"). Alternatively, when delays by the contractor obligate him to pay liquidated damages to the purchaser (see chapter XIX, "Liquidated damages and penalty clauses"), termination may be permitted after a specified amount of liquidated damages has accumulated. The amounts of unexcused delay or liquidated damages which would permit termination should be so quantified that their accumulation would result in a serious delay in completing the works.

(iii) *Defective construction*

12. The contract might entitle the purchaser to inspect the construction while it is in progress, and to notify the contractor to stop defective construction and to effect the construction in accordance with the contract (see chapter XVIII, "Delay, defects and other failures to perform"). The purchaser may be entitled under the contract to terminate the contract if the contractor fails to remedy within a reasonable or specified period of time after the notice defects which would prevent the works from operating in accordance with the contract. In addition, in cases where the contractor supplies a design for the whole or part of the works and both he and one or more other contractors are to construct according to that design, the contract might provide for the purchaser to notify the contractor who supplies the design of any defects in it which would prevent the works from operating as required by the contract, and to terminate the contract if the contractor does not make good the defects within a reasonable or specified period of time after the notice (see chapter XVIII, "Delay, defects and other failures to perform").

(iv) *Violation of restrictions on assignment and sub-contracting*

13. As discussed in chapter XXVII, "Transfer of contractual rights and obligations", the contract might prohibit the contractor, without the purchaser's consent, from assigning the contract so as to substitute another party for himself, or from assigning certain contractual rights and obligations. The contract might entitle the purchaser to terminate the contract if an assignment by the contractor in violation of those restrictions is valid under the law governing the assignment. However, the parties might consider whether the purchaser should also be entitled to terminate the contract even though the assignment is invalid under the law governing it.

14. The contract might also restrict the ability of the contractor to engage sub-contractors to perform his obligations (see chapter XI, "Sub-contracting"). The parties may wish to consider whether the purchaser should be able to terminate the contract if the contractor sub-contracts in violation of those restrictions.

(b) *Bankruptcy or insolvency of contractor*

15. The contract and its performance will be subject to mandatory legal rules in the event of the bankruptcy of a party. Under most legal systems, the assets of the bankrupt, including his rights and obligations under the contract, will pass from his control to that of an officer. This officer will usually cease carrying on the business of the bankrupt in the ordinary course, except to the extent necessary to protect the assets of the bankrupt and the rights of creditors. In addition, during the pendency of bankruptcy proceedings involving the contractor, the officer will be severely restricted in his ability to sub-contract or to purchase from third parties materials or supplies needed to carry out the work, or to make payments which fall due after the bankruptcy. The parties may therefore wish to consider whether the institution of bankruptcy proceedings in respect of the contractor should entitle the purchaser to terminate the contract. If so, the parties should take account of the relevant bankruptcy laws in drafting termination provisions. For example, in some legal systems a party to a contract cannot terminate the contract solely on the ground that the other party is bankrupt.

16. The parties may wish to consider whether the purchaser should have the right to terminate immediately upon the institution of bankruptcy proceedings, or only after a period of time. The possibility of immediate termination could enable the purchaser to prevent the contractor from incurring additional obligations to third parties for which the purchaser might be responsible. On the other hand, in the case of bankruptcy proceedings initiated against the contractor, the parties might wish to entitle the purchaser to terminate only after a specified period of time following notice to the contractor in order to give the contractor an opportunity to have the proceedings dismissed or stayed. It may be noted, however, that such an approach could result in loss to the purchaser in

some cases, e.g. by his being unable to engage another contractor until the lapse of the period of time.

17. The parties may wish to designate as a ground for termination by the purchaser not only bankruptcy, but also similar or related proceedings to which the contractor may be subject, and which could significantly interfere with his performance of the contract (e.g. receivership, liquidation, insolvency, assignment of assets and comparable proceedings under relevant laws).

18. When the contract requires the contractor to furnish a performance guarantee, the parties may wish to consider permitting the purchaser to terminate if the guarantor becomes subject to the proceedings of the type described above, and the contractor fails to arrange for the provision of a performance guarantee by another guarantor acceptable to the purchaser within a reasonable or specified period of time.

(c) *Termination for convenience*

19. The parties may wish to consider whether the purchaser should be entitled to terminate the contract at his convenience, i.e. without being justified by any grounds otherwise specified in the contract. In practice this right is given only to purchasers who are Governments or government entities, which may for policy reasons wish to have this right. The contract might provide that if a purchaser purports to terminate on a ground specified in the contract, and it is subsequently determined that termination under that ground was unjustified, the termination is to be regarded as a termination for convenience. As discussed in paragraphs 38 and 39, below, the consequences of the exercise by the purchaser of a right to terminate the contract at his convenience may differ from the consequences of his termination on other specified grounds. In particular, the cost to the purchaser of the exercise of this right may be such as to discourage him from doing so except in exceptional circumstances. If the purchaser is to be permitted to terminate at his convenience, the contract may permit the termination to be effective immediately upon notice to the contractor.<sup>2</sup>

2. *Unilateral termination by contractor*

(a) *Failure to perform*

20. The parties may wish to consider whether the contractor should be entitled to terminate in the event of a failure to perform by the purchaser. The purchaser's principal obligation under the contract is to pay the

<sup>2</sup>*Illustrative provisions*

"(1) The purchaser may at any time, and without the authorization of a court or any other authorization, terminate this contract or any part thereof for any reason other than those set forth in article ... by delivering a written notice of termination to the contractor.

"(2) If the purchaser purports to terminate this contract or any part thereof for a reason set forth in article ..., and it is subsequently determined in dispute settlement proceedings that termination for that reason was not justified, the termination shall be regarded as having been effected pursuant to the provisions of paragraph 1 of this article."

agreed price. However, he may also have obligations which are related to the contractor's right to receive payment, such as providing a letter of credit or accepting completed construction. The purchaser may have additional obligations under the contract, such as making the site available to the contractor, and in some cases obligations to perform or to provide for the performance of some of the construction.

(i) *Non-payment by purchaser; failures to perform interfering with contractor's right to payment*

21. A failure by the purchaser to pay the contractor, or failures which prevent the contractor from receiving payment, could entail serious consequences for the contractor. For example, if he finances his construction in part with interim payments he may be unable to proceed with the work in the absence of those payments. The parties may wish to provide that the contractor may notify the purchaser that he is required to pay sums due to the contractor (after setting off amounts owed by the contractor to the purchaser, such as the costs of repairing defective work, liquidated damages payable by the contractor, and authorized direct payments made by the purchaser to subcontractors (see chapter XI, "Subcontracting")), and to entitle the contractor to terminate the contract if the purchaser does not pay within a reasonable or specified period of time after the notice. This remedy may be limited to cases where the purchaser has failed to pay a certain percentage of the total price, or a certain amount. In addition, the contract might entitle the purchaser to terminate if the purchaser fails to provide an agreed payment guarantee or a letter of credit (see chapter XVII, "Security for performance"), or to accept a completed stage of the construction (see chapter XIII, "Completion, take-over and acceptance").

(ii) *Interference with or obstruction of contractor's work*

22. The contractor might be permitted to terminate the contract if the purchaser seriously interferes with or obstructs the contractor's work. This could occur, for example, if the purchaser fails to make the site or portions of the site available to the contractor on time. In contracts in which the purchaser has obligations with respect to the supply of materials for the construction, obstruction could occur from a failure to perform those obligations. The contract may provide for the contractor to notify the purchaser to cease an interference with or obstruction of his work, and entitle the contractor to terminate the contract if the purchaser fails to do so within a reasonable or a specified period of time.

(b) *Bankruptcy or insolvency of purchaser*

23. The parties may consider whether the contractor should be able to terminate the contract if the purchaser becomes subject to bankruptcy, insolvency or similar proceedings. Considerations similar to those discussed in paragraphs 15 to 17, above, concerning the bankruptcy of the contractor are also applicable here.

### 3. *Prevention of performance due to exempting impediment*

24. During the course of construction, events can occur which prevent either party from performing obligations under the contract. The contract might in some of these cases exempt the party from liability for failure to perform. However, it may obligate the party who is prevented from performing by an exempting impediment to notify the other party of the occurrence of the impediment, and provide for the parties to deliberate on what measures should be taken to deal with the exempting impediment (see chapter XXI, "Exemption clauses", chapter XXIII, "Variation clauses" and chapter XXIV, "Suspension clauses"). The parties might be able to estimate the likely duration of the exempting impediment, and thus the amount of time that the obligations affected by the impediment will not be able to be performed. This could provide a basis for a determination by the parties as to what action to take. For example, if the impediment is likely to persist only for a short period of time, the parties might merely suspend performance of the affected obligations for the duration of the impediment. If the impediment is likely to persist for a long period of time and seriously interfere with or prevent the completion of the construction or the payment of the contractor, the parties might agree to terminate the portion of the contract relating to the affected obligations, or, if necessary, the entire balance of the contract.

25. The parties may wish to provide in the contract that if performance is suspended due to an exempting impediment for a specified period of time, or if the cumulative duration of two or more suspensions exceeds a specified period of time, either party is entitled to terminate the contract (see chapter XXIV, "Suspension clauses"). The period of time which would entitle a party to terminate should be so quantified that suspension for this period would result in a serious delay in completing the works. If only a portion of the construction is suspended as a result of the exempting impediment, the contract might permit the terminating party to terminate only the part of the contract dealing with that portion. Under provisions such as these, the termination would be permitted because of the suspension of performance for an excessive amount of time, rather than because of the existence of the exempting impediment *per se*. Termination would be permitted in spite of the existence of the exempting impediment; the legal effect of the impediment would be to exempt the non-performing party from the payment of damages (see chapter XXI, "Exemption clauses").

### D. *Establishment of grounds for termination*

26. The parties should consider whether a party may terminate the contract upon his own assessment that grounds for termination exist, subject to challenge in dispute settlement proceedings, or whether the existence of grounds for termination must be verified by a third party. In contracts in which an engineer exercises independent functions (see chapter X, "Consulting engineer"), certification by the engineer of the occur-

rence of the events asserted to be grounds for termination could help to avoid disputes as to the existence of those grounds (see chapter XXIX, "Settlement of disputes").

### E. *Rights and obligations of parties upon termination*

#### 1. *Cessation of work by contractor*

27. It would be desirable for the contract to specify that upon termination by either party the contractor must cease construction and must cease incurring obligations to third parties such as sub-contractors and suppliers in respect of the construction.

28. In many instances it will not be feasible or advisable for the contractor simply to cease construction and leave the site at the moment the termination takes effect. Certain operations in progress may have to be completed, and measures may have to be taken to protect or secure various elements of the partially completed works. It is advisable for the contract to obligate the contractor to take those measures. With respect to the question of which party is to bear the cost of such measures, see subsection 5, below. The contract should also expressly obligate the contractor to vacate the site without delay once all work has finally stopped, or when ordered to do so by the purchaser, and to require him to ensure that persons or firms engaged by him also vacate the site in those circumstances.

#### 2. *Use and disposition of contractor's equipment and materials*

29. When the contract is terminated by the purchaser due to grounds attributable to the contractor, it might be important for the purchaser or a new contractor to be able to use equipment and materials belonging to the original contractor in order to continue the work. If so, the termination clause should expressly authorize this.

30. If the purchaser does not wish to use the contractor's equipment in continuing the construction, or if the purchaser is not otherwise given rights in respect of it, the contractor may be obligated to remove it from the site within a reasonable period of time. If he fails to do so, the purchaser could be empowered to have it removed at the contractor's expense, or to sell it through appropriate means and apply the proceeds towards sums owed to the purchaser by the contractor. Alternatively, the contract may entitle the purchaser to use the equipment upon payment of a rental, or to purchase it at a price to be agreed by the parties or established by an independent valuer. Parties should be aware, however, that these approaches may be subject to or restricted by mandatory rules of applicable law; parties should therefore take such rules into account in drafting provisions of this nature. The parties may wish to determine the extent of the purchaser's liability for loss of or damage to the equipment (see chapter XIV, "Passing of risk").

### 3. *Assignment of third-party contracts and assumption of liabilities*

31. When termination occurs there may exist outstanding contracts which the contractor has entered into with sub-contractors and suppliers. If the construction is to be completed by the purchaser or by another contractor engaged by the purchaser, the purchaser may wish to take over some of these contracts. Alternatively, he or the new contractor may wish to enter into new contracts with these sub-contractors or suppliers. This may be the case if the original contract is not assignable, or if the purchaser or new contractor does not wish to assume all of the obligations due from the terminated contractor to the sub-contractors or suppliers by taking an assignment of the contracts. The conclusion of such new contracts may be practicable only if the sub-contractors or suppliers are released from their contracts with the contractor. Therefore, in cases where the contract is terminated for grounds attributable to the contractor, parties should consider obligating the contractor to assign the contracts, if assignment is possible, or to terminate them, if requested by the purchaser.

32. When the assignment of a contract, or a new contract with a sub-contractor or supplier, is contemplated, difficulties may arise because of sums owed to these third parties by the contractor. The third party may not wish to continue his participation in the construction unless past sums owed to him by the original contractor are paid. Furthermore, the third party may refuse to deliver items which were contracted for prior to termination but for which payment has not yet been made, or may even take back equipment and materials which have already been delivered. The purchaser may therefore want the authority to pay the third party directly for sums owed to the latter by the original contractor, and to recover these payments from the original contractor. If the purchaser accepts an assignment of the third party contract, he will under most legal systems be obligated to pay these past-due sums. The contract should expressly authorize such direct payments and entitle the purchaser to recover them from the contractor.

### 4. *Drawings, descriptive documents and similar items*

33. If the purchaser intends to complete the work left unfinished by the terminated contractor, the purchaser may wish to obtain the drawings, designs, calculations, descriptions, documentation for know-how and engineering and other such items relating to the construction which has been completed by the contractor, as well as for construction yet to be completed. Obtaining such documentation or information may be important if the construction or technology is known only to the contractor, or if the items cannot for other reasons be created by an engineer or a new contractor. The contract should therefore obligate the contractor upon termination by the purchaser to deliver to the purchaser such of those items as are in the possession of the contractor. In some cases, however, the contractor may be prevented from doing so because a third party has industrial property rights in

respect of the items, and may not consent to their delivery to the purchaser. In addition, it might be desirable to obligate the contractor to create and deliver drawings and documents (e.g. operation manuals) which have not yet been created, particularly when it would be difficult or impossible for another contractor to create them. The purchaser might be required to compensate the contractor for such items, unless compensation has been included within past payments made to the contractor.

### 5. *Payments to be made by one party to other*

#### (a) *Termination for grounds attributable to contractor*

34. The parties may wish to provide that if the contract is terminated for failure to perform or bankruptcy of the contractor, or other grounds attributable to him, he is not entitled to payment for construction which he has not yet performed. However, the contract might entitle him to receive the portion of the price which is attributable to construction which he satisfactorily performed prior to termination. In a cost-reimbursable or unit price contract this price should be relatively easy to ascertain. In a lump sum contract the determination of the price attributable to construction which has been performed would be facilitated if the contract allocated portions of the price to specific elements of the construction (see chapter VII, "Price").

35. The purchaser may incur expenses in connection with the termination which he would not have incurred had the contract not been terminated and had the work been completed by the contractor. For example, he may have work done to secure or protect the partially-completed works until construction can resume with another contractor, or, if it is impossible to complete the works, he may incur penalties or expenses in connection with the termination of contracts with other contractors or suppliers. In addition, the cost of completing the construction not performed by the terminated contractor could exceed the amount which under the contract would have been due to the contractor in respect of that construction. In addition, the process of selecting and employing a new contractor could delay the completion of the works. So, too, could the time required for the new contractor to integrate himself into the project and continue from where the terminated contractor left off. Losses of this nature may be made compensable to the purchaser by way of damages (see chapter XX, "Damages").

#### (b) *Termination for grounds attributable to purchaser*

36. If the contract is terminated for grounds attributable to the purchaser, the contract may entitle the contractor to receive the portion of the price which is attributable to the construction which he has satisfactorily performed, and reimbursement for obligations reasonably incurred in the expectation of completing the works (e.g. for materials ordered). The contract may also obligate the purchaser to reimburse the contractor for his extra expenses occasioned by the termination. These could include, for example, the costs of any measures required to be taken

or requested by the purchaser to secure or protect the works, the cost of repatriating personnel and equipment, to the extent that this has not already been included in the amount to be paid to the contractor, and damages payable by the contractor for terminating contracts with sub-contractors or other third parties. Losses of this nature may be made compensable to the contractor by way of damages.

*(c) Termination arising from circumstances not attributable to either party*

37. The contract might provide that, if the contract is terminated for reasons not attributable to either party (i.e. suspension for a specified period of time because of an exempting impediment, see paragraph 25, above), the contractor is entitled to receive the portion of the price which is attributable to the construction which he has satisfactorily performed. The parties should consider, however, the most equitable way to deal with their respective expenses occasioned by the termination. One possibility is to share these expenses equally or in accordance with an agreed formula. Another possibility is for each party to bear his own expenses.

*(d) Termination for convenience*

38. If the contract permits the purchaser to terminate at his convenience, it might, in the event of such a termination, require the purchaser to pay to the contractor the portion of the price which is attributable to the construction satisfactorily performed prior to the termination, as well as for extra expenses incurred by the contractor incidental to the termination (see paragraph 36, above), to the extent that those costs are not already included in the amount to be paid to the contractor. The parties should consider whether the contractor should be entitled to be compensated for some or all of the lost profit on the portion of the contract remaining to be performed. On the one hand, the contractor might have forgone other contracting opportunities in anticipation of completing the contract in its entirety. On the other hand, an

obligation on the purchaser to compensate the contractor for his lost profit might make it financially prohibitive for the purchaser to exercise his right of termination for convenience.

39. At the time when the contract is terminated for convenience the purchaser may have received the design for the works from the contractor, but the value of the design may not yet be adequately reflected in the price which would be due to the contractor on the basis of the work which the contractor had satisfactorily performed. To deal with these cases the contract may specify that the purchaser must compensate the contractor for the design insofar as such compensation is not otherwise reflected in the price due to the contractor.

*(e) Damages, liquidated damages or penalties*

40. In addition to the payments mentioned above, if the termination is for grounds attributable to a party, the other party may be entitled to damages (see chapter XX, "Damages"), liquidated damages or penalties (see chapter XIX, "Liquidated damages and penalty clauses").

**F. Survival of certain contractual provisions**

41. In some legal systems termination of the contract might be interpreted as bringing to an end all contractual provisions, including those which the parties might wish to survive, such as the rights and obligations of the parties upon termination, guarantees for construction performed, remedies for defective performance, and provisions such as those concerning settlement of disputes and the preservation of confidentiality. The parties should take care to ensure that rights, obligations and remedies which they wish to survive do not lapse upon termination. To do so, the parties should specify in the contract those provisions which are to survive and continue to bind the parties even after termination.

**C. Future work in the area of the new international economic order: note by the secretariat (A/CN.9/277)**

[Original: English]

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## INTRODUCTION

1. At its eleventh session (1978), the Commission included in its work programme a topic entitled "The legal implications of the new international economic order", and accorded priority to the consideration of this topic. The Commission also established a Working Group on the New International Economic Order.<sup>1</sup> At its twelfth session (1979), the Commission considered possible subjects on which it might commence work, and requested its Working Group to make recommendations as to specific topics which could appropriately form part of the work programme of the Commission.<sup>2</sup>

2. At its first session (1980), the Working Group decided to propose to the Commission that work be undertaken on the harmonization, unification and review of contractual provisions commonly occurring in international contracts in the field of industrial development, such as contracts on research and development, consulting, engineering, supply and construction of large industrial works (including turn-key contracts or contracts *produit en main*), transfer of technology (including licensing), service and maintenance, technical assistance, leasing, joint venture, and industrial co-operation in general.

3. At its thirteenth session (1980), the Commission endorsed the view expressed by the Working Group that the subject noted above was of special importance to developing countries and to the work of the Commission in the context of the new international economic order. The Commission welcomed the recommendation of the Working Group, and requested the Secretary-General to carry out preparatory work in respect of contracts for the supply and construction of large industrial works and on industrial co-operation.<sup>3</sup>

4. At its fourteenth session (1981), the Commission decided that a legal guide should be prepared that would identify the legal issues involved in contracts for the supply and construction of large industrial works and should suggest possible solutions to assist parties, in particular from developing countries, in their negotiations. It also requested the Secretary-General to submit, at a future session, a preliminary study on specific features of industrial co-operation contracts after the preparation of the legal guide on contractual provisions relating to contracts for the supply and construction of large industrial works.<sup>4</sup>

5. The Working Group on the New International Economic Order proceeded with the examination of clauses to be found in contracts for the supply and construction of large industrial works at its second and third sessions, and has been examining draft chapters of the legal guide (hereinafter referred to as "the Guide") at its fourth to eighth sessions. It is expected that at its ninth session (1987) the Working Group will consider all the draft chapters of the Guide as revised by the secretariat in the light of the comments by the Working Group, and will thereby complete its mandate. It is further expected that the Guide will be placed before the Commission for approval at its twentieth session (1987).

6. At its second session (1981), the Working Group considered a note by the secretariat entitled "Clauses related to industrial co-operation".<sup>5</sup> In that note the secretariat observed that it did not have the resources to deal simultaneously with both contracts for the supply and construction of large industrial works, and for industrial co-operation. It also observed that despite a note verbale of 31 October 1980 from the Secretary-General soliciting from States members of the Commission copies of industrial co-operation contracts and other relevant materials, not a single contract had been received up to the date of the note. It may be mentioned that no contracts have been received up to the present date. The secretariat also noted that many of the issues in

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its eleventh session, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17 (A/33/17)*, para. 71.

<sup>2</sup>Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17 (A/34/17)*, para. 100.

<sup>3</sup>Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 143.

<sup>4</sup>Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17 (A/36/17)*, para. 84.

<sup>5</sup>A/CN.9/WG.V/WP.5.

relation to industrial co-operation which it had identified as possible subjects for study (see paragraph 21, below) also arose in relation to contracts for the supply and construction of large industrial works. In the light of those considerations, the Working Group agreed that the examination of contracts for industrial co-operation should be deferred.

7. With completion by the Commission of its work on the Guide now in sight, and in view of the fact that six years have elapsed since the deliberations at the Commission's thirteenth session on a possible work programme in the context of the new international economic order, the Commission may wish to consider its future work in this area. This report comments on some possible subjects which the Commission may wish to consider.

## I. Possible subjects for future work

### A. Contracts for industrial co-operation<sup>6</sup>

8. Contracts for industrial co-operation are of different types. However, certain characteristics are common to most of the types:

(a) The transactions reflected in these contracts, while containing elements similar to well-known categories such as the sale or lease of goods, also contain additional elements which result in mixtures of obligations which do not fall under recognized categories in most legal systems. In particular, the arrangements for remuneration in respect of obligations performed often do not fall within traditional patterns.

(b) The transactions are complex, consisting of several interrelated and interdependent obligations. The transactions sometimes include more than two parties.

(c) The transactions are intended to endure for several years (in some cases as long as 20 to 30 years).

(d) The interrelationship and interdependency of the obligations of the parties, and their long-term nature, create the need for close co-operation between the parties in the performance of the contracts, and for a relationship of mutual trust if the contracts are to be successfully implemented.

9. It is difficult to specify the types of contract which may be regarded as industrial co-operation contracts. Studies on this subject by the Economic Commission for Europe (ECE) have identified six main categories: licensing with payment in resultant products; supply of complete plants and production lines with payment in resultant products; co-production and specialization; sub-

contracting; joint ventures; and joint tendering and joint construction or similar projects.<sup>7</sup> It may be noted that the co-operation may extend to fields such as the transfer of technology, production of goods, or the exploitation of natural resources. The categories may overlap. Thus, a joint venture may be formed for joint tendering and construction. These categories cannot be regarded as exhaustive.

10. Within each of the categories mentioned above, the totality of the arrangement which is entered into will be tailored to the particular needs of the parties. For example, in the case of licensing with payment in resultant products, the parties may agree that the licensor pass on to the licensee improvements made to the technology after the date of the licence. Even closer co-operation may be envisaged by provision for joint research and development in the licensed process. In the case of supply of complete plants or production lines with payment in resultant products (often referred to as a buy-back agreement; see paragraph 35, below), payment may be envisaged not only with products of the plant, but also with other products manufactured by the purchaser of the plant.

11. Sub-contracting, i.e. the employment by one enterprise of another to produce goods which the first enterprise needs for the performance of contracts of supply entered into with third parties (see paragraph 17, below), often matures into co-production and specialization, together with joint marketing. The subject of sub-contracting covers the manufacture and supply of goods by the sub-contractor, and also includes the supply of services (e.g. when the personnel of a sub-contractor are more suitable for managing certain projects which the contractor has undertaken). In regard to the manufacture and supply of goods, the sub-contractor may merely process or finish materials supplied by the contractor, or may himself procure new materials and manufacture the goods in accordance with designs or technology provided by the contractor. In the case of co-production and specialization (see paragraph 17, below), additions to the basic arrangements may include co-operation in research and development in regard to production, and the joint operation of after-sales services. In regard to joint ventures, legislation regulating joint ventures may result in variations in their structure in different countries and the business activities which the joint ventures can undertake.

12. Contracts for industrial co-operation are normally concluded between two parties. Tripartite agreements, however, are also sometimes concluded. In such tripartite agreements, one of the parties is sometimes from a developing country. The contracts, whether bipartite or tripartite, may relate only to the countries of the parties (e.g. specialization in production in the respective countries), or to a third country (e.g. a joint venture to be

<sup>6</sup>A fuller description of these contracts is contained in *International Contracts in the Field of Industrial Development: Study by the Secretary-General* (A/CN.9/191) paras. 106-140. They are also described in *Guide on Drawing Up International Contracts on Industrial Co-operation* (United Nations publication, Sales No.E.76.II.E.14) and in *East-West Industrial Co-operation* (United Nations publication, Sales No.E.79.II.E.25).

<sup>7</sup>*Guide on Drawing Up International Contracts on Industrial Co-operation* (United Nations publication, Sales No. E.76.V.E.14), p. 2. The study by the Secretary-General (A/CN.9/191) treats joint ventures as a separate category.

established in a third country, or a joint tender for construction in a third country).

13. Contracts for industrial co-operation have been a feature of trade between the socialist states of Eastern Europe and developed market economy countries, in particular of Western Europe, for the past two decades. As a result, such contracts have been extensively examined and documented in studies prepared by the ECE.<sup>8</sup> Some of these studies include an examination of tripartite industrial co-operation contracts. They refer also to the financing arrangements for such contracts, and also cover some legal issues arising out of the contracts.<sup>9</sup> Comparable studies are not available of bipartite industrial co-operation contracts between enterprises from developed and developing countries.

14. In deciding whether work is to be undertaken in regard to industrial co-operation contracts, two questions need examination. First, whether these contracts are of significance in trade between developed and developing countries; second, if the answer to that question is in the affirmative, whether legal difficulties arise in relation to such contracts which may be alleviated by work of the Commission. With regard to the first question, while these contracts have contributed significantly to East-West trade in the past two decades, the extent to which they are of actual or potential importance to North-South trade is not easy to determine.<sup>10</sup> The information at present available to the secretariat in respect of each of the main categories of industrial co-operation contracts is noted in the immediately succeeding paragraphs.

15. There is evidence that contracts for the supply of complete plants and production lines with payment in

<sup>8</sup>See, for example, *Analytical Report on Industrial Co-operation Among ECE Countries* (United Nations publication, Sales No.E.73.II.E.11); *East-West Industrial Co-operation* (United Nations publication, Sales No. E.79.II.E.25); "Prospects for the expansion of East-West industrial co-operation" (TRADE/AC.21/R.3 and Add.1).

<sup>9</sup>*East-West Industrial Co-operation ...*, part B, chap. 1; "Legal-organizational and financial aspects of tripartite industrial co-operation: a review of recent Yugoslav experience" (TRADE/R.470); John R. Mikton, "Tripartite co-operation involving countertrade among European and developing countries", in the proceedings of the International Workshop on Countertrade, organized jointly by the International Association of State Trading Organizations of Developing Countries and Generalexport, Belgrade, Yugoslavia, 1985.

<sup>10</sup>In relation to the relevance of East-West experience in industrial co-operation to that between developed and developing countries, the second meeting (1981) of the *ad hoc* UNCTAD/UNIDO Group of Experts on Trade and Trade-related Aspects of Industrial Collaboration Arrangements noted as follows: "Some experts noted that many aspects of East-West trade and industrial co-operation may be relevant to similar co-operation between enterprises in developing and developed countries including at the intergovernmental level. In this connection, the Group noted the network of industrial and trade co-operation agreements which socialist countries had with many developing countries. However, other experts pointed out that while East-West experience provided useful guidelines for co-operation with developing countries, it might not be suitable or possible to extrapolate or transfer many of the practices applied in East-West trade and industrial co-operation to developing countries in view of the divergencies among these countries, e.g. as regards natural resource endowments, adequacy of infrastructure, and generally at the levels of industrial or economic development." (ID/WG.337/9/Rev.1), para. 58.

resultant products are entered into between developed and developing country enterprises. The fact that products have to be taken back as payment by the supplier of the plant from the developed country creates in the supplier an incentive to supply an appropriate plant and to train the personnel of the purchaser in the operation of the plant. It also creates an incentive in the purchaser from the developing country to operate the plant so as to produce high quality products which will be accepted in payment and be competitive on international markets.<sup>11</sup> There is much less evidence of the practice of licensing by developed country enterprises to developing country enterprises with payment in resultant products.<sup>12</sup>

16. Developing country enterprises are often parties to tripartite industrial co-operation contracts entered into for the purposes of joint tendering and joint construction.<sup>13</sup> In such cases the developing country enterprise will be a member of a consortium of contractors. It will generally supply local labour and locally available equipment and materials, and also sometimes supply building and civil engineering services. Such supply will generally be cheaper than supplies from a source outside the developing country, and payment for these supplies can absorb the local currency component in the funds available for a project. Where a project is located in a remote region or work has to be done under extreme conditions, participation by a developing country enterprise may be essential. Work has been undertaken by other organizations on the contractual terms needed to create consortia, and on the terms on which responsibility may be allocated among the members, and there would appear to be little need for work by the Commission on this subject.<sup>14</sup>

<sup>11</sup>There is no reliable data on the frequency of such transactions, although each transaction would be of considerable value. This category of transaction is also regarded as a form of countertrade. One publication, relying on data given by a selection of United States enterprises on their countertrade activities world wide, puts this category at 9 per cent of the total countertrade transactions entered into (Stephen F. Jones, *North-South Countertrade. Barter and Reciprocal Trade with Developing Countries* (London, Economist Intelligence Unit, 1984), chap. 3). Mikton states with reference to this type of transaction involving tripartite co-operation "This type of tripartite co-operation is the most frequently encountered today; it generally involves deliveries of engineering, erection and maintenance services or capital equipment (sometimes both) by the CMEA and Western parties in return for counter-deliveries of resultant goods by the developing country client. The resulting project may create new industrial capacity, expand exports, develop resources or otherwise contribute to the country's economic development" (see note 9, above).

<sup>12</sup>This practice is not noted in the World Intellectual Property Organization *Licensing Guide for Developing Countries*, WIPO publication No. 620 (Geneva, 1977).

<sup>13</sup>See references cited in note 9, above.

<sup>14</sup>For a fuller description of this type of association, see draft chapter III, "Procedure for concluding contract" of the Legal Guide on Drawing Up International Contracts for the Construction of Industrial Works (A/CN.9/WG.V/WP.17/Add.2). Issues relating to groups of firms acting as contractors are discussed in the *ECE Guide for Drawing up International Contracts between Parties Associated for the Purpose of Executing a Specific Project* (United Nations publication, Sales No.E.79.II.E.22). Guides and model forms on these joint ventures have also been produced by the Fédération Internationale Européenne de la Construction (FIEC) and the Organisme de Liaison des Industries Métalliques Européennes (ORGALIME). Work has also been undertaken by national associations, e.g. the Joint Venture Agreement for Tender and Execution of Turnkey Project, by the Japan Machinery Exporters Association.



17. International sub-contracting appears to be of some significance for the industrial development of developing countries, and it has been widely discussed.<sup>15</sup> "Sub-contracting consists of the manufacture by the sub-contractor of parts, components or semi-processed products in conformity with the specifications laid down by the principal firm. The inputs are often provided by the principal who, as a rule, also provides a varying amount of technical assistance, supplemented occasionally by financial backing".<sup>16</sup> Sub-contracting between enterprises from developed and developing countries has grown in relation to various sectors of industry. Nevertheless, legal difficulties in the drawing up of sub-contracts do not appear to be regarded as a constraint on sub-contracting.<sup>17</sup> A principal reason for this may be the fact that the main components involved in a sub-contract are well-known in international commerce: definition of the kind and quality of goods, a time-schedule for deliveries, specifying the price and mode of payment, and arrangements for transportation. Sub-contracting between parties sometimes develops into specialization and co-production, e.g. an arrangement under which each of two parties specializes in the production of different components of an item. The components are then put together by one party to produce the complete item, or the components are exchanged and each party produces the complete item. The extent to which such arrangements are at present entered into between enterprises of developed and developing countries is unclear.<sup>18</sup>

18. The material at present available to the secretariat therefore suggests that, of the well-recognized categories of contracts for industrial co-operation, that which may merit investigation at the present time is the supply of complete plants and production lines with payment in resultant products. The examination of this category has two further advantages. First, it may be regarded as a natural sequel to the study by the Commission of contracts for the supply of industrial works. Second, this

<sup>15</sup>Over the years, UNIDO has directed attention to this transaction; see for instance, *Subcontracting for Modernizing Economies* (United Nations publication, Sales No.E.74.II.B.12); H.C. Paruthi, "International subcontracting: an approach to economic and technical co-operation among developing countries" (ID/WG.308/3). A new study entitled "Small and medium enterprises, some basic development issues", including an examination of sub-contracting, will be published by UNIDO in 1986.

<sup>16</sup>"Trade-related industrial collaboration between firms of developing countries and developed countries: forms and policy issues" (TD/B/C.2/212), chap. 1, B, "International subcontracting," para. 28. A detailed examination of sub-contracting in relation to certain developing countries is contained in *Industrial Subcontracting: a New Form of Investment* (Paris, Organization for Economic Co-operation and Development, 1980).

<sup>17</sup>The OECD study, which examines international sub-contracting in relation to Haiti, Morocco, Tunisia, Sri Lanka and the Caribbean does not mention legal difficulties arising out of contract practice.

<sup>18</sup>"Looking into the future, it may be hypothesized that the contractual forms which are likely to gain prominence in North-South relations will be those which at present prevail between firms of developed countries, irrespective of their economic and social systems i.e. specialization and co-production, co-marketing, joint activities in R and D, and like arrangements. Such forms are actually materializing, but readily available information is so inadequate that no opinion can be ventured as to their relative importance" (TD/B/C.2/212), chap. 1, C, "Trade-related industrial collaboration ...", para. 50.

form of transaction is regarded as a form of countertrade and it is suggested below (see section C) that a further examination of countertrade practices may be justified.

19. The conclusions of the present survey of contract practice may accordingly be summarized as follows. Certain forms of contracts for industrial co-operation do not at present appear to be of much significance in trade between enterprises of developed and developing countries. Other forms, while assuming some significance, do not appear to present legal problems of a scale which would justify the undertaking of work by the Commission.

20. In making a decision concerning work in this area, the Commission may also wish to consider the possible end-products of the work. It was suggested (A/CN.9/191) that it might be conceivable to elaborate general conditions to be recommended for use by parties to a particular category of contract. An example of this type of instrument is the General Conditions of Specialization and Co-operation in Production between Organizations of Member Countries of the Council for Mutual Economic Assistance (CMEA), approved in 1979 by the CMEA Executive Committee. These General Conditions consist of detailed rules regulating the type of industrial co-operation in question, and dealing, *inter alia*, with the rights and obligations of the parties (section IV), the responsibility of the parties (section V), claims (section VI), arbitration (section IX) and applicable law (section X).

21. It was also suggested that the work might lead to the formulation of model clauses on certain issues. Among the issues suggested were the interdependence of the constituent parts of industrial co-operation complexes, the effects of *force majeure*, the effects of changed circumstances, revision of contract, termination and rescission, applicable law and settlement of disputes.<sup>19</sup> Such model clauses would need to be accompanied by explanatory texts, and it is not certain that a single model clause on a particular issue would be appropriate for all the categories of industrial co-operation contracts. The production of either general conditions or model clauses would entail the commitment of considerable time and resources.

22. In the circumstances, it is suggested that the preferable course might be to defer work in this area for a further period until the need for work is more clearly established. The secretariat might be requested to survey the further development of industrial co-operation contracts in trade between developed and developing countries,<sup>20</sup> and to report to the Commission at a future

<sup>19</sup>A/CN.9/191, para. 139.

<sup>20</sup>This difficulty of obtaining adequate evidence of contract practice has been felt even by other organizations with a potentially greater capacity to gather information on trade practice. "What was said in Chapter I about sub-contracting applies equally to the state of information concerning other forms of collaboration: case studies are rare; such studies as exist usually follow different methodologies, which often makes international comparison and generalization virtually meaningless. What seems to be badly needed as a first step is a systematic inventory of collaboration arrangements as practised in a number of

session if in the view of the secretariat work in the area might usefully be undertaken.

### B. Joint Ventures

23. At some past sessions of the Working Group on the New International Economic Order and of the Commission, suggestions have been made that work should be undertaken in the field of joint ventures. The suggestion has sometimes been that the work should relate to the construction of industrial works undertaken by a joint venture. The suggestion at other times appears to be that work should be directed to the legal aspects of joint ventures in general.

#### 1. Construction of industrial works by joint ventures

24. A joint venture may be described as an association of two or more persons for the purpose of implementing a project and includes, in varying degrees, the pooling by the associated persons of financial resources or other assets, the sharing by them of the control and management of operations, and the sharing of the profits and losses of the venture.

25. In the context of the construction of industrial works, joint ventures are often undertaken for one of two purposes. First, two or more enterprises may combine as a joint venture to undertake as a contractor the construction of industrial works for a purchaser. Such a joint venture project is, therefore, limited to the construction of the works. It has been suggested above that work on joint ventures undertaken for this purpose appears to be unnecessary.<sup>21</sup> Second, a joint venture between two or more enterprises for the construction of an industrial works may also include joint operation and management of the works, marketing the products produced by the works, and sharing the profits and losses of the venture. Such a joint venture is frequently created between an enterprise from a developing country and an enterprise from a developed country.

26. Joint ventures of the second type are attractive because they tend to satisfy the usual needs of the two parties in relation to industrial projects. The partner to the association from the developing country often obtains from the developed country partner technology, management and marketing skills, and capital. The ownership of the works which is constructed is usually vested in the partner from the developing country. The partner from the developed country often obtains access to the developing country market, and sometimes obtains cost

selected countries. Conducted along uniform methodological lines, such an inventory should provide basic information about the principal forms of such arrangements, their growth, frequency and sectoral distribution, about how these arrangements work in particular sectors and industries and about the types of entities involved. The inventory should provide the basis for studying in depth selected categories of arrangements and for determining the conditions which could optimize their use by the developing countries." (TD/B/C.2/212, para. 118; "Trade-related industrial collaboration ...").

<sup>21</sup>"Trade-related industrial collaboration ...".

advantages and assured raw materials supply by production in a developing country. A joint venture may also be considered by a developed country enterprise when direct investment in a developing country is either not feasible or not attractive. The sharing of the risks of the venture stimulates each party to perform his obligations with diligence.

27. The suggestion has been made that the value of the Guide might be enhanced by including in it (possibly as an annex) a discussion of the contractual arrangements which may be entered into for the construction of industrial works under the latter type of joint venture. Differing contractual arrangements may be entered into, depending on such factors as the construction capabilities of the partners, the source of the design for the works, any mandatory legal regulations which are applicable in the country where the works is to be constructed, and the extent to which the joint venture partners can supply equipment and materials needed for the works. Another factor which may affect the contractual arrangements is whether the partners have established a body corporate in which they both have shareholdings for the purpose of implementing the joint venture project (usually called an equity joint venture), or whether their association is solely based on contractual arrangements (usually called a contractual joint venture).

28. Where neither party has construction capabilities, the construction will have to be entrusted to one or more third parties. The works contracts with those parties are usually entered into by the joint venture corporate body, if such a body has been created, or by one of the joint venture partners. If the design for the works has been supplied by the developed country partner, it may be convenient for him to enter into that contract, as the construction can more effectively be supervised by him. Mandatory laws in some developing countries provide that certain aspects of the construction (e.g. building and civil engineering) have to be entrusted to local contractors. Some of the equipment and materials may be supplied by one or both of the parties, if they can do so at lesser cost than outside sources. Whether a single contractor or more than one contractor is engaged, the contracts entered into with the third parties will be of the type dealt with in the Guide (see chapter II, "Choice of contracting approach").<sup>22</sup>

29. In some cases, one or both of the parties may have some construction capabilities which they wish to utilize. In particular, a foreign partner who supplies the design and technology for the works may also have the capability of constructing the works. In such cases it is usual for the joint venture corporate body, or for the developing country partner, to enter into a contract with the developed country partner for the construction of the works. The developed country partner may himself construct the whole works, or, while being responsible for the whole construction, he may construct only a portion

<sup>22</sup>These arrangements are also noted in *Manual on the Establishment of Industrial Joint-venture Agreements in Developing Countries* (United Nations publication, Sales No. E.71.II.B.23).

of the works and sub-contract with others for the construction of the remaining portions. The contract entered into with the developed country partner, however, will also be of the type dealt with in the Guide. Whether the developed country partner has entered into the construction contract with the joint venture corporate body, or with the developing country partner, the corporate body or the developing country partner will require contractual safeguards that the construction will be effected in time and without defects by the developed country partner.

30. It is possible that the content of some of the terms in the construction contract with the developed country partner may deviate from usual commercial practice because of the mutual confidence existing between the two contracting parties (e.g. the amounts of liquidated damages or penalties for delay may be lower, greater periods of time may be allowed for remedying defects). A more significant deviation may concern the payment conditions for the construction. Payment to the developed country partner may take the form, for example, of a grant to him of share capital in the joint venture corporate body. However, the nature of the great majority of the clauses included in the construction contract, and their functions, will remain the same as in a contract with a third party. The treatment of contract clauses in the Guide will accordingly remain relevant.

31. It would therefore appear that a purchaser from a developing country who undertakes the construction of industrial works in the context of a joint venture agreement will obtain sufficient guidance from the existing contents of the Guide, and that the addition of an annex dealing with construction by joint ventures may not be justified.

## 2. Legal aspects of joint ventures in general

32. In the earlier study by the Secretary-General (A/CN.9/191) it was stated that "The research by UNIDO appears to show that it is impossible to find any joint venture that could be called typical or serve as a prototype for other agreements. In view of this finding and taking into account the work already done, the Commission may wish to conclude that, for the time being, no work should be commenced on joint venture contracts."<sup>23</sup> This recommendation appears to be still applicable.<sup>24</sup>

<sup>23</sup>This conclusion is reinforced by a later UNCTAD study "Trade-related industrial collaboration ...". "The contractual joint ventures comprise a variety of *ad hoc* or more permanent arrangements with profit and risk sharing as the only common denominator" (para. 81); "Indications are that *the flexibility of contractual joint ventures, where according to the objectives of the partners virtually any rules can be adopted, will make this form increasingly attractive to firms from both developed and developing countries*" (para. 83) (emphasis added); "As regards the equity form of joint venture, it should be clearly understood that there is no uniform model, even within a given sector" (para. 84).

<sup>24</sup>In addition to the guides and manuals referred to in A/CN.9/191, UNIDO has since produced "Guidelines for the establishment of industrial joint ventures in developing countries" (UNIDO/IS.361). At its 1986 session in Arusha, United Republic of Tanzania, the Asian-African Legal Consultative Committee decided to undertake a detailed examination of joint ventures.

## C. Countertrade<sup>25</sup>

33. At its eleventh session (1978) the Commission, in its decision on its new programme of work, decided to include as a priority item the subject of international barter and exchange.<sup>26</sup> At its twelfth session the Commission had before it a report of the Secretary-General entitled "Barter or exchange in international trade".<sup>27</sup> The Commission was of the view that barter-like transactions took too many different forms to admit of regulation by means of uniform rules. However, it decided to request the secretariat to include in the studies then being conducted in respect of contract practices consideration of clauses of particular importance in barter-like transactions. The Commission also requested the secretariat to approach other organizations within the United Nations engaged in studies on such transactions, and to report to it on the work being undertaken by those organizations.<sup>28</sup>

34. At its seventeenth session (1984) the Commission had before it a report of the Secretary-General entitled "Current activities of international organizations in the field of barter and barter-like transactions".<sup>29</sup> A number of delegations stated that they attached great importance to that subject, and that further consideration of it would be useful. It was agreed that, in the light of a report to be submitted by the secretariat at a future session on the developments in the field, the Commission might consider whether concrete steps in the field should be undertaken by it.<sup>30</sup>

35. There is no agreed definition of countertrade. The following types of transactions are, however, generally regarded as being forms of countertrade, although the terminology used below to describe the transactions is not universally adopted:

(a) *Compensation*: a transaction in which there is a direct exchange of goods between the parties. The goods may be of approximately equal value, with no payment of money by the parties involved. A transaction of this form is often called barter, or full compensation. In some cases, the goods to be supplied by each party are not of equal value, and the party supplying goods of lesser value makes good the difference in value by payment of money. This is sometimes referred to as partial compensation.

<sup>25</sup>In various reports submitted to the Commission, the subject has been referred to as international barter or exchange, or barter and barter-like transactions. At present the term countertrade is current in international usage.

<sup>26</sup>Report of the United Nations Commission on International Trade Law on the work of its eleventh session, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17 (A/33/17)*, paras. 67-69.

<sup>27</sup>A/CN.9/159.

<sup>28</sup>Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17 (A/34/17)*, paras. 21 and 22.

<sup>29</sup>A/CN.9/253.

<sup>30</sup>Report of the United Nations Commission on International Trade Law on the work of its seventeenth session, *Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 17 (A/39/17)*, para. 132.

Such a compensation transaction is generally reflected in a single contract. Compensation may sometimes involve more than two parties. Thus two contracts which are inter-linked may be entered into under which A in country X is to supply goods to B in country Y, and in return C in country Y is to supply goods to D in country X;

(b) *Counterpurchase*: a transaction between two parties under which the first party agrees to purchase goods of a certain value from the second, and in return the second agrees to counterpurchase goods of a certain value from the first. On their face the two contracts usually appear to be independent, the interdependence of the two purchases being created and defined by a third agreement between the parties (often called a protocol). Each transaction is settled in money. One of the principal objects of this form of transaction is to balance the expenditures of convertible currency on each side. It is usually provided that the counterpurchase obligation can be discharged by the person obligated arranging for a purchase by a third party. If the value of the counterpurchase is less than the value of the purchase, the difference in value is made good by the payment of money;

(c) *Buy-back agreement*: a transaction in which plant and production lines are supplied by one party to the other, to be paid for with products resulting from the operation of the plant. The transaction is usually reflected in a single long-term contract.

36. Other types of transactions are also sometimes included in discussions of countertrade. Two countries sometimes enter into an intergovernmental clearing agreement under which goods supplied by each country to the other are not paid for, but valued in a specified unit of account. At an agreed time a balance is struck between the values of the supplies, with the debtor country having to make good the imbalance. This system is sometimes referred to as countertrade under clearing arrangements. In some cases the country which is the creditor or debtor at the time the balance is struck may unofficially use a third party to make good the imbalance. The third party will purchase goods from the debtor country, and remit the proceeds to the creditor country. This type of dealing is sometimes referred to as switch trading.

37. Opinions differ widely on the proportion of international trade which is based on countertrade. It would appear, however, that the number of developing countries engaging in countertrade with developed countries has increased over the past few years.<sup>31</sup> On the part of developing countries, this increase has been motivated by

a variety of reasons: shortages of convertible currency to finance imports in the traditional manner, a desire to sell non-traditional products through the use of a developed country partner's marketing skill by nominating these products as goods to be taken in countertrade, a perception of countertrade as a means of obtaining a reliable and long-term market for primary commodities which are nominated as goods to be taken in countertrade, and a desire to obtain a competitive advantage over other suppliers of a commodity by requiring purchases of the commodity as the price for certain imports. Enterprises from developed countries are usually motivated to countertrade because certain exports are only possible if it is agreed that payment is to be in countertraded products. In addition, if there is strong competition for the award of a particularly advantageous contract, an enterprise may offer a countertrade commitment to obtain a competitive advantage. There also appears to be some amount of countertrade between developing countries.

38. The increase in countertrade activities has also resulted in institutional, commercial and legal developments. In some developed countries, institutions have been created both by governments and the private commercial sector which, while they do not engage in countertrade, give advice and information to traders wishing to enter into countertrade transactions. In a few cases, the institutions go beyond providing information and advice, and assist enterprises in concluding countertrade transactions (e.g. by finding buyers for goods offered in countertrade).<sup>32</sup> In addition, trading houses have grown with special interests and expertise in countertrade. They are willing to find buyers for products offered in countertrade, advise on financing, and thus facilitate the conclusion of countertrade transactions. In a few developing countries, there has been some degree of governmental intervention in the field of countertrade (e.g. through regulations providing that certain types of imports may be paid for only through countertraded products or prohibiting the offer of certain products in countertrade, or through administrative instructions to government state trading agencies to explore the possibility of countertrade when negotiating certain types of contract).

39. Among international organizations, work has continued on countertrade in the Economic Commission for Europe (ECE).<sup>33</sup> As a further step in this work, the secretariat of the ECE has proposed to the ECE Group of Experts on International Contract Practices in Industry the preparation of a guide on the drafting of contracts for

<sup>31</sup>See *Countertrade: Developing Country Practices* (Paris, Organization for Economic Co-operation and Development, 1985); *Primary Commodities: Countertrade and Co-operation Among Developing Countries* (Yugoslavia, Research Centre for Co-operation with Developing Countries, 1984); Jones, *op. cit.*; "International Workshop on Countertrade" (see note 9, above). The secretariat of the Economic and Social Commission for Asia and the Pacific has noted that it is exploring modalities to expand trade, such as the use of positive aspects of countertrade and other compensatory arrangements (E/ESCAP/TRADE/MMT/L.1, 14 March 1986).

<sup>32</sup>"Short-term compensation transactions in East-West trade: Institutional measures designed to assist exporters with countertrade obligations in some countries of the ECE region" (TRADE/R.499/Add.1).

<sup>33</sup>Since the date of the survey of the work of other organizations contained in "Current activities of international organizations in the field of barter and barter-like transactions" (A/CN.9/253), the following studies have been prepared by the ECE secretariat, "Short-term compensation transactions in East-West trade" (TRADE/R.499); "Institutional measures designed to assist exporters with countertrade obligations in some countries of the ECE region" (TRADE/R.499/Add.1); "Contractual features of countertrade transactions in East-West trade" (TRADE/GE.1/R.33/Add.1).

compensation transactions in East-West trade.<sup>34</sup> It was suggested that the guide could consist essentially in the following:

“(a) A comprehensive statement of the types of contracts and contractual clauses used in various forms of compensation transactions.

“(b) Indications of “best-practice” contractual provisions employed to avoid or overcome difficulties liable to arise in compensation trade.

“(c) Guidance on the provisions, both in substance and in form, which international experience suggests it is desirable to include in compensation contracts, differentiated as to type.”

A decision on this proposal was deferred by the Group of Experts to its twenty-eighth session (21–23 July 1986), and the ECE secretariat was requested to prepare a fresh note dealing with the legal aspects of compensation transactions.<sup>35</sup>

40. In its previous report, the UNCITRAL secretariat expressed the view that most of the studies on the subject of countertrade tend to indicate that problems encountered in such transactions were far more economic and financial than legal. Nevertheless, the report identified certain contract clauses which needed to be carefully drafted in order to give business efficacy to the transaction and to avoid disputes between the parties. These were clauses specifying the nature, quality and price of the goods to be offered for counterpurchase, clauses permitting assignment of counterpurchase obligations, penalty clauses for failures of performance by either party, and agreements defining the nature of the interdependence between the obligations of the two parties in countertrade transactions. The work done by the ECE has drawn attention to other contract clauses of importance included in countertrade transactions: clauses defining methods of price revision when deliveries are to occur over a long period, clauses giving the initial exporter the right to fulfil his countertrade obligations by purchase from a person other than the party to the export contract, clauses restricting markets in which goods which are counter-purchased may be sold, clauses specifying fulfilment schedules for a countertrade commitment, clauses defining payment conditions, clauses providing how proof of the fulfilment of countertrade obligations may be obtained (e.g. letters of release), clauses providing for performance guarantees from either party, and termination clauses. Other clauses which have been referred to are exemption clauses, choice of law clauses, and clauses providing for the settlement of disputes.

41. The main sources of information on countertrade at present available to the secretariat consist of published

material.<sup>36</sup> On the basis of this material, it is difficult to be certain as to the extent to which work directed to legal issues would be useful, or to determine the most useful form which such work might take. A consideration which supports the undertaking of work is that some informed circles believe that even among enterprises engaged in East-West trade, where countertrade has been a regular feature for a number of years, there is a need for a survey and analysis of contract practice and legal issues. Such a need would be much greater in relation to developing countries. As against this, it may be noted that many of the clauses referred to above are commonly used in international transactions, and their drafting in the setting of a countertrade transaction may not present very serious difficulties. Furthermore, it is not apparent that North-South countertrade contains contract structures or legal issues which are not present in East-West countertrade. The information and analysis that has developed over the years in relation to East-West trade may be useful to enterprises engaged in North-South trade. However, the extent to which this information and analysis is readily available in developing countries is uncertain. On balance, it appears probable that work by the Commission on legal issues arising in countertrade arrangements would be of benefit to developing countries.

42. If the Commission is of the view that work might be undertaken on countertrade, it may wish as a first step to request the secretariat to undertake a survey of contractual provisions occurring in countertrade arrangements, and of legal difficulties arising in relation to such provisions. The survey would be directed, in particular, to ascertaining the legal difficulties facing developing countries engaged in countertrade, and the possible means of alleviating their difficulties. In view of the absence in developing countries of information on and analysis of countertrade practices, the survey is likely to be in itself of great value. Further work may take the form of the preparation of a legal guide or the drafting of a model law, if the survey shows that work of this kind is feasible and will be useful.

43. The work proposed in the previous paragraph closely resembles that proposed in relation to East-West countertrade by the secretariat of the ECE to the ECE Group of Experts on International Contract Practices in Industry (see paragraph 39, above). If at its forthcoming twenty-eighth session (21–23 July 1986) the ECE Group of Experts decides to proceed with the work proposed to it, inter-secretariat consultations can be held to establish

<sup>34</sup>“Proposal for a guide on the drafting of compensation contracts in east-west trade” (TRADE/GE.1/R.33). The proposal was made to the twenty-seventh session of the Group, Geneva, 9–11 December 1985.

<sup>35</sup>Report of the twenty-seventh session (TRADE/GE.1/67), para. 16. The fresh note is contained in document TRADE/GE.1/R.34.

<sup>36</sup>The published work on countertrade cannot be easily divided into literature dealing with commercial issues and literature dealing with legal issues. The secretariat has found very few articles on countertrade in legal journals. There is a very large volume of articles and notes in commercial journals published in North America, West Europe and East Europe. It is probable that very little of this literature is available in developing countries. The documents of the ECE may be more readily available, though readers in developing countries may be inhibited from studying them by their overt orientation to East-West trade. The report of the “International Workshop on Countertrade” (see note 9, above) states “The dearth of information on countertrade practices and requirements in developing countries was a widely felt problem”.

co-ordination. Collaboration with other interested international organizations,<sup>37</sup> and with commercial organizations engaged in countertrade, would also be needed.

## D. Procurement

### 1. Introduction

44. The term procurement has no universally agreed meaning. It is sometimes regarded as one segment within a wider process known as supply management.<sup>38</sup> It is usual to apply the term to procedures for the purchase of goods and services on a commercial scale by governments, government entities, or private enterprises, and the term is sometimes used to include activities which occur after the conclusion of a contract. For example, the functional scope of procurement has been said to cover:

“(a) Specification of the kind and quantity of goods or services to be acquired;

“(b) Investigation of the market for supply, and contacts with potential suppliers;

“(c) Placing the order or contract, including negotiation of terms;

“(d) Supervising delivery and performance;

“(e) Taking necessary action in the event of inadequate performance;

“(f) Payment; and

“(g) Dealing with disputes.”<sup>39</sup>

45. Generally, however, the term procurement is used to cover only items (a), (b) and (c) above, and the present study considers procurement in that restricted meaning. In traditional legal terms, the area considered is that of the formation of contract. Suggestions have been made during past sessions of the Working Group on the New International Economic Order that work should be undertaken in this area.

### 2. Approaches to procurement

46. The international procurement of goods and services forms a necessary part of most industrial development projects undertaken by developing countries. An

<sup>37</sup>The secretariat has been informed by the International Centre for Public Enterprises in Developing Countries, Ljubljana, that the Centre has under study a survey of contract practice with specific reference to buy-back transactions. A study on the economics of buy-back has also been produced by UNIDO “Buy-back financing of international sales of factories” (UNIDO/EX.99).

<sup>38</sup>See *Supply Management. Towards Better Use of Equipment and Material Resources in Developing Countries* (United Nations publication, Sales No.78.II.H.5). This publication regards supply management as including supply policy and planning; procurement planning and standardization; purchasing; inventory control; shipping and parts administration; storage, distribution and maintenance; and usage and disposal.

<sup>39</sup>Gösta Westring, *International Procurement. A Training Manual* (International Trade Centre UNCTAD/GATT; UNITAR; World Bank, 1985), part A.1.1.

efficient procurement procedure leading to the selection of the most economical responsive supplier is of cardinal importance to the success of a project. In relation to the construction of industrial works the view is sometimes expressed that the selection of the appropriate supplier is as important as the drafting of an effective works contract, since with such a selection the possibility of difficulties arising during project implementation leading to legal conflicts between the parties is significantly reduced.

47. Because of its importance, procurement has been often examined from different but sometimes overlapping viewpoints. Many industrial development projects in developing countries are financed by international lending agencies (ILAs), of which the leading agency is the World Bank. ILAs wish to ensure that procurement with the use of money lent by them is used in accordance with certain policies. These policies are set forth in guidelines for procurement issued by the various ILAs,<sup>40</sup> and the policies are also embodied in the loan agreement between ILAs and borrowers.

48. Many ILAs have the following policy objectives: securing economy and efficiency in the procurement process; giving the widest range of suppliers an opportunity to compete on equal terms for the supply of the goods and services required; and, as development institutions, encouraging the growth of suppliers from the borrower's country. Some ILAs provide that in certain circumstances the goods or services to be procured should be supplied from, or purchased in, member countries of the ILA. These policies are reflected in the procurement procedures required by the ILAs. In particular, almost all ILAs require that international competitive tendering be followed as the norm for procurement.

49. International procurement by government agencies was also considered during the Tokyo round of multilateral trade negotiations in the framework of the General Agreement on Tariffs and Trade (GATT). During those discussions, it was recognized that there was a “need to establish an agreed international framework of rights and obligations with respect to laws, regulations, procedures and practices regarding government procurement with a view to achieving greater liberalization and expansion of world trade and improving the international framework for the conduct of world trade”.<sup>41</sup> The discussions led to

<sup>40</sup>See, for example, *Guidelines for Procurement under International Bank for Reconstruction and Development Loans and International Development Agency credits* (1984); *Guidelines for procurement of goods and construction services under Inter-American Development Bank loans* (1982); *Guidelines for procurement under Asian Development Bank loans* (1981); *Guidelines for procurement under loans extended by the Organization of Petroleum Exporting Countries Fund for International Development* (1982); *Rules of procedure for the procurement of goods and services by borrowers from the African Development Fund* (1976); *Guidelines for the borrower on procurement of goods and services and technical reporting requirements of the Saudi Fund for Development* (1979). There has also been published *Procurement of goods, Sample bidding documents* (1983) and *Procurement of works, Sample bidding documents* (1985), by the Inter-American Development Bank and the World Bank.

<sup>41</sup>Preamble to the Agreement on Government Procurement, Geneva, 12 April 1979.

the adoption of the GATT "Agreement on Government Procurement" (hereafter referred to as "the Agreement"). The Agreement is applicable to the procurement of products, but also applies to the procurement of services incidental to the supply of products if the value of these incidental services does not exceed that of the products themselves. The Agreement is not, however, applicable to service contracts *per se*. For the Agreement to be applicable to a procurement contract the goods and services to be procured must have a value of SDR 150,000 or more.<sup>42</sup> One of the main objectives of the Agreement is that in procurement by a government which is a party to the Agreement, products or suppliers of other parties to the Agreement should not be discriminated against,<sup>43</sup> while another is to provide for the transparency of laws, regulations, procedures and practices regarding government procurement. The Agreement also provides that in the implementation and administration of the Agreement, the parties thereto should take into account the developmental, financial and trade needs of developing countries, and it contains several provisions directed to this end.<sup>44</sup> The Agreement favours optimum effective international competition in tendering procedures, and contains detailed rules to be observed in those procedures.<sup>45</sup>

50. The European Economic Community (EEC) has considered procurement from the standpoint of the economic integration of the Community countries. "The free movement of goods and services between the Member States of the European Community is one of the fundamental principles of the Treaty of Rome establishing the Community. Public supplies must therefore also be assured of the same freedom of movement, even if their administration is subject to special procedures. It is therefore essential to co-ordinate these procedures and make them 'transparent' in order to ensure that suppliers are guaranteed full information and equal treatment in tendering for such contracts. This will also help to eliminate such barriers to freedom of movement as the exclusion of non-national tenders, and to promote genuine competition in Europe".<sup>46</sup>

51. Many countries, including some developing countries, have laws regulating government procurement. These laws have various objectives, for example, securing

<sup>42</sup>Article 1, 1(a).

<sup>43</sup>The Agreement does not apply to all government procurement, but only to procurement by a governmental entity which the government in question has listed in an annex to the Agreement.

<sup>44</sup>Article III.

<sup>45</sup>Article V.

<sup>46</sup>*Public Supply Contracts in the European Community* (Brussels, Office for Official Publications of the European Communities, 1982), sect. 2. The policies expressed in this passage have been given effect to by Council Directive of 26 July 1971 concerning the co-ordination of procedures for the award of public contracts (*Official Journal of the European Communities*, No. 11, 1971), and Council Directive of 21 December 1976 co-ordinating procedures for the award of public supply contracts (*Official Journal of the European Communities*, Nos. 20, and L13). The EEC is a party to the GATT Agreement, as are the individual member States of the EEC.

a wide choice of suppliers, the observance of fairness in the selection process, conformity with other government rules and regulations (e.g. regulating the expenditures of foreign exchange, or financial accountability), and the conferment of preferences on national tenderers.

### 3. Nature of procurement law

52. Procurement laws and regulations are drafted to reflect a variety of policy choices. A requirement that, absent very exceptional circumstances, procurement must be on the basis of international competitive tendering reflects a policy that the purchasing entity's interests are best served by having the widest possible choice of suppliers. A requirement that advertising of invitations to tender should be on a global basis giving all potential readers of the advertisement an approximately equal time to submit tenders reflects a desire to confer equality of opportunity on tenderers. The requirement that a certain margin of preference is to be given to tenderers from the country of the purchasing entity reflects a policy fostering local industry. A requirement that tenders must be opened in public reflects a policy that publicity is a safeguard against unfair practices in the award of tenders. The range of policy issues involved is wide, and within major policy issues are sometimes to be found what may be termed sub-issues: on one view, after tenders have been submitted on the basis of international invitations to tender stating the criteria for award, no negotiations should be conducted with tenderers after the opening of tenders, and the contract should then be awarded to the tenderer who has submitted the lowest responsive tender as judged in accordance with the stated criteria. On another view, negotiations are permissible after the opening of tenders, since negotiations with responsive tenderers may lead to further advantageous terms being offered to the purchasing entity.

53. Procurement laws and regulations also reflect the essentially procedural character of procurement, and contain requirements which are needed for the orderly carrying out of the procurement process. For example, they contain requirements as to the form in which tenders have to be submitted, the number of copies of tenders to be submitted, the time for the opening of tenders, and the procedure to be followed at the opening. Such rules will have little policy content. Other procedural rules, however, may reflect an overall concern with efficiency or fairness in the procurement process, e.g. a rule that, after the opening of tenders, each page of each tender is to be initialled by the opening authority to prevent subsequent tampering.

54. While procurement laws and regulations govern specific aspects of procurement procedures, these procedures also operate within the framework of an applicable legal system. This will usually be the legal system of the country of the purchasing entity. That legal system may impose obligations of good faith during negotiations, determine the extent to which a tender may be revoked or amended, or the point of time at which a contract is

concluded between the tenderer and the purchasing entity.

55. An examination of the legal rules regulating procurement in a sample selection of developing countries reveals a varied picture. Some countries have procurement rules which have historically formed part of the system of law prevailing in that country, while in others the rules are recent developments. Some countries have rules with detailed provisions covering many procedural aspects, others have rules only dealing with a few elements of tendering procedures and leaving considerable discretion to the procurement entity in the manner of administering the procedures, while yet others do not appear to have any rules. In the latter countries, the procurement procedure appears to be devised on an *ad hoc* basis when an individual case for procurement arises. Many countries have a tradition of awarding high value contracts on the basis of competitive tendering, but a few have a preference for award on the basis of negotiation alone, or on the basis of a combination of tendering and negotiation. The general impression gained is that the procurement rules and practices are compounded of rules contained in inherited legal traditions and of the commonly understood elements of the competitive tendering process.<sup>47</sup> The Agreement has up to date been accepted by very few developing countries.<sup>48</sup>

#### 4. Possible work

56. In view of the importance of the subject to developing countries, it is suggested that the Commission should undertake work on procurement. This work might be conducted in two stages. The first stage might consist of a study of the major issues arising in procurement. Major issues to be considered would include the choice of procurement methods by a purchasing entity, the documents to be prepared to implement a particular method, issues connected with the submission of tenders (including the obligations of the parties after a tender has been submitted), legal issues related to the evaluation of tenders, and the conclusion of a contract based on an award. In examining the issues, the study might include descriptions of commonly used procedures, articulate policies in favour of and against particular procedures, and, to the extent possible, describe how the issues are dealt with in the procurement rules and practices of developing countries. Such a study would be valuable in informing governments and government entities of relevant policy considerations, and would enable them to reassess the adequacy of their rules and practices.

57. In regard to areas of procurement to be dealt with, the study might focus on the procurement of various types

<sup>47</sup>One authority has remarked: "It has been difficult to find any up-to-date studies showing what methods of procurement are applied in developing countries" (Westring, *op. cit.*, sect. A.2.3.2.).

<sup>48</sup>It may be remembered that in any event the Agreement applies only to the procurement of products and services incidental to the supply of products.

of industrial works and infrastructural projects and public facilities such as harbours and hospitals. This focus would be justified by the importance of such projects for developing countries. Whether the procurement of goods alone could also be conveniently covered in the study might be left for investigation by the secretariat.

58. As a second stage of the work, and depending on the extent of the need revealed by the study, the work might develop into the formulation of rules regulating procurement. Such rules could be models for governments, government entities and private enterprises in developing countries in formulating rules appropriate to their needs.

59. The secretariat has already undertaken some research in the area of procurement for the purpose of drafting the chapter dealing with the conclusion of a works contract in the Guide.<sup>49</sup> The secretariat is of the view that it would be undesirable to expand the scope of that chapter to encompass a study of the kind described in the previous paragraph. The study envisaged above would differ in approach from that adopted in a draft chapter of the Guide, in that a draft chapter is primarily directed to advising a purchaser of industrial works in regard to drafting. Furthermore, the particular draft chapter would need to be expanded to an extent which would result in an imbalance between that chapter and other draft chapters of the Guide. In addition, the further research on procurement needed to accomplish the objectives set forth in the previous paragraph would delay the completion of the Guide. It may be noted, however, that the fact that materials on procurement have already been collected by the secretariat in connection with the work on the Guide would enable it to commence work on this subject immediately following the completion of work on the Guide.

## II. Conclusions as to future work

60. The conclusions reached in the present Note as to future work in the area of the new international economic order may be summarized as follows. With regard to contracts for industrial co-operation (section A, above), it is suggested that work be deferred till the need for it is more clearly established (paragraphs 18–21 above). With regard to joint ventures (section B, above), it is suggested that where an enterprise from a developing country has combined with an enterprise from a developed country in a joint venture whose objects include the construction of industrial works, the Guide will provide sufficient assistance to the enterprise from the developing country (paragraphs 27–30 above). In regard to the legal aspects of joint ventures in general, it is noted that the forms of

<sup>49</sup>Chapter III, "Procedure for concluding contract".



joint venture agreements are very different and that accordingly it is difficult to envisage work which the Commission can usefully undertake in this area (paragraph 31, above).

61. It is noted that at present countertrade (section C, above) forms an increased part of the trade of many developing countries, and it is suggested that work might

be undertaken to ascertain and resolve legal difficulties experienced by developing countries in this area (paragraph 41, above). It is also noted that procurement (section D, above) is an area of great importance to developing countries, and that a study of major issues arising in procurement might be beneficial. This study might be followed at a later stage by the drafting of model rules regulating procurement (paragraphs 55–58, above).

### III. LIABILITY OF OPERATORS OF TRANSPORT TERMINALS

#### A. Report of the Working Group on International Contract Practices on the work of its ninth session (New York, 6–17 January 1987) (A/CN.9/275)

[Original: English]

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## INTRODUCTION

1. At its sixteenth session in 1983, the Commission decided to include the topic of liability of operators of transport terminals in its programme of work, to request the International Institute for the Unification of Private Law (UNIDROIT) to transmit its preliminary draft Convention on that topic to the Commission for its consideration, and to assign work on the preparation of uniform rules on the topic to a working group. The Commission deferred to its seventeenth session the decision on the composition of the working group.<sup>1</sup>

2. In response to the request made at the sixteenth session, UNIDROIT transmitted its preliminary draft Convention to the Commission. At its seventeenth session in 1984, the Commission decided to assign to its Working Group on International Contract Practices the task of formulating uniform legal rules on the subject. It further decided that the mandate of the Working Group should be to base its work on the UNIDROIT preliminary draft Convention and the Explanatory Report thereto prepared by the secretariat of UNIDROIT, and on the study of the UNCITRAL secretariat on major issues arising from the UNIDROIT preliminary draft Convention, which was before the Commission at its seventeenth session (document A/CN.9/252), and that the Working Group should also consider issues not dealt with in the UNIDROIT preliminary draft Convention, as well as any other issues which it considered to be relevant.<sup>2</sup>

3. At its eighth session, the Working Group engaged in a comprehensive consideration of issues arising in connection with the liability of operators of transport terminals in preparation for its formulation of detailed uniform rules (document A/CN.9/260). It decided to postpone its decision on the form in which the rules should be cast until after it had established the substance and content of the rules (*ibid.*, para. 13).

4. The Working Group consists of all 36 States members of the Commission: Algeria, Australia, Austria, Brazil, Central African Republic, China, Cuba, Cyprus, Czechoslovakia, Egypt, France, German Democratic Republic, Germany, Federal Republic of, Guatemala, Hungary, India, Iraq, Italy, Japan, Kenya, Mexico, Nigeria, Peru, Philippines, Senegal, Sierra Leone, Singapore, Spain, Sweden, Trinidad and Tobago, Uganda, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland, United Republic of Tanzania, United States of America and Yugoslavia.

5. The Working Group held its ninth session in New York from 6 to 17 January 1986. All members were

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its sixteenth session, *Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17 (A/38/17)*, para. 115.

<sup>2</sup>Report of the United Nations Commission on International Trade Law on the work of its seventeenth session, *Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 17 (A/39/17)*, para. 113.

represented except Central African Republic, Cyprus, Guatemala, Nigeria, Senegal, Singapore, Uganda and United Republic of Tanzania.

6. The session was attended by observers from the following States: Argentina, Canada, Fiji, Greece, Holy See, Lesotho, Netherlands, Oman, Pakistan, Republic of Korea, Switzerland and Turkey.

7. The session was also attended by observers from the following international organizations:

- (a) *United Nations organs*  
United Nations Conference on Trade and Development (UNCTAD)
- (b) *Intergovernmental organizations*  
Central Commission for the Navigation of the Rhine  
Hague Conference on Private International Law  
International Institute for the Unification of Private Law (UNIDROIT)  
Organization of African Unity (OAU)
- (c) *International non-governmental organizations*  
International Air Transport Association (IATA)  
International Association of Ports and Harbors  
International Chamber of Commerce (ICC)  
International Forest Products Transport Association  
International Maritime Committee (Comité maritime international, CMI)

8. The Working Group elected the following officers:

*Chairman:* Mr. Michael Joachim Bonell (Italy)

*Vice-Chairman:* Mr. Krister Thelin (Sweden)

*Rapporteur:* Mr. Kuchibhotla Venkatramiah (India).

9. The following documents were placed before the session:

- (a) Provisional agenda (A/CN.9/WG.II/WP.54);
- (b) Liability of operators of transport terminals: certain factual and legal aspects of operations performed by operators of transport terminals, note by the secretariat (A/CN.9/WG.II/WP.55);
- (c) Liability of operators of transport terminals: draft articles of uniform rules on the liability of operators of transport terminals and comments thereon, note by the secretariat (A/CN.9/WG.II/WP.56).

10. The following documents were also made available at the session:

- (a) Co-ordination of work: some recent developments in the field of international transport of goods, report of the Secretary-General (A/CN.9/236);
- (b) Liability of operators of transport terminals, report of the Secretary-General (A/CN.9/252);

- (c) Liability of operators of transport terminals: issues for discussion by the Working Group, note by the secretariat (A/CN.9/WG.II/WP.52 and Add.1);
- (d) Liability of operators of transport terminals: additional issues for discussion by the Working Group, note by the secretariat (A/CN.9/WG.II/WP.53).

11. The Working Group adopted the following agenda:

- (a) Election of officers;
- (b) Adoption of the agenda;
- (c) Formulation of uniform legal rules on the liability of operators of transport terminals;
- (d) Other business;
- (e) Adoption of the report.

## DELIBERATIONS AND DECISIONS

### I. Method of work

12. The Working Group agreed that the present session would be devoted to crystallizing the significant issues emerging from the draft articles of uniform rules on the liability of operators of transport terminals, which had been prepared by the secretariat (A/CN.9/WG.II/WP.56) (hereinafter referred to as the "secretariat draft"), and attempting to agree on texts of draft articles containing, where appropriate, alternative provisions, to serve as a basis for consultations by delegations with relevant circles within their countries and for the further work of the Working Group. It was agreed that the final choice among alternative provisions of the draft articles and the precise drafting of the draft articles would be left for a future session. The Working Group recalled its decision at its previous session to decide upon the form in which the uniform rules should be adopted after it had established the substance and content of the rules.

13. The Working Group engaged in an initial discussion of the secretariat draft. It then convened an informal working party and assigned to it the task of synthesizing the views expressed during that discussion into draft articles containing, where appropriate, alternative provisions. The informal working party prepared texts for draft articles 1, 2, 3 and 4, which were then reviewed by the Working Group.

14. The texts of draft articles 1, 2, 3 and 4 proposed by the informal working party are reproduced in chapter II of this report after the report of the substantive discussion by the Working Group with respect to draft articles 1, 2, 3 and 4, respectively, of the secretariat draft. The Working Group considered the texts proposed by the informal working party to be a good basis for further consultations and for the future work of the Working Group. For guidance in consideration of the texts, the Working Group agreed that at the end of each text notes should be

added incorporating comments made at the meetings of the informal working party, as amended by the Working Group. The notes are reproduced in chapter II of this report after the texts of the draft articles to which they relate.

## II. Consideration of draft articles of uniform rules on the liability of operators of transport terminals

15. The following paragraphs reflect the substance of the discussion with respect to each of the draft articles.

### Article 1

#### A. Text proposed by Secretariat

16. It was generally agreed that the terminology used to refer to the various concepts incorporated in the article should be clear and consistent, and that attention should be paid to possible difficulties in translating terms into various languages. A view was expressed that the definition of "operator" in paragraph (1) should be simple, since a definition which was too detailed could inadvertently exclude entities which should be covered.

#### Paragraph (1)(a)

17. A view was expressed that the categories of operators to be governed by the uniform rules should not depend upon the existence of a contractual relationship between the operator and his customer. In that connection it was observed that in some legal systems a person could assume obligations with respect to goods by taking them in his charge, and a contract was not necessary in order for those obligations to come into existence. It was accordingly suggested that the word "engaged" in paragraph (1)(a) should be avoided, and that the paragraph should refer to an "undertaking" to perform operations with respect to goods by agreement or by taking them in charge. According to another suggestion, it was not necessary to state the way in which the undertaking could be given (i.e. by agreement or by taking the goods in charge).

18. The Working Group considered the words "against remuneration" appearing in paragraph (1)(a). According to one view the words should be deleted. In that connection it was observed that operators who unloaded goods for a customer often stored the goods for a period of time without further charge to the customer (this practice is sometimes referred to as "free time"). There was a danger that a court might regard storage during "free time" as not being "against remuneration", thus excluding that storage from the scope of the uniform rules. According to another view, the words "against remuneration" should be retained. A third view was that instead of "against remuneration" the definition of "operator" should contain the notion that the operator was one who performed terminal operations as a "commercial" activity. The prevailing view was that a formulation should be used in the definition of "operator" which

expressed the idea that the rules would apply to entities who were engaged in the business or activity of providing transport-related services, without dealing with the question of whether particular operations were remunerated.

19. A view was expressed that the definition of "operator" should not contain a reference to services performed "during" carriage, in order to avoid the implication that the rules were intended to apply to a carrier while he was responsible for the goods as a carrier under an international transport convention or national law. The prevailing view, however, was that the word "during" should be retained if the words "before" and "after" carriage were included. In that regard it was noted that the unloading and taking in charge of goods by an operator between two stages of carriage might be regarded as occurring "during" carriage, and retention of the word "during" would ensure that the rules applied to the operator in such a case. It was suggested that an implication that the uniform rules were intended to apply to a carrier while he was responsible for the goods in his capacity as a carrier could be avoided by other means, e.g. by including the phrase "acting in a capacity other than that of a carrier" or a provision such as paragraph (1)(b) of article 1 of the secretariat draft (see paragraph 25, below), or by a provision such as article 15 of the secretariat draft.

20. It was questioned whether the words "with a view to handing the goods over to any person entitled to take delivery of them", which appeared in article 1(1)(a) of the secretariat draft, were necessary. A view was expressed that those words would exclude the situation where the operator was the final destination of the goods, and would emphasize the nature of the operators contemplated by the uniform rules. It was generally agreed, however, that the words were unnecessary, since an operator would always take the goods in charge with a view to handing them over to someone else.

21. The Working Group considered the questions of the types of operations and the types of operators which should be covered by the uniform rules and how those operations should be referred to in the definition of an operator. A view was expressed that the application of the uniform rules should not be limited to purely storage operations, since such a limitation would not accord with modern transport practices, particularly in the case of container terminals, in which the operator's function was to act as an interface in the transfer of goods between two means of transport or between the consignor or consignee and the means of transport. Storage might be involved in that function, but it was not always the primary function of the operator; other handling operations were often equally or more important.

22. It was generally agreed that the uniform rules should not apply in the case of stevedores, airport cargo handlers or similar entities who were engaged by terminal operators only to unload the goods, carry them into or through the terminal and load them on to a means of transport, where those entities did not exercise care,

custody and control over the goods. On the other hand, a view was expressed that the uniform rules should apply to those entities if they did exercise care, custody and control over the goods. It was also generally agreed that the uniform rules should not apply to an entity, such as a public port authority, who leased facilities within the terminal area to other entities, but who did not take the goods in charge, or assume responsibility for the goods other than providing security for the area. An additional view was expressed that the uniform rules should cover the storage of goods in a bonded customs warehouse. A further view was that they should not cover the long-term storage of goods, as in the case of a distribution centre, and that they should not cover salvors.

23. A view was expressed that an appropriate delimitation of the scope of application of the uniform rules could be achieved by having the rules apply only when "safekeeping" was included as an essential element among the operations undertaken by the operator. It was generally agreed that the application of the uniform rules should not depend upon whether "safekeeping" was a primary operation or performed ancillary to other operations. According to another view, however, it was questioned whether the uniform rules should use the word "safekeeping". It was not clear what was meant by that word, and, if it was used, it might have to be defined, as had been done in the secretariat draft (see, also, paragraph 26, below). In that connection a suggestion was made that rather than the term "safekeeping", another formulation might be used to indicate the essential element which was required for the rules to apply. A suggestion was made that the phrase "care, custody and control over the goods" might be used. However, in that connection it was suggested that the word "care" should not be used, because in some legal systems using the word could be interpreted as enabling an operator to avoid the application of the uniform rules by contractually excluding his duty of care with respect to the goods. On the other hand, a view was expressed that from the economic point of view it might be attractive for the customer to have the opportunity to choose between a liability system based on presumed fault, as provided for in the secretariat draft, and a less costly liability system under which the operator would be able to restrict his liability exclusively to liability for loss or damage caused by gross negligence on his part or on the part of his servants or agents. Such a liability system might be appropriate, in particular in cases where the goods were stored in open air storage yards to which third parties, such as carriers, freight forwarders or consignees, had a right of access in order to inspect the goods, to sort them or to treat them in any other manner. A view was expressed that the phrase "care, custody and control" was broader than "safekeeping", and that the use of that phrase, rather than "safekeeping", would result in the application of the uniform rules to entities who did not exercise safekeeping. According to another view, however, the phrase was synonymous with "safekeeping".

24. With respect to how the definition of "operator" should refer to the operations other than safekeeping, a

view was expressed that the definition should specify the types of other operations to be covered. In that connection a suggestion was made that the operations enumerated in article 3(2) of the secretariat draft should be incorporated in the definition. A further suggestion was that the operations of trimming, dunnaging and lashing should be added to that enumeration. The view was expressed that the enumerated operations should be merely examples of the additional operations to be covered, rather than an exhaustive list. According to another view, the definition of "operator" should not specify the operations other than "safekeeping", or "care, custody and control", and should merely refer to the performance of safekeeping or the exercise of care, custody and control in combination with or for the purpose of performing other transport-related operations. A further suggestion was to refer to operations which facilitated the delivery of the goods to the person entitled to receive them. A view was expressed that the operations covered by the uniform rules should only be those which the operator had undertaken to perform.

*Paragraph (1)(b)*

25. It was generally agreed that the uniform rules should not apply to a carrier during the period of his responsibility for the goods as a carrier under an international transport convention or national law, but that they should apply to a carrier when he had the goods in his charge outside that period. A view was expressed, however, that paragraph (1)(b) should be deleted, and the formulation used in article 1(1) of the UNIDROIT preliminary draft Convention, i.e. "acting in a capacity other than that of a carrier", should be used, since that formulation was simpler. According to another view, the UNIDROIT formulation had the danger of being interpreted so as to exclude the application of the rules to carriers in all cases. Accordingly, it was suggested that paragraph (1)(b) should provide that a carrier was not to be considered to be an operator when he was responsible for the goods under an international transport convention or national law. Another suggestion was to refer to applicable rules of law governing carriage, rather than to an international transport convention or national law.

*Paragraph (2)*

26. Differing views were expressed as to whether "safekeeping" should be defined. According to one view, if the word was used in the uniform rules, it should be defined. Various suggestions were made with respect to how "safekeeping" should be defined. One suggestion endorsed the definition set forth in paragraph (2) of article 1 of the secretariat draft. In connection with that definition, however, it was observed that the phrase "in an area in respect of which he has a right of access and use in common with others" could give rise to problems in some legal systems. Another suggestion was that "safekeeping" should be defined as the exercise of care, custody and control over the goods. A third suggestion was that "safekeeping" contemplated traditional operations of warehousing and storage, although according to another view the word could be interpreted more

broadly. A fourth suggestion was that the direct transfer of goods from one means of transport to another without their becoming stationary should be excluded from safekeeping. In that connection, however, the view was expressed that whether or not safekeeping existed, and therefore whether or not the entity would be regarded as an operator subject to the rules, should not depend upon whether or not the goods became stationary. A fifth suggestion was that "safekeeping" should be defined as an obligation to maintain the goods in the same condition in which they were received by the operator.

*Paragraph (3)*

27. The definition of "goods" in paragraph (3) was found to be acceptable.

*Paragraphs (4) and (5)*

28. A view was expressed that, since each international transport convention defined the type of carrier that was subject to the convention, the uniform rules should not introduce a new definition of "carrier", which could conflict with the definitions in the conventions. In accordance with that view it was suggested that the uniform rules should only refer to the definitions of carriers in the international transport conventions. It was observed, however, that that approach could present a problem in the case of a carrier defined in a convention to which a State adopting the uniform rules was not a party. According to another view, the uniform rules did not need to define "carrier" other than to state that the word included multimodal transport operators.

29. It was generally agreed that the word "carrier" would need to be defined only if the term "international carrier" was defined. If the approach proposed by the informal working party with respect to article 2 were adopted, neither "carrier" nor "international carrier" would need to be defined, but "international carriage" would require definition.

**B. Texts proposed by informal working party and notes relating thereto**

30. The informal working party proposed the following texts for article 1 of the uniform rules. After the texts are the notes which the Working Group agreed should be added for guidance in consideration of the texts.

**Article 1**

For the purposes of this [Convention] [Law]:

*[Alternative 1]*

- (1) (a) "Operator" means a person who undertakes the care, custody and control of goods for the purpose of providing or procuring transport-related services with respect to the goods, by agreement or by taking the goods in charge.

(b) "Transport-related services" includes such services as storage, warehousing, loading, unloading, stowage, trimming, dunnaging or lashing.

(c) A person shall not be considered to be an operator to the extent that he is responsible for the goods as a carrier or multimodal transport operator under applicable rules of law governing carriage.

[Alternative 2]

(1) "Operator" means any person acting in a capacity other than that of a carrier, who undertakes the safekeeping of goods before, during or after carriage, whether or not in combination with other transport-related operations, either by agreement or by taking in charge such goods from a shipper, carrier, forwarder or any other person, with a view to their being handed over to any person entitled to take delivery of them.

[(2) "Safekeeping" means the exercise by a person of care, custody and control over goods [in an area under his control] [in an area under his exclusive control or in an area in respect of which he has a right of access and use in common with others].]

[Alternative 3]

(1) "Operator" means any person who performs or procures the performance of cargo handling operations such as loading, unloading, stowage, trimming, dunnaging, or lashing with respect to goods involved in international carriage [before, during or after carriage], to the extent that safekeeping constitutes part of the operations.

(2) "Safekeeping" means the exercise by a person of care, custody and control over goods [in an area under his control] [in an area under his exclusive control or in an area in respect of which he has a right of access and use in common with others], except that the direct transfer of goods from one means of transport to another without their becoming stationary shall not be regarded as safekeeping].

\* \* \*

(3) "Goods" includes any container, trailer, chassis, barge, pallet or similar article of transport or packaging, if not supplied by the operator.

(4) "International carriage" means any carriage in which the place of departure and the place of destination are located in two different States; however, if and to the extent that the carriage of the goods is to be performed in separate stages which are the subject of individual transport contracts, "international carriage" shall cover only those parts of the carriage in respect of which the place of departure and the place of destination are situated in different States].

**Notes**

a. Under alternative 1, the essential undertaking of an operator must be the "care, custody and control" of the goods for the purpose of providing or procuring transport-related services with respect to the goods. Under alternative 2, the essential undertaking must be the "safekeeping" of the goods. Alternative 2 presents the possibility of limiting the definition of an operator to a person who undertakes traditional operations of storage and warehousing, perhaps together with certain additional transport-related operations (which could be mentioned in article 3). This limitation could be achieved by omitting the definition of "safekeeping" in paragraph (2) of alternative 2, and interpreting "safekeeping" to refer only to storage and warehousing. Such an approach could be narrower than the approach in alternative 1 if the phrase "care, custody and control" in alternative 1 is interpreted to refer to a broader range of situations than storage and warehousing.

b. Alternative 2 might also be narrower than alternative 1 if the definition of "safekeeping" in paragraph (2) of alternative 2 is limited to "the exercise by a person of care, custody and control over goods in an area under his control". On the other hand, alternative 2 could be broader than alternative 1 if the definition of "safekeeping" in paragraph (2) of alternative 2 is not included, and the word "safekeeping" is interpreted more broadly than "care, custody and control".

c. Alternative 1 could include stevedores and airport cargo handlers if they exercise care, custody and control over the goods. A view was expressed, however, that those entities should not be regarded as operators covered by the uniform rules. Another view was expressed that alternatives 2 and 3 could also cover such entities, depending upon what was done with the words within square brackets in the definition of safekeeping.

d. As in the case of alternative 2, under alternative 3 "safekeeping" is an essential element of the definition of "operator". However, alternative 3 presents the possibility of specifying that the direct transfer of goods from one means of transport to another without their becoming stationary is not to be regarded as safekeeping. This language could also be included in the definition of safekeeping in alternative 2.

e. Alternatives 1 and 3 present ways in which operations in addition to "care, custody and control" or "safekeeping" could be incorporated into the definition of operator.

f. Under alternatives 1 and 3, the essential element (i.e. either "care, custody and control" or "safekeeping") is linked with other operations, while under alternative 2 an entity would be considered an operator whether or not safekeeping was linked with other operations. A view was expressed that as the services and operations mentioned in alternatives 1 and 3 were

only examples, those alternatives were not narrower than alternative 2 and could in practice cover all safekeeping situations.

g. Alternatives 1 and 2 present different ways in which to exclude from the definition of "operator" a carrier while he is responsible for the goods under legal rules governing carriage. In alternative 1 this might be achieved by sub-paragraph (b); in alternative 2 it might be achieved by the words "acting in a capacity other than that of a carrier".

h. Paragraph (4) presents two alternative approaches to defining "international carriage". One approach would be to exclude the language contained within square brackets, the other would be to include that language. Possible consequences of each approach are discussed in the notes to the text of draft article 2 proposed by the informal working party.

## Article 2

### A. Text proposed by Secretariat

31. With respect to sub-paragraph (a) in alternative 1 and paragraph (1)(a) in alternatives 2 and 3 in the secretariat draft, one view supported the approach in those paragraphs, i.e. referring to goods located in the territory of the State. The prevailing view, however, was that the paragraphs should refer to operations performed in the territory of the State. In support of that view it was suggested that there was a danger that a reference to goods located in the territory of the State might be interpreted as requiring the goods to be located there when the claim was brought, rather than when the loss or damage occurred, and the goods might have been moved out of the State by the time a claim was brought.

32. A view was expressed that those paragraphs would not be needed if the uniform rules were adopted as a model law. In support of that view it was suggested that a State which had implemented the model law would normally apply it in respect of loss or damage arising from operations performed in the State; and whether it would apply the law in respect of loss or damage arising from operations performed in another State could be left to its rules of private international law. According to another view, however, the paragraphs should be included even if the uniform rules were adopted as a model law.

33. With respect to the remainder of alternatives 1, 2, and 3, it was generally agreed that the uniform rules should apply only to operations performed in respect of goods involved in international carriage. A question was raised, however, concerning the scope of the concept of involvement in international carriage. It was generally agreed that goods should be regarded as being involved in international carriage while they were covered by a combined or multimodal transport contract in which the place of departure and the place of destination were

located in two different States. Accordingly, terminal operations performed with respect to such goods should be covered by the uniform rules, even where, as part of the combined or multimodal transport, the operator received the goods from a domestic carrier and handed the goods over to a domestic carrier. A question was raised, however, as to whether the uniform rules should apply in the case where the operator received the goods from a domestic carrier and handed them over to a domestic carrier as part of segmented, rather than combined or multimodal, transport of goods between two States (e.g. where both domestic carriers were covered by one separate transport contract, or where each domestic carrier was covered by a separate transport contract). A view was expressed that the uniform rules should not apply in those cases. However, an example was given of the case where the operator received the goods from a domestic carrier and handed them over to a domestic carrier for carriage to an airport or a seaport, which could be located nearby, to be loaded on to a ship or airplane for international carriage. A view was expressed that the uniform rules should apply to the operations of the operator in such a case. It was generally agreed that the uniform rules should apply to operations performed by an operator in relation to goods involved in a stage of segmented transport which was covered by a separate contract in which the place of departure and the place of destination were located in two different States.

34. According to another view, the uniform rules were not needed for operations performed while the goods were covered by a unimodal or multimodal transport contract, since the carrier would be subject to a satisfactory liability regime in such cases; moreover, any question of recourse by a carrier against an operator could be resolved between them without the uniform rules.

35. Alternative 1 of article 2 in the secretariat draft received some support. A view was expressed that that alternative was the easiest to apply of the three alternatives of article 2. According to another view, however, alternative 1 was too vague. In that connection a view was expressed that it was important for the operator to be able to determine when the uniform rules applied. A view was also expressed that the alternative was too broad, since it could apply in situations where the operator received the goods from a domestic carrier and handed them over to a domestic carrier.

36. Alternative 3 of article 2 was regarded as too detailed and complex, and did not receive significant support.

37. The greatest degree of support was expressed for the general approach in alternative 2 of article 2. A view was expressed that the approach was sufficiently flexible and adequately limited the application of the uniform rules to operations performed in the context of international carriage. However, a view was expressed that paragraph (2) of alternative 2 should be replaced by a definition of "international carriage". According to that view, "international carriage" should be defined as car-



riage in which the place of departure and the place of destination were located in two different States; in the case of segmented transport, "international carriage" should cover only those segments in which the place of departure and the place of destination were situated in two different States. A suggestion was made that the definition should be placed in article 1, rather than in article 2.

38. A view was expressed that in order to deal with the case where goods became involved in international carriage while they were in the hands of an operator, or ceased to be involved in international carriage while they were in the hands of an operator, the presumption provided for in paragraph (6) of alternative 3 should be incorporated into article 2.

39. A view was expressed that article 2 should contain a provision to the effect that the uniform rules would not apply if the operator proved that he did not know and could not have known from the information and documentation presented to him that the goods were involved in international carriage.

40. A view was expressed that the uniform rules should apply only when maritime transport was involved. In support of that view it was suggested that since in most cases maritime transport was international, it would not be necessary to attempt to limit further the application of the uniform rules to operations in relation to goods involved in international carriage.

## B. Texts proposed by informal working party and notes relating thereto

41. The informal working party proposed the following texts for article 2 of the uniform rules. After the texts are the notes which the Working Group agreed should be added for guidance in consideration of the texts.

### Article 2

(1) [Alternative 1] This [Convention] [Law] applies whenever:

- (a) the goods are located within the territory of [a contracting] [this] State, and
- (b) the goods are involved in international carriage.

[Alternative 2] This [Convention] [Law] applies whenever the ["operations"] are performed:

- (a) in the territory of [a contracting] [this] State, and
- (b) in relation to goods which are involved in international carriage.

(2) When goods in the charge of the operator which were not involved in international carriage upon being

taken over by the operator later become involved in international carriage, or goods in the charge of the operator which were involved in international carriage upon being taken over by the operator later cease to be involved in international carriage, any loss or damage suffered by the goods is rebuttably presumed to have occurred while they were involved in international carriage.

(3) However, this convention shall not apply where the operator proves that he did not know and could not have known from the information and documentation presented to him that the goods were involved in international carriage.

### Notes

a. A question has been raised as to whether subparagraph (a) of paragraph 1 would be required or might produce inappropriate results if the uniform rules were adopted as a model law.

b. "International carriage" would be defined in paragraph (4) of article 1 as proposed by the informal working party. A definition of that term as "any carriage in which the place of departure and the place of destination are located in two different States" could be interpreted broadly. When read in connection with article 2, for example, it could have the result that in the case of segmented transport of goods from one State to another the uniform rules would apply to terminal operations performed in relation to goods during a wholly domestic segment of the transport. A narrower approach might be achieved by including in the definition of "international carrier" the language contained within square brackets in paragraph (4) of the text of draft article 1 proposed by the informal working party. Under that language a segment would be regarded as "international carriage" only if, for that segment, the place of departure and the place of destination were situated in two different States.

c. In alternative 2 of paragraph (1), the word "operations" would be replaced by whatever formulation was used in article 1 to describe the covered operations.

### Article 3

#### A. Text proposed by Secretariat

42. It was observed that paragraph (1) might be understood to mean that the operator was responsible for the goods whenever he performed any operation in relation to them within the basic period of responsibility set forth in paragraph (1), including the operations mentioned in paragraph (2), and that in such a case the extended period of responsibility under paragraph (2) would overlap with the period of responsibility under paragraph (1). It was pointed out, however, that the times when goods were taken over or delivered could not always be precisely

identified and an operator might in some cases perform operations with respect to the goods before having taken them over or after having delivered them. Paragraph (2) would extend the basic period of liability in paragraph (1) to cover those situations. A suggestion was made that paragraph (1) should refer to the taking over of the goods by the operator for the purpose of safekeeping.

43. A view was expressed that the limit of the period of the operator's responsibility should be the time when the operator handed the goods over or made them available to a person entitled to take delivery of them, so as to exclude the application of the uniform rules if the customer failed to take delivery of the goods.

44. A view was expressed that the words "such operations as" within square brackets in paragraph (2) should be retained so as to make clear that the enumeration was not exhaustive. That would ensure that loss or damage occurring during an operation closely related to loading or unloading, but not specifically mentioned in paragraph (2), would be covered by the rules. It was suggested that the operations of trimming, dunnaging and lashing should be added to the operations mentioned in paragraph (2). According to another view, however, it was not necessary to add those operations. It was generally agreed that the ways in which the operations were referred to in articles 1 and 3 should be consistent.

#### **B. Text proposed by informal working party and notes relating thereto**

45. The informal working party proposed the following texts for article 3 of the uniform rules. After the text are the notes which the Working Group agreed should be added for guidance in consideration of the text.

##### **Article 3**

(1) The operator shall be responsible for the goods [referred to in article 1] from the time he has taken them in charge [for safekeeping] until the time he has handed them over [or made them available] to the person entitled to take delivery of them.

(2) If the operator has undertaken to perform or to procure performance of such transport-related services as discharging, loading, stowage, trimming, dunnaging or lashing of the goods, even before their being taken in charge or after their being handed over, the period of responsibility shall be extended so as to cover such additional operations also.

##### **Notes**

a. In order to be subject to the uniform rules an entity would have to undertake to perform the operations mentioned in article 1. The purpose of the present

article is to provide that once the entity qualifies as an operator by undertaking to perform those operations he is responsible for the goods under the uniform rules from the time he takes them in charge until the time he hands them over, or, if the final bracketed language in paragraph (1) is included, until he makes them available to the person entitled to take delivery of them. The final form of the present article will depend upon the formulation adopted for article 1.

b. It may be desirable to clarify the concepts of "taking in charge" and "handing over".

c. If alternative 2 of article 1 is chosen, and the words "for safekeeping" are included in paragraph (1) of article 3, the initial period of responsibility could be regarded as the period of safekeeping, and if so, paragraph (2) of article 3 would be required in order to extend the period of responsibility to cover operations performed before or after safekeeping. If "for safekeeping" is not included in paragraph (1), and if the period between taking the goods in charge and handing them over adequately describes the period of time during which the operator could perform operations with respect to the goods intended to be covered by the uniform rules, then paragraph (2) might not be needed.

d. A question was raised whether article 3 would be needed if alternative 3 of article 1 were chosen.

##### **Article 4**

#### **A. Text proposed by Secretariat**

46. Reference was made to the large number of documents that were used in connection with the international transport of goods. It was generally agreed that the documentation requirements of the uniform rules should be minimal, so as not unduly to add to the burden of documentation in international transport.

##### *Paragraphs (1) and (2)*

47. Considerable support was expressed for the view that an operator should be obligated to issue a document only if requested to do so by the customer. According to another view, however, issuance of a document should be compulsory. It was generally agreed that in the document the operator should acknowledge receipt of the goods. A view was expressed that the operator should also state in the document such particulars concerning the condition and quantity of the goods as was requested by the customer of the operator, as far as those particulars could be ascertained by reasonable means of checking. In that connection, it was observed that in some cases, e.g. with sealed containers, it might be excessively burdensome to require the operator to open and perhaps strip the containers in order to check the condition of the goods, and the operator might be prevented from opening sealed containers by customs laws or other laws. A suggestion

was accordingly made that the rules should specify that "reasonable means of checking" did not require the opening of sealed containers.

48. A question was raised as to whether the word "customer" should be used in paragraph (1) and elsewhere, or whether reference should be made to the person with whom the operator was in a contractual relationship. It was generally agreed that reference in the rules to the contract between the parties should be avoided, and that the word "customer" should be retained.

49. It was generally agreed that, in paragraph (1), the operator should be obligated to issue the document within a reasonable, rather than a specified, period of time.

50. A proposal was made that the title of article 4 should be changed to "Acknowledgement of the receipt", and that the article should obligate the operator, at the time he takes the goods in charge, to acknowledge his receipt of the goods by signing a dated document presented by the customer. The document should indicate the date on which the goods were taken in charge, the person entitled to receive the goods, and the description of the goods necessary for their identification, and the operator should note on the document any inaccuracy or inadequacy of the particulars concerning the description of the goods as far as he could ascertain them by reasonable means of checking. If the operator failed to acknowledge receipt of the goods he should be presumed to have received them on the date and in the condition as declared by the customer. In support of that proposal it was noted that in the case of the transfer of goods by the operator from one person or entity to another within a short period of time, it was unrealistic to require the customer to make a formal request for a document or for particulars concerning the goods, and that the rules should only require the operator to sign a document tendered by the customer. In connection with the proposal, however, it was observed that the customer might not present a document to the operator.

#### *Paragraph (3)*

51. It was generally agreed that the substance of paragraph (3) was acceptable. A view was expressed that, if the issuance of a document was compulsory, the language included within square brackets should be deleted.

#### *Paragraph (4)*

52. Considerable support was expressed for the substance of paragraph (4). According to a contrary view, however, it was preferable to leave the matters referred to in that paragraph to be dealt with by national law. It was also noted that certain terms appearing in paragraph (4), such as "apparently good condition" or "presumption", might not be familiar in some legal systems.

53. With respect to the words "it is proven that" within square brackets, one view favoured retaining the words,

while another view favoured deleting them. In favour of retaining the words it was suggested that it would not be appropriate for the operator to be presumed to have received the goods in apparently good condition unless it was proved that the customer had requested the operator to issue a document or to state on the document information concerning the condition of the goods. It was noted that in some cases disputes could exist as to whether those requests had been made. In favour of deleting the words, it was noted that the question of whether such requests had been made could relatively easily be placed in issue in legal proceedings, and that the words were therefore unnecessary.

54. It was noted that the operator might not know whether he had received the goods, or might deny that he had received them. The view was accordingly expressed that the presumption referred to in paragraph (4) should not arise if the operator did not have an opportunity to check the goods.

55. According to one view, the word "rebuttable" should be deleted from paragraph (4). According to another view, it should be retained, since in some legal systems there existed the concept of an irrebuttable presumption.

56. It was noted that under its present wording paragraph (4) would give rise to a presumption that the operator received the goods in apparently good condition if he refused to state on the document the condition of the goods, even though in the case of sealed containers he would not be obligated to open the container to ascertain the condition of the goods. In that connection a suggestion was made that the presumption should be limited to the condition of the goods that could have been ascertained with reasonable means of checking.

#### *Paragraphs (5) and (6)*

57. It was generally agreed that the paragraphs were in substance acceptable. A view was expressed that a stamp or notation on an existing document should be sufficient. A suggestion was made that paragraph (6) should also provide for the operator to sign the document himself. It was noted, however, that the operator would not usually be a natural person.

#### **B. Texts proposed by informal working party and notes relating thereto**

58. The informal working party proposed the following texts for article 4 of the uniform rules. After the texts are the notes which the Working Group agreed should be added for guidance in consideration of the texts.

#### **Article 4**

(1) [Alternative 1] The operator shall [in all cases], without unreasonable delay, either:

[Alternative 2] Unless and to the extent that such requirement is waived by the customer, the operator shall, without unreasonable delay, either:

[Alternative 3] At the request of the customer the operator shall, without unreasonable delay, either:

[Alternative 4] The operator may, at his option, either:

[Alternative 5] The operator may, and at the customer's request shall, without unreasonable delay, either:

(a) acknowledge his receipt of the goods by signing a document produced by the customer identifying the goods and stating their condition and quantity, or

(b) issue a signed document acknowledging his receipt of the goods and the date thereof, and stating their condition and quantity insofar as they can be ascertained by reasonable means of checking.

(2) If the operator fails to act in accordance with either sub-paragraph (a) or (b) of paragraph (1), he is rebuttably presumed to have received the goods in apparently good condition.

(3) The document referred to in sub-paragraph (b) of paragraph (1) of this article may be issued in any form which preserves a record of the information contained therein.

(4) A document under this article shall be signed by the operator or on his behalf by a person having authority from him. The signature may be made in handwriting, printed, in facsimile, perforated, stamped, in symbols, or made by any other mechanical or electronic means.

[(5) The absence from the document of one or more of the particulars referred to in paragraph (1) of this article shall not affect the legal character of the document as a document of the operator.]

### Notes

a. The various alternatives to paragraph (1) reflect various approaches to the question of whether and the extent to which the operator should be obligated to issue a document. The final wording of this provision could contain elements of one or more of the alternatives.

b. A view was expressed that if the operator was obligated to issue a document only at the request of his customer, the value of the presumption provided for by paragraph (2) would be limited.

c. A view was expressed that the phrase "without unreasonable delay" in paragraph (1) was misleading, and that a definite period of time should be specified.

d. Sub-paragraph (a) of paragraph (1) is intended to take account of the practice in some terminals.

e. The phrase "reasonable means of checking" in sub-paragraph (b) of paragraph (1) is not intended to require an operator to open sealed containers.

f. With respect to paragraph (4), a view was expressed that if another person was authorized to sign a document on behalf of the operator, his ability to do so by mechanical and similar means should be restricted.

g. A view was expressed that paragraph (5) was needed in order to preserve the legal character of the document. According to an opposing view, however, such a provision was important in transport conventions where the transport document was negotiable, constituted a document of title to the goods or served as the contract of carriage; however, that was not the case with the document of the operator, and paragraph (5) was therefore unnecessary.

h. In accordance with a decision of the Working Group at its eighth session, this draft article does not deal with negotiable documents.

### Article 5

59. The Working Group considered whether the uniform rules should deal with delay by the operator in handing over the goods. The prevailing view was that the uniform rules should deal with delay. In support of that view it was noted that delay could occur for a number of reasons and was a problem which existed in practice. If the uniform rules did not deal with delay, the liability of the operator for delay would be governed by disparate rules in national legal systems. Some legal systems permitted the operator to restrict or exclude liability for delay by contract. Providing a uniform legal regime for delay would benefit cargo interests, and also carriers who were subject to liability for delay under international transport conventions and who would seek recourse against operators for delay. In other legal systems, delay could expose the operator to severe liability under national law. Dealing with delay in the uniform rules would enable the operator to benefit from the uniform defences and limits of liability in cases of delay.

60. According to an opposing view, however, the uniform rules should not deal with delay. Delay was not a significant problem in practice. It was noted that if the goods could not be found they could be treated as lost, with liability imposed on the operator accordingly. Due to the different types of operators, operations and goods to be covered by the uniform rules, it would be difficult to define what constituted delay.

### Paragraph (1)

61. It was noted that under paragraph (1) it was incumbent upon the claimant to prove that the occurrence which caused the loss or damage took place during

the period of the operator's responsibility for the goods, and that once he did so the burden would be on the operator to prove that he, his servants or agents took all measures that could reasonably be required to avoid the occurrence and its consequences. It was observed that in the performance of his functions the operator might make use of the services of a person who was not a servant or agent. It was generally agreed that reference to such a person should be added to paragraph (1).

62. It was generally agreed that the operator should have the burden of proof referred to in paragraph (1) in respect of loss of or damage to the goods occurring while he was responsible for them, since the goods would be in his possession and he would have the knowledge and evidence of the circumstances concerning the loss or damage. It was noted, however, that contracts for terminal operations often imposed the burden of proof upon the customer to prove that damage caused during the stuffing and stripping of containers was due to the fault of the operator, and it was suggested that that practice should be taken into account in paragraph (1).

63. A view was expressed that the uniform rules should deal with the liability of an operator for damage caused by him to a means of transport which delivered goods to him or took goods away from him. In that connection it was noted that the financial consequences of the damage could be great. The prevailing view, however, was that the rules should deal only with the liability of the operator for loss of or damage to goods or property taken over by him for safekeeping (which might include containers, chassis, trailers, or similar items) but that liability for damage to property not taken over for safekeeping was beyond the scope of the rules to be elaborated.

64. A view was expressed that the operator should be required to prove only that he took all measures that could reasonably be required "of him", since some operators might not be equipped to take measures which might be regarded as reasonably required. The prevailing view, however, was that the liability of the operator should be subject to an objective standard, rather than a subjective one, and that the words "of him" should not be added.

65. With respect to the sentence within square brackets at the end of paragraph (1), a view was expressed that the sentence should be retained. The prevailing view, however, was that the sentence should be deleted, since the operator, who was often engaged in a commercial activity, should be responsible for the acts of his servants or agents, whether or not they acted within the scope of their employment.

#### Paragraph (2)

66. Differing views were expressed with regard to paragraph (2). In support of deleting that paragraph it was suggested that the paragraph would interfere with and limit the standard of liability set forth in paragraph (1). It was also suggested that the paragraph was

unnecessary, since a court would in any case consider the factors mentioned in it. A further view was expressed that the precise scope and meaning of the words "*inter alia*" were not clear. In support of retaining the paragraph, it was suggested that pointing out certain factors to be taken into consideration by courts in determining what measures were reasonably required would promote uniformity in court decisions and would be of help in those legal systems in which the concept of reasonableness was not familiar. It was also suggested that by virtue of the words "*inter alia*" in paragraph (2), that paragraph would not limit the liability imposed in paragraph (1); a court would be free to consider other relevant circumstances. A suggestion was made that the concerns of those who favoured deleting the paragraph might be met by providing that "due regard shall be had to all of the circumstances of the case, including, *inter alia*, the nature of the goods and the nature of the operations to be performed by the operator".

#### Paragraph (3)

67. Paragraph (3) was found to be acceptable.

#### Paragraph (4)

68. Paragraph (4) was found to be acceptable. A suggestion was made, however, that the drafting of the language towards the end of the paragraph should be improved by referring to "a reasonable time after receiving a request for the goods by the person".

#### Paragraph (5)

69. It was observed that it might not be appropriate to enable the claimant to treat the goods as lost if they were not in fact lost, but were not handed over within 60 days for reasons known to both parties (e.g. an industrial dispute). It was also observed, however, that in such cases the operator might avoid liability for loss by proving, in accordance with paragraph (1), that the delay in handing over occurred despite his having taken measures that could reasonably have been required to avoid the delay.

70. It was noted that under paragraph (5) the 60-day period would commence on the date when the customer requested the goods. It was generally agreed that the paragraph should provide for the period to commence on the date agreed to by the parties for handing over of the goods, or, in the absence of such an agreement, on the date when the customer requested the goods. In that connection it was observed that the operator might be obligated to hand over the goods at a time agreed upon by the parties, without a request.

71. A view was expressed that in the case of goods which were stationary within a terminal, 60 days was an excessive amount of time before the customer could treat the goods as lost. It was suggested that 10 or 14 days would be more appropriate.

**Article 6***Paragraph (1)*

72. It was generally agreed that even if the uniform rules were cast in the form of a model law, the limits of liability should be expressed by reference to the Special Drawing Right as defined by the International Monetary Fund. If the rules were cast in the form of a convention, the unit of account provision adopted by the Commission at its fifteenth session<sup>3</sup> should be used.

73. A view was expressed that a mechanism should be provided for revision of the limits of liability. It was observed that in the case of a convention one of the two provisions adopted by the Commission at its fifteenth session for revising limits of liability<sup>4</sup> could be used, but that in the case of a model law problems could exist in choosing a forum to effectuate the revision. In that connection it was suggested that if the uniform rules were adopted as a model law, the adoption of the rules could be accompanied by an expression that it would be desirable for the limits to be revised periodically so as to take account of inflation. According to another suggestion a revision of the limits should take account of limits existing in international transport conventions which were in force.

74. Various views were expressed as to whether the uniform rules should establish a single limit of liability, or whether the limit should depend upon the mode or modes of transport served by the operator. According to one view the rules should establish a single limit. In support of that view it was observed that the operator might not always know by what mode of transport the goods were delivered to him or were taken away from him, and he would in those cases not know which limit applied. Furthermore, a multiplicity of possible limits would cause undue confusion and uncertainty. It was also observed that with respect to certain modes of transport the limits of liability were not settled.

75. According to another view, if the goods were delivered to or taken away from the operator by maritime transport, the limits applicable to maritime transport should apply; if maritime transport was not involved, a higher limit should apply. According to a third view, the limit should be the limit applicable either to the mode of transport by which the goods were delivered to the operator or the mode by which they were taken away from him, whichever limit was higher.

*Paragraphs (2) and (3)*

76. The paragraphs were found to be acceptable.

*Paragraph (4)*

77. A question was raised as to what would be the result if the enumeration of packages or shipping units in the document issued by the operator differed from that in the transport document. Subject to clarification of that point, the paragraph was found to be acceptable.

*Paragraph (5)*

78. Paragraph (5) was found to be acceptable.

**Article 7**

79. In connection with paragraph (2), it was generally agreed that not only servants and agents of the operator, but also other persons of whose services the operator made use, should be entitled to avail themselves of the defences and limits of liability available to the operator under the uniform rules.

80. A view was expressed that if, in paragraph (1) of article 5, the operator was to be liable for loss, damage or delay resulting from acts of his servants, agents or other persons, those persons should be able to avail themselves of the defences and limits of liability available to the operator even if they acted outside their scope of employment. A suggestion was made that the reference to scope of employment in paragraph (2) of article 7 should therefore be deleted.

**Article 8**

81. With respect to paragraph (1), the prevailing view was that the operator should not lose the benefit of the limit of liability as a result of the acts of his agents or other persons of whose services he made use. It was observed in that regard that the operator could receive more favourable insurance rates if the possibility of his losing the benefit of the limit of liability was restricted.

**Article 9**

82. Various views were expressed with respect to the approach taken in article 9. It was observed that the article imposed certain obligations on the consignor of the goods, who would often not be in a contractual relationship with the operator. A view was accordingly expressed that the obligation imposed upon the consignor in the article should instead be imposed on the customer of the operator. It was also observed that the consignor of the goods could be far removed from the operator in the chain of transport, and it was suggested that the obligations imposed on the consignor in article 9 should instead be imposed on the "depositor" or "user" of the terminal. A further view was expressed that since the purpose of the uniform rules was to regulate the liability of the operator for loss of or damage to goods taken in charge by him, the rules should not deal with obligations owed to the operator by another person.

<sup>3</sup>Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17 (A/37/17 and Corr. 1 and 2 (English only))*, para. 63, annex I.

<sup>4</sup>*Ibid.*, para. 63, annexes II and III.

83. The prevailing view, however, was that the problems arising in connection with dangerous goods were so important that they should be dealt with in the uniform rules, and the approach taken in article 9 was appropriate. In that connection a suggestion was made that the uniform rules should clarify that the "consignor" was the person who initially shipped the goods.

84. A view was expressed that paragraphs (2) and (3) should deal with the case where the operator did have knowledge of the dangerous character of the goods and the goods damaged or threatened to cause damage to property of the operator, in addition to the case where he did not have knowledge. In particular, it was suggested that paragraph 2(b) should permit the operator to destroy the goods or render them innocuous even if he knew of their dangerous character. According to another view, the operator should be able to invoke the rights under paragraphs (2) and (3) unless he had actual, rather than implied, knowledge of the dangerous character of the goods.

85. It was generally agreed with respect to paragraph (2)(a) that the loss for which the consignor would be liable to the operator should include not only any damage to the property of the operator but also the costs to the operator of destroying the goods or rendering them innocuous and any liability imposed on him as a result of loss or damage caused by the dangerous goods. A view was expressed, however, that it might be appropriate to provide limits to the liability of the consignor towards the operator. With respect to paragraph (2)(b) it was generally agreed that the operator should be able not only to destroy the goods or render them innocuous, but also to dispose of them by other means.

86. A suggestion was made that the operator's customer should be required to disclose to the operator any special storage requirements for the goods deposited or their perishable nature, in view of the objective liability imposed on the operator in article 5.

#### **Article 10**

87. It was observed that a container in respect of which the operator had rights of security would often be owned by a person other than the owner of the goods (e.g. by a container leasing company) and with whom the operator was in no contractual relationship. The view was accordingly expressed that the operator should be obligated to make reasonable efforts to notify the owner of a container leased by the customer before exercising a right to sell the container. According to additional views, the operator should be obligated to make reasonable efforts to notify owners of all goods subject to a right of sale by the operator, and the rules should require the operator to account to the customer for the balance of the proceeds of the sale in excess of the sums due to the operator. According to another view, however, issues concerning the exercise of the right of sale, including notice and

disposition of the proceeds of the sale, should be left to be dealt with by the applicable rules of national law.

88. A view was expressed that paragraph (3) served no purpose, as it permitted the operator to sell the goods only to the extent permitted by and in accordance with applicable law, which would be the case even without such a provision. According to another view, if paragraph (3) specified which law should apply in dealing with those issues, the paragraph could be useful to avoid conflict of laws problems if the uniform rules were adopted in the form of a convention; in that case the law referred to should be the law of the place where the operations were performed by the operator.

#### **Article 11**

89. It was generally agreed that the approach in article 11 was acceptable, except that the article should not treat loss and partial loss differently. In that connection, paragraph (2) should be deleted, and paragraph (1) should refer only to loss, rather than to partial loss.

90. A further view was expressed that the article should not distinguish between apparent and non-apparent loss and damage; rather, there should be a single notice period which was long enough to take into account the problem that in some cases loss or damage might not be discoverable until the goods reached their final destination. It was generally agreed, however, that the notice periods should be different for apparent and non-apparent loss and damage.

#### **Article 12**

91. It was generally agreed that there should not be a separate limitation period for loss or damage caused by intentional or reckless acts or omissions and for loss or damage caused by other conduct; accordingly, the bracketed language after the first sentence in paragraph (1) should be deleted.

92. It was noted that in some legal systems the running of the limitation period could be interrupted by means other than by instituting arbitral or judicial proceedings, and it was suggested that account should be taken of those means in the article.

93. It was generally agreed that in the case of total loss of the goods, the limitation period should commence on the day the operator notified the person entitled to make a claim that the goods were lost, or, if no such notice was given, on the day that person could treat the goods as lost in accordance with article 5.

#### **Article 13**

94. It was generally agreed that paragraph (1) was acceptable.

95. Differing views were expressed with respect to paragraph (2). According to one view, the paragraph was useful to ensure that the parties could agree to a different liability regime for processing operations, and it should be retained. The prevailing view, however, was that the uniform rules were not intended to cover processing operations, and therefore the paragraph was unnecessary and should be deleted.

96. It was observed that paragraph (1) referred only to a contract for the "safekeeping of goods", and it was suggested that the provision should be made to correspond with the scope of the operations intended to be covered by the uniform rules, which could include operations in addition to safekeeping.

#### Article 14

97. It was generally agreed that article 14 should be deleted if the uniform rules were adopted in the form of a model law. It was suggested that in such a case the model law should provide that the reports of the Working Group and the Commission dealing with the elaboration of the model law should be used as a guide to its interpretation.

#### Article 15

98. Article 15 was found to be acceptable, including the language within square brackets. It was noted that that language was necessary in order to take account of the fact that some States adopted international transport conventions by means of legislation.

### III. Other business and future work

99. The Working Group, taking account of already scheduled meetings of other organs dealing with topics in the field of international transport which would be attended by some representatives of member States and observers of the Working Group, decided to recommend to the Commission that the tenth session of the Working Group should be held at Vienna from 1 to 12 December 1986. It also decided to recommend that, unless it completed its work at the tenth session, the eleventh session of the Working Group should be held for two weeks in New York during the first half of 1987, prior to the twentieth session of the Commission.

## B. Working papers submitted to the Working Group on International Contract Practices at its ninth session

### 1. Liability of operators of transport terminals: certain factual and legal aspects of operations performed by operators of transport terminals: note by the secretariat (A/CN.9/WG.II/WP.55)

[Original: English/French]

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## INTRODUCTION

1. The Commission, at its seventeenth session (1984), assigned to its Working Group on International Contract Practices the task of formulating uniform legal rules on the liability of operators of transport terminals (hereinafter referred to as "operators").<sup>1</sup> The Working Group commenced its work on this topic at its eighth session, held at Vienna from 3 to 13 December 1984 (A/CN.9/260). In accordance with the decision of the Commission at its seventeenth session,<sup>2</sup> the Working Group decided to base its work on document A/CN.9/252, as well as on the preliminary draft Convention on the Liability of Operators of Transport Terminals adopted by the International Institute for the Unification of Private Law (UNIDROIT) and the Explanatory Report thereto prepared by the UNIDROIT secretariat.<sup>3</sup>

2. At its eighth session the Working Group engaged in a comprehensive consideration of the issues arising in connection with the liability of operators before attempting to draft detailed uniform rules (A/CN.9/260, para-

graph 12). These deliberations were based on two working papers prepared by the UNCITRAL secretariat (A/CN.9/WG.II/WP.52 and WP.53). In the context of its consideration of the scope of the uniform rules, the Working Group requested the secretariat to prepare a study on various aspects of the issue, taking into account operations performed by operators as well as circumstances relating to various modes of transport. It also requested that the study consider legal aspects of the issue arising from various international transport conventions, including the points of time at which a carrier's responsibility for the goods began and ended, which could result in the liability of a carrier overlapping that of an operator and which could have implications for recourse actions by a carrier against an operator (A/CN.9/260, paragraph 27).

3. This report has been prepared pursuant to the above-mentioned requests. It deals with various factual and legal matters relevant to the issue of the scope of the uniform rules, and also contains a section describing practices with respect to inspection of goods taken over by operators and documentation issued by operators.<sup>4</sup> A draft of articles of uniform rules taking into account the discussion in this report is contained in document A/CN.9/WG.II/WP.56.

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its seventeenth session, *Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 17 (A/39/17)*, paras. 105 to 113; see, also, Report of the United Nations Commission on International Trade Law on the work of its sixteenth session, *Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17 (A/38/17)*, paras. 109 to 115.

<sup>2</sup>Report of the United Nations Commission on International Trade Law on the work of its seventeenth session, *Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 17 (A/39/17)*, para. 113.

<sup>3</sup>The UNIDROIT preliminary draft Convention is reproduced in A/CN.9/252, annex II; the Explanatory Report is reproduced in A/CN.9/WG.II/WP.52/Add.1.

<sup>4</sup>In addition to engaging in its own investigations and research for the preparation of this report, the UNCITRAL secretariat was provided with a draft of a report prepared by the secretariat of the United Nations Conference on Trade and Development (UNCTAD) on rights and duties of container terminal operators and users (see A/CN.9/260, para. 96). The final version of that report will be presented to the 12th session of the UNCTAD Committee on Shipping, which will be held from 10 to 21 November 1986.

## I. Overview of operators dealing with goods involved in carriage

4. There exists a wide variety of types of operators who deal with goods involved in carriage. They do not fall into neat categories; rather, they present considerable overlapping of functions as well as wide disparities with respect to such factors as the nature of the operator, the types of goods with which they deal, the operations they perform, and the parties with whom they are in contractual relationship and for whom they perform their services. Moreover, as will be seen, the nomenclature which has traditionally been used to describe various types of operators is not a satisfactory way of distinguishing between them. The following discussion presents certain characteristics of such operators in a systematic manner designed to facilitate a treatment of some of the issues arising in the context of legal rules governing the liability of operators of transport terminals.

5. Some operators render comprehensive terminal services for carriers or cargo interests (i.e. consignors and consignees), including loading and unloading of goods, storage, and the types of operations described in section III, below, within premises which they occupy, usually as owners or lessees. These operators include those who operate airports and sea, river, rail and road terminals. Such operators very often serve more than one mode of transport. For example, sea or river terminals usually have rail and road links, and often load and unload railway wagons and lorries, in addition to ships or river craft. An inland road or rail facility may serve both rail and road transport. Airports also have road and often rail links, although airport personnel seldom load or unload goods on to or from means of transport other than aircraft. Sometimes such operators lease space or facilities within their terminals to other operators, as in the case of an operator of a rail terminal at which storage space is leased to road carriers or freight forwarders.

6. There exist other types of operators who offer more limited types of services in respect of goods than those described above but who still perform their operations within areas occupied by them. Such operators may limit their services to one principal type of operation. They include, for example, operators of "consolidation centres", who consolidate goods for transport, e.g. by containerizing goods of one or more consignees, and who break down containerized or other consolidated shipments which have been transported internationally for delivery to one or more consignees. They also include operators of warehouses who store goods prior to, during or after carriage. Warehouse operators may engage in short-term storage directly related to transport (e.g. by storing goods waiting to be loaded on to a means of transport or to be picked up by the consignee after unloading (often called transit storage)), long-term storage, or both. Customs or bonded warehouses store goods pending the completion of customs formalities. Consolidation centres and warehouses may be located within or near the premises of other operators who load or unload the goods on to or from the means of transport; however,

warehouses used for long-term storage are often located a distance from the place where the goods are loaded or unloaded.

7. There also exist operators who perform certain types of operations with respect to goods, but who do not have their own premises where they perform such operations. Rather, they perform their operations on goods located within the premises of another operator or within or on the means of transport. Such operators include those who supply labour and equipment to be used by a second operator, a carrier or a cargo interest to unload goods from a means of transport and deposit them in a terminal owned by the second operator or load them directly on to another means of transport, or to load goods from a terminal owned by a second operator onto a means of transport. (In sea transport such operators are sometimes referred to as longshoremen or stevedoring companies.) They also include various types of operators who inspect goods, fumigate goods, and perform similar operations in the premises of another operator or within or on the means of transport.

8. As already indicated, the distinction among the various types of operators who perform operations in respect of goods involved in carriage is blurred, because the functions and operations performed by one type of operator are also performed by other types. An effort to distinguish between various types of operators is not assisted by reference to the traditional nomenclature used for entities who perform services other than carriage in connection with international transport. For example, operators styling themselves as stevedoring companies may perform certain other operations in addition to their traditional function of loading and unloading goods. They may also have premises of their own where they store the goods or keep them during the performance of those operations. Storage and other types of operations, including loading and unloading of goods, may also be performed by operators known as ship-brokers or ship's agents, dock agents, and landing agents, as well as by freight forwarders (whether they act as principals or as agents for cargo interests). Warehouse operators often perform various operations in addition to storage. An inland road/rail terminal may act as a storage and distribution centre (see paragraph 17, below). Carriers sometimes operate their own sea, road or rail terminals where they store goods and perform handling and other operations. Certain manufacturing enterprises operate their own terminals in connection with their import of raw materials or export of their products; such operations may also be performed at these terminals for other enterprises. Finally, a combined or multimodal transport operator may undertake carriage and all storage, handling and other operations in respect of the goods from the time they are taken over from the consignor until the time they are handed over to the consignee.

9. With respect to their ownership, some operators are state enterprises or publicly owned; this is often the case with rail terminals and airports, as well as with customs warehouses (although bonded warehouses are frequently

privately owned). Other operators are owned by private commercial enterprises. Some are owned by enterprises whose sole business is to store or perform terminal operations with respect to goods involved in carriage; others are owned by enterprises involved in other aspects of the transport of goods (e.g. carriers, freight forwarders); still others are owned by manufacturing or trading enterprises. Some are owned by entities comprised of various combinations of the enterprises mentioned above.

10. Operators represent a wide range of levels of technical and operational sophistication. Some are heavily labour-intensive and use equipment and handling techniques of relatively low levels of sophistication. Others employ equipment and techniques of highly advanced levels of technological and engineering sophistication. These facilities are generally able to handle goods with greater speed and efficiency, and often with less risk of loss of or damage to the goods, than less sophisticated ones.

## II. Types of goods involved in carriage

11. The goods handled by operators are of many different types. These include unitized goods (e.g. goods unitized in containers, roll-on/roll-off (RO/RO) carriers, and barge-carrying vessels); break-bulk goods; bulk goods (e.g. ores, cement, grains; goods of this nature may also be containerized or transported in bags as break-bulk cargo); and liquid goods (such goods may also be containerized). Some operators specialize in serving particular types of goods (e.g. containerized goods, bulk goods, liquid goods, timber, ores); others serve a wide variety of goods. Specialization in particular types of goods often represents a relatively advanced stage of development in the organization of transport-related operations serving a particular area. Some operators, such as operators of sea terminals, sometimes store, and even manage the distribution of, empty containers belonging to a carrier or a container supplier, as well as other equipment associated with the transport of goods, such as chassis for the road transport of containers or barges for the transport of goods on barge-carrying vessels.

12. The differing characteristics of and circumstances associated with various types of goods often result in differing practices of operators with respect to each type. These differing practices include differences as to:

(a) Methods of handling (e.g. containers may be handled with gantry cranes, straddle carriers, and fork-lift trucks; bulk cargo may be loaded and unloaded with scoops, conveyor belts running between the terminal and the means of transport, or chutes; break-bulk cargo may be handled with cranes and fork-lift trucks; liquid cargo may be loaded and unloaded through pipes or tubing);

(b) Types of operations performed (e.g. operations may be performed with respect to certain types of goods which are not performed with respect to other types, such as cleaning grain, compacting coal to avoid spontaneous

combustion, edging timber (e.g. cutting the ends to make uniform stacks), washing and disinfecting containers: see chapter III, below);

(c) Methods of storage (e.g. containers, RO/RO vehicles and some bulk goods may be stored in open areas, while other goods (e.g. grain, break-bulk goods) are stored in covered or sheltered areas; refrigerated containers with perishable goods must be connected to an electricity supply to run the refrigeration mechanism);

(d) The flow of goods through the premises of the operator (e.g. full containers are usually kept in a container terminal only for short periods of time; they are either transferred directly from one means of transport to another or are kept within the terminal for a maximum of a few days to await loading on to a means of transport or pick-up by the consignee; break-bulk goods are often kept for longer periods of time); and

(e) Practices concerning inspection of goods taken over by an operator (e.g. goods which are enclosed in sealed containers or RO/RO vehicles, and some bulk goods, are seldom inspected, while uncrated machinery is normally inspected (see chapter VI, below)).

## III. Operations performed with respect to goods involved in carriage

13. The following overview of the various types of operations performed with respect to goods involved in carriage is provided in order to facilitate consideration of the scope of the uniform rules (discussed in chapter IV, below).

### A. Loading and unloading of goods

14. Although goods are sometimes loaded on to and unloaded from means of transport by carriers or by cargo interests, they are typically loaded and unloaded by operators. The identity of the party who loads and unloads the goods and the legal regime applicable to these operations is important since, statistically, goods are at greatest risk of damage during these operations.

15. When goods are unloaded by an operator, they are removed from the means of transport by the personnel and equipment of the operator. At that point, various things might happen to the goods. For example, they may be loaded directly on to another means of transport without ever touching the ground or they may be carried within the premises of the operator before being loaded directly on to another means of transport; they may be put on the ground for a very short period of time and then loaded on to another means of transport; they may be brought to a transit shed or transit area within the premises of the operator to await loading on to another means of transport or pick-up by the consignee; they may be brought to a customs or bonded warehouse pending clearance of customs formalities; or they may be brought to a long-term storage area. The situations in the case of

loading of goods on to a means of transport are essentially the opposites of those just described.

16. An operator may perform various operations ancillary to loading and unloading operations while the goods are on board or within a means of transport. Such operations may include, for example, stowage (placing cargo in proper order in the hold of a means of transport), trimming (distributing the load in the means of transport), dunnage (placing material about or below cargo to prevent damage during transport), and lashing of containers on board a vessel. In some cases, such as cargo aboard an ocean vessel, such operations are usually performed by the operator under the supervision of the master of the vessel. In other cases, these operations may be performed without the supervision of the carrier, such as when they are performed in respect of goods loaded on to a rail wagon on a private siding within the premises of the operator.

### **B. Storage of goods**

17. Goods may be kept or stored by an operator under various circumstances. As mentioned above, outbound goods may be kept for short periods of time in a transit shed or transit area or kept or stored in a warehouse for varying periods of time prior to loading on to the means of transport, while inbound goods may also be kept or stored in a customs or bonded warehouse. Sometimes, consignors and consignees store goods with operators for indefinite or long periods of time until they are needed. (Such goods should probably not be regarded as being involved in carriage: see chapter IV, B, below.) In some cases, a cargo interest may use an operator as a distribution centre, his goods being taken over from the carrier by the operator and stored within the premises of the operator until the cargo interest instructs the operator to release or deliver the goods to a customer of the cargo interest or to load the goods on to a means of transport to be transported to the customer. In effect, the cargo interest uses such an operator to store his inventory. In such cases the operator may also engage in pick-up and delivery of goods (see paragraph 22, below).

18. While the goods are being kept or stored by the operator, various other operations, such as many of those discussed in the following paragraphs, may be performed with respect to the goods by the operator or by some other person.

### **C. Packing and packaging of goods; stuffing and stripping of containers**

19. An operator may be requested by his customer to pack or re-pack goods in packaging which is suitable for transport. For example, goods received by the operator in bags may be placed into smaller bags. In addition, the operator may repair packaging which has been damaged, whether the packaging was received by the operator in the damaged condition or suffered damage while in the charge of the operator.

20. An operator may also be requested by his customer to package goods for commercial marketing, e.g. by filling bottles with wine received in tanks. The performance of such operations usually takes place during long-term storage or at distribution centres (see paragraph 17, above).

21. Some operators may also stuff or strip containers. Stuffing operations may involve consolidating shipments of several consignors into a single container (e.g. a container owned by the carrier, a container leasing company or the operator); or goods of a single consignor may be stuffed into a container (which may also be owned by the carrier, a container leasing company, or the operator, or by the consignor). An operator may also strip containers received by him under circumstances analogous to those just described.

### **D. Carriage of goods by operator**

22. Operators sometimes undertake to transport goods between their premises and places outside their premises. For example, some operators pick up goods from consignors or deliver goods to consignees. Others transport goods between a main terminal and a warehouse or consolidation centre located away from the main terminal, which may be owned by the operator who owns the main terminal or by a different operator. Operators of distribution centres sometimes pick up goods from their customers for storage prior to transport, and carry goods to their ultimate destinations on instructions from their customers. In the case of barge-carrying vessels, the vessel may moor offshore and the barges containing the goods may be unloaded into the water to be towed to the terminal by tug boats owned by the operator of the terminal.

### **E. Preparation or processing of goods**

23. Operators sometimes engage in operations involving the preparation or processing of goods. In some cases, these operations change the nature, condition or quantity of the goods; in other cases, they do not. Still other cases fall somewhere in between. Examples of preparation or processing operations are the following: cleaning and fumigating grains; ripening fruit; drying timber; edging timber; de-salting hides; processing iron ore to improve its characteristics or to increase its iron content (this involves, e.g., washing, grinding, screening, processing into pellets or briquettes); grinding soybeans and manufacturing soymeal and oil from ground beans.

### **F. Operations with respect to empty containers**

24. Some operators store containers for their owners (e.g. carriers or container leasing companies). They often deodorize, disinfect, clean and repair these containers. In addition, they may manage the stocks and distribution of containers on behalf of their owners.

#### IV. Issues relating to scope of application of uniform rules

25. Prevailing views were expressed at the eighth session of the Working Group concerning two issues bearing upon the scope of application of the uniform rules: that the rules should apply only when safekeeping was involved, and that the rules should apply only in the context of international transport (A/CN.9/260, paragraphs 14 and 23). These issues are discussed in the following subsections.

##### A. Safekeeping of goods

26. Since safekeeping of goods is a key element in the delimitation of the scope of application of the uniform rules, it is important for there to exist within the Working Group a common understanding as to the meaning of safekeeping. Also, it will be useful for the uniform rules themselves to define what is meant by this term.

27. For the purpose of determining the scope of application of the uniform rules, safekeeping may be defined as the exercise by an operator of custody over goods within an area under his control. This definition has two key elements: the concept of custody and that of an area being under the control of the operator.

##### 1. Custody

28. The concept of custody connotes the keeping, guarding, care, or security of the goods. It carries with it the notion of the goods being within the immediate physical control of the one exercising custody. It would usually not be applied in cases where a person has the overall legal responsibility over or ownership of goods, but does not have immediate physical control. In some cases, whether goods are within the custody of an operator may depend upon provisions of the contract between the operator and his customer, or upon laws, regulations or usages applicable at the place where the goods are located. For example, when an operator performs loading or unloading operations, or operations on or within a means of transport, such as stowage, dunnage, lashing or trimming (see paragraph 16, above), such contractual provisions, laws, regulations or usages may determine whether and, if so, when, the goods come into or leave the custody of the operator. In the case of operators such as stevedores or longshoremen who simply supply labour and equipment to be used in loading or unloading goods and who perform their operations exclusively within a means of transport or within the premises of another operator, such operators would often not be considered to have custody of the goods during the operations performed by them.

##### 2. Area under control of operator

29. The area under the control of the operator includes an area where the operator is an exclusive occupant (e.g. as an owner or as a lessee). The operator would be an

exclusive occupant in the area within the boundaries of the terminal or other premises of the operator and, in most cases, the water areas adjacent to quays where vessels serviced by the operator are moored. In the case of offshore loading and unloading terminals for bulk or liquid goods, vessels moor alongside loading and unloading platforms which are linked to the shore terminal by a pipe or other conveyor of the goods to and from the vessel. The offshore platform and conveyor would be regarded as areas under the control of the operator.

30. The area under the control of the operator should perhaps also include areas where the operator is not an exclusive occupant, but to which he has a right of access and use in common with other operators or other entities, such as wharves which are shared by two or more operators. An operator using such a wharf or comparable area could be deemed to have the area within his control during the time when he has an exclusive right to its use for the purpose of loading, unloading or performing other operations with respect to goods.

31. The Working Group may wish to consider whether the area under the control of the operator for the purpose of defining safekeeping should be limited to the types of areas described in the preceding paragraphs, or whether the operator should be considered to be in control of any area which he occupies for the performance of operations with respect to the goods, even those which he does not occupy exclusively, such as areas within the premises of carriers or other operators. Such an approach would considerably broaden the scope of safekeeping. It would, for example, include operations performed by operators within or on board a means of transport (e.g. stowage, dunnage, lashing and trimming). It would also include the operations of longshoremen and stevedores, if the goods were within the custody of those operators.

##### 3. Application of definition in concrete cases

32. To assist in a further understanding of the possible scope of the definition of safekeeping proposed above, the following paragraphs contain examples of concrete situations which would and which would not constitute safekeeping.

33. The following situations would be covered by the definition of safekeeping proposed above, and would be covered by the uniform rules if the requisite relation to international carriage also existed (see section B, below):

(a) When the goods (including, e.g., those within containers as well as the containers themselves) are in indefinite or long-term storage within an area under the control of the operator;

(b) When the goods are kept by the operator in a transit shed or transit area under his control;

(c) During those portions of loading and unloading operations when the goods are within the custody of the operator in an area under his control (see paragraph 28, above);

(d) When the goods are unloaded by the operator from one means of transport, brought within an area under his control and immediately loaded on to another means of transport, whether or not the goods ever become stationary within the area or actually touch the ground. In such cases safekeeping would exist during the period when the goods were within the custody of the operator and within an area under his control. Note may be taken of the case of a sea terminal dealing with bulk goods or with containers where equipment of the operator extending beyond the edge of the quay picks up the goods from one vessel moored alongside the quay and immediately deposits them in another vessel, also moored alongside the quay, without bringing the goods back over the edge of the quay. In most cases the mooring area adjacent to the quay would be included within the premises owned by or leased to the operator, or would be an area to which the operator had a right of access and use in common with others, and safekeeping could thus be said to exist during the performance of those operations. Where it is not, safekeeping would not exist;

(e) While the goods are within the custody of the operator within an area under his control and are undergoing any other operations (e.g. packing and re-packing, packaging, consolidation, preparation and processing: see chapter III, C and E, above);

(f) While goods are in or on a rail wagon or lorry chassis within an area under the control of the operator, during such time as the wagon or chassis is within the custody of the operator (e.g. until the road or rail carrier takes over the chassis or wagon);

(g) While goods are on a barge in water alongside the operator's quay, during such time as the barge is within the custody of the operator (e.g. until it is taken over by the carrier of the barge), if the water area is under the operator's control.

34. In the following situations the goods would not be within the safekeeping of the operator under the definition proposed above:

(a) During operations performed by an operator with respect to goods on or within a means of transport and performed under the control of the carrier, as in the cases of stowage, dunnage, lashing, and trimming. These operations would be excluded because they do not take place within an area under the operator's control as defined above, and in most cases also because the goods are not in the custody of the operator (see paragraph 28, above);

(b) During those portions of loading and unloading operations when the goods are not within the custody of the operator or within an area under his control;

(c) During operations performed by an operator while the goods are within an area under the control of another operator (see paragraph 7, above), for example, in the case of stevedores or longshoremen who simply remove the goods from a means of transport located within or alongside the premises of another operator, and either deposit the goods in those premises or carry the

goods through those premises and load them on to another means of transport. The goods would not be within the safekeeping of the operator who performed those operations, although they could be within the safekeeping of the operator within whose premises the goods were deposited or carried if that operator could be said to have custody of them;

(d) During other operations performed with respect to goods, such as fumigation and inspection (see paragraph 7, above), while the goods were within the custody of, and an area under the control of, another operator or a carrier. The goods would be in the safekeeping of the operator who has the custody of the goods, and not the one performing the operations.

### B. Relationship with international carriage

35. With respect to the required relationship of the uniform rules with international carriage, a choice may be made as to the focus of this relationship. The following possibilities exist: (a) that the safekeeping and other operations to be covered by the rules must be related to international carriage, and (b) that the goods to be covered by the uniform rules must be involved in international carriage. The approach designated as (a) was the one adopted in the UNIDROIT preliminary draft Convention (article 2 (b)). The choice between these two approaches may make little difference with respect to the points of time at which the uniform rules apply or cease to apply. However, for ease of analysis, and on the theory that the objective of the uniform rules is to deal with liability for loss of or damage to goods while the operator is responsible for them, rather than a failure of the operator to achieve certain results from particular operations, the following discussion will be based on the approach designated as (b), without, however, prejudging the ultimate result on the issue. The discussion would apply equally to either approach.

36. With respect to the nature and extent of the required involvement of the goods in international carriage, and thus the breadth of application of the uniform rules, the following illustration may be considered:

(domestic) (domestic) (int'l) (domestic) (domestic)  
 consignor — A — B — C — D — consignee  
 [——— State X ———] [——— State Y ———]

In this illustration goods are transported domestically to operator A (e.g. an inland road or rail terminal) located in State X. There, they are taken over by another domestic carrier and transported to operator B (e.g. a sea terminal) also located in State X. At B, the goods are loaded on to a means of transport (e.g. a ship) and transported internationally to operator C (e.g. a sea terminal) located in State Y. There, they are taken over by a domestic carrier and transported to operator D (e.g. an inland road or rail terminal) located in State Y. They are then transported to the consignee.

37. The Working Group may wish to consider whether the uniform rules should cover goods in the custody of all of the operators in the chain of transport from the consignor to the consignee (i.e. A, B, C and D). Such a result may be appropriate when the goods are covered by a contract for multimodal transport or combined transport, in which the multimodal transport operator (MTO) or combined transport operator (CTO) undertakes to perform or procure the carriage of the goods as a principal from the consignor to the consignee. In such a case the goods would be legally as well as factually involved in international carriage at all stages in the chain of transport. Moreover, in the case of an MTO who is subject to a unitary liability regime such as will exist under the United Nations Convention on International Multimodal Transport of Goods (the "Multimodal Convention") when it comes into force, his right of recourse against each operator within the chain would be best protected by subjecting all of them to the uniform rules, since the liability regime applicable to the operator under the uniform rules would be similar to that applicable to the MTO under the Multimodal Convention. In the case of the CTO, the question of protecting the right of recourse against an operator by co-ordinating the liability regimes applicable to the CTO and to the operator would in some cases be less important. Combined transport contracts typically provide in essence that in cases where the loss or damage can be proved to have occurred during a particular stage of carriage, the liability of the CTO is governed by the mandatory liability regime (i.e. one which cannot be departed from by contract) applicable to that stage under an international convention or national law. In such cases, therefore, the regime governing the liability of the CTO would be the same as the regime governing an operator against whom he seeks recourse. However, the question of recourse is important for a CTO where loss or damage can be proved to have occurred while the goods were in the custody of an operator, but the liability regime under national law can be departed from by contract. In such cases the CTO is typically subject to a more severe liability regime under his combined transport contract with his customer than the regime governing the operator's liability to the CTO.

38. Even in the case of segmented transport (i.e. when each stage of the transport is performed pursuant to a separate contract and is governed by a separate liability regime) the goods could be regarded as being factually involved in international carriage while they are in the custody of all of the operators in the chain of transport. There would be maximum uniformity if the uniform rules covered goods in the custody of all such operators. However, it may be questioned whether such uniformity is necessary. In this regard it may be noted that operators A and D in the illustration in paragraph 36, for example, each take over the goods from a domestic carrier and hand them over to another domestic carrier. The liabilities of those carriers for loss of or damage to the goods would be governed by domestic law. The goods in the custody of such operators are not involved in international carriage in the legal sense; and operations performed by these operators with respect to the goods

would not be immediately relevant to the relationship between parties to a contract of international carriage (see, e.g., paragraphs 67 and 68, below). Since an international carrier (other than an MTO or a CTO, discussed in the previous paragraph) would not be responsible for the goods in the custody of the operators, the necessity to protect the right of recourse of an international carrier does not arise. It therefore might be considered unnecessary for an international uniform regime to govern the liability of those operators, whether from the point of view of a claim by the cargo interest directly against the operator, or a recourse action by a carrier against the operator.

39. With regard to the way in which the involvement of the goods in international carriage is to be formulated in the uniform rules, the Working Group at its eighth session favoured an objective approach (A/CN.9/260, paragraph 20). If it were desired that the uniform rules cover goods in the custody of all operators within the chain of transport of goods from one State to a destination in another State (e.g. in the custody of operators A, B, C and D in the illustration in paragraph 36), the rules might provide that they apply to goods involved in carriage in which the place of departure and the place of destination are situated in two different States.<sup>5</sup> However, such a formulation might give rise to questions in particular situations. An example is the following case: in the illustration given in paragraph 36, above, operator A, who received the goods from the domestic carrier, is a distribution centre (see paragraph 17, above); when the goods were transported to A, the consignor had not yet sold the goods and thus had not determined their ultimate destination, but he instructed A to store the goods pending further instructions; one month later, the consignor sold the goods to a foreign buyer and instructed A to hand them over to a domestic carrier to be transported to B, who would hand the goods over to the international carrier. In such case a question may arise as to whether the goods became involved in international carriage when they were handed over by the consignor to A, or only when they were handed over by the domestic carrier to B. It may be noted that in the case given even when A is instructed to hand the goods over to a domestic carrier for transport to B, he might not know that the goods will ultimately be transported to another State. The transport documentation which would be handled or seen by A would not necessarily show that the goods were to be transported internationally (see paragraphs 46 to 49, below).

40. Another approach may be, for reasons given in paragraph 38, above, to limit the scope of the uniform rules to goods which are in the custody of an operator who deals directly with an international carrier (e.g. goods in the charge of operators B and C in the illustration in paragraph 36, above). A starting point for such an approach might be to provide that goods are

<sup>5</sup>This is in essence the approach adopted in the UNIDROIT preliminary draft Convention (article 2(b)) and one which received support within the Working Group (see A/CN.9/260, paras. 20 and 21).

involved in international carriage if the operator takes over the goods from an international carrier, i.e., one who carries the goods from a place of departure in one State to a place of destination in another State, with instructions to hand them over to someone entitled to take delivery of them (e.g. another carrier or the consignee), and when the operator takes over the goods from anyone (e.g. the consignor or a carrier) with instructions to hand them over to an international carrier. In both cases, the instructions might appear on a document accompanying the goods (e.g. a transport document or a cargo manifest); or they may be communicated to the operator by a relevant party (e.g. a carrier or a cargo interest) or his agent. The reasons for the requirement in each case that the indicated instructions be given to the operator when he takes over the goods are the following. Where the consignor hands over the goods without an undertaking to deliver the goods to an international carrier (e.g. the case where a supplier delivers goods to a distribution centre with instructions to store the goods for an indefinite period of time until they are sold by the supplier and the supplier further instructs the distribution centre regarding to whom to hand them over), it may not be realistic to consider the goods to be involved in international carriage unless and until the operator is instructed to hand the goods over to an international carrier (see paragraphs 43 and 44, below), or unless they are the subject of a combined or multimodal transport contract (see paragraph 42, below). Similarly, when an operator takes over goods from an international carrier without instructions as to their further disposition, the international carriage might be regarded as having ended when he takes them over. It may be noted that cases in which an operator takes over goods without instructions as to their further delivery are often cases where the goods are to be stored by the operator for an indefinite or long period of time (e.g. by a distribution centre pending instructions from his customer regarding to whom to deliver the goods) or where the operator is the final destination of the goods. The requirement that the goods be taken over by the operator with instructions as to their delivery would exclude these cases from the uniform rules. (However, such goods might later be deemed to be involved in international carriage if the customer later instructs the operator to deliver them to an international carrier: see paragraphs 43 and 44, below). If the Working Group wished to include within the coverage of the uniform rules the cases described above in which the operator takes over the goods without instructions as to their delivery, it could provide simply that the goods are considered to be involved in international carriage if the operator handed them over to an international carrier or took them over from an international carrier.

41. If it is decided that an international carrier should be covered by the uniform rules during a period when he is not responsible for the goods under an international convention or even under national law governing carriage (see paragraph 50, below), then the goods may be considered to be involved in international carriage when he takes them over, as well as during any period when he retains them after his responsibility as a carrier ends.

42. In some cases, goods which are the subject of a contract for multimodal transport or combined transport may be within the custody of an operator, who is not the MTO or CTO, in circumstances other than those mentioned above. For example, the operator may receive the goods from a consignor or a domestic carrier with instructions to hand them over to a domestic carrier. The Working Group may wish to consider whether such goods should also be considered to be involved in international carriage. First, such goods may in a factual sense be regarded as being involved in international carriage. Second, considering such goods to be involved in international carriage and thereby making the uniform rules applicable to them would protect the right of recourse against the operator by an MTO, and in many cases by a CTO (see paragraph 37, above).

43. The Working Group may wish next to consider cases in which goods which are not involved in international carriage might be converted into being involved in such carriage while still in the custody of the same operator. For example, goods may be deposited with an operator by his customer for storage with no instructions as to their delivery and for an indefinite period of time, and the customer may later decide to transport the goods internationally. Or, the operator may receive the goods from a person or entity who is not an international carrier, with instructions to deliver to another person or entity who is not an international carrier, and the customer may later change his mind and instruct the operator to deliver the goods to an international carrier. With respect to such situations, an approach may be to provide that the goods are converted to being involved in international carriage when the operator agrees to deliver the goods to an international carrier. Such an agreement might occur, for example, when the operator enters into a new contract with his customer in which he undertakes to deliver the goods to an international carrier, when he accepts instructions from his customer to effect such delivery, or, if such instructions have not previously been accepted, when he begins to implement such instructions.

44. The uniform rules may also deal with the case where goods which are involved in international carriage may cease to be so involved. This could occur when the operator takes over goods from a person who is not an international carrier with instructions to deliver them to an international carrier, or takes over goods from an international carrier with instructions to deliver them to a person entitled to take delivery of them (who may or may not be an international carrier), and either the instructions concerning delivery are withdrawn or amended, or the operator cannot comply with such instructions (e.g. due to an inability to locate the person or entity who is to receive the goods or the failure of such person to take over the goods). In such cases the question of involvement of the goods in international carriage might be resolved in the following ways:

(a) *Where the operator has taken over the goods from a person who is not an international carrier with instructions to deliver the goods to an international carrier. If the instructions are withdrawn or amended so as to require*



delivery of the goods to an entity who is not an international carrier or if the operator cannot effect delivery to the international carrier, one approach may be to provide that the goods are not considered to have been involved in international carriage at all from the time the operator took them over. The theory behind this approach is that the goods would not have actually entered international transport. Another approach may be as follows: in the case of the withdrawal or amendment of the instructions, to provide that the goods cease to be involved in international carriage from the time of the withdrawal or amendment of the instructions; in the case of inability of the operator to effect delivery to the international carrier, to provide that the goods cease to be involved in international carriage either after the expiration of a reasonable period of time after the operator has placed the goods at the disposal of the international carrier or at such time as the operator and his customer may agree. In any event, if the operator later agrees to deliver the goods to an international carrier (e.g. by accepting instructions to deliver the goods to an international carrier), or becomes able to deliver the goods to the international carrier, the goods might be considered as being involved in international carriage from the time of such agreement or when the operator begins to effect such delivery, as the case may be. The operator may be regarded as beginning to effect such delivery when, for example, he prepares the goods for transport or moves them from a long-term storage area to a transit area;

(b) *Where the operator has taken over the goods from an international carrier with instructions to deliver them to a person entitled to take delivery of them.* An approach may be to provide that the involvement of the goods in international carriage ends when the original instructions concerning delivery are withdrawn, or, if the person to whom the operator was instructed to deliver the goods cannot be located or the operator otherwise cannot effect such delivery, either upon the expiration of a reasonable period of time after the operator has placed the goods at the disposal of that person, or at such a time as the operator and his customer may agree.<sup>6</sup> It may be questioned whether the international carriage should be considered finally to have come to an end upon such events, or whether the goods might again be considered to be involved in international carriage if the operator later agrees to deliver the goods to an international carrier, or when the operator begins to effect delivery to the original international carrier, as the case may be.

45. Under the approaches discussed above it may be difficult in some cases to establish whether loss or damage suffered by the goods occurred while they were involved in international carriage, or before such involvement began or after it ended. To deal with such cases, the

<sup>6</sup>For example, general conditions of one operator contain the following provision: "The temporary warehousing which [the operator] performs in the scope of its stevedoring services, lasts up to 14 days after the goods have been unloaded from the vehicle, unless a shorter or longer term has been agreed upon. After this time-limit, the client has either to remove the goods, or to make an agreement on public warehousing of the goods, in compliance with these General terms and conditions."

uniform rules might provide a rebuttable presumption that the loss or damage occurred while the goods were involved in international carriage.

46. An additional question which the Working Group may wish to consider in connection with the formulation of the requisite relationship with international carriage is the possibility of applying a particular formulation satisfactorily in practice. This may be viewed from two perspectives – that of the operator and his insurer being able to determine whether or not goods are involved in international carriage at or before the time when the operator takes over the goods (e.g. with respect to the operator's liability insurance coverage and the price to be charged by the operator for his services), and that of an operator and his insurer, and a court or arbitral tribunal, being able to make this determination after a question or dispute has arisen. It may also be important for the operator to know at the time when he takes over goods whether they are involved in international carriage if his obligations in respect of documentation are different under the uniform rules from what they would be under the otherwise applicable law.

47. It may not be necessary for an operator or his insurer to identify with certainty at the time of taking over the goods whether that particular consignment of goods is or is not involved in international carriage, and thus subject to the liability regime under the uniform rules. With respect to liability insurance coverage, for example, an operator may obtain coverage on a blanket basis, under which the insurer would cover the operator's liability for all goods in his custody, whether liability was under the legal regime of the uniform rules or not. The cost of such coverage would be an overall premium based upon an estimate that a certain percentage of the goods coming within the custody of the operator would be subject to the liability regime under the uniform rules, and the rest would be subject to another liability regime. This overall cost would be incorporated by the operator in his general pricing scheme. With respect to documentation which the operator is obligated to issue, the operator would not have to know the status of the goods when he takes them over if the document which he issues is adequate to satisfy his obligations both under the uniform rules and under rules of law which would otherwise apply (e.g. if he routinely issues a document which includes at least the information which he would be obligated to include if the goods were covered by the uniform rules). His normal document would be more likely to satisfy the requirements of the uniform rules if these requirements were restricted to a minimum.

48. In any event, under the approach described in paragraph 39, above (i.e. where the uniform rules apply to goods involved in carriage in which the place of departure and the place of destination are situated in two different states), in most cases it would be evident to an operator when he takes over goods whether or not the goods were involved in international carriage. For example, the goods may be accompanied by a transport document or another document indicating that the places

of departure and destination are located in two different States. Moreover, in the illustration given in paragraph 36, above, operators B and C (who hand the goods over to and take them over from the international carrier) would know of the involvement of the goods in international carriage. Under the approach described in paragraphs 40 to 42, above (i.e. limiting the scope of the uniform rules to goods which are in the custody of an operator who deals directly with an international carrier), there is an even greater likelihood that the operators who would be subject to the rules would know of the involvement of the goods in international carriage.

49. Even if it is not necessary for an operator to be able to identify with certainty at the time of taking over goods whether the goods are involved in international carriage, when goods do suffer loss or damage while in the custody of the operator, it would ultimately have to be determined whether or not the operator's liability was governed by the uniform rules (e.g. in the context of negotiation between the operator and his insurer, or between the operator or his insurer and the claimant or, if necessary, in dispute settlement proceedings). Either of the approaches to formulating the requisite link with international carriage discussed above (i.e. those discussed in paragraph 39 and in paragraphs 40 to 42), could be applied with reasonable facility in negotiations or by dispute settlement bodies to determine whether or not the goods were involved in international carriage.

## V. Periods of responsibility of carrier

50. The following discussion concerns the periods of responsibility of carriers<sup>7</sup> engaging in various modes of transport of goods under international transport conventions.<sup>8</sup> The time when this responsibility begins and ends are of relevance in two respects. First, in some cases a carrier in charge of goods may be responsible for the goods under the convention only for part of the period during which the goods are in his charge, and may be responsible for the goods as a bailee for the remaining time. By virtue of international transport conventions a degree of uniformity has been achieved as to the liability of carriers for loss of or damage to goods during periods of carriage regulated by the conventions; however, the liability of carriers for loss of or damage to goods in their custody outside those periods remains subject to disparate rules contained in contracts between carriers and cargo interests, and in rules of national law. The Working Group might consider it desirable to promote uniformity with respect to the liability of carriers for loss or damage occurring during those later periods by having the uniform rules on the liability of operators cover the safekeeping of goods by carriers during those periods. A consideration of the situations which may arise in this

regard might assist the Working Group in considering this issue.

51. Second, during a period when the goods are in the custody of an operator, the carrier may also be responsible for the goods, either as a carrier under an international transport convention or as a bailee. If so, and if the goods suffer loss or damage during this period, the carrier would be liable to the cargo interest and would seek recourse from the operator. The ability of the carrier to obtain full recourse would depend upon the extent to which the rules governing the liability of the operator coincide with the rules governing the liability of the carrier.

52. International transport conventions vary with respect to the points of time when the responsibility of a carrier for goods as a carrier under the conventions begins and ends. Relevant provisions of such conventions are set forth in the following paragraphs.

### A. International transport conventions

#### 1. Carriage of goods by sea

53. *International Convention for the Unification of Certain Rules of Law relating to Bills of Lading (1924)* [Original: French]. The carrier's responsibility for the goods as a carrier covers the period "from the time when the goods are loaded on to the time they are discharged from the ship" (article 1(e)). The Convention provides that the carrier or shipper may enter into an "agreement, stipulation, condition, reservation or exemption as to the responsibility and liability of the carrier or the ship for the loss or damage to, or in connection with, the custody and care and handling of goods prior to the loading on, and subsequent to the discharge from, the ship on which the goods are carried by sea" (article 7).

54. *United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg)* ("Hamburg Rules") Article 4 provides as follows:

"1. The responsibility of the carrier for the goods under this Convention covers the period during which the carrier is in charge of the goods at the port of loading, during the carriage and at the port of discharge.

"2. For the purpose of paragraph 1 of this article, the carrier is deemed to be in charge of the goods

"(a) from the time he has taken over the goods from:

(i) the shipper, or a person acting on his behalf; or

(ii) an authority or other third party to whom, pursuant to law or regulations applicable at the port of loading, the goods must be handed over for shipment;

<sup>7</sup>The term "carrier" as herein used includes a multimodal transport operator under the Multimodal Convention.

<sup>8</sup>It should be noted that the issues discussed in this section also arise when no international convention is applicable to the international carriage, and when the carriage is governed by national law.

“(b) until the time he has delivered the goods:

- (i) by handing over the goods to the consignee; or
- (ii) in cases where the consignee does not receive the goods from the carrier, by placing them at the disposal of the consignee in accordance with the contract or with the law or with the usage of the particular trade, applicable at the port of discharge; or
- (iii) by handing over the goods to an authority or other third party to whom, pursuant to law or regulations applicable at the port of discharge, the goods must be handed over.

“3. In paragraphs 1 and 2 of this article, reference to the carrier or to the consignee means, in addition to the carrier or the consignee, the servants or agents, respectively of the carrier or the consignee.”

#### 2. Carriage of goods by air

55. *Convention for the Unification of Certain Rules relating to International Carriage by Air (1929)* (“*Warsaw Convention*”) [Original: French]. The period of the carrier’s responsibility is the period of “carriage by air”, i.e. the “period during which the luggage or goods are in charge of the carrier, whether in an aerodrome or on board an aircraft, or, in the case of a landing outside an aerodrome, in any place whatsoever” (article 18(2)). If carriage by land, sea or river outside an airport takes place as part of the performance of carriage by air for the purpose of loading, delivery or trans-shipment “any damage is presumed, subject to proof to the contrary, to have been the result of an event which took place during the carriage by air” (article 18(3)).

#### 3. Carriage of goods by road

56. *Convention on the Contract for the International Carriage of Goods by Road (CMR) (1956)*. The carrier is liable for loss of or damage to the goods “occurring between the time when he takes over the goods and the time of delivery...” (article 17(1)).

57. When the carriage cannot be carried out in accordance with the terms of the consignment note, or when the carrier cannot effect delivery of goods after their arrival at the destination,

“the carrier may immediately unload the goods for account of the person entitled to dispose of them and thereupon the carriage shall be deemed to be at an end. The carrier shall then hold the goods on behalf of the person so entitled. He may however entrust them to a third party, and in that case he shall not be under any liability except for the exercise of reasonable care in the choice of such third party” (article 16(2)).

#### 4. Carriage of goods by rail

58. *Agreement concerning the International Carriage of Goods by Rail (SMGS) (1966)* [Original: French].

“The railway shall be liable ... from the time of acceptance for carriage until delivery of the goods at the station of destination, or, where goods are forwarded to a country whose railways are not party to the present Agreement, until dispatch of the goods with a waybill conforming to that laid down in the other international agreement” (article 22(1)).

59. *Appendix B to the Convention concerning International Carriage by Rail (COTIF) (1980)*.

“The railway shall be liable for loss or damage resulting from the total or partial loss of, or damage to, the goods between the time of acceptance for carriage and the time of delivery ...” (article 36(1)).

“Acceptance is established by the application to the consignment note and, where appropriate, to each additional sheet, of the stamp of the forwarding station, or accounting machine entry, showing the date of acceptance” (article 11(1)). This procedure “must be carried out immediately after all the goods to which the consignment note relates have been handed over for carriage” and the relevant charges have been paid or a security has been deposited. “The procedure shall be carried out in the presence of the consignor if he so requests” (article 11(2)). “The handing over of goods for carriage shall be governed by the provisions in force at the forwarding station” (article 20(1)).

“Loading shall be the duty of the railway or the consignor according to the provisions in force at the forwarding station, unless otherwise provided in the Uniform Rules or unless the consignment note includes a reference to a special agreement between the consignor and the railway” (article 20(2)). “The consignor shall be liable for all the consequences of defective loading carried out by him ... The burden of proof of defective loading shall rest upon the railway” (article 20(3)).

“It shall be equivalent to delivery to the consignee if, in accordance with the provisions in force at the destination station:

- “(a) the goods have been handed over to Customs or *Octroi* authorities at their premises or warehouses, when these are not subject to railway supervision;
- “(b) the goods have been deposited for storage with the railway, with a forwarding agent or in a public warehouse” (article 28(2)).

“The provisions in force at the destination station or the terms of any agreements with the consignee shall determine whether the railway is entitled or obliged to hand over the goods to the consignee elsewhere than at the destination station, whether in a private siding, at his domicile or in a railway depot. If the railway hands over the goods, or arranges for them to be handed over

in a private siding, at his domicile or in a depot, delivery shall be deemed to have been effected at the time when they are so handed over. Save where the railway and the user of a private siding have agreed otherwise, operations carried out by the railway on behalf of and under the instructions of that user shall not be covered by the contract of carriage" (article 28(3)).

### 5. Multimodal transport of goods

#### 60. *United Nations Convention on International Multimodal Transport of Goods (1980)*:

"The responsibility of the multimodal transport operator for the goods under this Convention covers the period from the time he takes the goods in his charge to the time of their delivery" (article 14(1)). (The delimitation of this period is comparable to the delimitation of the period during which a carrier is responsible for goods under the Hamburg Rules (see paragraph 54, above)).

### B. Summary

61. The identification of precise points of time when the responsibility of a carrier under an international transport convention begins and ends (e.g. when the goods are considered to have been loaded or unloaded, when the carrier is considered to have taken the goods over or taken them in charge, and when he is considered to have delivered them) is extremely complex, subject to differing interpretations,<sup>9</sup> and sometimes depends upon the particular facts of individual cases, including the provisions of the contract between the parties. However, for the purposes of the work of the Working Group, the following general observations may be relevant.

62. Under all international transport conventions, the carrier is responsible for the goods as a carrier during the period of actual transport, and he would not be considered an operator during that period. Therefore, the question of whether the uniform rules on the liability of operators should apply during that period does not arise. Also, since a separate operator is not involved during that period, the question of recourse does not arise.

<sup>9</sup>For example, in some legal systems, under the Warsaw Convention, the carrier ceases to be "in charge" of goods at an airport when the goods are handed over to the consignee or when they have been made available to the consignee. In other legal systems a carrier ceases to be in charge of the goods when he can no longer exercise control and supervision over the goods, e.g. when he complies with an obligation to deliver the goods to the customs authorities at an airport. In still other legal systems the responsibility of the carrier under the contract of carriage does not cease until he ceases to be legally (as distinct from factually) in charge of the goods, and he does not cease to be legally in charge until the goods are accepted by the consignee or his agent. This may occur before, when or after the goods are physically handed over to the consignee or his agent. Some legal systems following the latter approach have held the carrier responsible as a carrier even when the goods were in a customs warehouse. Similarly, questions may arise as to when goods are "loaded" or "unloaded" under the Hague Rules, or when goods are "placed at the disposal" of the consignee under the Hamburg Rules and Multimodal Convention.

63. The situation is more complex with respect to the periods prior to the time when the goods have been loaded on to the means of transport and after they have been unloaded. For example, some shipping companies own facilities where goods are stored and handled prior to or after transport by them, as do railways, road carriers and combined and multimodal transport operators. Prior to loading, the goods may be handed over by the consignor directly to the carrier. The responsibility of the carrier under the regime established by some transport conventions commences when he takes the goods over<sup>10</sup> (e.g. under the Hamburg Rules, Warsaw Convention, CMR, SMGS and Multimodal Convention). Under the Hague Rules, however, the carrier does not become subject to the mandatory liability regime provided therein until the goods are loaded. If he has custody of the goods before that time, he could be regarded as a bailee. Under the Hague Rules the carrier may enter into any agreement or stipulation regarding his responsibility and liability for the goods during that period, as well as during the period after unloading when he retains custody of the goods. Such an agreement could, for example, extend the applicability of the liability regime under the Hague Rules to the periods of time prior to loading or after unloading, or it could limit or exclude liability for loss of or damage to goods during those periods.

64. In other cases prior to loading, the consignor might hand over the goods to an operator for keeping or storage and subsequent loading on to the means of transport. The operator might act either for the consignor or the carrier; also, the operator might be one to whom the goods are required by law to be handed over (e.g. a customs authority) prior to loading for export. If the operator were acting for the consignor, the carrier would normally have no responsibility for the goods. If the operator were acting for the carrier, the carrier might be responsible for the goods prior to loading as a carrier under an international transport convention, or as a bailee, depending upon when, under the convention, his responsibility as a carrier began (e.g. upon taking the goods over or upon loading). In either case, if the carrier were held liable for loss or damage occurring while the goods were in the custody of the operator, he would seek recourse against the operator. In the case of the handing over of the goods by a consignor to a customs authority or similar entity, questions may arise as to when the goods had been handed over by the consignor or taken over by the carrier.

65. The situation at the end of transport is comparable to the situation before the beginning of transport. After unloading, the goods may be retained by the carrier, or they may be deposited with an operator engaged by the carrier or by the consignee or with a customs authority. The points of time when the responsibility of a carrier for the goods under the international transport convention

<sup>10</sup>Sometimes the responsibility commences when the goods are located in specific places, e.g. under article 4(1) of the Hamburg Rules, at a port. That raises the question, however, whether a container yard operated as part of a port, but not physically contiguous to the berthing facilities, is a part of the port under that text.

ends vary widely. For example, such responsibility may end when the goods are unloaded (as under the Hague Rules), when the goods are handed over to the consignee or his agent (as in some cases under the Hamburg Rules, COTIF and Multimodal Convention), when the goods are deposited for storage (as in some cases under COTIF), when the goods are handed over to customs authorities (as in some cases under the Hamburg Rules, COTIF and Multimodal Convention); when the goods are placed at the disposal of the consignee (as in some cases under the Hamburg Rules and Multimodal Convention), or when the carrier ceases to be "in charge" of the goods (as under the Warsaw Convention). In some of these cases the goods may remain in the custody of the carrier or of an operator engaged by him after his responsibility as a carrier under the international transport convention has ended (e.g. after the goods are unloaded, or after the goods are placed at the disposal of the consignee). The results with respect to the status of the carrier after his responsibility as a carrier under an international transport convention ends, and the overlapping of the liability of the carrier with that of an operator and its implications with respect to recourse actions, are analogous to those prior to the beginning of transport and discussed in the previous paragraph.

## VI. Inspection of goods taken over by operator

66. During transport, when goods are handed over by one party and taken over by another they are often inspected as to their apparent or observable condition and as to their quantity (i.e. weight, count, volume or dimensions). The results of the inspection may be recorded in a document issued by the party who takes over the goods. Such documents may serve as evidence of the condition or quantity of the goods when they were taken over by the various carriers and intermediaries in the transport chain, and thus help to establish the stage at which any loss of or damage to the goods occurred. This would be relevant in an action by a cargo interest against a carrier or an operator, or by a carrier against an operator in a recourse action. The last party in the transport chain – the consignee – usually must, within a short period of time after taking over the goods, inspect the goods and notify the relevant parties of any loss or damage. If he fails to do so he may lose the right to claim for such loss or damage.

67. When an inspection is performed upon goods taken over by an operator, the inspection will in some cases be immediately relevant only to the contractual relationship between the operator and his customer. Thus, when an operator acting for a consignor takes over the goods from the consignor, or an operator acting for a carrier takes over the goods from the carrier, an inspection establishing the condition or quantity of the goods when the operator took them over will be immediately relevant only in a claim by the consignor against the operator, or in a claim by the carrier against the operator, as the case may be.

68. In many cases, however, an inspection of goods taken over by an operator will also be immediately relevant to the relationship between the parties to a contract of carriage. For example, if a carrier under an international transport convention becomes responsible for goods as a carrier upon taking them over, and an operator acts in his behalf in taking goods over from a consignor or another carrier, an inspection at the time of taking over the goods by the operator would establish the condition of the goods at the time the carrier became responsible for them as a carrier, and would be relevant in a claim by the cargo interest against the carrier under the contract of carriage. It would also be relevant in a recourse action by the carrier against the operator, and in an extra-contractual claim by the cargo interest against the operator.

69. Similarly, if at the end of carriage the goods are taken over from a carrier by an operator acting for the consignee, an inspection is relevant in a claim by the consignee against the carrier as well as in one against the operator. Moreover, in such cases the operator might be obligated by law or by his contract with the consignee to protect the rights of the consignee against the carrier, by giving due notice to the carrier of any loss of or damage to the goods discovered upon taking them over.

70. The current practices with respect to the inspection of goods taken over by operators vary widely. Whether an inspection is performed at all, and if so, the scope of the inspection, depends on such factors as the nature of the goods, the equipment available to the parties, the time and expense involved in an inspection, the nature and duration of the operations to be performed by the operator, whether the inspection is relevant to the rights of his customer under a contract of carriage (see paragraphs 67 and 68, above) and the scope of the inspection needed under the law governing the carriage. When goods are transferred by the operator directly from one means of transport to another, they are seldom inspected unless the customer of the operator requests an inspection. An inspection is also sometimes dispensed with where only very short-term storage is involved. When an inspection is performed, usually only certain particulars concerning the goods are checked. For example, inspection of containerized goods is normally limited to checking the apparent condition of the container and counting the number of containers loaded or unloaded. Containers may in some cases be weighed (e.g. when there exist grounds to doubt the weight noted on a transport document). Inspecting the condition of goods is sometimes dispensed with where the risk of damage to the goods is small (e.g. in the case of iron ore). Such goods are in many cases, but not always, weighed. The weighing of goods may in some cases be too time-consuming or expensive, as in the case of large quantities of bulk cargo of low specific value. The counting of goods consisting of a large number of items may in some cases be impractical, and may be replaced by weighing or checking volume. In some cases, the operator may take samples of the goods for analysis, but usually only upon the request of his customer.

71. When an inspection is performed upon goods taken over by an operator from a carrier, and also when the operator hands the goods over to a carrier, it is often, but not always, performed in the presence of representatives of the operator as well as of the carrier. In some cases, a representative of the cargo interest may also be present.

72. With respect to documentation issued by operators, here, too, the practice varies. In some cases no document is ever issued (e.g. in cases in which the goods are within the custody of the operator for only a short period of time, such as in the case of direct transfer of goods from one means of transport to another). Also, in some cases, an operator who takes over goods issues certain documents relating to the transport of the goods (e.g. an airport operator may issue a cargo manifest, or on behalf of the carrier, an air waybill), and does not issue a separate depository document. In other cases a deposit-

ory document is issued only upon request of the customer; in still other cases it is issued as a matter of course. The contents of the document and the time of issuance depend in part upon the scope and time of the inspection. In some cases an operator issues a simple receipt for the goods. This may take the form of a separate document, or may be simply a stamp upon an existing document, such as a transport document. In other cases, a document is issued containing information relevant to the condition or quantity of the goods when they were taken over. Even when the document contains information about the condition or quantity of the goods, it may contain a reservation, such as "customer's information" or "said to contain", in effect denying responsibility for the accuracy of the information. Such reservations are included in cases where inspection was performed when the operator took over the goods, as well as in cases where an inspection was not performed.

**2. Liability of operators of transport terminals: draft articles of uniform rules on the liability of operators of transport terminals and comments thereon: note by the secretariat (A/CN.9/WG.II/WP.56)**

[Original: English]

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## INTRODUCTORY NOTE

1. This document contains the text of draft articles of uniform rules on the liability of operators of transport terminals, together with comments on those draft articles, to serve as a basis for discussion by the Working Group in connection with the formulation of uniform rules. A decision has not yet been taken as to the ultimate form of the rules. However, at its eighth session the Working Group agreed that its discussions should proceed under the assumption that the uniform rules would have a normative character (e.g. a convention or a model law) rather than a contractual character (e.g. general contract conditions) (A/CN.9/260, paragraph 13). For ease of analysis, the present text has been drafted as a model law. The substance of the draft articles would be the same under either a convention or a model law. However, a convention would contain certain additional provisions, such as a preamble and final clauses. Such provisions could be provided at a later time if the Working Group decided that the uniform rules should be cast in the form of a convention (see *ibid.*, paragraph 90).

2. The comments following each draft article generally do not repeat points made with respect to the same or similar articles of the UNIDROIT preliminary draft Convention on the Liability of Operators of Transport Terminals (reproduced in A/CN.9/252, annex II, and hereinafter referred to as the "UNIDROIT draft") in the Explanatory Report to that draft text prepared by the UNIDROIT secretariat (reproduced in A/CN.9/WG.II/WP.52/Add.1, annex).

### Draft articles of uniform rules on the liability of operators of transport terminals

#### Article 1

#### DEFINITIONS

For the purposes of this Law:

(1) (a) "Operator of a transport terminal" (hereinafter referred to as "operator") means any person engaged against remuneration who undertakes the safekeeping of goods before, during or after carriage with a view to handing the goods over to any person entitled to take delivery of them.

(b) A carrier may be considered to be an operator under this Law, except that he shall not be considered to be an operator in respect of goods during the period of his responsibility for the goods under an international transport convention or national law governing unimodal, combined or multimodal transport.

(2) "Safekeeping" means the exercise of custody over goods in an area under the exclusive control of the person exercising the custody or in an area in respect of which he has a right of access and use in common with others.

(3) "Goods" includes any container, trailer, chassis, barge, pallet or similar article of transport or packaging, if not supplied by the operator.

(4) "Carrier" means any person who concludes a unimodal, combined or multimodal transport contract as a principal and who assumes responsibility for the performance of the contract.

[(5) "International carrier" means any carrier who performs carriage in which the place of departure and the place of destination are located in two different States.]

#### Comments

1. *Paragraph (1)(a) and (b)* The use in a legal text of the term "operator" rather than "OTT" as a shorthand expression for operator of a transport terminal may be preferable from a stylistic point of view.

2. The phrase "person engaged against remuneration" has been included rather than the phrase "person ... who undertakes against remuneration the safekeeping of goods", which appears in the UNIDROIT draft (article 1(1)), for the following reason. Under the UNIDROIT draft, the safekeeping must be undertaken against remuneration. However, in the frequent cases where an operator undertakes to perform certain handling or other operations with respect to goods within his safekeeping, it is likely that the remuneration received by the operator will be more for those operations than for the safekeeping, which will be ancillary to the operations. In some of these cases a question may arise as to whether safekeeping has been undertaken against remuneration.

3. The phrase "acting in a capacity other than that of a carrier", which appears in article 1(1) of the UNIDROIT draft, has been omitted and paragraph (1)(b) has been included in the present draft article. Among the consequences of paragraph (1)(b) are the following. By virtue of the definition of "carrier" in paragraph (4), it would exclude from the scope of the uniform rules carriers performing a unimodal transport contract during their periods of responsibility for the goods under an international transport convention or national law governing carriage. The carriers excluded would be those who actually carry the goods (e.g. "actual carriers" under article 1(2) of the Hamburg Rules) as well as carriers who conclude contracts of carriage with shippers but who entrust the actual carriage to other carriers (e.g. "carriers" under article 1(1) of the Hamburg Rules). Paragraph (1)(b) of the present draft article would also exclude from the scope of the uniform rules combined and multimodal transport operators during their periods of responsibility for the goods under international conventions or national laws governing combined or multimodal transport contracts. For example, when the United Nations Convention on International Multimodal Transport of Goods (the "Multimodal Convention") comes into force, if an entity (e.g. a freight forwarder) entered into a multimodal transport contract with a consignor to transport and deliver goods to a consignee,

he would be responsible for the goods under the Convention from the time when he took them in his charge from the consignor until the time of delivery to the consignee. As a result, at no time during that period would he be subject to the uniform rules. Thus, if the goods were in his custody for safekeeping during that period, he would be subject to the Convention and not to the uniform rules. However, if he engaged a terminal operator to store and handle the goods during that period, the terminal operator, not being subject to an international transport convention or national law governing carriage, would be subject to the uniform rules, thus protecting the right of recourse by the multimodal transport operator against the terminal operator.

4. An entity might enter into a combined transport contract as a principal with a consignor to transport goods from the consignor to the consignee using different modes of transport, and the combined transport contract might not be covered by an international transport convention or national law governing carriage. Rather, during certain stages of the combined transport, such as the actual carriage of the goods, the entity would be governed by an international transport convention or national law governing carriage (see A/CN.9/WG.II/WP.55, paragraph 37). If the goods were in the custody of the combined transport operator during the period of his responsibility for the goods under such a convention or national law, he would not be subject to the uniform rules in respect of those goods. However, he would be subject to the uniform rules in respect of goods within his custody outside that period of responsibility.

5. The phrase "with a view to their being handed over ..." would exclude the case where the operator is the final destination of the goods. In such a case the international carriage may be regarded as having ended when the goods are handed over to the operator, if not before, and any operations performed by the operator would not be in respect of goods involved in international carriage.

6. *Paragraph (2)* Since the draft uniform rules are based upon the safekeeping of goods by the operator, a definition of "safekeeping" may be desirable. The scope and elements of such a definition are discussed in A/CN.9/WG.II/WP.55, paragraphs 26 to 34.

7. *Paragraph (3)* The inclusion of containers, RO/RO vehicles, barges, pallets, and similar items within the definition of "goods" means that they would be within the scope of the uniform rules. The liability regime would therefore extend, for example, to empty containers which the operator undertook to store for their owners. This would mean, among other things, that the evidentiary effect of a document issued by an operator in respect of containerized cargo would relate to the condition of the container, as well as to that of the goods inside. Also, the rules relating to the operator's rights of security in the goods might also cover the container and similar items (but see comment 7 to draft article 10). It may be noted, however, that in some legal systems a container belonging to a ship is assimilated to the ship, and liability for

damage to such a container is governed not by general legal rules relating to damage to goods, but by rules of maritime law relating to damage to the ship. Other legal systems have treated containers as part of the packing of the goods. States in which a container belonging to a ship is assimilated to the ship and governed by maritime law may have to decide whether liability for damage to the container should continue to be governed by maritime law or whether it should be governed by the uniform rules.

8. *Paragraph (4)* This paragraph is designed to make it clear that the word "carrier" includes combined and multimodal transport operators acting as principals. It is adapted from article 1(2) of the Multimodal Convention. For a discussion of some of the consequences of this definition see comments 3 and 4 to the present draft article.

9. *Paragraph (5)* This definition may be added if needed (see comment 3 to article 2, below).

## Article 2

### SCOPE OF APPLICATION

#### [Alternative 1]

This Law applies whenever:

- (a) the goods are located within the territory of this State, and
- (b) the goods are involved in carriage in which the place of departure and the place of destination are situated in two different States.

#### [Alternative 2]

(1) This Law applies whenever:

- (a) the goods are located within the territory of this State, and
- (b) the goods are involved in international carriage.

(2) Goods are involved in international carriage if:

- (a) they have been taken over by the operator from an international carrier with instructions to hand them over to someone entitled to take delivery of them, or
- (b) they have been taken over by the operator from any person with instructions to hand them over to an international carrier, or
- (c) they are the subject of a combined or multimodal transport contract in which the place of departure and the place of destination are situated in two different States.

(3) Notwithstanding the foregoing, goods in the charge of an international carrier before the period of his



responsibility for the goods as a carrier under an international transport convention or national law governing carriage begins or after such responsibility ends are involved in international carriage.

[Alternative 3]

- (1) [As paragraph (1) of alternative 2]
- (2) [As paragraph (2) of alternative 2]
- (3) [As paragraph (3) of alternative 2, plus the following:] However, if the carrier is unable to deliver the goods to a person entitled to receive them under the contract of carriage, the goods cease to be involved in international carriage at such time as the operator and his customer may agree, or in the absence of such an agreement, upon the expiration of a reasonable period of time after the carrier has placed the goods at the disposal of the person.
- (4) Goods which are not by virtue of paragraph (2) of this article considered to be involved in international carriage when they are taken over by the operator become involved in international carriage when the operator is instructed to hand over the goods to an international carrier.
- (5)
  - (a) If the operator has taken over the goods from a person who is not an international carrier with instructions to hand them over to an international carrier, and the instructions are withdrawn or are amended so as to require the operator to hand over the goods to a person who is not an international carrier, the goods cease to be involved in international carriage from the time of the withdrawal or amendment of the instructions. However, if the operator is later instructed to hand over the goods to an international carrier, the goods shall be considered to be involved in international carriage from the time of the instruction.
  - (b) If the operator has taken over the goods from a person who is not an international carrier with instructions to hand them over to an international carrier, and the operator cannot hand them over, the goods cease to be involved in international carriage at such time as the operator and his customer may agree, and in the absence of such an agreement, upon the expiration of a reasonable period of time after the operator has placed the goods at the disposal of the international carrier. However, if the operator later becomes able to hand over the goods to the international carrier, or if he is instructed to hand over the goods to another international carrier, the goods shall be considered to be involved in international carriage when the operator begins preparations to hand over the goods or is instructed to hand over the goods to the other international carrier.
  - (c) If the operator has taken over the goods from an international carrier with instructions to hand them over to a person entitled to take delivery of

them, and the instructions are withdrawn, the goods cease to be involved in international carriage upon the withdrawal of the instructions. However, if the operator is later instructed to hand over the goods to a person entitled to take delivery of them, the goods shall be considered to be involved in international carriage from the time of the instruction.

- (d) If the operator has taken over the goods from an international carrier with instructions to hand them over to a person entitled to take delivery of them, and the operator cannot hand them over, the goods cease to be involved in international carriage at such time as the operator and his customer may agree, and, in the absence of such an agreement, after the expiration of a reasonable period of time after the operator has placed the goods at the disposal of the person entitled to take delivery of them. However, if the operator becomes able to hand over the goods to an international carrier, or if he agrees to hand over the goods to an international carrier, the goods shall be considered to be involved in international carriage when the operator begins preparations to hand over the goods or from the time of the instruction, as the case may be.
- (6) When pursuant to this article goods in the charge of the operator which were not involved in international carriage upon being taken over by the operator later become involved in international carriage, or goods in the charge of the operator which were involved in international carriage upon being taken over by the operator later cease to be involved in international carriage, any loss or damage suffered by the goods is rebuttably presumed to have occurred while they were involved in international carriage.

*Comments*

1. *General* See A/CN.9/WG.II/WP.55, paragraphs 35 to 49.
2. *Alternative 1* Subparagraph (b) sets forth the approach described in A/CN.9/WG.II/WP.55, paragraph 39. It is the simplest and most flexible of the three alternatives dealing with the required link with international transport, but also the broadest, since it would cover goods in the charge of all operators within the chain of transport of goods from one State to another, even operators who take over goods from a domestic source (e.g. the consignor or a domestic carrier) and hand them over to a domestic recipient (e.g. another domestic carrier or the consignee). In addition, this formulation may give rise to uncertainty in particular cases (see, e.g., A/CN.9/WG.II/WP.55, paragraph 39).
3. *Alternative 2* This alternative sets forth the approach described in A/CN.9/WG.II/WP.55, paragraphs 40 to 42. It is still relatively simple and easy to apply, and is narrower than the approach in alternative 1, since it would, under paragraph (2)(a) and (b) (and subject to the exception in paragraph (2)(c)), cover only goods in the

custody of an operator who took them over from an international carrier or was to hand them over to an international carrier. Under paragraph (2)(c), goods would be covered during the entire period of time when they were the subject of a combined or multimodal transport contract (see A/CN.9/WG.II/WP.55, paragraph 42). The approach reflected in this alternative would in general provide greater certainty in respect of its application than the approach reflected in alternative 1. As pointed out in the last sentence of A/CN.9/WG.II/WP.55, paragraph 40, this approach could be simplified even further by eliminating the requirements in paragraph (2)(a) and (b) concerning the instructions given to the operator. However, this would result in expanding somewhat the scope of the uniform rules. With respect to paragraph (3), see A/CN.9/WG.II/WP.55, paragraph 41. If the approach in alternative 2 is adopted, "international carrier" should be defined. A proposed definition is set forth in draft article 1(5).

4. *Alternative 3* This alternative incorporates alternative (2), but also deals with situations in which goods which were not involved in international carriage when they were taken over by the operator might later become involved in international carriage, and in which goods which are involved in international carriage might cease to be so involved while they are still in the custody of the operator (see A/CN.9/WG.II/WP.55, paragraphs 43 to 45). It may be readily seen that attempting to deal with issues such as these becomes complicated. The Working Group might wish to consider whether it would be preferable not to deal with these issues, even though this would exclude from the scope of the uniform rules some goods which were not involved in international carriage when they were taken over by the operator but which might be viewed as later having become involved in international carriage (e.g. if the operator was later instructed to hand the goods over to an international carrier), and even though it would continue to cover by the uniform rules some goods the involvement of which in international carriage might be viewed to have ceased. Both types of situations are more fully discussed in A/CN.9/WG.II/WP.55, paragraphs 43 and 44.

### Article 3

#### PERIOD OF RESPONSIBILITY

(1) The operator is responsible for the goods from the time he has taken them over until the time he hands them over to a person entitled to take delivery of them.

(2) If the operator has undertaken to perform or to procure the performance of [such operations as] loading, unloading, stowage, trimming, dunnage or lashing of the goods before taking them over or after handing them over, the period of responsibility is extended so as to cover the periods of time when such operations are performed.

#### Comments

1. *Paragraph (1)* The basic period during which the operator is responsible for the goods under the present draft article is the period from the time he takes them over until the time he hands them over. The operator is responsible for the goods during this period regardless of what operations are performed in respect of them. (By virtue of draft article 1(1)(a), the operator must have undertaken the safekeeping of the goods.)

2. *Paragraph (2)* This article extends the period of responsibility to cover cases in which certain operations are performed by the operator before taking the goods over or after handing them over. With the bracketed language, these operations would simply be illustrations of the types of operations intended to be covered. Without the bracketed language, only the stated operations would be covered.

### Article 4

#### ISSUANCE OF DOCUMENT

(1) The operator shall at the request of his customer [, and within [a reasonable period of time] [... hours/days]] issue a document [stating the date of its issuance,] identifying the goods, acknowledging his receipt thereof and stating the date on which they were taken over by him.

[(2) [(*Alternative 1*) The document shall also state the condition [and quantity] of the goods as far as [it] [they] can be ascertained by reasonable means of checking [, and shall contain the following additional information ...].]

[(*Alternative 2*) The document shall also state such particulars concerning the condition and quantity of the goods as the customer of the operator requests be included in the document, as far as those particulars can be ascertained by reasonable means of checking.]

(3) A document issued by the operator constitutes *prima facie* evidence of his taking over the goods as stated therein [, whether the document was issued upon the request of his customer or without such a request].

[(4) If [it is proven that] the customer has requested the operator to issue a document in respect of goods which he has taken over or has requested the operator to state on the document the condition of the goods, but the operator fails to do so, the operator is rebuttably presumed to have received the goods in apparently good condition.]

(5) A document required pursuant to this article may be issued in any form which provides a record of the information contained therein.

(6) (a) The document shall be signed on behalf of the operator by a person having authority from him.

(b) The signature on the document may be made in handwriting, printed in facsimile, perforated, stamped, in symbols, or made by any other mechanical or electronic means.

#### Comments

1. *General* See A/CN.9/260, paragraphs 29 to 40; A/CN.9/WG.II/WP.55, paragraphs 66 to 72. It may be considered that the requirements in the uniform rules concerning the document to be issued by the operator should be designed so as to balance the interests of the customer in having a document containing certain information with the general interest in avoiding undue hindrances to the flow of goods and undue delays of means of transport (e.g. delays of means of transport to which goods are transferred by the operator resulting from delays in the issuance of documentation by the operator).

2. In accordance with the prevailing view at the eighth session of the Working Group (A/CN.9/260, paragraph 38), provisions concerning a negotiable document are not included in this draft article.

3. *Paragraph (1)* See A/CN.9/260, paragraphs 29 to 31, 35 and 36. This paragraph reflects the prevailing view at the eighth session of the Working Group that an operator should be obligated to issue a document only on request of the customer (A/CN.9/260, paragraph 31). The document would constitute a simple receipt. If a time limit for issuance of the document is to be included (see A/CN.9/260, paragraphs 35 and 36), it may be expressed either as "a reasonable period of time", or as a specified period of time (e.g. hours or days); the former would permit greater flexibility, taking into account the wide variety of circumstances which would be covered by the uniform rules. While a time limit might be necessary when the document is a document of title to the goods, in order, for example, to enable the customer to dispose of or grant security in the goods without delay, such circumstances do not exist where, as here, the document is not a document of title. A requirement that the document state the date of its issuance would be needed only if the paragraph contained a time limit for issuance of the document.

4. *Paragraph (2)* See A/CN.9/260, paragraph 32. Alternative 1 of this paragraph requires certain information to be included in the document, such as their condition or quantity, in addition to acknowledging receipt of the goods and indicating the date thereof. Depending on the circumstances, quantity could refer to count, weight or volume. Suggestions were made within the Working Group that certain additional information should be required, such as whether the operator claimed rights of security in the goods and, if so, the charges in respect of which such rights were claimed, and a statement that the goods were covered by the uniform rules

(see A/CN.9/260, paragraph 92). Such information could, if the Working Group so decided, be added to alternative 1. In addition, this alternative might obligate the operator to include in the document any discrepancy between information contained in a transport document accompanying the goods concerning the condition or quantity of the goods and the condition or quantity of the goods ascertainable by him with reasonable means of checking. Alternative 2 of this paragraph would obligate the operator to include information concerning the condition or quantity of the goods only if so requested by his customer. Such an approach may be considered appropriate in view of the fact that the uniform rules are to apply to a wide variety of operators, operations and goods, and that in some cases goods are not inspected even as to their apparent condition (see A/CN.9/WG.II/WP.55, paragraph 70). Under both alternatives of paragraph (2), only such information concerning the condition or quantity of the goods which could be obtained by reasonable means of checking would be included in the document. This may obviate the necessity of dealing with the question of the effect of any reservations the operator may include in the document (e.g. "said to contain", "customer's count and weight").

5. *Paragraph (3)* This paragraph represents the prevailing view of the Working Group at its eighth session (A/CN.9/260, paragraph 34) that the document issued by the operator should constitute *prima facie* evidence that the goods were taken over and that their condition and quantity were as stated therein. The bracketed language would make it clear that the legal effect of the document would arise when the document was issued upon the request of the customer as well as when it was issued without such a request.

6. *Paragraph (4)* See A/CN.9/260, paragraph 37. With respect to the consequences of a failure of the operator to issue a document or to state the condition of the goods if requested to do so, under this paragraph the operator would be rebuttably presumed to have received the goods in apparently good condition. It could in some cases lead to unjust results if the presumption were not rebuttable. For example, if the goods were damaged during carriage and an operator who took the goods over from the carrier failed to issue a document or to state the condition of the goods, an irrebuttable presumption that the goods were received in good condition could prejudice a claim by a cargo interest against the carrier for the damage, particularly in the case where the operator was acting for the cargo interest. It thus may be preferable for a presumption to be rebuttable.

7. Paragraph (4) does not provide a sanction for late issuance of a document (i.e. if the uniform rules provide a time limit for issuance of the document; see comment 3 to present draft article).

8. The Working Group may wish to consider the desirability of creating a presumption, even a rebuttable one, of receipt of goods in good condition when the operator having been requested to issue a document or to

state the condition of the goods fails to do so. In some cases a legitimate question may arise as to whether the customer requested a document, or whether he requested that information concerning the condition of the goods be stated on the document. On the other hand, an obligation to issue a document or to state the condition of the goods upon request would be of little value if there existed no sanction for a failure to do so. One possible approach to this problem might be to impose on the claimant the burden of proving that a proper request was made, and to provide for the presumption if the claimant met this burden. This approach is reflected in the bracketed words "it is proven that" in paragraph (4). Yet another approach would be to require that a document stating any apparent loss or damage be issued in all cases.

9. *Paragraph (5)* See A/CN.9/260, paragraphs 32 and 33. This paragraph enables the operator to issue a document by traditional means (e.g. a paper document), as well as by any other means, as long as a record of the information contained in the document is provided. This provision would be satisfied, for example, by noting on a transport document covering the goods the information required to be stated on the document. It would also be satisfied by transmitting that information by computer to the customer's computer, since a record of the information would be available to the customer in his own computer. A provision such as the one contained in this paragraph would, in addition, be satisfied by a technique of documentation in international trade which is still only in the conceptual stage—the recording of information relating to goods involved in trade on a programmable micro-circuit card. Such a card could, for example, contain information required to be on a transport document and information required to be submitted to customs authorities. Information to be contained in a document issued by the operator could also be entered and preserved on the card, and could be retrieved by the customer on a monitor screen or on a paper print-out.

10. The Working Group might consider it unnecessary to include a provision enabling the operator to employ mechanical or electronic techniques for preserving information required to be included in the document, and, if he uses such techniques, to require him to issue a receipt and grant the customer access to the other stored information (such as is provided in article 5 of Montreal Protocol No. 4 to amend the Convention for the Unification of Certain Rules relating to International Carriage by Air signed at Warsaw on 12 October 1929 as amended by the Protocol done at the Hague on 28 September 1955) (see A/CN.9/260, paragraph 33). First, an operator would not need to be authorized to preserve information by any means, whether by noting the information on a piece of paper and putting it in a file, or by storing the information in a computer. Second, there would be no need for the uniform rules to deal with a situation in which an operator stored certain information not contained in the receipt, as there is in Montreal Protocol No. 4. Under the Warsaw Convention the air waybill must contain certain information concerning the places of departure and destination of the goods and certain agreed stopping places. One copy

of the air waybill serves as a receipt for the consignor while another copy accompanies the goods during transport. The purpose of Montreal Protocol No. 4 is to permit carriers to separate the receipt function of the air waybill from its function as a document accompanying the goods. With respect to the information to be included in the air waybill, such as the destination and routing, article 5 of Montreal Protocol No. 4 enables the tangible document which the carrier must issue to be simplified, while requiring the rest of the required information concerning the goods to be available by other means (e.g. by computer) over the entire course of the transport of the goods, and particularly at stopping places en route. Such a provision may be valuable in the case where, as in carriage by air, the goods are in motion. This circumstance, however, does not exist with respect to goods which are essentially stationary in the custody of an operator.

11. *Paragraph (6)* Subparagraphs (a) and (b) have been adapted from the Multimodal Convention, article 5(2) and (3).

## Article 5

### BASIS OF LIABILITY

(1) The operator is liable for loss resulting from loss of or damage to the goods [, as well as for delay in handing over the goods to a person entitled to receive them,] if the occurrence which caused the loss or damage [or delay] took place during the period of the operator's responsibility for the goods as defined in article 3 of this Law, unless he proves that he, his servants or agents took all measures that could reasonably be required to avoid the occurrence and its consequences. [However, the operator is not liable for loss or damage [or delay] which he proves arose from acts of his servants or agents outside their scope of employment.]

[(2) In determining what measures could reasonably be required to avoid the occurrence and its consequences due regard shall be had, *inter alia*, to the nature of the goods and the nature of the operations to be performed by the operator.]

(3) Where a failure on the part of the operator, his servants or agents to take the measures referred to in paragraph (1) of this article combines with another cause to produce loss or damage [or delay] the operator is liable only to the extent that the loss resulting from such loss or damage [or delay] is attributable to that failure, provided that the operator proves the amount of the loss not attributable thereto.

[(4) Delay in handing over the goods to a person entitled to receive them occurs when the operator fails to hand them over to that person within the time expressly agreed upon by the operator or, in the absence of such agreement, within the time following a request for the goods by that person which it would be reasonable to

require of a diligent operator, having regard to the circumstances of the case.]

(5) If the operator does not hand over the goods at the request of the person entitled to take delivery of them within a period of 60 consecutive days following the request, the person entitled to make a claim for the loss of the goods may treat them as lost.

#### Comments

1. *General* See A/CN.9/260, paragraphs 41 to 47. As requested by the Working Group at its eighth session (see A/CN.9/260, paragraph 46), this draft article includes provisions dealing with delay. With some types of operators (e.g. those who are highly mechanized or computerized), delay may be less of a potential problem than with other types. Causes for delay may include, for example, delay in processing paperwork, and error in recording the storage location of the goods in the records of the operator (such events might result in delay in cases where the goods are to be handed over by the operator within a relatively short period of time), as well as misdelivery, resulting in the necessity to retrieve the goods and deliver them to the proper recipient. In considering whether the uniform rules should deal with liability for delay, the Working Group may also wish to take into consideration that the question of delay is closely related to the performance of the contract between the operator and his customer, a matter with which the uniform rules in general do not deal.

2. *Paragraph (1)* See A/CN.9/260, paragraph 41. With regard to the final sentence within brackets ("However, the operator is not liable ..."), see A/CN.9/260, paragraph 42.

3. *Paragraph (2)* The measures which should reasonably be taken by an operator to prevent loss of or damage to the goods vary widely, depending upon the type of operator, the operations performed by him and the type of goods. The rules governing the liability of the operator for loss of or damage to the goods should be flexible enough to take into account all circumstances in which they would apply. Such flexibility might already be achieved by the reference in paragraph (1) to "measures reasonably required to avoid the occurrence". A provision such as that contained in paragraph (2) might give greater assurance of such flexibility.

4. *Paragraph (3)* See A/CN.9/260, paragraph 43. The wording of this section has been adapted from that of article 5(7) of the United Nations Convention on Carriage of Goods by Sea, 1978 (Hamburg) (the "Hamburg Rules") and article 6(3) of the UNIDROIT draft.

5. *Paragraph (4)* See A/CN.9/260, paragraphs 44 to 46. The wording of this paragraph has been adapted from that of article 5(2) of the Hamburg Rules.

6. *Paragraph (5)* See A/CN.9/260, paragraph 47.

## Article 6

### LIMITS OF LIABILITY

(1) The liability of the operator for loss resulting from loss of or damage to goods according to the provisions of article 5 of this Law is limited to [(state amount in national currency)] [an amount in (state national currency) equivalent to ... units of the Special Drawing Right as defined by the International Monetary Fund] per package or other shipping unit, or [(state amount in national currency)] [an amount in (state national currency) equivalent to ... units of the Special Drawing Right as defined by the International Monetary Fund] per kilogramme of gross weight of the goods lost or damaged, whichever is the higher.

[(2) The liability of the operator for delay in handing the goods over according to the provisions of article 5 of this Law is limited to an amount equivalent to ... times the charges payable to the operator for his services in respect of the goods delayed, but not exceeding the total of such charges payable to the operator pursuant to his contract or agreement with his customer.]

[(3) In no case shall the aggregate liability of the operator under both paragraphs (1) and (2) of this article exceed the limitation which would be established under paragraph (1) for total loss of the goods with respect to which such liability was incurred.]

(4) For the purpose of calculating which amount is the higher in accordance with paragraph (1), the following rules apply:

(a) Where a container, trailer, chassis, barge, pallet or similar article of transport or packaging is used to consolidate goods, the packages or other shipping units enumerated in a document issued by the operator or in a transport document covering the goods as packed in such article of transport or packaging are deemed to be packages or shipping units. Except as aforesaid the goods in such article of transport or packaging are deemed to be one shipping unit.

(b) In cases where the article of transport or packaging itself has been lost or damaged, that article, if not owned or otherwise supplied by the operator, is considered to be one separate shipping unit.

(5) The operator may agree to limits of liability exceeding those provided in paragraph[s] (1) [(2) and (3)].

#### Comments

1. *General* See A/CN.9/260, paragraphs 48 to 53.

2. *Paragraph (1)* See A/CN.9/260, paragraphs 48 to 52. If the rules are cast in the form of a model law, the Working Group may wish to consider whether the text of the model law should leave it to each State to insert whatever amount in its national currency it deems appropriate, or whether, as a vehicle for the unification of

law, the model law should give some guidance as to what the amount should be or even should link such amount to a uniform international standard. Under the second version within each of the two series of brackets in paragraph (1) ("an amount in (state national currency) equivalent to ..."), the legislation adopted by a State implementing the model law would link the amount of the limit expressed in national currency to a stated number of Special Drawing Rights of the International Monetary Fund.

3. If the uniform rules are adopted as a model law and a recommended limit of liability is expressed in Special Drawing Rights the Working Group may wish to consider whether that limit of liability should be periodically reviewed by the Commission or in some other forum.

4. *Paragraph (2)* This paragraph sets forth a limit of liability for delay (see A/CN.9/260, paragraph 46) expressed as a percentage of the charges payable to the operator for his services in respect of the goods (i.e. excluding, for example, sums advanced by the operator for, e.g., customs payments and to be reimbursed to the operator by his customer), subject to a maximum limit. This paragraph is adapted from article 6(1)(b) of the Hamburg Rules.

5. *Paragraph (3)* This paragraph is adapted from article 6(1)(c) of the Hamburg Rules. As a consequence of the introduction of an aggregate limit such as that contained in this paragraph, in a case of heavy physical damage coupled with extensive economic losses resulting from delay, the operator's liability would not exceed the per-package or per-kilogramme limit. Such a provision would not be needed if the uniform rules do not deal with delay (see comment 1 to draft article 5, above).

6. *Paragraphs (4) and (5)* These paragraphs are adapted from article 6(2) and (4) of the Hamburg Rules.

### Article 7

#### APPLICATION TO NON-CONTRACTUAL CLAIMS

(1) The defences and limits of liability provided for in this Law apply in any action against the operator in respect of loss of or damage to the goods for which he is responsible under this Law, [as well as delay in delivery of such goods,] whether the action is founded in contract, in tort or otherwise.

(2) If such an action is brought against a servant or agent of the operator, [or another person of whose services the operator makes use for the performance of the safekeeping and operations referred to in article 3 of this Law,] such [servant or agent] [servant, agent or person], if he proves that he acted within the scope of his employment, is entitled to avail himself of the defences and limits of liability which the operator is entitled to invoke under this Law.

(3) Except as provided in article 8 of this Law, the aggregate of the amounts recoverable from the operator and from any persons referred to in paragraph (2) of this article shall not exceed the limits of liability provided for in this Law.

### Comments

See A/CN.9/260, paragraphs 79 and 80. The "other person of whose services the operator makes use" referred to in paragraph (2) (and by reference in paragraph (3)) could in some legal systems be a person other than a servant or agent of the operator, such as a stevedoring company engaged as an independent contractor by the operator. The Working Group may wish to enable such a person to benefit from the defences and limits of liability provided to an operator under the uniform rules, even though the liability of such a person is not otherwise governed by the uniform rules. First, by virtue of paragraph (2) the defences and limits of liability also extend to servants and agents of the operator, even though their liability is also not otherwise covered by the rules. Second, the policies behind extending the defences and limits of liability to servants and agents of the operator may also apply to other persons engaged by the operator to perform operations in respect of goods covered by the rules (e.g. to prevent a claimant from avoiding the defences and limits of liability under the uniform rules by claiming directly against the servant, agent or other person; and to avoid questions of the vicarious liability of the operator for acts or omissions of the servant, agent or other person when the liability of the servant, agent or other person is determined without the benefit of the defences and limits of liability under the uniform rules).

### Article 8

#### LOSS OF RIGHT TO LIMIT LIABILITY

(1) The operator is not entitled to the benefit of the limit of liability provided for in article 6 of this Law if it is proved that the loss or damage [or delay] resulted from an act or omission of the operator [himself] [or of an agent of the operator [or another person of whose services the operator makes use for the performance of the safekeeping and operations referred to in article 3 of this Law] [acting within the scope of his employment]] done with the intent to cause such loss or damage [or delay], or recklessly and with knowledge that such loss or damage [or delay] would probably result.

(2) Notwithstanding the provision of paragraph (2) of article 7 of this Law, a servant or agent of the operator [or another person of whose services the operator makes use for the performance of the safekeeping and operations referred to in article 3 of this Law] is not entitled to the benefit of the limit of liability provided in article 6 of this Law if it is proved that the loss or damage [or delay] resulted from an act or omission of such servant or agent

[or person] done with the intent to cause such loss or damage [or delay] or recklessly and with knowledge that such loss [or delay] would probably result.

#### Comments

1. *General* See A/CN.9/260, paragraphs 54 to 56.
2. *Paragraph (1)* With the bracketed phrase "or of an agent of the operator [or another person of whose services an operator makes use for the performance of the safekeeping and operations referred to in article 3 of this Law]" the operator would lose the limit of liability even if the indicated act or omission was committed by his agent or other person (see comment to draft article 7). The bracketed word "himself" includes servants and employees of the operator. For this reason, the word "servants" is omitted from this paragraph.
3. The Working Group may wish to consider whether the operator should lose the right to limit his liability due to an act or omission of his servant, agent or other person of whose services he makes use only if the act or omission were committed within the scope of the servant's, agent's or person's employment. In this regard it may be noted that intentional acts (e.g. theft) are often regarded as outside the scope of employment.

#### Article 9

##### SPECIAL RULES ON DANGEROUS GOODS

- (1) The consignor shall mark or label dangerous goods as dangerous in a suitable manner and in accordance with any applicable international, national or other rule of law or regulation relating to dangerous or hazardous goods. If he packs dangerous goods, he shall do so in a suitable manner and in accordance with any such rule of law or regulation.
- (2) Where the consignor hands over dangerous goods to the operator or any person acting on his behalf, the consignor shall inform the operator of the dangerous character of the goods and, if necessary, any special handling requirements and precautions to be taken. If the consignor fails to do so and the operator does not otherwise have knowledge of their dangerous character:
  - (a) the consignor shall be liable to the operator for all loss resulting from such goods; and
  - (b) the goods may at any time be destroyed or rendered innocuous, as the circumstances may require, without payment of compensation.
- (3) The provisions of subparagraphs (a) and (b) of paragraph (2) of this article may be invoked by any

operator who is responsible for the goods under this Law whether or not he took over the goods from the consignor, unless the operator had knowledge of the dangerous character of the goods when he took them over.

#### Comments

1. *General* See A/CN.9/260, paragraphs 73 to 77. This article is adapted from article 13 of the Hamburg Rules and article 23 of the Multimodal Convention.
2. It will be noted that this draft article imposes obligations on the consignor, and, under paragraph (2)(a), imposes liability on the consignor towards the operator. In some cases the operator will not be in a contractual relationship with the consignor and will be far removed from the consignor in the chain of transport. This approach was adopted for the purpose of drafting the present draft article in view of the requests of the Working Group referred to in comment 1, above. If the Working Group wished, another approach could be adopted, whereby the provisions concerning dangerous and perhaps perishable goods could be expressed, for example, by excluding the liability of the operator for loss of or damage to the goods if they were not properly marked, labelled or packed and if he was not informed of their dangerous or perishable nature. Even under such an approach, however, the substance of paragraph (2)(a) and (b) could still be included. If the uniform rules also deal with the liability of the consignor, it may be considered whether a reference in the title of the rules only to operators of transport terminals is appropriate.
3. *Paragraph (1)* See A/CN.9/260, paragraph 73. International and national rules, as well as other rules and regulations (e.g. regulations promulgated by a port authority or a terminal operator) regulate the packing, marking, labelling and documentation of dangerous and hazardous goods. Therefore, it may be desirable to require such packing, marking and labelling to be in accordance with such rules and regulations.
4. No provisions have been included concerning perishable goods. Suggestions were made at the eighth session of the Working Group regarding provisions concerning the right of the operator to reject perishable goods presented by his customer (see A/CN.9/260, paragraph 74), and an exception in the case of such goods to the obligation of the operator to hand over the goods in the same condition in which he received them (see A/CN.9/260, paragraph 75). However, the existing draft articles do not provide for the obligation of the operator to accept goods presented by his customer or his obligation to hand over the goods since, in general, the draft does not deal with the contractual obligations of the parties. Therefore, provisions such as those mentioned above may be unnecessary. On the other hand, as noted in comment 2 to this draft article, it would be possible to exclude liability of the operator for loss of or damage to perishable goods, as well as to dangerous goods, if they were not properly marked, labelled or packed.

**Article 10****RIGHTS OF SECURITY IN GOODS**

(1) The operator has a right of retention over the goods for costs and claims relating to the safekeeping and operations performed by him in respect of the goods during the period of his responsibility for them. However, nothing in this Law prevents the operator and his customer from extending by agreement the right of retention of the operator, or affects the validity or effect of any right of security otherwise available under the law of this State.

(2) The operator is not entitled to retain the goods if a sufficient guarantee for the sum claimed is provided or if an equivalent sum is deposited with a mutually accepted third party or with an official institution in this State.

[(3) In order to obtain the amount necessary to satisfy his claim, the operator is entitled to sell the goods over which he has exercised the right of retention provided in this article to the extent permitted by and in accordance with the applicable law.]

*Comments*

1. *General* See A/CN.9/260, paragraphs 63 to 67.

2. Paragraphs (1) to (3) are adapted from article 5 of the UNIDROIT draft.

3. *Paragraph (1)* See A/CN.9/260, paragraphs 63 and 65. This paragraph has two effects. First, it enables the parties to extend the right of retention by agreement so as to create a general lien (i.e. enabling the operator to retain the goods as security for charges due to him from the customer other than in respect of the goods retained). The ability to extend the right of retention is not expressly conditioned upon the ability to do so under national law, since it is unlikely that a rule of national law would prohibit the parties from agreeing to extend the operator's right of retention. Second, this paragraph preserves the validity and effect of any other right of security which is available under national law (e.g. a non-possessory security interest in the goods created by agreement of the parties, if such an agreement is valid under national law).

4. *Paragraph (2)* See A/CN.9/260, paragraph 64.

5. *Paragraph (3)* See A/CN.9/260, paragraphs 65 and 67. This paragraph permits the operator to sell the goods if such a right is provided in the applicable law. The exercise of the right of sale must be in accordance with that law. It may be noted, however, that many legal systems do not contain general provisions concerning the sale of property retained as security; rather, a separate right of sale is provided and regulated in particular contexts. A right of sale would in most cases not already exist in respect of the operators who are the objects of the uniform rules. The Working Group may therefore wish to

consider whether a right of sale should be created by the uniform rules, and not linked to an existing right of sale under national law.

6. No provision has been included in this draft article concerning the resolution of a possible conflict between the rights of security exercised by the operator and the rights of a third person in the goods (see A/CN.9/260, paragraph 66). In the absence of such a provision such a conflict would be dealt with by rules of law other than the uniform rules. Moreover, conflicts between the rights of security of an operator and the rights of a consignee under a contract of carriage or transport document covered by an international transport convention could be resolved by a provision such as that contained in draft article 15.

7. In the case of unitized goods it should be noted that the rights of security provided in this article would, as a consequence of the definition of "goods" in draft article 1(3), cover not only the goods themselves but also the container or similar item in which the goods are unitized. Such items are often not owned by the person who owns the goods (e.g. they are often owned by carriers, container leasing companies or freight forwarders), and the exercise by the operator of his rights of security in respect of such items could conflict with the rights of their owners. If the Working Group wished to exclude such items from being covered by the rights of security provided in this draft article, a provision such as the following could be added: "The rights of security provided by this article extend to a container, trailer, chassis, barge, pallet or similar article of transport or packaging only if the operator has given to the owner of such article an undertaking of safekeeping in respect thereof". Under such a provision, the rights of security would apply, for example, in respect of a container which is stored by an operator for its owner.

**Article 11****NOTICE OF LOSS OR DAMAGE [OR DELAY]**

(1) Unless notice of partial loss or of damage, specifying the general nature of the loss or damage, is given to the operator not later than the working day after the day when the goods were handed over to the person entitled to take delivery of them, the handing over is *prima facie* evidence of the handing over by the operator of the goods as described in the document issued by the operator, or, if no such document was issued, in good condition.

[(2) The provisions of paragraph (1) apply correspondingly if notice is not given to the operator of total loss of goods not later than the working day after the day when the goods may be treated as lost under article 5 of this Law.]

[(3) Where the partial loss or damage is not apparent, the provisions of paragraph (1) apply correspondingly if notice is not given within ... consecutive days after the



day when the goods [were handed over to the person entitled to take delivery of them] [reached their final destination [, but in no case later than ... consecutive days after the day when the goods were handed over to the person entitled to take delivery of them]]. [However, if the claimant had no opportunity to discover the loss or damage within the said period of time, the provisions of paragraph (1) apply correspondingly if notice is not given within ... consecutive days after the claimant had an opportunity to discover the loss or damage, but in no case later than ... consecutive days after the day when the goods were handed over by the operator.]]

(4) If the operator participated in a survey or inspection of the goods at the time when they were handed over to the person entitled to take delivery of them, notice need not be given to the operator of loss or damage ascertained during that survey or inspection.

(5) In the case of any actual or apprehended loss or damage, the operator and the person entitled to take delivery of the goods must give all reasonable facilities to each other for inspecting and tallying the goods.

[(6) No compensation shall be payable for loss resulting from delay in handing over the goods unless notice has been given to the operator within 60 consecutive days after the day when the goods were handed over to the person entitled to take delivery of them.]

(7) (a) Notice required to be given by this article may be given in any form which provides a record of the information contained therein.

(b) For the purpose of this article, notice given to a person acting on the operator's behalf is deemed to have been given to the operator.

#### Comments

1. *General* See A/CN.9/260, paragraphs 81 to 89. "Partial loss" as used in paragraphs (1) and (3) refers to a shortage in a consignment of goods handed over to the person entitled to take delivery of them. It may be desirable for the recipient of the goods to be obligated to notify the operator of the partial loss shortly after he receives the consignment, even though under draft article 5(5) the goods could not be treated as lost until 60 days after a request that they be handed over. Such notice would enable the operator to begin to search immediately for the partially lost goods.

2. *Paragraph (2)* This paragraph requires notice of a total loss of goods to be given. It has been placed within square brackets because of a view expressed within the Working Group that notice of total loss should not be required (see A/CN.9/260, paragraph 81). In this regard, the Working Group may wish to consider that under draft article 5(5) the goods may be treated as lost 60 days after a request that they be handed over. As a result of such request, the operator would know whether or not he was able to deliver any of the goods, and a notice of total loss may therefore be unnecessary.

3. *Paragraph (3)* It may be noted that loss of or damage to goods taken over by a carrier might not be apparent to the carrier, and might not become known to him until a claim is brought against him for the loss or damage. The Working Group may wish to take this into consideration in deciding upon the time limits and choosing among the various approaches reflected within square brackets in this paragraph.

4. *Paragraph (7)* Subparagraph (a) enables the operator to give notice by traditional means (e.g. in writing) as well as by any other means (e.g. by computer-to-computer communication), as long as a record of the information contained in the notice is provided (see comment 9 to draft article (4)). Subparagraph (b) might be included in order to permit notice of loss, damage or delay to be given to an agent of the operator (e.g. where the operator is a freight forwarder or a carrier).

### Article 12

#### LIMITATION OF ACTIONS

(1) Any action under this Law is time-barred if judicial or arbitral proceedings have not been instituted within a period of two years. [However, an action in which the loss of or damage to the goods [or delay in handing over the goods] resulted from an act or omission of the operator done with the intent to cause such loss or damage [or delay], or recklessly and with knowledge that such loss or damage [or delay] would probably result, is time-barred if such proceedings have not been instituted within a period of ... years.]

(2) The limitation period commences on the day on which the operator hands over the goods or part thereof to a person entitled to take delivery of them, or, in cases of total loss of the goods, [on the last day on which the goods should have been handed over] [on the day the operator notifies the person entitled to make a claim that the goods are lost, or, if no such notice is given, on the day that person may treat the goods as lost in accordance with article 5 of this Law].

(3) The day on which the limitation period commences is not included in the period.

(4) The operator may at any time during the running of the limitation period extend the period by a declaration in writing to the claimant. The period may be further extended by another declaration or declarations.

(5) A recourse action by a carrier [or another person] against the operator may be instituted even after the expiration of the limitation period provided for in the preceding paragraphs if instituted within [90] days after the carrier [or person] has been held liable in an action against himself [or has settled the claim upon which such action was based].

*Comments*

1. *General* See A/CN.9/260, paragraphs 57 to 62.

2. *Paragraph (1)* See A/CN.9/260, paragraph 57. The final sentence, in brackets, reflects a view expressed in A/CN.9/260, paragraph 57. However, the Working Group may wish to consider that in some jurisdictions such a provision might be applied so as to enable a claimant to prolong the basic two-year limitation period simply by alleging intentional or reckless conduct. In other jurisdictions, a longer limitation period might be applied where the loss, damage or delay is proved to have resulted from intentional or reckless conduct. However, such proof would be made in the very proceedings in respect of which the question of which limitation period should apply would be raised. The parties would thus have to participate in proceedings which could result in a finding that the proceedings themselves were time-barred because intentional or reckless conduct had not been proved.

3. *Paragraph (5)* See A/CN.9/260, paragraph 59.

**Article 13****CONTRACTUAL STIPULATIONS**

(1) Unless otherwise provided in this Law, any stipulation in a contract for the safekeeping of goods concluded by an operator or in any document evidencing such a contract is null and void to the extent that it derogates, directly or indirectly, from the provisions of this Law. The nullity of such a stipulation does not affect the validity of the other provisions of the contract or document of which it forms a part.

[(2) Notwithstanding the provisions of paragraph (1) of this article, the operator and his customer may agree that the provisions of this Law concerning liability for and claims in respect of loss of or damage to goods do not apply, or apply with modifications, in respect of loss of or damage to goods within the responsibility of the operator under article 3 of this Law occurring in connection with processing operations performed by the operator which by their nature alter the condition or quantity of the goods.]

(3) Notwithstanding the provisions of paragraph (1) of this article, the operator may agree to increase his responsibilities and obligations under this Law.

*Comments*

1. See A/CN.9/260, paragraphs 90 and 91.

2. *Paragraph (1)* The phrase "unless otherwise provided ..." would encompass, for example, the agreements referred to in paragraphs (3), and 5(b) and (d) of alternative 3 of draft article 2.

3. *Paragraph (2)* This paragraph may be included if the Working Group wishes the parties to be able to agree that liability for loss of or damage to the goods in connection with the processing of goods within the responsibility of the operator is to be governed by a legal regime other than the uniform rules. One reason for such an approach may be that such operations are not factually associated with the transport of goods but rather are more in the nature of manufacturing (see A/CN.9/WG.II/WP.55, paragraph 23).

**Article 14****INTERPRETATION OF THIS LAW**

In the interpretation and application of the provisions of this Law, regard shall be had to its international character and to the desirability of promoting international uniformity with respect to the treatment of the issues dealt with in this Law.

*Comments*

See A/CN.9/260, paragraph 94.

**Article 15****INTERNATIONAL TRANSPORT CONVENTIONS**

This Law does not modify any rights or duties which may arise under an international convention relating to the international carriage of goods which is binding on this State, [or any law of this State relating to the international carriage of goods].

*Comments*

See A/CN.9/260, paragraph 93.

## IV. INTERNATIONAL COMMERCIAL ARBITRATION

### Co-ordination of work: activities of international organizations on certain aspects of arbitration: report of the Secretary-General (A/CN.9/280)

[Original: English]

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#### INTRODUCTION

1. The Commission, at its fourteenth session, decided that, to further strengthen the co-ordinating role of the Commission, the secretariat should select a particular area of international trade law for intensive consideration and submit a report on the work of other organizations in that area.<sup>1</sup> The area selected for this year's report is

international commercial arbitration, which has been a field of prime interest and successful activity of the Commission since its inception.

2. The scope of the present report is shaped by the following characteristics of this area, viewed from the perspective of harmonization and progressive development of legal rules. A considerable degree of uniformity has been achieved by various multilateral treaties, with global or regional orientation, sometimes devoted to special categories of disputes or certain aspects of arbitration. A prominent example is the Convention on the

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its fourteenth session, *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17 (A/36/17)*, para. 100.

Recognition and Enforcement of Foreign Arbitral Awards, concluded by the United Nations Conference on International Commercial Arbitration at New York on 10 June 1958 and at present adhered to by 69 States.<sup>2</sup>

3. As regards the level of non-convention law, the Commission has laid a solid and promising foundation for achieving greater harmony and substantive improvement by adopting the UNCITRAL Model Law on International Commercial Arbitration.<sup>3</sup> It is to be expected that States will favourably respond to the recommendation of the General Assembly, in its resolution 40/72 of 11 December 1985, that "all States give due consideration to the Model Law on International Commercial Arbitration, in view of the desirability of uniformity of the law of arbitral procedures and the specific needs of international commercial arbitration practice."

4. Finally, as regards the contractual level, the Commission has made a major contribution by preparing and adopting in 1976 the UNCITRAL Arbitration Rules. Unlike other arbitration rules, these Rules are not tied to one particular arbitral institution or other special body such as a trade association. Thus, they offer a viable, and increasingly chosen, option to parties who wish to use the same set of rules in various parts of the world, whether their arbitration would be *ad hoc* or administered by one of the many arbitral institutions offering services under the UNCITRAL Arbitration Rules. The practical attractiveness of this option is enhanced by the growing number of arbitral institutions or centres which use the UNCITRAL Arbitration Rules as their own institutional rules or otherwise act as appointing authority and provide administrative services in cases conducted under these Rules.

5. In light of the above, one may conclude that, in the area of international commercial arbitration, a considerable degree of harmonization has been achieved or a basis therefor provided. Nevertheless, there remain a number of issues or aspects of arbitration which are not, at least not completely, covered.

6. In selecting the issues dealt with in this report and in determining the manner of their presentation, the secretariat was guided by the following considerations. Of the many issues discussed at international forums and of the various aspects covered by special rules, guides or recommendations of international organizations only those are dealt with here which are intended, or may be expected, to contribute in some way to the harmonization

<sup>2</sup>Other pertinent examples include the European Convention on International Commercial Arbitration (Geneva, 1961), the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (Washington, 1965), the Convention on Settlement by Arbitration of Civil Law Disputes Arising from Relations of Economic, Scientific and Technical Co-operation (Moscow, 1972) and the Inter-American Convention on International Commercial Arbitration (Panama, 1975).

<sup>3</sup>Report of the United Nations Commission on International Trade Law on the work of its eighteenth session, *Official Records of the General Assembly, Fortieth Session, Supplement No. 17 (A/40/17)*, paras. 332-333 and annex I.

of the legal rules and which are, at least in part, clearly within the realm of arbitration.<sup>4</sup>

7. The presentation of issues in this report is influenced by the fact, typical of the field of arbitration, that legal developments are often initiated by discussions at international congresses and seminars. Normally stimulated by problems encountered in practice, these discussions help to determine the desirability and feasibility of a possible harmonization effort and provide useful guidance in the search for solutions. The report, therefore, includes a number of excerpts or summaries of such discussions, sometimes of consecutive congresses reflecting the development of the views. In order to present an accurate and complete picture as regards the desirability and feasibility of any initiative towards harmonization, the report includes even those discussions which led an organization to decide not to undertake further efforts. Finally, where one of the selected issues was dealt with, or at least touched upon, in the course of the preparation of the UNCITRAL Model Law on International Commercial Arbitration, the report recalls the relevant discussion in the Commission or the Working Group on International Contract Practices.

8. The primary purpose of this report is to provide and disseminate information on the activities of international organizations in respect of the selected aspects of arbitration. The considerations of these organizations and any text elaborated by them are thus presented in some detail and at times reproduced verbatim. The secretariat did not deem it appropriate, at this stage, to submit any comments on these texts or any assessment of the desirability or feasibility of any future involvement of the Commission. However, such comments and assessment could be included in any future study by the secretariat, if the Commission were to determine that one or more of the issues presented here warranted closer examination.<sup>5</sup>

## I. Multi-party arbitration

### A. International Council for Commercial Arbitration

9. International arbitration in multi-party commercial disputes was the subject of the Interim Meeting of the International Council for Commercial Arbitration held in 1980 at Warsaw.<sup>6</sup> The general report to that International Symposium,<sup>7</sup> noting that commercial projects often

<sup>4</sup>Thus not included in the report are, for example, the rules of the ICC International Centre for Technical Expertise (*ICC Brochure*, No. 307, 1977) and the Draft Rules for an Arbitral Referee Procedure, prepared by a working party of the ICC Commission on International Arbitration (ICC document No. 420/272, 15 April 1985).

<sup>5</sup>Some specific suggestions as to the possible scope of such a study are set forth below (see "Conclusions", paras. 72-75).

<sup>6</sup>*International Arbitration in Multi-party Commercial Disputes, Materials of an International Symposium, Warsaw, June 29th-July 2nd 1980*, (Warsaw, Polish Chamber of Foreign Trade, 1982).

<sup>7</sup>G. Bernini, Arbitration in multi-party business disputes, in *General Report, ibid.*, pp. 12-22; published also in International Council for Commercial Arbitration, *Yearbook Commercial Arbitration* (Deventer, Kluwer), vol. V-1980, pp. 291-300.

involve several parties, distinguished between two types of multi-party commercial disputes.

10. The first type of multi-party dispute is one which may arise from a multilateral contract, that regulates rights and obligations among more than two contracting parties. A joint venture or a consortium agreement may be an example of such a multilateral contract.<sup>8</sup> An arbitral clause in such contract would normally bind all parties and oblige them to participate in a multi-party arbitration. Problems may arise, however, concerning the appropriate number of arbitrators and their appointment, in particular in those cases where it is difficult or impossible to foresee, at the time of conclusion of the contract, the precise number and identity of the parties who might be involved in a later arbitration.<sup>9</sup>

11. The second type of multi-party dispute is one which may stem from a contractual "network" consisting of several independent but commercially related contracts. For example, a party engages a contractor to complete a project, and the contractor concludes one or more ancillary contracts with a third person or third persons for the purpose of completing or taking part in the completion of the project.<sup>10</sup> Since each arbitral clause normally relates only to the contract in which it is contained, a given issue involving several parties to different contracts may be the subject of separate arbitral proceedings. A particular concern is, as noted in the general report, the possibility of conflicting awards with the ensuing result of uncertainty and distrust of arbitration.<sup>11</sup>

12. The results of the deliberations may be seen from the summing up of the various views, according to which the participants of the Symposium:

"1. Noted that in the framework of contemporary international trade and economic co-operation, the realization of major projects is in many cases achieved by means of multi-party business transactions which may be laid down in a multi-party contract or in a network of separate and legally independent contracts executed between different parties.

"2. Recognized that in the case of disputes arising out of or in connection with multi-party contracts or separate but interrelated contracts the business transaction in its entirety is likely to be affected.

"3. Expressed the view that, upon the occurrence of such disputes, in many cases consolidation of a number of separate arbitral proceedings, as well as the intervention and/or summoning to an instituted proceeding of persons who are parties to multilateral or related contracts into one arbitration may be desirable with a view to avoiding conflicting awards and duplication of efforts. Other views were expressed that such consoli-

ation into one proceeding might not be desired by all parties or might lead to practical difficulties in conducting arbitration cases.

"4. Heard reports that under certain legal systems, where parties have agreed to arbitration in multi-party transactions (e.g. in joint venture contracts) or in a network of related agreements, courts may interpret such agreements as a basis for ordering a consolidation of arbitral proceedings or for parties to intervene or to be summoned, whereas under other legal systems courts will not act to bring about consolidation of arbitral proceedings, or to bring about such intervention or summoning.

"5. Noted that agreements of parties who desire to consolidate arbitral proceedings or to make other arrangements for coordinating the conduct of cases may be found either in the original contract or in a separate agreement after a dispute has arisen.

"6. Pointed out that when the agreement of the parties provides that arbitration will be administered by an arbitral institution the administering body can contribute to the creation of a system of consolidation and coordination, based on the will of the parties, by suggesting model clauses for this purpose, or by providing guidelines or by other appropriate means (e.g. by suitable methods for the appointment of the arbitral tribunal). This possibility was widely viewed as one of the advantages of using administered arbitration in multi-party transactions.

"7. Considered in detail specific contractual clauses which might be used in multi-party transactions but did not reach agreement on any particular form, that being a matter deserving further study and review.

"8. Expressed the view that conciliation might be a valuable alternative for resolving multi-party disputes because it can help to avoid many of the complexities and difficulties of arbitration in such cases. In that connection, welcomed and encouraged the efforts of the United Nations Commission on International Trade Law to develop UNCITRAL Conciliation Rules; noted that such Rules are desirable in order to promote greater harmonization between conciliation and arbitration and to provide a flexible uniform system of conciliation which would be acceptable in all geographic regions and legal, social and economic systems; and expressed appreciation to UNCITRAL for the opportunity granted to ICCA to assist, through consultation, in the preparation of UNCITRAL Conciliation Rules.

"9. Noted that, where consolidation of arbitral proceedings is not desired by the parties, other methods can be used to lessen the danger of conflicting awards. This includes, *inter alia*, the set of the same arbitrators, presentation of the same witnesses and evidence, and the same technical expertise."<sup>12</sup>

<sup>8</sup>*Ibid.*, p. 13.

<sup>9</sup>*Ibid.*, p. 14.

<sup>10</sup>*Ibid.*, pp. 13-14.

<sup>11</sup>*Ibid.*, pp. 14-15.

<sup>12</sup>Summary of various views expressed at the Symposium, *International Arbitration in Multi-party ...*, pp. 220-223.

## B. International Chamber of Commerce

### 1. Guide on Multi-party Arbitration under the Rules of the ICC Court of Arbitration

13. At its Congress at Manila in 1981, the International Chamber of Commerce (ICC) adopted the Guide on Multi-party Arbitration under the Rules of the ICC Court of Arbitration.<sup>13</sup> The purpose of the Guide is to avoid difficulties concerning multi-party disputes. The Guide does not contain a set of rules to be applied to a multi-party arbitration; it explains issues arising in such an arbitration and possible approaches thereto, and advises parties on how to establish multi-party proceedings before the ICC Court of Arbitration.

14. The Guide suggests several points which should be agreed upon in advance where participants in a project wish that any disputes arising among all or some of them will be resolved by a single arbitral tribunal in a comprehensive arbitration proceeding. These points include the right of any party adhering to the arrangement: (a) to pursue any type of claim against any other adhering party regardless of whether or not they are parties to the same contract; (b) to intervene in any arbitration proceeding between two or more other adhering parties, again, regardless of whether or not they are parties to the same contract; (c) to involve one or more adhering parties in the arbitration; (d) to obtain the recognition of or compliance with any award on the part of all of the other adhering parties, whether or not they were parties to the arbitration proceeding, so long as they were given an adequate opportunity to become parties. In all these cases the adhering party must provide evidence of an actual interest.<sup>14</sup>

15. Other points on which suggestions are made in the Guide include: (a) renouncement by an adhering party of the possibility to challenge the jurisdiction of the arbitral tribunal; (b) restricting the multi-party arbitration to a limited number of participants, which may be advisable in projects involving a large number of participants; (c) aspects of the formulation of the arbitration agreement in the case of a multilateral contract or in the case of several related contracts, and, with respect to the latter case, the conclusion of a separate multi-party arbitration protocol or the insertion of a uniform arbitral clause in each contract; (d) difficulties that may arise in any multi-party dispute with respect to the number and the appointment of arbitrators, and the possibility of involving the ICC Court of Arbitration in the appointment of the whole arbitral tribunal, envisaging either direct appointment or confirmation of any appointments made by the parties.<sup>15</sup>

16. At the time of adoption of the Guide, the ICC was studying model agreements which could be included in pertinent contracts. However, in order not to impede further developments in the area and to permit the parties to set their own guidelines, the ICC refrained from including such model agreements in the Guide.

<sup>13</sup>ICC Brochure, No. 404, 1982.

<sup>14</sup>*Ibid.*, pp. 4-5.

<sup>15</sup>*Ibid.*, pp. 5-7.

17. After the completion of the Guide, work continued on the preparation of model clauses to be used in agreeing on multi-party arbitration. In the course of that work, the following two draft texts have been elaborated: draft guidelines for ICC multi-party arbitration,<sup>16</sup> together with a draft multi-party arbitration clause.<sup>17</sup> Work on these two draft texts has not yet been completed.

### 2. Draft guidelines for ICC multi-party arbitration

18. The draft guidelines for ICC multi-party arbitration are designed to provide a procedural framework for a multi-party arbitration administered by the ICC Court of Arbitration. The guidelines, the applicability of which is based on the agreement of parties expressed in the model multi-party arbitration clause (see below, para. 26), apply together with the "Rules for the ICC Court of Arbitration". However, in view of the special aspects of multi-party arbitration, the draft guidelines expressly state that the parties (or, failing agreement of the parties, the arbitral tribunal) may adopt special rules governing the multi-party proceedings.<sup>18</sup>

19. According to the draft guidelines, the ICC Court of Arbitration will not organize a multi-party arbitration under the ICC Rules unless a party to a pending or proposed ICC arbitration makes a specific request to that effect in the form required and within the prescribed period of time.<sup>19</sup> If the ICC Court of Arbitration is satisfied of the *prima facie* existence of an agreement for an ICC multi-party arbitration, but no party has made a request for a multi-party arbitration, the ICC Court will generally not proceed with the appointment or confirmation of an arbitrator until the secretariat of the ICC has enquired of the parties whether any related disputes exist.<sup>20</sup> If there is a controversy as to the existence of a binding agreement for ICC multi-party arbitration, the ICC Court of Arbitration may apply article 8(3) of the ICC Rules.<sup>21</sup>

20. Regarding the constitution of the arbitral tribunal, the parties to the multi-party arbitration have the right to appoint the arbitral tribunal by common agreement. If the parties have not appointed the arbitral tribunal within the prescribed period of time, the ICC Court of Arbitration will either extend the period or appoint the arbitral tribunal.<sup>22</sup>

<sup>16</sup>ICC Document No. 420/276, annex I.

<sup>17</sup>*Ibid.*, annex II.

<sup>18</sup>*Ibid.*, annex I, no. II, "Definitions and basic rules".

<sup>19</sup>*Ibid.*, no. III, "Request for multi-party arbitration".

<sup>20</sup>*Ibid.*, no. IV, "Organisation of a multi-party arbitration by the ICC Court".

<sup>21</sup>*Ibid.*; article 8(3) of the ICC Rules provides: "Should one of the parties raise one or more pleas concerning the existence or validity of the agreement to arbitrate, and should the Court be satisfied of the *prima facie* existence of such an agreement, the Court may, without prejudice to the admissibility or merits of the plea or pleas, decide that the arbitration shall proceed. In such a case any decision as to the arbitrator's jurisdiction shall be taken by the arbitrator himself."

<sup>22</sup>ICC document No. 420/276, 30 January 1986, annex I, No. V, "Appointment of the arbitrator".

21. The draft guidelines advise parties to limit the number of parties who may participate in an ICC multi-party arbitration, either by indicating a maximum number of parties, or by identifying the parties who may participate in such an arbitration. Unless all the parties to an ICC multi-party arbitration have specifically agreed otherwise, the draft guidelines provide that there may be no more than four parties to the arbitration.<sup>23</sup>

22. It is further provided that the disputes to be settled in an ICC multi-party arbitration must be connected to each other, and in each dispute there must be one party who is also a party to every other dispute to be settled in that multi-party arbitration. Furthermore, after the arbitral tribunal has been appointed, no new party may join or intervene in the multi-party arbitration unless all the parties and the arbitral tribunal unanimously consent thereto.<sup>24</sup>

23. As to the conduct of multi-party arbitral proceedings, the draft guidelines provide that, whatever procedural rules govern the proceedings in an ICC multi-party arbitration, the arbitral tribunal must ensure equal treatment of all the parties. In that context, provision is made, for example, for the right of each party to be heard, to consider documents on the file, to participate in hearings, and to be represented or assisted by counsel of its choice.<sup>25</sup>

24. The draft guidelines further advise prospective users of the ICC multi-party arbitration services to consult professional counsel as to the suitability of the standard ICC multi-party arbitration clause, since the circumstances of each case may render it desirable or essential to vary the terms of the clause. The standard clause may need to be varied, in particular, with regard to matters dealt with in the 1981 ICC Guide on Multi-party arbitration such as the appointment of arbitrators, or specifying contracts which fall within (or outside) the scope of a multi-party arbitration.<sup>26</sup>

25. Where the ICC Court of Arbitration or (after receiving the file) the arbitral tribunal is satisfied that a multi-party arbitration would not be practicable or that the interests of a party might be prejudicially affected by it, the ICC Court of Arbitration or the arbitral tribunal, as the case may be, is empowered by the draft guidelines to decide on a severance of the proceedings. In such an event, the ICC Court of Arbitration would either appoint the arbitrator or arbitrators already appointed in the multi-party arbitration as arbitrator or arbitrators in the separate arbitration, or appoint another person or persons to act in the separate arbitration. The separate arbitration would then proceed and be decided as if it had never been subject to the multi-party arbitration procedure.<sup>27</sup>

### 3. Draft multi-party arbitration clause

26. The latest draft of the ICC multi-party arbitration clause reads as follows:

"1. All disputes arising in connection with the present contract shall be finally settled under the Rules of Conciliation and Arbitration of the International Chamber of Commerce by one or more arbitrators appointed in accordance with the said Rules.

"2. The parties to the present clause agree that:

"(a) If any such dispute raises issues which are the same as or are connected with issues raised in a related dispute arising in connection with a contract between a party to this contract and a third party and provided that such related dispute is to be or has been submitted to arbitration under the ICC Rules,

"(b) and if the parties to such related dispute have themselves agreed, in their original arbitration agreement or any subsequent agreement, that such related dispute shall be finally settled in an ICC Multi-Party Arbitration together with any dispute which might arise under a connected contract,

"(c) and provided that one or other of the parties to this contract also requires or accepts the same after learning of the said connected dispute,

"then such dispute hereunder and such related dispute shall be finally settled by the same arbitrator or arbitrators who shall be appointed by common agreement amongst all the parties to the arbitration combined in this way, or by the Court of Arbitration of the ICC in accordance with the Guidelines for ICC Multi-Party Arbitration.

"The ICC Court of Arbitration shall decide whether a dispute is prima facie to be settled in an ICC Multi-Party Arbitration, but the final decision shall be made by the arbitrator or arbitrators."<sup>28</sup>

## II. Taking of evidence in arbitral proceedings

### A. International Council for Commercial Arbitration

27. Questions of evidence in international commercial arbitration were considered by a working party of the Vth International Arbitration Congress organized by the International Council for Commercial Arbitration.<sup>29</sup> The introductory report to the working party, noting that legal writing on issues of evidence in international commercial arbitration was scarce, largely based its analysis on a 1974 international symposium which considered the way of presenting evidence in arbitration from the point of view

<sup>23</sup>*Ibid.*, no. VI, "Parties to an ICC multi-party arbitration".

<sup>24</sup>*Ibid.*

<sup>25</sup>*Ibid.*, no. VII, "Equal treatment".

<sup>26</sup>*Ibid.*, no. VIII, "Additional provisions".

<sup>27</sup>*Ibid.*, no. IX, "Severance of cases".

<sup>28</sup>ICC Document No. 420/276, 30 January 1986, annex II.

<sup>29</sup>The Congress was held from 7 to 10 January 1975 in New Delhi; the reports and discussions of the Congress are published in *Proceedings of the Fifth International Arbitration Congress* (New Delhi, New Indian Council of Arbitration, 1975).

of different legal systems.<sup>30</sup> Referring to that symposium, the report noted that, despite many important differences in the law and practice in the field of evidence in international commercial arbitration, there existed some possibilities for international harmonization and rapprochement in that respect.<sup>31</sup> On the basis of that report, the working party discussed practices which might be commonly acceptable for presenting evidence in international arbitral proceedings.

28. As a result of those discussions, the working party made, and the Congress supported, the following recommendations:

"1. It is desirable to formulate, for the benefit of parties and arbitrators, guidelines for presenting evidence in international commercial arbitration.

"2. It is suggested that ICCA undertake the task of framing such guidelines, which should be consonant with the UNCITRAL Arbitration Rules in the form finally adopted.

"3. In framing the guidelines, consideration should be given to such matters as distinguishing between different types of evidence, collection of evidence, methods of introducing and receiving evidence, including modes of examining witnesses and presenting expert opinions.

"4. In framing the guidelines consideration should be given to the problems arising out of the refusal by a party to the arbitration to produce evidence on grounds of State security, confidentiality, professional privilege, etc."<sup>32</sup>

With respect to the recommendations, the Congress was "confident that potential areas of fundamental agreement can be found and that effective guidelines can be established."<sup>33</sup>

29. At the VIIIth International Arbitration Congress of ICCA, to be held from 6 to 9 May 1986 in New York, one of the two working groups will be devoted to comparative arbitration practice. The discussions on practical questions of procedure, including issues of evidence, will be based on a hypothetical case commented upon from the point of view of different legal systems.

### B. International Bar Association

30. The Council of the International Bar Association adopted on 28 May 1983 the Supplementary Rules

<sup>30</sup>The symposium, organized by the International Committee for Commercial Arbitration (re-named in 1975 to International Council for Commercial Arbitration), was held from 14 to 16 February 1974 in London; the materials of the symposium are published in a special issue of *Arbitration*, vol. 41, No. 2 (April 1974).

<sup>31</sup>J. Jakubowski, "Proposals for promoting the development of practices which might be commonly acceptable for presenting evidence in international commercial arbitration", report to working party II of the Vth International Arbitration Congress, in *Proceedings of the Vth International Arbitration ...*, p. C IIa 1.

<sup>32</sup>*Proceedings of the Vth International Arbitration ...*, p. E38.

<sup>33</sup>*Ibid.*

Governing the Presentation and Reception of Evidence in International Commercial Arbitration.<sup>34</sup> The initiative to prepare such rules arose from discussions in Committee D (Procedures for Settling Disputes) of the Section on Business Law of the International Bar Association. The preparatory work for the Rules was done by a subcommittee formed by Committee D.<sup>35</sup>

31. The subcommittee considered that it would be fruitless to make yet a further attempt at a complete set of arbitration rules, since a variety of well-known rules existed already and were in international circulation, and were most unlikely to be replaced by yet a further set of rules.<sup>36</sup> It was therefore decided that the rules to be prepared should be confined to the mechanics of presenting or receiving evidence in a commercial arbitration.<sup>37</sup> The largest problem encountered by the subcommittee in its work was "the well-known difference between the Common Law adversarial approach to the laying out of a case for judicial consideration and the Civil Law's inquisitorial system". As a result, the subcommittee "tried to go through the sort of negotiations that would be carried out in practice if lawyers and arbitrators from Common Law and Civil Law systems actually had to sit down together and agree upon a procedure for an actual arbitration between parties of a Civil Law and of a Common Law country".<sup>38</sup>

32. In an introduction to the Rules, the International Bar Association presents the Rules in the following way:

"These Supplementary Rules are the product of a working party of Committee D (Procedures for Settling Disputes) of the Section on Business Law of the International Bar Association.

"They are solely concerned with the presentation and reception of evidence in arbitrations and are recommended by the International Bar Association for incorporation in, or adoption together with, institutional and other general rules or procedures governing international commercial arbitrations.

"Even if not specifically adopted by agreement between the parties, they can serve as a guide to arbitrators conducting such arbitrations when the parties in contention come from law areas having rules of procedures derived from different systems.

"They may be referred to as the I.B.A. Rules of Evidence.

<sup>34</sup>Published in a brochure of the International Bar Association; also published in International Council for Commercial Arbitration, *Yearbook Commercial Arbitration* (Deventer, Kluwer), vol. X-1985, pp. 152-156, and in *Arbitration International*, vol. 1, No. 2 (July 1985), pp. 124-128.

<sup>35</sup>D.W. Shenton, "International Bar Association, Supplementary Rules Governing the Presentation and Reception of Evidence in International Commercial Arbitration", Explanatory note, *Yearbook Commercial Arbitration*, (Deventer, Kluwer), vol. X-1985, p. 145; that text, with minor editorial changes and entitled "An introduction to the IBA rules of evidence", was published in *Arbitration International*, vol. 1, No. 2 (July 1985), pp. 119-124.

<sup>36</sup>*Ibid.*, pp. 146-147.

<sup>37</sup>*Ibid.*, p. 147.

<sup>38</sup>*Ibid.*, p. 147.



"It is recommended that when the parties desire to adopt the I.B.A. Rules of Evidence as supplementary to the general rules applicable to a particular arbitration, the following additional clause be adopted:

"The I.B.A. Rules of Evidence shall apply together with the General Rules governing any submission to arbitration incorporated in this Contract. Where they are inconsistent with the aforesaid General Rules, these I.B.A. Rules of Evidence shall prevail but solely as regards the presentation and reception of evidence."

33. The conduct of taking evidence in arbitral proceedings is dealt with in the I.B.A. Rules by general clauses and by special rules on particular means of evidence. In so far as the I.B.A. Rules and the general arbitration rules are silent, the arbitral tribunal may conduct the taking of evidence as it thinks fit (art. 1(2)). Another general clause confers upon the arbitral tribunal, in addition to the powers available under the applicable procedural law and the general arbitration rules, a number of further powers, including the authority to exercise all the powers it deems necessary to make the arbitration effective and its conduct efficient as regards the taking of evidence (art. 7, in particular (h)).

34. With respect to particular means of evidence, the Rules provide that each party is required to list the documents on which it desires to rely, to exchange such list with every other party, and to deliver the list to the arbitral tribunal. Unless a document has been so listed it may not be produced at the hearing without the consent of the arbitral tribunal. Furthermore, the Rules oblige each party to provide the arbitral tribunal with a copy of each document in its list. A party is entitled to a copy of any document listed by another party upon offer of payment of the reasonable copying charge (art. 4(1), (2) and (3)).

35. As to the duty to produce a document, the Rules give each party a right to request any other party to produce any document relevant to the dispute. A condition for such a request is that the requested document passed between the requested party and a third party who is not a party to the arbitration. The Rules empower the arbitral tribunal, upon application by one of the parties or of its own volition, to order a party to produce any relevant document within the party's possession, custody or control. If a party fails to comply with such an order, the arbitral tribunal will draw its conclusions from that failure (art. 4(4), (5) and (6)).

36. With respect to evidence by witnesses, article 5 of the Rules provides that, prior to the hearing of a witness, the testimony must normally be presented in the form of a written statement signed by the witness. This written statement must include, *inter alia*, (a) a description of any connection of the witness with any of the parties; (b) a description of his background, qualifications, training and experience if these are relevant to the dispute or the testimony; (c) a full statement of the evidence desired to be presented through the testimony of that witness; (d) a

reference as to whether the witness is a witness of fact or an expert, and whether the witness is testifying from his knowledge, observation or experience, or from information and belief, and, if the latter, the source of the knowledge. In this context it may be noted that it is considered to be proper for a party to interview a witness or a potential witness.

37. After the statement has been presented, the witness would testify orally if both parties agree to it or if the arbitral tribunal so decides. The witness will first be examined by the arbitral tribunal and then by the party presenting the witness, whereupon other parties may cross-examine the witness. However, the arbitral tribunal is given complete control over the procedure relating to examining a witness, including the right to limit or deny the right of a party to examine, cross-examine or re-examine the witness. Moreover, the Rules empower the arbitral tribunal to call a witness, whether the parties agree thereto or not.

38. As to the role of the arbitral tribunal regarding expert evidence, article 7(e), (f) and (g) provides that the arbitral tribunal has the right to rely on its own expert knowledge, to appoint experts to assist the arbitral tribunal or to give expert evidence or reports in the arbitration, to regulate the right of the parties to call expert witnesses, and to make provisions with regard to their activities and the presentation of their evidence.

### III. International court assistance in taking evidence in arbitral proceedings

#### *Hague Conference on Private International Law*

39. The issue of international court assistance in taking evidence in arbitral proceedings was raised by the Permanent Bureau of the Hague Conference on Private International Law at a 1984 session of the Special Commission on General Matters and Policy of the Hague Conference, whose mandate included the preparation of decisions to be taken concerning future work of the Hague Conference.<sup>39</sup> That initiative of the Permanent Bureau was prompted by discussions on the same issue in the UNCITRAL Working Group on International Contract Practices during the preparation of the UNCITRAL Model Law on International Commercial Arbitration.

40. It may be recalled that in those discussions the prevailing view was, at first, that if court assistance in arbitral proceedings were to be regulated at all in the Model Law, a provision on international court assistance would be useful.<sup>40</sup> Later, however, the view prevailed that it was not feasible for a model law on arbitration to

<sup>39</sup> *Conclusions of the Special Commission of January 1984 on General Matters and Policy of the Conference*, Permanent Bureau of the Conference, Preliminary document No. 1 (April 1984) for the attention of the Fifteenth Session, chap. B XIV, pp. 15 and 17.

<sup>40</sup> Report of the Working Group on International Contract Practices on the work of its fifth session (A/CN.9/233), para. 36.

regulate a complex matter such as unilateral obligations of domestic courts to give assistance to foreign arbitral tribunals. In support of that latter view it was noted, in particular, that international court assistance in taking evidence was an issue which fell within the domain of international co-operation between States and that such international co-operation could only be achieved in a satisfactory way by international instruments such as conventions or bilateral treaties.<sup>41</sup>

41. The precise issue raised by the Permanent Bureau before the Special Commission was whether the 1970 Hague Convention on the Taking of Evidence Abroad in Civil or Commercial Matters could be extended in order to permit arbitrators to forward requests for the taking of evidence directly to courts or authorities in a place other than that where the arbitration proceedings were taking place.<sup>42</sup> No decision was taken by the Special Commission as to the substance of the issue, and the Permanent Bureau was requested to prepare a note on the desirability of such an extension of the 1970 Hague Convention.<sup>43</sup>

42. In a note prepared subsequently, the Permanent Bureau discussed the question whether it would be useful and desirable for the Hague Conference to undertake work on the subject of international court assistance in taking evidence in arbitral proceedings.<sup>44</sup> With respect to that question, the Permanent Bureau stated the following:

"It seems indeed that in practice the recourse to a proceeding for the taking of evidence abroad is not very frequent, since most often the parties to the arbitration are the ones who arrange for the necessary proof in support of their arguments to be presented to the arbitration tribunal. What seems to happen most often is that, when a person refuses to testify, the party who has an interest in having him heard does not insist at any cost in obtaining his statement, but rather prefers to do without testimony which might be unfavourable to him. However, there may be cases in which a procedure for taking of evidence would turn out to be useful, for example when witnesses do not refuse to testify but are prevented for financial or physical reasons from appearing before the arbitral tribunal. In addition, the examination of physical evidence in a country which is very distant from the place of arbitration may turn out to be less costly by the way of assistance from the national courts of that country than by the travel of the arbitral tribunal itself.

"Before submitting the problem examined in this note to the Member States of the Conference, the Permanent Bureau made contact unofficially with cer-

<sup>41</sup>Report of the Working Group on International Contract Practices on the work of its sixth session (A/CN.9/245), paras. 42 and 43.

<sup>42</sup>See note 39.

<sup>43</sup>See note 39.

<sup>44</sup>Note on the obtaining of evidence abroad in arbitration proceedings drawn up by the Permanent Bureau, annex 11 relating to Point XIV of the Conclusions of the Special Commission on General Matters and Policy of the Conference (Prel. Doc. No. 1 for the attention of the Fifteenth Session).

tain international arbiters known by it to have had long practical experience in this field. The questions were whether, during the long period of activity in international arbitration of the persons contacted, they had encountered practical problems raised by the impossibility of obtaining testimony or examining physical evidence, and what in fact happens when an arbitral tribunal in order to make its award must absolutely hear a witness who refused to appear.

"The replies of the arbiters contacted, with only one exception, were rather discouraging; in fact, there do not seem to be serious problems, since the parties to the arbitration proceedings seem always to make arrangements among themselves, or if not, then prefer to do without the testimony.

"However, the arbiters contacted did not deny that it could be useful for an international treaty to deal with the question. Although the philosophy which underlies arbitration is opposed to recourse to national authorities (except naturally in the stage of enforcement of the award), an international treaty which would give the possibility for an arbitral tribunal or a party to an arbitration, where the need was felt, to obtain the deposition of a witness or to gather physical proof could seem very useful in practice and bring assistance to the smooth functioning of arbitral justice."<sup>45</sup>

43. On the basis of a decision of the Fifteenth Session of the Hague Conference on Private International Law,<sup>46</sup> the question of using the 1970 Hague Convention for the taking of evidence in arbitral proceedings was referred to a Special Commission of the Hague Conference, which was convened for the purpose of considering the technical operation of the 1970 Hague Convention. Concerning the desirability of using the 1970 Convention for that purpose, a number of experts in the Special Commission

"expressed the view that there was little need for such a facility in practice. Certain experts thought that arbitrators or litigants in arbitral proceedings might use the Convention as it stood by making their request through the courts in the countries where the arbitral tribunal sat. In particular, the experts from the Nordic countries and the United States pointed out that under domestic law courts may render assistance for the production of evidence abroad in the context of arbitral proceedings."<sup>47</sup>

44. As to the technical aspects of extending the Convention for use in the context of arbitral proceedings, the Special Commission reached the following conclusions:

"1. Opinion was divided as to whether any possible protocol to the Convention should provide that appli-

<sup>45</sup>*Ibid.*, pp. 5 and 7.

<sup>46</sup>*Hague Conference on Private International Law*, Commission I, Procès verbal No. 4, Fifteenth Session, general affairs, Meeting of 18 October 1984, No. 15.

<sup>47</sup>*Report on the Second Meeting of the Special Commission on the Operation of the Hague Convention of 18 March 1970 on the Taking of Evidence Abroad in Civil or Commercial Matters*, 28-31 May 1985 (The Hague, Permanent Bureau of the Conference, July 1985), chap. II, p. 26.

cations (letters of request) for the taking of evidence abroad should be made through a forwarding Central Authority in the State where the arbitral tribunal sat, or should provide that such application could be made directly to the Central Authority in the State where the evidence was to be taken.

"2. It was generally agreed that any such protocol should provide an option for the taking of evidence abroad by commissioners (cf. article 17 of the Convention). [48]

"3. There was a consensus that it would be difficult, if not impossible, to distinguish in establishing the scope of such a protocol among the differing types of arbitral tribunals which exist in practice, such as tribunals operating under the auspices of arbitration institutes or tribunals which apply or do not apply the UNCITRAL rules."<sup>49</sup>

45. The Hague Conference on Private International Law has not yet made a final decision on whether or not to continue work on the issue of international court assistance in taking evidence in arbitral proceedings.

#### IV. Law applicable to arbitration agreements

##### *Hague Conference on Private International Law*

46. The Hague Conference on Private International Law decided in 1980 to include in its agenda of future work the question of the law applicable to arbitration clauses.<sup>50</sup> That decision was considered by a Special Commission on General Matters and Policy of the Hague Conference, which was convened in 1984 for the purpose of examining the Conference's work in progress and of preparing the decisions to be taken concerning future work. The Special Commission determined, with respect to the question whether there was a need for a convention on the law applicable to arbitration clauses, that it was too early to decide that question and that it was necessary to await the conclusions of an expert consulted by the Permanent Bureau of the Conference.<sup>51</sup> It was therefore

<sup>48</sup>Article 17 of the Convention reads:

"In a civil or commercial matter, a person duly appointed as a commissioner for the purpose may, without compulsion, take evidence in the territory of a Contracting State in aid of proceedings commenced in the courts of another Contracting State if —

(a) a competent authority designated by the State where the evidence is to be taken has given its permission either generally or in the particular case; and

(b) he complies with the conditions which the competent authority has specified in the permission.

"A Contracting State may declare that evidence may be taken under this Article without its prior permission."

<sup>49</sup>*Report on the Second Meeting of the Special Commission ...*, pp. 26 and 28.

<sup>50</sup>*Actes et documents de la quatorzième session, 6 to 25 October 1980*, (The Hague, The Hague Conference on Private International Law, 1982), vol. I, "Miscellaneous matters", p. 1-64.

<sup>51</sup>Conclusions of the Special Commission of January 1984 on General Matters and Policy of the Conference, Permanent Bureau of the Conference, Preliminary doc. No. 1, (April 1984), for the attention of the Fifteenth Session, chap. B IV, p. 9.

concluded not to propose the deletion of that topic from the agenda, and that close contacts with UNCITRAL, which was dealing with more general questions concerning arbitration, should be maintained.<sup>52</sup>

47. As to the work of UNCITRAL to which reference is made in the foregoing conclusion, it may be recalled that the Working Group on International Contract Practices discussed the question whether any general conflict of laws rules should be prepared as part of the Model Law on International Commercial Arbitration.<sup>53</sup> That discussion should be seen against the following background.

48. The draft model law, as it was discussed by the Working Group at its seventh session, provided, in the context of setting aside an award and in the context of recognition and enforcement of an award, a rule on the law governing the validity of arbitration agreements. In both contexts, the primarily applicable law was the one to which the parties had subjected the arbitration agreement. Where there was no indication of a choice of law by the parties, in the context of setting aside the applicable law was the law of the court which was to decide the issue of setting aside (art. 34(2)(a)(i)), and in the context of recognition and enforcement it was the law of the country where the award had been made (art. 36(1)(a)(i)). In both contexts, the applicable law was the same since under the prevailing view in the Working Group,<sup>54</sup> which was later adopted by the Commission,<sup>55</sup> the place of arbitration was the exclusive determining factor for the applicability of article 34, and, under article 31(3),<sup>56</sup> the award was deemed to have been made at the place of arbitration.

49. The rules contained in articles 34(2)(a)(i) and 36(1)(a)(i) could not be regarded as general and complete conflict of laws provisions. First, they provided an express solution only in the context of setting aside and recognition or enforcement while a solution for the time before the making of the award or even before the commencement of arbitral proceedings was to be arrived at by interpretation. Second, they provided no solution for the cases where the parties had not subjected the arbitration agreement to a particular law and it could not be ascertained where the arbitral award was to be made.

50. The view of the Working Group during its discussions in 1984 was that harmonization of conflict of laws rules relating to arbitration was desirable but that it was not appropriate to envisage inclusion of general conflict of laws rules on arbitration agreements in the model law, which the Commission was expected to adopt in 1985. It was understood that the Commission might wish to consider the matter and decide on its possible future course of action, in particular, as regards the co-ordina-

<sup>52</sup>*Ibid.*, p. 7.

<sup>53</sup>Report of the Working Group on International Contract Practices on the work of its seventh session (A/CN.9/246), para. 198.

<sup>54</sup>*Ibid.*, paras. 167 and 171.

<sup>55</sup>Article 1(2) of the UNCITRAL Model Law on International Commercial Arbitration.

<sup>56</sup>Report of the Working Group on International ..., para. 112.

tion of work between it and the Hague Conference on Private International Law, which was considering the preparation of a convention on the law applicable to the validity of arbitration clauses.<sup>57</sup>

51. The Commission, at its eighteenth session in 1985, discussed merely the question whether the rule on the validity of the arbitration agreement contained in article 34(2)(a)(i) was an appropriate one. The discussion was prompted by the proposal

“to substitute the words ‘or there is no valid arbitration agreement’ for the words ‘or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of this State’. It was pointed out that the conflict of laws rule contained in that latter wording, which was taken from the 1958 New York Convention [art. V(1)(a)], was inappropriate in that it declared as applicable, failing a choice of law by the parties, the law of the place of arbitration. The place of arbitration, however, was not necessarily connected with the subject-matter of the dispute. It was unjustified to let the law of that State determine the issue with global effect, which would be the effect of a setting aside by virtue of article 36(1)(a)(v) of the model law or article V(1)(e) of the 1958 New York Convention; it was also said that such a result would be in conflict with a modern trend to determine the issue in accordance with the law of the main contract.

“It was stated in reply that it was preferable to retain the present text not simply because it was the wording of the 1958 New York Convention but also because the rule was in substance a sound one. It was pointed out that the rule recognized party autonomy, which was important in view of the fact that some legal systems applied the *lex fori*. Furthermore, to use the place of arbitration as a secondary criterion was beneficial in that it provided the parties with a degree of certainty which was lacking under the proposed formula. There were also doubts as to whether in fact a trend could be discerned in favour of determining the question of the validity of the arbitration agreement according to the law of the main contract.”<sup>58</sup>

52. The Commission, after deliberation, decided to retain the conflict of laws rule on the validity of the arbitration agreement as contained in article 34(2)(a)(i) of the Model Law.<sup>59</sup>

53. When the Fifteenth Session of the Hague Conference (1984) discussed the question of a unification of conflict of laws rules dealing with arbitration agreements, it was decided to delete that question from the working programme of the Hague Conference.<sup>60</sup> In connection

with that decision, it was stressed by the Chairman of the Session

“that deletion of this question would in no way exclude cooperation with UNCITRAL in the future, even in this field. Furthermore, deletion would not prevent the matter from being taken up again at a later date if this were to be felt necessary.”<sup>61</sup>

## V. Adaptation or supplementation of contracts by third persons

### A. International Council for Commercial Arbitration

54. Questions pertaining to adaptation and supplementation were a subject of the Vth and the VIIth International Arbitration Congresses organized by the International Council for Commercial Arbitration (ICCA).<sup>62 63</sup>

55. On these questions, the Vth International Arbitration Congress adopted the following resolution:

“[The Congress:]

“Strongly re-affirms the great value of arbitration, not only for traditional types of disputes arising in international trade, but also in connection with long-term contracts of the type which are now so often used to implement international commercial transactions for scientific, technical and industrial development. Such long-term transactions are becoming increasingly important in world trade and are also a significant factor in establishing conditions which assist in maintaining world progress.

“Notes that one of the principal problems in connection with long-term contracts is the question of whether arbitrators have the power to fill gaps and resolve deadlocks which may arise during the life of the agreement. Such gaps may occur when parties postpone specific agreement on certain points because of lack of complete information when a contract is first formed; when unforeseen or unforeseeable events occur due to changes in economic, technical or political conditions; when inevitably vague expressions are used in the contract and when parties to joint ventures disagree on the conduct of their joint enterprise. Reports received by the Congress indicate that the power of arbitrators to fill such gaps in a binding manner varies in different nations and under different legal systems. Such differences may be minimised by overcoming the stress on theoretical speculation and dogmatic construction and getting closer to reality.

<sup>61</sup>*Ibid.*

<sup>62</sup>The Vth International Arbitration Congress was held from 7 to 10 January 1975 in New Delhi; the reports and discussions of that Congress are published in *Proceedings of the Vth International Arbitration Congress*, (New Delhi, Indian Council of Arbitration, 1975).

<sup>63</sup>The VIIth International Arbitration Congress was held from 7 to 11 June 1982 in Hamburg; the reports and discussions of that Congress are published in International Council for Commercial Arbitration, *New Trends in the Development of International Commercial Arbitration and the Role of Arbitral and other Institutions*, ICCA Congress series No. 1, Pieter Sanders, ed. (Deventer, Kluwer, 1983).

<sup>57</sup>*Ibid.*, paras. 200 and 201.

<sup>58</sup>Report of the United Nations Commission on International Trade Law on the work of its eighteenth session, *Official Records of the General Assembly, Fortieth Session, Supplement No. 17 (A/40/17)*, paras. 283 and 284.

<sup>59</sup>*Ibid.*, para. 285.

<sup>60</sup>Hague Conference on Private International Law, Commission I, Procès verbal No. 2, Fifteenth Session, general affairs, Meeting of 16 October 1984, No. 52.

"Recognises that agreement by the parties to widen the scope of arbitration to fill such gaps and break such deadlocks can be of great practical assistance in forming and performing long-term contracts. Such agreement must be expressed by a drafting technique which is appropriate to meet difficulties that may arise under different national laws.

"To this end, the Congress urges that the comparative law studies on this subject which have been so fruitfully begun during the deliberations in New Delhi be continued in order that information concerning the law and practice in this regard can be collected and disseminated and so that methods to utilise this valuable function of arbitration may be further developed. The Congress therefore suggests that ICCA sponsor and encourage such studies with the aim of reaching a practical result, as, for example, the preparation of model clauses."<sup>64</sup>

56. Adaptation and supplementation of contracts was a subject discussed by a working group of the VIIth International Arbitration Congress which adopted the following resolution:

"A. The Working Group received reports which focused attention on the problems of adaptation of contracts.

"Such problems may arise in three types of instances:

- "1. application of hardship or revision clauses;
- "2. contracts in which certain points have been left open;
- "3. cases in which one of the parties contends that unforeseen circumstances should lead to a revision of the contract, in spite of it not containing any revision clause.

"B. The Working Group considers that the best way of solving those problems is by mutual agreement of the parties revising or completing their contractual arrangements.

"Lacking such agreement, the following solutions are to be considered:

- "1. If there is a hardship or revision clause, the same should be applied through arbitration.
- "2. Where certain points have been left open in the contract, arbitrators, in many countries, do not have the power to complete it but, in such countries, may be able to determine the prejudice resulting from the refusal to negotiate in good faith, if any, and allow damages in compensation of such prejudice.
- "3. In case of unforeseen circumstances and if the contract does not contain a revision clause, the arbitrators should not modify the contract, except if the law applicable to the contract allows it and if the parties have expressly granted such a power to the arbitrators.

"C. The Working Group noted that, in order to provide improved procedures for resolving disputes involving adaptation of contracts, an arbitral organization has established new rules in this regard."<sup>65</sup>

### B. International Chamber of Commerce

57. The International Chamber of Commerce adopted in 1978 the Rules on the Regulation of Contractual Relations, which provide a procedure for adaptation or supplementation of contracts.<sup>66</sup> The purpose of this procedure is to enable parties to call upon a third person to intervene in the case where the parties cannot agree on how to adapt or supplement their contract. The parties may have an interest in such an intervention of the third person, for example, in the following situations: (a) where the parties deferred the insertion of a particular provision in their contract; (b) where the parties agreed that their contract would be adapted if the economic equilibrium of the contract were affected by a change of circumstances; (c) where the parties agreed that certain decisions relating to the implementation of the contract would be made jointly.<sup>67</sup>

58. The third person fulfils his task by either formulating a recommendation or taking a decision, depending on the choice of the parties (art. 11(1)). When the third person makes a recommendation, the Rules provide that the parties must consider it in good faith (art. 11(2)). When the third person takes a decision, that decision is binding on the parties to the same extent as the contract in which it is deemed to be incorporated, and the parties are to give effect to such a decision as if it were the expression of their own will (art. 11(3)).

59. In connection with the ICC Rules, a model clause is provided for parties to use in agreeing on the procedure under the Rules. According to the model clause, in the event that the parties are unable to agree to apply all or any of the provisions of a specified article of their contract, they should apply to the ICC Standing Committee for the Regulation of Contractual Relations. The Standing Committee will administer the proceedings in which a third person (or a board of three persons if the parties so agree) appointed in accordance with the Rules will carry out the task assigned by the parties.

60. The functions of the ICC Standing Committee in administering the proceedings under the Rules include the following: (a) the confirmation of the third person, whom the parties are to nominate by agreement, or the appointment of the third person in the absence of such agreed nomination; (b) in a case where the tasks under the Rules are to be performed by a board of three members, the confirmation of two members of whom

<sup>65</sup>*New Trends in the development ...*, p. 269.

<sup>66</sup>The ICC Rules on the Regulation of Contractual Relations are published in *Adaptation of Contracts*, ICC Brochure No. 326 (Paris, International Chamber of Commerce, 1978).

<sup>67</sup>*Ibid.*, pp. 7-8.

<sup>64</sup>*Proceedings of the Vth International Arbitration ...*, pp. E39-E40.

each is nominated by a party, and the appointment of the chairman of the board; (c) the challenge or replacement of the third person; (d) the fixing of the amount of deposit to cover the costs of the proceedings; (e) the extension or shortening of the period of time for carrying out the task of the third person; (f) approval as to form of a recommendation or decision made by the third person; (g) determining the place where the third person's recommendation or decision is deemed to have been issued; (h) fixing of costs of proceedings.

61. The procedure to be followed by the third person in carrying out his task is dealt with in article 9 of the ICC Rules as follows:

- "1. Within the limits arising from the applicable contract clause and from any other agreement arrived at between the parties and included in their written memoranda, the third person is empowered to make any decision intended to resolve the questions concerned.
- "2. The third person may obtain any information which he deems necessary in order to carry out his mission.
- "3. The parties undertake to provide the third person with every facility for the carrying out of his mission and to communicate to him any information or document which he may require to that end.
- "4. In the execution of his mission the third person shall afford each party equal treatment in all respects and equal opportunity to present its views, and to reply to the comments of the other party.
- "5. The third person shall hear the parties orally either on his initiative or upon the request of one of the parties.
- "6. Any person intervening within the framework of these Rules undertakes to respect the confidential nature of the proceedings."

62. As to the effect of proceedings under the ICC Rules, article 10 of the Rules prescribes that, unless otherwise provided by the parties, the action of bringing a case before the Standing Committee does not of itself have any effect on the contract until the third person has made his recommendation or taken his decision.

63. With respect to the formulation of a recommendation or a decision by the third person under the ICC Rules, it is provided, *inter alia*, that (a) unless otherwise provided by the parties, the third person must give reasons for his recommendation or decision (art. 12(2)); (b) where a board of three members is to make a recommendation or a decision it will be made by a majority of votes; (c) failing a majority of votes, the chairman of the board will formulate the recommendation or take the decision alone (art. 12(3)); (d) the third person's recommendation or decision is deemed to be

issued at the place agreed upon by the parties or, failing such agreement, as determined by the Standing Committee (art. 12(4)).

64. It should be noted that the procedure under the ICC Rules is conceived and characterized not as one of arbitration but as being "clearly of a contractual nature".<sup>68</sup> This concept was chosen, in particular, for legal reasons, namely the disparity between national laws as regards the powers of arbitrators to adapt contracts or to fill gaps.

65. This disparity, which had prompted the search for practical solutions by the participants of the above ICCA Congresses, and the extent to which mechanisms of a contractual nature were available under legal systems, were important factors in the considerations of the UNCITRAL Working Group on International Contract Practices on the question whether a provision on adaptation and supplementation of contracts should be included in the draft model law:

"19. The Working Group recognized the usefulness of procedures to which parties, in particular parties to long-term contracts, might resort in order to have their contracts adapted or supplemented and also recognized that procedural safeguards contained in such procedures would enhance legal certainty in international trade. For this reason some support was expressed for a provision in the model law granting the power to the arbitral tribunal to adapt and supplement contracts. Since some legal systems already granted such power to arbitral tribunals, unification of rules on this power was considered desirable. It was also felt that, once rules on the power of arbitral tribunals to adapt and supplement contracts had been internationally agreed in a model law, such rules would be more acceptable to States which had no provisions on or did not allow adaptation and supplementation of contracts in the framework of arbitration.

"20. However, after extensive discussion, the view prevailed that adaptation and supplementation of contracts should not be dealt with in the model law. It was pointed out that there was no need for regulating this question in the model law since many legal systems already provided, outside the domain of arbitration, mechanisms for third party assistance in adapting and supplementing contracts. Also, there were great difficulties in unifying arbitral procedures on adaptation and supplementation of contracts.

"21. It was further noted that in adaptation and supplementation of contracts it was difficult to separate questions pertaining to procedural law and questions pertaining to substantive law and that, therefore, the model law, as a system of procedural rules, should not contain rules which may touch upon substantive rights of the parties. This difficulty in separating procedural and substantive questions would cause problems in interpretation of such rules. However, while recognizing this difficulty, it was noted by others that it should

<sup>68</sup>*Ibid.*, p. 8.

and could be made clear in the model law that only procedural aspects were regulated without regulating substantive conditions for adapting or supplementing a contract.

"22. In regard of the practical effects of a rule on adaptation and supplementation of contracts it was also observed that in international trade suppliers of equipment and large industrial works were often economically stronger than buyers and that procedures for adaptation and supplementation of contracts might be used to the advantage of suppliers.

"23. There was general agreement that the discussion in the Working Group was useful because it revealed the complexity of problems relating to adaptation and supplementation of contracts and possible solutions to these problems. This might prompt national legislators to adopt rules on adaptation and supplementation of contracts or improve existing rules taking into account the needs of modern international trade. Once national rules in this field and practice on the basis of such rules would be more developed, a harmonization might be achieved more easily."<sup>69</sup>

## VI. Code of ethics for arbitrators in international commercial arbitration

### *International Bar Association*

66. A draft of a code of ethics for arbitrators was discussed at the Seventh Conference of the International Bar Association held in Singapore from 30 September to 4 October 1985.<sup>70</sup> On the basis of the discussions at that Conference, a new draft text was drawn up for consideration by a working party established by a decision of the Singapore Conference.<sup>71</sup> It is expected that a draft text to be prepared by the working party will be discussed at the next conference of the International Bar Association, which is to be held in New York in September 1986.

67. The proposal to discuss such a code was prompted by the fact that the duty of the arbitrators to maintain the attitude of independence and impartiality was prominently reflected in important international arbitration rules, such as the UNCITRAL Arbitration Rules, the Arbitration Rules of the International Centre for Settlement of Investment Disputes, the Rules of Conciliation and Arbitration of the International Chamber of Commerce, or the Rules of the London Court of International Arbitration, and that, nevertheless, none of those rules

provided definitions of the concept of impartiality and independence.<sup>72</sup>

68. A related consideration was that there existed no internationally agreed standards or guidelines, and that, as a result, the arbitrators, parties and courts involved in international commercial arbitration were referred to national criteria as to what was to be considered proper conduct in such arbitration. Those national criteria, however, might not provide coherent guidance in an international case inasmuch as they might be based on case law arising from isolated instances or might be influenced by concepts which were not appropriate for general application.<sup>73</sup>

69. The purpose of the code would be to establish the manner in which the abstract qualities required of the arbitrators, namely impartiality, independence, competence, diligence and discreetness, may be assessed in practice. For that purpose, the code would deal in detail, for example, with the following issues:

(a) The fundamental duty of the arbitrators to proceed diligently and efficiently to provide the parties with a just and effective resolution of their disputes, and their duty to be and remain free from bias;

(b) The duties of a prospective arbitrator when accepting the appointment, in particular as regards the question whether he is able to discharge his duties without bias, whether he is competent to determine the issues in dispute, whether he is familiar with the procedure to be applied and has an adequate knowledge of the language of the arbitration, and whether he is able to give to the arbitration the time and attention which the parties are reasonably entitled to expect;

(c) The considerations relating to actual or to apparent bias, and in this context the code would deal with the situations that may give rise to the appearance of bias, including current and past business relationships between an arbitrator and a party or a potentially important witness, or certain social or professional relationships between those persons, or any previously expressed opinion of an arbitrator on a question which may be relevant to the dispute;

(d) Facts or circumstances that should be disclosed by a prospective or appointed arbitrator, e.g. past or present relationships between an arbitrator and a party, the extent of any prior knowledge an arbitrator

<sup>72</sup>J. M. H. Hunter and J. Paulsson, "A code of ethics for arbitrators in international commercial arbitration?", *International Business Lawyer*, April 1985, p. 153.

<sup>73</sup>With respect to a need for a set of internationally acceptable guidelines for arbitrators it was noted that, in the domestic context, there was one such set of guidelines already in existence, namely the *1977 Code of Ethics for Arbitrators in Commercial Disputes* prepared jointly by the American Arbitration Association and the American Bar Association. However, it was noted that, while the Code contained many features that were also useful and appropriate for international arbitration, it was developed in reaction to a number of judicial decisions that were applicable solely in the United States of America (Hunter and Paulsson, *loc. cit.*).

<sup>69</sup>Report of the Working Group on International Contract Practices on the work of its sixth session (A/CN.9/245), paras. 19-23.

<sup>70</sup>"Code of Ethics for Arbitrators", discussion draft, International Bar Association, sect. on Business Law, Committee D - Procedures for Settling Disputes, Singapore conference. The draft text, which was distributed to the participants of the Conference, has not been published.

<sup>71</sup>International Bar Association, "Code of ethics for international arbitrators", unpublished.

may have of the dispute, the nature of any previous relationship with any fellow arbitrator, including prior joint service as an arbitrator, the extent of any prior commitments which may interfere with the discharge of his duties as an arbitrator; other issues are the addressees and form of disclosure, and a deemed waiver as a result of a failure by a party to make objection to an arbitrator in relation to matters disclosed prior to participation of that party in a further stage of the proceedings;

(e) Communications of the arbitrators with the parties, including the question to what extent it is proper for an arbitrator to be in contact with only one party, or the question how an arbitrator should react if he learns of an improper communication between another arbitrator and a party; and in this connection the draft code raises the question whether a distinction should be made between an arbitrator appointed unilaterally by a party and an arbitrator appointed by both parties or by a third person or institution;

(f) Discussions between the arbitrators and the parties regarding fees and expenses of the arbitrators;

(g) The duty of the arbitrators to devote such time and attention to the arbitration as the parties may reasonably require and their duty to conduct the arbitration in such a manner that costs do not rise to an unreasonable proportion of the interests at stake;

(h) Restrictions regarding the discussions between an arbitrator and a party of a settlement proposal and consequences of such a discussion, and the position of the arbitral tribunal as a whole or of the presiding arbitrator regarding settlement proposals;

(i) The right of a dissenting arbitrator to make known to the parties his dissent and the reasons therefor, or his right to disclose any fundamental procedural irregularity or fraud to the parties, and the relation of these rights to the duty of the arbitrator to avoid a breach of the confidentiality of the deliberations of the arbitral tribunal.

70. As to the legal nature of the code, the introductory note mentions that the code could not be directly binding either on arbitrators or on the parties, unless the code was adopted by agreement. Whilst the International Bar Association hopes that arbitral institutions would take it into account when considering challenges to arbitrators, it has emphasized that the code would not be intended to create grounds for the setting aside of awards by national courts.<sup>74</sup> A further position taken in this regard is that international arbitrators should in principle be granted immunity from suit under national laws, except in extreme cases of wilful or reckless disregard of their legal obligations. Accordingly, the International Bar Association wishes to make it clear that it would not be the intention of the code to create opportunities for aggrieved parties to sue international arbitrators in national courts.

<sup>74</sup>See introductory note to International Bar Association, "Code of ethics for international arbitrators".

The normal sanction for breach of an ethical duty should be removal from office, with consequent loss of entitlement to remuneration.<sup>75</sup>

71. In this context, the Commission may wish to recall that the idea of preparing a code of ethics was mentioned during the early discussion of possible features of a model law on international commercial arbitration. In conjunction with the decision not to deal with questions of liability of arbitrators for any misconduct or error in arbitral proceedings, the agreement of the Working Group on International Contract Practices was not to attempt the preparation of a code of ethics for arbitrators.<sup>76</sup>

## CONCLUSIONS

72. The Commission, in addition to taking note of this report, may wish to consider whether any of the issues of arbitration presented herein warrant further examination. If so, it may request the secretariat to submit to a future session a study which may be prepared in consultation with the organization whose text or draft text the Commission wished to examine more closely. Such a study would present the complete text of any selected rules, guide, guidelines, code or clause, together with detailed comments by the secretariat on that text. It could further include general considerations concerning the desirability and feasibility of efforts on a global level and some suggestions as to any possible future course of action of the Commission.

73. In this respect, various approaches and options might be studied depending on the nature of the chosen issue and the orientation of the organization or the text concerned. For example, if the I.B.A. Rules of Evidence were to be selected by the Commission, the secretariat could include comments on their universal applicability and acceptability so as to assist the Commission in determining later whether, for instance, to recommend their use, or to envisage the preparation of an amended text, or to formulate similar supplementary rules specifically geared to the UNCITRAL Arbitration Rules.

74. The last mentioned possibility would probably feature among the more viable options in the area of multi-party arbitration, if the Commission were to select that area for closer examination. Any study, based on the draft texts prepared by the ICC, could thus include, in its considerations on the desirability and feasibility of a guide or a model clause, the suggestion to tailor such a text to the UNCITRAL Arbitration Rules, including the functions of an appointing authority acting under the Rules. Another approach worthy of study could be to envisage a text without any link to a given set of

<sup>75</sup>*Ibid.*

<sup>76</sup>Report of the Working Group on International Contract Practices on the work of its third session (A/CN.9/216), para. 51.



arbitration rules. At any rate, it seems clear that a possible later involvement of the Commission would aim at a text which had a global scope of application and was not tied to one particular arbitral institution.

75. Further points to be included in a study might relate to the level of statutory law. For example, the secretariat could prepare a survey of national laws on such questions

as court involvement in consolidating arbitral proceedings or in deciding certain issues (e.g. appointment of arbitrator) left open by parties adhering to a basic multi-party arrangement. The secretariat might also be requested to monitor legal developments in this area, and possibly in the area of adaptation and supplementation of contracts, and to suggest at an appropriate time consideration of a harmonization effort by way of model provisions of law.

## V. AUTOMATIC DATA PROCESSING

### Legal implications of automatic data processing: report of the Secretary-General (A/CN.9/279)

[Original: English]

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## INTRODUCTION

1. The Commission at its seventeenth session in 1984 decided to place the subject of the legal implications of automatic data processing to the flow of international trade on its programme of work as a priority item.<sup>1</sup> It was also decided that a decision would be made at a subsequent session whether to refer the subject to a Working Group for the purpose of identifying areas where solutions or the establishment of an international common understanding would be desirable. This report is submitted to the Commission pursuant to that decision.

2. The report discusses in chapter I the activities of organizations engaging in work relevant to the legal implications of automatic data processing to the flow of international trade, including the work of the Commission itself. In chapter II a short analytical summary is presented of the topics on which work has been undertaken and suggestions are made as to future actions the Commission may wish to take in this field.

### I. International organizations active in the field

#### A. United Nations Commission on International Trade Law (UNCITRAL)

3. Without awaiting a decision whether to refer the subject of the legal implications of automatic data processing to a Working Group, the Commission has explored the implications of the new technology in several respects and has taken the new methods of communication and documentation into account in its other work.

##### 1. Legal value of computer records

4. At its eighteenth session in 1985 the Commission had before it a report by the secretariat on the legal value of computer records (A/CN.9/265). As part of the preparation for the report, the secretariat had prepared a questionnaire on the use of computer-readable data as evidence in court proceedings. At the same time and in co-operation with the secretariat of the Commission, the Customs Co-operation Council prepared a questionnaire on the acceptability to customs authorities of a goods declaration in computer-readable form and the subsequent use of such a declaration in court proceedings. The information contained in the replies to both questionnaires was used in the preparation of the report.

5. The report came to the conclusion that on a global level there were fewer problems in the use of data stored in computers as evidence in litigation than might have been expected. Almost all of the countries that replied to the questionnaire appeared to have legal rules which were

at least adequate to permit the use of computer records as evidence and to permit the court to make the evaluation necessary to determine the proper weight to be given to the data or document.

6. The report noted that a more serious legal obstacle to the use of computers and computer-to-computer telecommunications in international trade arose out of requirements that documents be signed or that documents be in paper-based form.

7. After discussion of the report the Commission adopted the following recommendation:

"The United Nations Commission on International Trade Law

"*Noting* that the use of automatic data processing (ADP) is about to become firmly established throughout the world in many phases of domestic and international trade as well as in administrative services,

"*Noting also* that legal rules based upon pre-ADP paper-based means of documenting international trade may create an obstacle to such use of ADP in that they lead to legal insecurity or impede the efficient use of ADP where its use is otherwise justified,

"*Noting further* with appreciation the efforts of the Council of Europe, the Customs Co-operation Council and the United Nations Economic Commission for Europe to overcome obstacles to the use of ADP in international trade arising out of these legal rules,

"*Considering* at the same time that there is no need for a unification of the rules of evidence regarding the use of computer records in international trade, in view of the experience showing that substantial differences in the rules of evidence as they apply to the paper-based system of documentation have caused so far no noticeable harm to the development of international trade,

"*Considering also* that the developments in the use of ADP are creating a desirability in a number of legal systems for and adaptation of existing legal rules to these developments, having due regard, however, to the need to encourage the employment of such ADP means that would provide the same or greater reliability as paper-based documentation,

"(a) *Recommends* to Governments:

(i) to review the legal rules affecting the use of computer records as evidence in litigation in order to eliminate unnecessary obstacles to their admission, to be assured that the rules are consistent with developments in technology, and to provide appropriate means for a court to evaluate the credibility of the data contained in those records;

(ii) to review legal requirements that certain trade transactions or trade related documents be in writing, whether the written form is a condition to the enforceability or to the validity of the transaction or document, with a view

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its seventeenth session, *Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 17 (A/39/17)*, para. 136.

to permitting, where appropriate, the transaction or document to be recorded and transmitted in computer-readable form;

(iii) to review legal requirements of a handwritten signature or other paper-based method of authentication on trade related documents with a view to permitting, where appropriate, the use of electronic means of authentication;

(iv) to review legal requirements that documents for submission to governments be in writing and manually signed with a view to permitting, where appropriate, such documents to be submitted in computer-readable form to those administrative services which have acquired the necessary equipment and established the necessary procedures;

“(b) *Recommends* to international organizations elaborating legal texts related to trade to take account of the present Recommendation in adopting such texts and, where appropriate, to consider modifying existing legal texts in line with the present Recommendation.”<sup>2</sup>

## 2. *Electronic funds transfers*

8. At its fifteenth session in 1982, on the basis of a report of the Secretary-General (A/CN.9/221), the Commission decided to prepare a legal guide on electronic funds transfers and requested the secretariat to begin its preparation in co-operation with the UNCITRAL Study Group on International Payments.<sup>3</sup> The draft chapters of the legal guide were before the Commission at its seventeenth and eighteenth sessions in 1984 and 1985.

9. At its eighteenth session, the Commission requested the Secretary-General to send the draft legal guide on electronic funds transfers to Governments and interested international organizations for comment.<sup>4</sup> It also requested the secretariat, in co-operation with the UNCITRAL Study Group on International Payments, to revise the draft in the light of the comments received for submission to the nineteenth session of the Commission in 1986 for consideration and possible adoption. The report of the Secretary-General to the nineteenth session contains proposed modifications to the draft based on the comments received. The report recommends that:

(a) The Commission adopt the legal guide on electronic funds transfers and request that it be published in an appropriate manner; and that

(b) The Commission decide to prepare model rules leading to the harmonization of the law governing domestic as well as international funds transfers (A/CN.9/277).

<sup>2</sup>Report of the United Nations Commission on International Trade Law on the work of its eighteenth session, *Official Records of the General Assembly, Fortieth Session, Supplement No. 17 (A/40/17)*, para. 360.

<sup>3</sup>Report of the United Nations Commission on International Trade Law on the work of its fifteenth session, *Official Records of the General Assembly, Thirty-seventh Session, Supplement No. 17 (A/37/17)*, para. 73.

<sup>4</sup>Report of the United Nations Commission on International Trade Law on the work of its eighteenth session, *Official Records of the General Assembly, Fortieth Session, Supplement No. 17 (A/40/17)*, para. 342.

## 3. *What constitutes “signature”*

10. Article 14(3) of the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg Rules) provides that

“The signature on the bill of lading may be in handwriting, printed in facsimile, perforated, stamped, in symbols, or made by any other mechanical or electronic means, if not inconsistent with the law of the country where the bill of lading is issued.”<sup>5</sup>

11. The model of the Hamburg Rules provision on signature is followed in article 5 of the United Nations Convention on International Multimodal Transport of Goods prepared by UNCTAD<sup>6</sup>, in the new amendments to the IMO Convention on Facilitation of International Maritime Traffic (see para. 29) and in article 4(10) of the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/274) which will be before UNCITRAL at its current session. It is also followed in draft article 4(4) of the draft articles of uniform rules on the liability of operators of transport terminals, as proposed by the UNCITRAL Working Group on International Contract Practices at its ninth session held in New York from 6 to 17 January 1986 (A/CN.9/275, para. 58). However, since no decision has yet been taken by the Working Group on whether the uniform rules should be cast in the form of a model law or a convention, the words “if not inconsistent with the law of the country where the [document] is issued” have not been included.

## 4. *What constitutes “writing”, “document”, “notice”*

12. Article 7(2) of the UNCITRAL Model Law on International Commercial Arbitration, adopted by the Commission at its eighteenth session in 1985, provides that an arbitration agreement is in writing if it is contained in a document signed by the parties or in an exchange of letters, telex, telegrams or of “other means of telecommunication which provide a record of the agreement, ...”.<sup>7</sup>

13. The Working Group on International Contract Practices has used a simplified version of the formulation used in the Model Law in its version of article 4(3) of the draft articles on uniform rules on the liability of operators of transport terminals as follows:

“The document referred to in subparagraph (b) of paragraph (1) of this article may be issued in any form which preserves a record of the information contained therein” (A/CN.9/275, para. 58).

14. The comment to the draft article as previously submitted by the secretariat points out that this formulation would cover a document in paper-based form, a

<sup>5</sup>A/Conf.89/13, annex I.

<sup>6</sup>TD/MT/Conf.16

<sup>7</sup>Report of the United Nations Commission on International Trade Law on the work of its eighteenth session, *Official Records of the General Assembly, Fortieth session, Supplement No. 17 (A/40/17)*, annex I.

document created by teletransmission of data to the computer of the customer, as well as a document in the form of data recorded on a micro-circuit card accompanying the goods (A/CN.9/WG.II/WP.56).

15. Article 11(7)(a) of the same draft articles as submitted by the secretariat and considered by the Working Group provides that

“Notice required to be given by this article may be given in any form which provides a record of the information contained therein” (A/CN.9/WG.II/WP.56).

## B. Work related to trade facilitation

### 1. Economic Commission for Europe

#### (a) Working Party on Facilitation of International Trade Procedures

16. Although the Working Party is institutionally a sub-organ of the Economic Commission for Europe, it has become the effective central organ for discussing trade facilitation policies and activities on a global basis. The Working Party began its activities in 1961 under another name to develop a standard layout key, now known as the United Nations Layout Key, which could be used to produce a range of fully-aligned international trade, transport and official documents. Following the development of the Layout Key, the Working Party turned its attention to the simplification of international trade procedures themselves. By the 1970's the Working Party was promoting the replacement of traditional paper-based documents by methods allowing a more rapid exchange of information through telex and more recently through computerized interchange of trade data. Its primary activities in this regard have been to foster the development of a Trade Data Elements Directory, a Trade Data Interchange Directory and the registration of technical application protocols.

17. As the Working Party became interested in facilitating the use of automatic data processing in international trade, it became concerned over legal impediments to that use. As a result, it has the subject of legal aspects of trade data interchange as a regular item on its agenda. The primary role of the Working Party in this area has been to identify legal problems and to urge other competent organizations to take the appropriate actions. In particular it has recommended that:

(a) Governments and international organizations study the possibility of permitting authentication of documents used in international trade by means other than signature so that information contained in the documents may be prepared and transmitted by electronic or other automatic means of data transfer;<sup>8</sup>

(b) Facilities should be developed for the preparation of bills of lading in the country of destination, using

automatic data processing and transmission so as to avoid delays and demurrage caused by the need to send documents by mail;<sup>9</sup>

(c) Montreal Protocol No. 4 of 1975 to the Warsaw Convention should be brought into effect as soon as possible through ratification by Governments, so that the air waybill requirement may be abolished, where desirable;<sup>10</sup> and that

(d) Customs authorities in importing countries should implement the 16 June 1981 recommendation of the Customs Co-operation Council concerning the transmission and authentication of goods declarations which are processed by computer.<sup>11</sup>

18. At its sixteenth session in September 1982, the Working Party considered a report which identified the main problems of a legal character regarding automatic data processing encountered in the work of the Working Party and suggested that action be taken in respect of those problems in the competent international forums (TRADE/WP.4/R.185/Rev.1). The conclusion reached in the document, and supported by the Working Party, was

“that there is an urgent need for international action to establish rules regarding legal acceptance of trade data transmitted by telecommunications. Since this is essentially a problem of international trade law, the United Nations Commission on International Trade Law (UNCITRAL) would appear to be the central forum” (para. 4).

The document was reprinted as an annex to document A/CN.9/238 and submitted to UNCITRAL at its sixteenth session in 1983. The decision of the Commission to place the subject of the legal implications of automatic data processing to the flow of international trade on its agenda as a priority item was a direct consequence of that report.

19. At its twenty-first session in March 1985 the Working Party “invited the UNCITRAL, CCC, ICC, OECD and other interested organizations to participate actively in the development of uniform rules for communication agreements” (UNCA) (TRADE/WP.4/151, para. 8). The draft UNCA, which was prepared by the Nordic Legal Committee in the context of the activities of the Working Party, has been submitted to ICC for further action (see paras. 59–60).

#### (b) Inland Transport Committee

20. The Group of Experts on Customs Questions has had referred to it a proposal aimed at the introduction of a special micro-circuit card for the international transport of goods. The note prepared by the secretariat to present the proposal to the fifty-fifth session of the Group of

<sup>8</sup>Recommendation No. 18, facilitation measure 7.3, ECE/TRADE/141.

<sup>10</sup>*Ibid.*, facilitation measure 7.5.

<sup>11</sup>*Ibid.*, facilitation measure 9.4. See also facilitation measures 9.5 and 9.8. The recommendation of the Customs Co-operation Council is discussed in para. 39, below.

<sup>8</sup>Recommendation No. 14, TRADE/WP.4/INF.63.

Experts held at Geneva from 7 to 11 October 1985 concentrated on the technical considerations (Trans./GE.30/R.183). However, it was recognized in the note that there would be legal and administrative considerations before the card could be used to its fullest advantage.

21. The proposal represents a plan to provide a transition from the existing international paper-based TIR carnet system to a system using the micro-circuit card as the access device to a dedicated telematics network for customs transit. The TIR system is an international system of customs transit for road transport, the application of which has gradually spread throughout Europe, the Middle East and North Africa. The system is based on a procedure which has two major elements:

(a) A unique TIR carnet is used for each trip. This carnet includes two forms for each country whose territory has to be crossed (including the country of departure and the country of destination). These forms provide the identification of the vehicle, an indication of the travel itinerary and a description of the goods. They constitute a uniform customs transit document, one copy being used when entering a country and the other when leaving a country;

(b) The TIR carnet is also evidence of the guarantee given to each customs administration by the guarantee chain. To this end, the carnet is authenticated to the guarantee chain which sells the carnets and arranges for its follow-up. All carnets, with counterfoils duly stamped by customs officials, have to be returned to the guaranteeing association.

22. The note by the secretariat points out that micro-circuit cards could not be substituted for paper documents without reaching an international agreement. Such an agreement would initially be given for a limited time in order to test the system. Official paper documents would be used in parallel with the cards during the test period. The ultimate changes to be considered to the TIR Convention and other relevant legal texts would depend upon the success of the tests.

23. After extensive discussion by the Group of Experts on the technical features of the use of a micro-circuit card for customs purposes, and especially in the context of the TIR system, it was decided that the secretariat would present a feasibility study of the proposal to the Group at a subsequent session (TRANS/GE.30/47).

## 2. International Maritime Organization (IMO)

24. The Convention on Facilitation of International Maritime Traffic (London, 9 April 1965) has as its purpose the facilitation of "maritime traffic by simplifying and reducing to a minimum the formalities, documentary requirements and procedures on the arrival, stay and departure of ships engaged in international voyages". As of 1 October 1984, there were 53 Contracting States to the Convention. Implementing standards and recommended practices are contained in an annex to the

Convention, which can be amended through a simpler and faster procedure than can the Convention itself. Since 1977 several amendments to the annex, or to the Convention, have been adopted or proposed in order to facilitate the use of automatic data processing in the preparation and submission of the documentation required for the entry and exit of ships from ports.

25. In November 1977, standard 2.15 was amended by the Conference of Contracting Governments by adding a new sentence at the end of the standard as follows:

"Documents produced by electronic or other automatic data processing techniques, in legible and understandable form, shall be accepted."

26. Although the 1977 amendment to standard 2.15 seemed to refer only to paper-based documents produced by automatic data processing, by 1979 maritime facilitation authorities were anxious to permit the use of non-paper media for documentation. In this regard, in operative paragraph 1 of its resolution A.452 (XI) of 15 November 1979, the IMO Assembly:

"1. *Recommends* that, in applying Standard 2.15:

(a) the possibility of accepting, for certain documents, non-paper media, subject to prior agreement (including the method of authentication) between the parties concerned, should be explored;

(b) the presentation of data in any automatic data processing (ADP output) document should follow the layout of the Standardized Model Forms;

(c) any substantial deviation from that layout should require prior agreement between the parties concerned."

27. Earlier in 1979 the Facilitation Committee had already considered proposals to amend the Convention and its annex to remove provisions which impeded the use of ADP techniques.<sup>12</sup> At its third session (17 September 1979) the intersessional working group agreed that, to remove any impression that the Convention was documentary-based, the recurrent phrase "formalities, documentary requirements and procedures", which appears in the preamble and articles III, IV, VIII and XIII of the Convention, should be amended to read: "formalities, information requirements and procedures". An alternative proposal, made at a subsequent meeting, was that the definition of "document", which had originally been adopted by ECE and which was referred to in Assembly resolution A.452 (XI), i.e. "document-data carrier with data entries", be inserted into the annex to the Convention. It was thought, however, that the term "data carrier" should also be clarified by including in the annex the ECE definition: "data carrier—medium designed to carry records of data entries".

<sup>12</sup>The following history of the work in the Facilitation Committee is taken from section 5 of the report of its fifteenth session, held from 1 to 5 October 1984 (FAL 15/15).

28. At its fifteenth session in 1984, the Facilitation Committee decided that, in order to make it unnecessary to amend the Convention, it would adopt a "harmonized interpretation" of the term "documentary requirements", which reads as follows:

"The term 'documentary requirements' appearing in the preamble and in articles III, IV, VIII and XIII of the Convention, shall be understood to mean such requirements whether the information required is conveyed on paper or on any other media that can be accepted by the party concerned" (FAL 15/15, annex 3).

The IMO Council, at its fifty-third session, noted the harmonized interpretation agreed to by the Committee.

29. The Committee also unanimously agreed on the text of a number of amendments to the annex to the Convention relevant to automatic data processing (FAL 15/15, annex 2). These amendments would:

(a) Insert in the annex the definitions of "document" and "data carrier" already discussed above;

(b) Add to those standards and recommended practices which call for the public authorities to accept various documents that are signed and dated by a specified person the possibility for the document to be "authenticated in a manner acceptable to the public authority concerned";

(c) Add a new recommended practice that public authorities should take into account the facilitation implications which may result from the introduction of automatic data processing and transmission techniques, and should consider these in collaboration with shipowners and all other interested parties;

(d) Amend standard 2.15 to read:

"Public authorities shall accept information conveyed by an legible and understandable medium, including documents handwritten in ink or indelible pencil or produced by automatic data processing techniques."

(e) Add a new standard 2.15.1 to read:

"Public authorities shall accept a signature, when required, in handwriting, in facsimile, perforated, stamped, in symbols, or made by any other mechanical or electronic means, if such acceptance is not inconsistent with national laws. The authentication of information submitted on non-paper media shall be in a manner acceptable to the public authority concerned".

30. A diplomatic Conference was held from 5 to 7 March 1986, during which those amendments to the annex to the Convention were adopted. Amendments adopted by the Conference enter into force six months after the date on which the Secretary-General notifies the Contracting States of their adoption by the Conference. The Secretary-General notified the Contracting Govern-

ments of the actions of the Conference on 1 April 1986, as a result of which the amendments to the annex will enter into force on 1 October 1986.

### 3. *International Civil Aviation Organization (ICAO)*

31. The basic documentation requirements for air carriage are found in the Warsaw Convention, and the Warsaw Convention as amended by the Hague Protocol. The Convention and the Protocol require the issue of passenger tickets, baggage claim receipts and air waybills with specific information printed on them. In respect of passenger tickets (documents of carriage) and baggage checks the Guatemala Protocol, which is not in force, provides in its articles II and III:

"Any other means which would preserve a record of the information indicated in (a) and (b) of the foregoing paragraph may be substituted for the delivery of the document referred to in that paragraph."

32. In respect of the carriage of goods, Montreal Additional Protocol No. 4, which is also not in force, provides:

"2. Any other means which would preserve a record of the carriage to be performed may, with the consent of the consignor, be substituted for the delivery of an air waybill. If such other means are used, the carrier shall, if so requested by the consignor, deliver to the consignor a receipt for the cargo permitting identification of the consignment and access to the information contained in the record preserved by such other means.

"3. The impossibility of using, at points of transit and destination, the other means which would preserve the record of the carriage referred to in paragraph 2 of this Article does not entitle the carrier to refuse to accept the cargo for carriage."

33. In view of the fact that neither the Guatemala Protocol nor Montreal Protocol No. 4 are in force, the facilitation provisions in regard to air traffic do not deal extensively with the possibilities for use of ADP. Standard No. 4.4 of annex 9, "Facilitation", to the Convention on International Civil Aviation (Chicago, 1944) provides:

"Contracting States shall accept commercial documents required for the clearance of air cargo, when produced by electronic data-processing techniques, provided they are in legible and understandable form and that they contain the required information."

### 4. *International Rail Transport Committee (CIT)*

34. CIT has taken the occasion of the entry into force of the Convention Concerning International Transport by Rail (COTIF) on 1 May 1985 to align the model rail consignment note more closely to the United Nations Layout Key. At the same time it has begun to study the legal conditions for a replacement of this document by an instrument using automatic data transmission.

35. A report submitted to the Governing Committee of CIT held at Sandefjord, Norway from 12 to 16 September 1985 pointed out that COTIF, appendix B (CIM), article 8(4)(g) permitted States, by agreement, or the railroad authorities, by supplementary agreements or by provisions in the published tariffs, to derogate from the documentary requirements of CIM so as to permit the transport of goods under the cover of the automatic transmission of data. Furthermore, CIM contained no requirement of a manual signature on the consignment note.

36. The report pointed out that the major concerns of a legal nature involved in the replacement of the consignment note by automatic transmission of data were:

- (a) The legal value of the computer records;
- (b) The necessity of a writing under the laws of some countries for the conclusion of a commercial transaction or to be able to prove the existence of the transaction;
- (c) The legal value of the authentication of a message by electronic means; and
- (d) The allocation of legal responsibility for errors or the loss or corruption of data in transmission.

The report concluded that studies should commence on the technical requirements for the replacement of the consignment note by automatic transmission of data in co-operation with other organizations interested in the question, and particularly user organizations and customs authorities. In the light of the evaluation of those studies, the examination of the legal questions might be undertaken, also in co-operation with the other interested organizations.

37. The Governing Committee accepted the recommendations of the report.

##### 5. Customs Co-operation Council (CCC)

38. The Council has an active programme to encourage co-operation among customs authorities in the use of automatic data processing. Although much of this co-operation is at a technical level involving exchange of information and agreement on such matters as codes to represent standard data elements, the Council has also adopted several recommendations more directly applicable to the legal implications of the use of automatic data processing.

39. On 16 June 1981 the Council adopted a recommendation concerning the transmission and authentication of goods declarations which are processed by computer. The Council, after noting that it is technically possible to authenticate computer-processed goods declarations by the use of various methods including passwords or code words and identification cards and that the general adoption of electronic or other automatic means of data transfer might be precluded unless changes were made in

existing national laws and international conventions and in current commercial practice concerning signature,

*“Recommends* that States, whether or not Members of the Council, and Customs or Economic Unions should:

“1. Allow, under conditions to be laid down by the Customs authorities, declarants to use electronic or other automatic means to transmit to the Customs Goods declarations for automatic processing. Such declarations may be transmitted either by direct link between the data processing systems of the Customs and those of declarants or on magnetic or other ADP media;

“2. Accept, under conditions to be laid down by the Customs authorities, that Goods declarations which are transmitted by electronic or other automatic means to Customs be authenticated other than by handwritten signature.”

40. Although the 1981 recommendation anticipated the gradual elimination of paper-based goods declarations, for an extended period of time many declarants who used computers in their business operations could use them more efficiently to produce paper-based goods declarations if they had greater freedom in the format for presentation of the data. Therefore, on 16 June 1982 the Council adopted a recommendation whose operative paragraph reads as follows:

*“Recommends* that States, whether or not Members of the Council, and Customs or Economic Unions should authorize declarants, under conditions to be laid down by the Customs or other competent authorities, to produce their Goods declarations by means of computer or other automatic printers, on preprinted forms or on plain paper. Such authorization may be made subject, in particular, to the condition that declarations produced in this manner substantially conform to the official model specified by the Customs or other competent authorities.”

41. Following its examination of the report of the Working Party on Facilitation of International Trade Procedures on legal problems in automatic data processing referred to in paragraph 18, above, the Computer Working Party of the Council initiated a study of the extent to which goods declarations could be prepared by computer, as recommended in the 1982 resolution, or submitted directly in computer readable form, as recommended in the 1981 resolution, and the extent to which computer records of goods declarations could be used as evidence in litigation. A questionnaire was prepared in collaboration with the UNCITRAL secretariat and replies were received from Customs Authorities of 11 States.

42. On the basis of the study a draft resolution has been prepared for presentation to the Council in June 1986 which, because of the importance of customs requirements to the flow of international trade, is reproduced in full as follows:



**"DRAFT RESOLUTION OF THE CUSTOMS CO-OPERATION COUNCIL CONCERNING THE USE OF COMPUTER-READABLE DATA AS EVIDENCE IN COURT PROCEEDINGS**

*"The Customs Co-operation Council,*

*"Anxious to:*

- facilitate the operation of current Customs ADP systems and the development of planned systems,
- facilitate the greatest possible use of ADP techniques for the transmission of Goods declarations to the Customs by electronic or other automatic means (e.g. magnetic tapes, flexible disks, teletransmission, etc.) and the subsequent acceptability of such data as evidence in court proceedings,
- see that participants in international trade can be provided with some degree of legal certainty insofar as the use of computer techniques and the admissibility in court of computer-readable data are concerned,
- contribute to the creation of greater interest in the development of a legal framework for the acceptance of international trade data transmitted by electronic or other automatic means as evidence in court proceedings,

*"Noting that:*

- existing legislation often refers exclusively to traditional paper documents,
- the existing legislation of many States requires a handwritten signature,
- few court decisions exist to date concerning the admissibility of computer-readable data as evidence,

*"Having regard to:*

- the Council's Recommendation dated 16 June 1981 concerning the transmission and authentication of Goods declarations which are processed by computer,
- the 'Recommendation on the facilitation of identified legal problems in import clearance procedures', adopted in March 1979 by the Working Party on Facilitation of International Trade Procedures of the Economic Commission for Europe,
- the 'Recommendation on the authentication of trade documents by means other than signature', also adopted in March 1979 by the above-mentioned Working Party,
- the Recommendation on the legal value of computer records, adopted in June 1985 by the United Nations Commission on International Trade Law (UNCITRAL),

*"Considering that:*

- the general adoption of electronic or other automatic means of data transfer might be precluded unless changes are made in existing national laws and international Conventions and in current commercial practice concerning signature,

- insofar as the acceptance and implementation of the above-mentioned CCC Recommendation is concerned, it is essential that teletransmitted information and other computer-readable data can be used in any subsequent court proceedings,
- the need for a traditional signature necessitates the production of traditional paper documents,
- ADP techniques make it possible to authenticate Goods declarations otherwise than by handwritten signatures,
- alternative authentication methods include, *inter alia*, the issue by Customs to authorized users only of a special identification card, cassette or badge, etc. containing magnetically recorded information unique to the user including a user password or code which the user must insert into a card, cassette or badge reader prior to transmitting Goods declaration data to a Customs ADP system,
- the need to change and modernize legislation in order to ensure the acceptability of teletransmitted data as evidence in court proceedings is of prime importance in order to eliminate the need to complete and sign paper Goods declarations and supporting documents containing data which are also teletransmitted,
- the elimination of such paper documents would constitute a direct saving and a trade facilitation measure and would enhance the maximum use of ADP techniques and the introduction of paperless transactions,
- it is desirable to remove from existing legislation provisions which obstruct the use of ADP techniques,

*"Expresses its full support for the review of legal requirements concerning documents and signature with a view to giving authentication of computer-readable data by means other than handwritten signature (for example, use of identification cards, badges, cassettes, etc., incorporating a user password or code) the same legal effect or status as a traditional handwritten signature,*

*"Suggests that in the review of legal requirements concerning documents and signature, due consideration should be given, inter alia, to the following principles:*

- both documentary and alternative information requirements and transmission methods should be explicitly provided for in legislation and in regulations,
- both handwritten and other paper-based signatures and alternative mechanical, electronic or other authentication methods should be explicitly provided for in legislation and in regulations,
- terms such as "document" should be defined in legislation and in regulations by using internationally acceptable definitions which take account of computer media (tapes, disks, microfilm, etc.),

"Urges States and Customs or Economic Unions to bring this Resolution to the attention of the competent authorities at the national and international levels" (Doc. 33.000, appendix I).

### C. Other work related to automatic data processing

#### 1. Council of Europe

##### (a) Data privacy

43. The Council of Europe opened to signature the Convention for the Protection of Individuals with Regard to Automatic Processing of Personal Data on 28 January 1981. The Convention is open to ratification by the member States of the Council of Europe as well as to accession by non-member States. The Convention entered into force on 1 October 1985, after ratification by France, Germany, Federal Republic of, Norway, Spain and Sweden. Moreover, the Convention has been signed by Austria, Belgium, Denmark, Greece, Iceland, Italy, Luxembourg, Portugal, Turkey and the United Kingdom of Great Britain and Northern Ireland. The first meeting of the consultative committee established under article 18 of the Convention will take place in June 1986.

44. In addition, the Committee of Ministers has adopted the following recommendations in respect of data privacy: (1) Recommendation No. R(81)1 on regulations for automated medical data banks, (2) Recommendation No. R(83)10 on the protection of personal data used for purposes of scientific research and statistics, (3) Recommendation No. R(85)20 on the protection of personal data used for purposes of direct marketing, and (4) Recommendation No. R(86)6 on the protection of personal data used for social security purposes. The Committee of Experts on Data Protection is currently examining the data protection problems posed by the employment sector and the police sector and has recently directed its attention to certain data-protection problems caused by the introduction and use of new technologies.

##### (b) Admissibility of recordings on computers as evidence

45. The Committee of Ministers adopted, on 11 December 1981, its Recommendation No. R(81)20, on the Harmonization of Laws relating to the requirement of written proof and to the admissibility of reproductions of documents and recordings on computers. According to the Rules appended to the Recommendation, each member State should "designate which books, documents and data may be recorded on computers" (art. 1(1)). These records, if made in conformity with the Rules, would be admitted as evidence in judicial proceedings and "be presumed to be a correct and accurate reproduction of the original document or recording of the information it relates to, unless the contrary is proven" (art. 2).

46. The conditions under which a computer recording must be made to conform to the Rules are found in articles 3 and 5 as follows:

#### "Article 3

"1. Reproductions or recordings made under the responsibility of the person referred to in Article 1 must conform to the following general rules. They must:

"a. correspond faithfully to the original document or the information to which the recording relates, as the case may be;

"b. be reproduced or recorded in a systematic way and without gaps;

"c. be made in accordance with the working instructions, laid down consistently with national law and preserved as long as the preservation of the reproductions or recordings;

"d. be preserved with care, in a systematic order, and be protected against any alteration.

"2. When a document which has been reproduced or has been used for a recording is destroyed, the following particulars must be preserved together with the recording and in the reproduction, if possible, or otherwise with it:

"a. the identity of the persons under whose responsibility the reproduction or recording has been made and of the person effecting it;

"b. the nature of the document;

"c. the place and date of the reproduction or recording;

"d. any defects observed during the reproduction or recording."

#### "Article 5

"1. The following rules shall apply to computer programmes:

"a. the programme write-up, files descriptions and programme instructions must be directly legible and kept carefully up to date under the responsibility of the person referred to in Article 1;

"b. the documents referred to in 'a' above must be preserved in a communicable form for so long a time as the recordings to which they relate.

"2. If, for whatever reason, the data recorded are transferred from one computer to another, the person referred to in Article 1 must establish that there is concordance.

"3. The following rules apply to computer systems generally:

"a. the system must contain the safeguards necessary in order to avoid any alteration of the recording;

"b. the system must also make it possible to reproduce at any moment the information recorded in a directly legible form."

## 2. Organization for Economic Co-operation and Development (OECD)

47. OECD has engaged in several studies of the economic effect of the new technology and has explored the major policy options available to its member States in this field in an attempt to co-ordinate the actions of the Governments. In this regard on 11 April 1985, the Governments of OECD member countries adopted a Declaration on Transborder Data Flows in which, *inter alia*, they declared their intention to "develop common approaches for dealing with issues related to transborder data flows and, when appropriate, develop harmonized solutions".

48. In December 1980, OECD adopted the Guidelines Governing the Protection of Privacy and Transborder Data Flow of Personal Data. Since that time OECD has retained an active interest in the implementation of the Guidelines and has served as a forum for the continuing discussions on the effect of national regulation of data transmission and telecommunications on transborder data flow.

49. The OECD Committee for Information, Computer and Communications Policy has commissioned a number of studies exploring legal issues arising out of the new technology. Two survey studies were published in 1983 under the title "An exploration of legal issues in information and communication technologies". At the Second OECD Symposium on Transborder Data Flows, held in London from 30 November to 2 December 1983, papers on legal issues were grouped under the headings "privacy protection and transborder data flows", "liability issues and transborder data flows" and "other legal aspects of transborder data flows".<sup>13</sup>

50. Other legal topics which have been the subject of discussion by the Committee include computer crime, copyright of computer software and conflict of laws and jurisdiction. In regard to this latter topic, it has been suggested that if the topic were to be addressed by OECD, the Hague Conference on Private International Law could be involved in the work (see paras. 53-55).

51. In 1983 the Committee on Financial Markets sponsored a study by Professor J. R. S. Revell, entitled "Banking and Electronic Funds Transfers", which considered several legal issues.

52. The Committee on Consumer Policy has established a Working Party on Consumers and Banking with the mandate to undertake an in-depth study on consumer policy issues arising from the development and introduction of electronic funds transfer systems. A questionnaire sent to member States enquires into a number of relevant legal issues.

<sup>13</sup>Transborder Data Flows; Proceedings of an OECD Conference held December 1983 (Amsterdam, North Holland, 1985).

## 3. Hague Conference on Private International Law

53. In June 1981 the Permanent Bureau of the Conference submitted a note to the Special Commission on "The protection of privacy and transborder flows of personal data" (Preliminary Document No. 1). The note indicated that the interest of the Permanent Bureau in the subject had been stimulated by receipt of the OECD "Recommendation concerning guidelines governing the protection of privacy and transborder flows of personal data" together with the explanatory memorandum. The explanatory memorandum showed that throughout the discussions of the OECD Group of Experts in preparation of the Guidelines, great attention had been paid to problems of conflict of laws and, above all, to questions as to which courts should have jurisdiction over specific issues in that field. The note from the Permanent Bureau briefly described the difficulties the Group of Experts had experienced in attempting to determine an appropriate connecting factor for the application of a single national law in the case of international computer networks where, because of dispersed locations and rapid movement of data, several connecting factors could occur in a complex manner.

54. The note concluded that, if anything were to be done in the field of conflict of laws, the Hague Conference would appear to be the organization best equipped to undertake the work. The Permanent Bureau did not at that time, however, suggest that the subject be put on the agenda for future work of the Conference, but only that it be given a free hand to discuss the matter with other organizations and to communicate the interest of the Conference to those organizations.

55. The matter was considered again at the fifteenth session of the Conference in October 1984 at which time the Conference invited "the Permanent Bureau to undertake exploratory studies on: ... conflicts of laws occasioned by transfrontier data flows, and to undertake this study in liaison with the international organizations concerned, in particular the United Nations Commission on International Trade Law (UNCITRAL)" (Doc. Trav. No. 1).

## 4. International Chamber of Commerce (ICC)

### (a) Policy statements on telecommunications and transborder data flows

56. The ICC has issued a number of policy statements on telecommunications and transborder data flows directed towards the business community.

### (b) Documentary credits

57. The 1983 revision of the Uniform Customs and Practice for Documentary Credits (ICC publication No. 400) recognizes the use of telecommunications and automatic data processing in two ways. Articles 12, 16(d) and 18 state rules governing the use of telecommunications between two banks when a credit is opened or amended

or when an issuing bank refuses documents. Article 22(c) provides the conditions under which banks will accept documents on the following terms:

“Unless otherwise stipulated in the credit, banks will accept as originals documents produced or appearing to have been produced:

- i. by reprographic systems;
- ii. by, or as the result of, automated or computerized systems,
- iii. as carbon copies,

if marked as originals, always provided that, where necessary, such documents appear to have been authenticated.”

58. Since article 22(c) would permit documents to be accepted as originals even though the data was teletransmitted to the location of the issuing bank and a paper-based document was produced by a computer system at that place, the provision could be considered to be a first step towards the adoption of rules for documentary credits based on documents in computer form.

(c) *Uniform rules for communication agreements (UNCA)*

59. ICC is undertaking the preparation of uniform rules for communication agreements, based upon a draft text prepared by the Nordic Legal Committee in the context of the work of the ECE Working Party on Facilitation of International Trade Procedures (Working Party).<sup>14</sup> As a result of the use of open communication systems between user groups of mixed disciplines, the institutional structure and explicit or implicit body of technical, operational and legal rules developed by closed-user groups will not be available. UNCA is intended to provide legal rules available for voluntary adoption by parties to international trade transactions who are using such open communication systems.

60. The first meeting of the Committee was held at ICC, Paris, on 16–17 January 1986 and was attended by representatives of the European Insurance Committee, Customs Co-operation Council, ICC, International Organisation for Standardisation, UNCTAD and the UNCITRAL secretariat (Document No. 374/3). The second meeting will be held on 6 May 1986.

### 5. *European Communities*

61. The Commission communication to the Council on a “Work programme for creating a common information market” (COM (85) 658, 29 November 1985), which was favourably received by the Council on 18 March 1986, identified a number of legal issues as requiring priority action. Issues that are already being studied include:

- (a) Access to information held by the public sector;

(b) Inconsistencies in legal rights and obligations applicable to different categories of information providers;

(c) Legal issues relating to telebanking and tele-shopping.

Results of these studies are expected by the end of the year. The contractors are the Centre de Recherches Informatique et Droit, Namur, Belgium, Gesellschaft für Mathematik und Datenverarbeitung mbH, Bonn, Federal Republic of Germany and Institute of Informatics and Law, Free University of Amsterdam, Netherlands.

62. A group of experts from all member States of the Community was established in May 1985 under the name of “Legal Observatory for the European Information Market” to advise the Commission of the European Communities on activities in the field of legal issues affecting the new technology information sector. In this connection an international conference on “Paperless Trading and the Law in the EEC” was held in Brussels on 17–18 March 1986 by the Comité Européen (European Committee) *Lex Informatica Mercatoriaque* (CELIM). A CELIM working group will be meeting later this year to prepare its conclusions for the attention of the European Commission and of any interested organisation.

63. A study is being prepared on copyright which will include discussion of software and database protection.

### 6. *International Maritime Committee (CMI)*

64. Following the recommendation by the CMI Colloquium on Bills of Lading held at Venice from 30 May to 1 June 1983 that “Uniform rules for incorporation in sea waybills should be prepared and their adoption encouraged”, a Sea Waybills Group was created to study the problem. The Sea Waybills Group reported to the conference of CMI held at Lisbon, from 19 to 25 May 1985, the following recommendation:

“The Sea Waybills Group having considered a number of potential problems flowing from the arrival of cargo at its destination before the arrival of the relevant negotiable bill of lading, and the use of non-negotiable documents, such as Sea Waybills, and new techniques such as electronic data processing or creation of a central bill of lading registry and recognizing the necessity of minimizing the uncertainties flowing from it;

“*Recommends:*

That the Executive Council appoint an International Sub-Committee to study the above mentioned questions and to find solutions thereto, possibly through uniform rules or an international convention, taking into account, among others, the development of a ‘paper-less’ system” (LIS/SWB-9).

The recommendation was adopted by the conference and the International Sub-Committee is in the process of formation.

<sup>14</sup>The draft UNCA is reproduced in ECE document TRADE/WP.4/300 and in ICC document No. 374/1.

## 7. *International Law Association (ILA)*

65. The Committee on International Monetary Law of ILA is preparing a draft model law on time of payment of a monetary obligation. The changes in banking procedures which have been caused by the use of computers and telecommunications have raised questions as to when the payment of the underlying monetary obligation between the banks' customers takes place as well as to when the funds transfer is final between the bank customers and the banks.

### II. Analytical summary

66. The relatively large number of projects undertaken to date can be grouped within a fairly small number of categories.

#### A. *Privacy*

67. The early concerns for the threat to personal privacy, the parallel concerns for loss of national sovereignty resulting from data processing of nationally generated data in computers located in other countries and the concern that differing national enactments would lead to a severe restriction on transnational data flow, all of which led to adoption of the OECD Privacy Guidelines and the Council of Europe Convention, have not subsided. The discussion over the implementation of these two texts, as well as of the national legislation adopted in a number of countries, can be expected to continue for some time as the constantly changing technology and changing uses for computers and telecommunications create new problems. The question of conflicting rules in different States remains a potentially serious problem, to be solved either by the further harmonization of substantive rules or by the adoption of rules on conflict of laws as is under consideration by the Hague Conference.

#### B. *Evidence*

68. The three organizations which have actively considered the legal value of computer records as evidence have taken different approaches to the problem depending on the orientation of their programme of work. The report of the UNCITRAL secretariat came to the conclusion that on a global level there were fewer problems in the use of data stored in computers as evidence than might have been expected. The report noted that a more serious obstacle to the use of computers and computer-to-computer telecommunications in international trade arose out of requirements that documents be signed or that documents be in paper-based form. On the basis of that report the Commission recommended that Governments review their legislation in order to eliminate unnecessary obstacles to the use of computers and computer-to-computer telecommunications in international trade. However, neither the report nor the Commission recommendation gave specific criteria to guide national authorities in that task.

69. Council of Europe Recommendation No. R(81)20 was designed to establish uniform criteria under which its member States could shorten or eliminate the period for the retention of written records. Since one means of eliminating the retention of written records is to transfer the data from written records to microfilm or to a computer record, or to generate or receive the data directly in that form, the Recommendation included minimum criteria to be met for such data to fulfil legal requirements as a substitute for written records. One consequence of fulfilling those legal requirements would be that the data would be admissible as evidence.

70. Organizations that are interested in replacing particular paper-based documents with computer-to-computer teletransmission face the question whether the record of the teletransmission will be acceptable as evidence in the courts of particular States in case of dispute. The question has been raised, for example, by CIT in the context of eliminating the rail consignment note. Of these organizations, only the Customs Co-operation Council has made public its conclusions. The draft resolution to be presented to the Council in June 1986 sets forth in great detail the desirability for removing "from existing legislation provisions which obstruct the use of ADP techniques" and suggests certain principles that should be followed. Since these legal questions go beyond the law governing customs matters, the resolution urges States and Customs or Economic Unions to bring this resolution to the attention of the competent authorities at the national and international levels.

#### C. *Substitution of data transmission for written document*

71. As pointed out in document A/CN.9/265, many documents used in domestic and international trade are required by law to be in paper-based form. Although organizations such as the ECE Working Party on Facilitation of International Trade Procedures, the UNCTAD Trade Facilitation Programme and UNCITRAL have given general support to the elimination of requirements of paper-based documents, such requirements must be eliminated in respect of specific documents by national and international authorities. Work has been undertaken to replace specific documents by the following international organizations:

CCC	—	goods declaration
CIT	—	rail consignment note
CMI	—	bill of lading
ECE	—	TIR carnet
ICAO	—	air waybill
IMO	—	various documents required by port and customs authorities
UNCITRAL	—	written form of arbitration agreement, documents and notices issued by operators of transport terminals

72. The work required of an organization to promote the substitution of data transmission for paper-based documents differs widely depending on the type of document and the relationship of the organization to the document. However, the type of work undertaken may involve both technical agreement on message specifications and protocols, including security measures and authentication techniques, and changes in legislation or other legal texts.

#### **D. Use of electronic authentication in place of signature**

73. UNCITRAL, IMO, the Customs Co-operation Council and the ECE Working Party on Facilitation of International Trade Procedures have urged that electronic means of authentication be legally acceptable. Several legal texts prepared by UNCITRAL, UNCTAD and IMO include such a provision.

#### **E. Liability**

74. It has been recognized that the use of computers and their linkage by telecommunications has given rise to new ways in which parties to transactions and third persons could be harmed by the failure of messages to be transmitted or to be acted upon, by the corruption of data and by the improper divulgence of information. The uncertainty as to the extent of liability such harm for and the right of the parties to allocate the resulting loss by contractual agreement are often mentioned as concerns in the substitution of electronic documents for paper-based documents.

75. The UNCITRAL Legal Guide on Electronic Funds Transfers considers many aspects of the problem in the context of electronic funds transfers. Although some of the considerations discussed there are particular to electronic funds transfers, many are common to other uses of data transmission. The ICC rules on interbank compensation for late funds transfers would deal with a limited aspect of the problem. The work in OECD on liability problems in transnational data flow has been of general interest.

#### **F. Regulation by contract**

76. It has been suggested that many of the outstanding legal problems having to do with such matters as the evidentiary effect of the record in a computer of a message received, authentication by electronic means, responsibility for security and liability for erroneous transmission could be settled between any two parties to a data communication. When the parties are using a closed-user communication system, the rules of the system might

settle these questions. When the parties are using an open communication system, these questions might be settled by contract. The replies to the questionnaire sent by the Customs Co-operation Council showed that the customs authorities in several countries were already using this technique by requiring parties desiring to submit a goods declaration in computer-readable form to agree by contract to the conditions governing such submissions.<sup>15</sup> At a more general level, ICC is preparing a draft uniform rules for communication agreements in co-operation with a number of the organizations discussed in this report.

#### **G. Changes in legal rules of underlying transactions**

77. In addition to consideration of the legal rules directly applicable to the use of automatic data processing in one of its several forms, some consideration has been given to the changes in rules governing the underlying transactions called for by the new technology. The UNCITRAL Legal Guide on Electronic Funds Transfers, the preparation by ICC of interbank rules for late funds transfers, the ICC Uniform Customs and Practice for Documentary Credits and the ILA study on uniform rules governing the time of payment partake of this type of activity. The OECD study of consumer policy issues arising from the development and introduction of electronic funds transfer systems includes a number of legal issues of this nature. It can be expected that the CMI study on sea waybills will not only affect the rules governing sea waybills but will also include, or have implications for, the issuance of documentary letters of credit based on waybills or automatic data transmission rather than on bills of lading.

### CONCLUSION

78. A number of international organizations are interested in one or more aspects of the legal implications of automatic data processing to the flow of international trade, as are national authorities in corresponding areas of activity. As public data networks become more generally available and teletransmission of trade data becomes more common, it can be expected that even more organizations and national authorities will show interest in the matter.

79. This survey of work in the field shows that the nature of the subject leads each of the organizations to approach only a portion of the problems involved and to do so from a particular point of view. While there is already a substantial degree of co-operation between the organizations concerned by the exchange of documents and, to some degree, by attendance as observers at meetings of other organizations, a further degree of co-

<sup>15</sup>See the reply of Denmark quoted in A/CN.9/265, note 27.

ordination of activity and of approach would seem to be desirable. In view of the Commission's decision at its eighteenth session to place the subject of the legal implications of automatic data processing to the flow of international trade on its programme of work as a priority item, leadership in this effort at co-ordination might be undertaken by the Commission.

80. This co-ordination might take the form of a meeting in late 1986 or early 1987 to which all interested interna-

tional organizations would be invited. The meeting might be devoted to exploring the full range of legal problems that could presently be anticipated to arise in connection with the use of computers and the international teletransmission of trade data. Agreement might be reached on the problems on which work should be undertaken and the appropriate organization or organizations which might undertake that work. The conclusions reached at this meeting might be presented to the Commission at its twentieth session.

## VI. CO-ORDINATION OF WORK

### Current activities of international organizations related to the harmonization and unification of international trade law: report of the Secretary-General (A/CN.9/281)

[Original: English]

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## INTRODUCTION

1. The General Assembly, in resolution 34/142 of 17 December 1979, requested the Secretary-General to place before the United Nations Commission on International Trade Law, at each of its sessions, a report on the legal activities of international organizations in the field of international trade law, together with recommendations as to the steps to be taken by the Commission to fulfil its mandate of co-ordinating the activities of other organizations in the field.

2. In response to that resolution, detailed reports on the current activities of other organizations related to the harmonization and unification of international trade law have been issued at regular intervals, the last one having been submitted at the sixteenth session in 1983 (A/CN.9/237 and Add.1–3).

3. This report is one in the series mentioned and has been prepared in order to update and supplement the report submitted at the sixteenth session of the Commission. The information it contains is that supplied by international and other organizations regarding their activities in the field of international trade law up to 30 June 1985. Developments subsequent to that date have been referred to where this has been possible. Further information is available directly from the organizations concerned.

4. The activities of UNCITRAL related to the harmonization and unification of international trade law are referred to briefly in this document for the sake of completeness. The current work of UNCITRAL is summarized each year in the reports of the Commission's annual sessions. The reports and the background documents are subsequently reprinted in the *Yearbook* of the United Nations Commission on International Trade Law.

5. Two additional reports, which together with this present one have been prepared for the nineteenth session of UNCITRAL, provide more detailed information on the work of international organizations on certain aspects of international trade law. One of these documents, “Legal implications of automatic data processing: report of the Secretary-General” (A/CN.9/279) includes a review of the work of UNCITRAL and other organizations on that subject. The other document describes the activities of international organizations on certain aspects of international commercial arbitration (A/CN.9/280).

6. The work of the following organizations is described in the present report:

(a) *United Nations bodies and specialized agencies*

CTC	Centre on Transnational Corporations
	paragraphs 36, 72–73, 77, 78, 79–83

ECA	Economic Commission for Africa paragraphs 249–250	UNESCO	United Nations Educational, Social and Cultural Organization paragraphs 100, 101–102, 103, 104, 105
ECE	Economic Commission for Europe paragraphs 15–17, 52, 144, 248–250, 251–253, 254–256, 257, 258, 259	UNIDO	United Nations Industrial Development Organization paragraphs 38–39, 40, 41–42, 43–44, 45, 46, 47, 53, 89, 90
ECLAC	Economic Commission for Latin America and the Caribbean paragraphs 249–250, 253	WIPO	World Intellectual Property Organization paragraphs 92–93, 94–96, 99, 101–102, 105, 106–107
ESCAP	Economic and Social Commission for Asia and the Pacific paragraphs 37, 249–250	World Bank	paragraphs 57–60
FAO	Food and Agriculture Organization paragraphs 27, 31–33, 34–35, 75		
GATT	General Agreement on Tariffs and Trade paragraphs 7–12, 245–247	(b) <i>Other international organizations</i>	
ICAO	International Civil Aviation Organization paragraphs 154–157	AALCC	Asian-African Legal Consultative Committee paragraphs 61–65, 70–71, 173, 174–177
ICSID	International Centre for Settlement of Investment Disputes paragraph 66	CCC	Customs Co-operation Council paragraph 252
ILO	International Labour Organisation paragraphs 222–225		Council of Europe paragraphs 203–205, 206, 231–232
IMO	International Maritime Organization paragraphs 123–124, 130–131, 135–139, 261	CMEA	Council for Mutual Economic Assistance paragraphs 19–20, 21, 48, 67–69, 117, 178, 207
ITC	International Trade Centre paragraphs 239–240	EEC	European Economic Community paragraphs 187, 188, 195, 197–201, 202, 208–217
UNCITRAL	United Nations Commission on International Trade Law paragraphs 4–5, 18, 23, 54–56, 91, 110, 111–112, 115–116, 158, 160–163, 170–172, 264–265		The Hague Conference on Private International Law paragraphs 113–114, 180, 189–190, 191–192, 233–235, 236
UNCTAD	United Nations Conference on Trade and Development paragraphs 24–27, 28–30, 74, 84–86, 87–88, 97, 118, 119–122, 125, 126–129, 132–134, 135–139, 140, 141–142, 143, 159, 160–163, 164, 165–166, 168, 227, 241–243, 257	ICPE	International Centre for Public Enterprises in Developing Countries paragraph 89
UNDP	United Nations Development Programme paragraphs 36, 215	LAIA	Latin American Integration Association paragraphs 253, 263
UNEP	United Nations Environment Programme paragraphs 219–221, 226	OTIF	Organisation Intergouvernementale pour les Transports Internationaux Ferroviaires paragraphs 145–149
		UNIDROIT	International Institute for the Unification of Private Law paragraphs 13–14, 150–153, 193–194, 228, 229–230, 237–238

(c) *International non-governmental organizations*

CMI	Comité Maritime International (IMC) paragraphs 135–139, 169
FIDIC	Fédération Internationale des Ingénieurs Conseils paragraphs 49, 50, 51, 76, 177
ICC	International Chamber of Commerce paragraphs 22, 98, 108–109, 177, 181–182, 196, 218, 244, 260, 262
ICCA	International Council for Commercial Arbitration paragraphs 183–186
ISO	International Organization for Standardization paragraph 167

**I. International commercial contracts in general****A. GATT: government procurement**

7. The purpose of the GATT Agreement on Government Procurement 1981 is to open to foreign suppliers contracts awarded by certain government bodies of its signatory countries. The Agreement provided that three years after it came into force negotiations would take place aimed at improving and broadening it. The procedures and a timetable to be adopted during these negotiations were agreed upon at the meeting of the Committee on Government Procurement held in November 1983.

8. During 1983 the Committee carried out a detailed examination of national laws, regulations and procedures relating to the implementation of the Agreement. After considering the adequacy and effectiveness of the Agreement, as requested in the November 1982 Ministerial Declaration, the signatories concluded that the Agreement was a significant first step towards plurality in the area of government procurement. They considered that it had, on the whole, worked satisfactorily, although its commercial impact would be felt only gradually.

9. The re-negotiation provided for in the Agreement continued during 1984. Many detailed technical amendments were put forward for improvements, including a number of suggestions made in the context of the special and differential treatment afforded to developing countries. The Committee also began, as required by the Agreement, to explore the possibility of expanding its scope to include service contracts, without prejudice, however, to the consideration elsewhere of the general position of GATT in relation to services. Pilot studies are being carried out on architectural and consulting engineering services, on insurance services and on management consulting services, as these relate to govern-

ment procurement. Parties wishing to do so are also carrying out pilot studies on the procurement of data processing services and freight forwarding services.

10. In 1984 the Committee on Government Procurement, which supervises the Agreement, continued its examination of national implementing legislation and practices. Many technical issues were considered. Discussions took place, *inter alia*, on the practices related to tendering or negotiating contracts, the frequency of tenders being advertised under the Agreement, problems related to the procedures for the evaluation of the qualification of suppliers; time limits for the submission of bids; delivery deadlines and the treatment of high-priced bids.

11. *A Practical Guide to the GATT Agreement on Government Procurement* was published in March 1985. This *Guide* is intended to inform the business community and officials of the Agreement, how it is applied by its participants and of the manner in which it can help potential suppliers. It also assists in making clearer government practices in this field.

12. The first dispute panel to be set up under the Agreement was established by the Committee on Government Procurement in February 1983 at the request of the United States of America. That panel, the Panel on Value Added Tax and Threshold, was asked to determine whether or not the practice of the EEC of excluding value added tax from the contract price of EEC member State government purchases contravened the Agreement. Previous attempts to solve the dispute, which arose under an EEC Council Directive on public supply contracts, through consultations and conciliation within the Committee had failed. The Panel found the EEC practice to be inconsistent with the Agreement. In May 1984, the Committee on Government Procurement adopted the report of the Panel (see *GATT Focus*, the GATT secretariat's monthly newsletter, No. 29, May-June 1984). In further discussion of the case in 1984, the Committee was told by the EEC that it was expecting to receive from the Council of the European Communities a mandate which would enable it to negotiate a solution to the issue.

**B. UNIDROIT: general principles applicable to international commercial contracts**

13. The UNIDROIT Study Group on the Progressive Codification of International Trade Law at its first session, held at Rome from 10 to 14 September 1979, examined the first two chapters of a code of general principles applicable to international commercial contracts. The chapters thus considered relate to the formulation and interpretation of such contracts. Following the intention expressed by some of the members of the Study Group to co-operate with the UNIDROIT secretariat in the preparatory work on the future chapters of the code,

the President of UNIDROIT set up a small working group that has met six times since 1980. In addition to the first two chapters mentioned on formulation and interpretation (Study L-Doc. 24 and 25), two other chapters dealing with defects in consent that may affect the validity of a contract (mistake, fraud, threat, unequal bargaining power and gross disparity) have been drafted (Study L-Doc. 26) and work on a chapter on performance has been concluded (Study L-Doc. 34).

14. The Governing Council of UNIDROIT discussed this item in detail at its sixty-fourth session. It examined both the state of the work in general and the provisions of the chapters already prepared. The Council renamed the project, replacing the title "progressive codification of international trade law" with "general principles for international commercial contracts". It also set a time limit of three years within which the informal working group, which is elaborating the draft general principles, should conclude its work. The Governing Council will consider any new texts elaborated by the group at its sixty-fifth session. Meanwhile, the seventh meeting of the working group is taking place in April 1986.

### C. Counter-trade practices

#### 1. ECE

15. At its thirty-second and thirty-third sessions, held in December 1983 and December 1984, the ECE Committee on the Development of Trade continued to devote attention to developments in the field of compensation trade. As a further step in the work of the Committee in analysing the development and consequences of compensation trade, it was agreed that the secretariat of ECE should prepare an analytical study of short-term commercial compensation in the ECE region which would focus on the problems encountered in such transactions, in particular those involving such matters as product quality, re-export restrictions, bureaucratic delays and after-sales service. The problems of quantitative restrictions and anti-dumping procedures were also to be examined. The study was discussed at the thirty-fourth session of the Committee on the Development of Trade in December 1985 (ECE/TRADE/153). The thirty-fifth session of the Committee will be held in December 1986.

16. Some differences of opinion in respect of the manner in which compensation trade should be dealt with in the future programme of work of the Committee, whether it should be made a special item in the agenda or whether it should retain its previous position, were expressed at the sessions mentioned above. It was suggested that the problems involved in short-term compensation transactions should be the subject of a future *ad hoc* meeting on compensation trade. The proposal of the Executive Secretary that the Group of Experts on International Contract Practices in Industry should be invited to consider preparing guidelines on compensation transactions, once the *Guide on Drawing Up International*

*Contracts for Services Relating to Maintenance, Repair and Operation of Industrial and Other Works* (see paragraph 52 below) is completed, was endorsed by several delegations.

17. The ECE secretariat has issued two new studies dealing with compensation trade in the ECE region: "Compensation trade in the ECE region: a survey of quantitative estimates" (TRADE/AC.19/R.1) and "Financing of large-scale compensation projects in east-west trade since 1970: mechanisms, patterns and trends" (TRADE/R.484).

### 2. UNCITRAL

18. At its seventeenth session in 1984, UNCITRAL had before it a report of the Secretary-General on the activities of other organizations within and outside the United Nations in respect of legal aspects of barter and barter-like transactions (A/CN.9/253).

### D. CMEA: general conditions governing delivery of goods

19. During the period from 1983 to the present, the CMEA Conference on Legal Questions has continued its work on the preparation of recommendations for the improvement of the "General Conditions of Delivery of Goods Between the Organizations of the Member Countries of the Council for Mutual Economic Assistance" (GCD CMEA, 1968/1975, version of 1979). This revision is to take into account the practical experience gained in the application of the General Conditions, together with proposals for the inclusion of a greater liability for the non-fulfilment or improper fulfilment of obligations, including indemnification for direct losses. The CMEA Standing Commission on Foreign Trade is also developing proposals for tightening the requirements in respect of the technical level and quality of mutually traded goods, including machinery and equipment. It is intended that, once formulated, the proposed amendments and additions to the General Conditions will be adopted into the Conditions by a decision of the CMEA Standing Commission on Foreign Trade and be put into effect by the individual countries on the basis of that Commission's recommendations and in accordance with their national legislation.

20. Work on the comparative study of the national legal norms of the CMEA member countries as applied to contracts governed by the CMEA General Conditions continued under the auspices of the Conference on Legal Questions during 1983 and 1984. A result of this work is the projected publication by the CMEA secretariat, in the first quarter of 1986, of "The Contract Law of the CMEA Member Countries and the Socialist Federal Republic of Yugoslavia: General Principles". This publication is being prepared under the leadership of Professor H. Braginsky of the Union of Soviet Socialist Republics and is financed by contributions from CMEA member

States. It will contain a survey of the national legislation of these countries in respect of the conclusion and execution of contracts, and as regards liability for their non-performance.

#### E. CMEA: contractual system

21. In January 1985 the CMEA Council's Executive Committee approved a report, prepared by the CMEA Conference on Legal Questions, aimed at improving the system of contracts for the implementation of measures agreed upon by the CMEA member countries. This report contains an analysis of the system of agreements in effect in the area of economic, scientific and technical cooperation and proposes basic guidelines for the improvement of the contractual system of the CMEA member countries. In accordance with a decision of the Executive Committee, the principles elaborated in this report are intended for use by the CMEA countries and the CMEA branch organs, as they see fit, when drawing up multilateral agreements and civil law contracts.

#### F. ICC: force majeure and hardship clauses

22. The ICC Commission on International Commercial Practice has completed its work on model *force majeure* and hardship clauses. The model clauses are accompanied by an explanatory brochure (ICC Publication No. 421).

#### G. UNCITRAL: Uniform Rules on Contract Clauses for an Agreed Sum Due Upon a Failure of Performance

23. UNCITRAL adopted the Uniform Rules on Contract Clauses for an Agreed Sum Due Upon a Failure of Performance at its sixteenth session in May-June 1983. By resolution 38/135 of 19 December 1983, the General Assembly recommended that States give serious consideration to the Uniform Rules and, where appropriate, implement them in the form of either a model law or a convention. (For the text of the Uniform Rules, see "Report of the United Nations Commission on International Trade Law on the work of its sixteenth session". *Official Records of the General Assembly, Thirty-eighth Session, Supplement No. 17 (A/38/17)*).

## II. Commodities

### A. UNCTAD: commodity agreements

24. The UNCTAD Agreement establishing the Common Fund for Commodities, concluded on 27 June 1980 (TD/IPC/CF/CONF/25, United Nations publication, Sales No. E.81.II.D.8), has remained open for signature and ratification beyond the deadline prescribed by the Agreement for fulfilling the requirements for entry into force (30 September 1983) until the ratifying countries decide otherwise. By January 1986 the UNCTAD Agree-

ment establishing the Common Fund for Commodities had been ratified by 90 countries, accounting for 57.87 per cent of the Fund's directly contributed capital, and the conditions for entry into force as regards the voluntary contributions to the Second Account of the Fund had been met. Pledges of voluntary contributions announced total \$US 255 million, i.e. 91 per cent of the target (\$US 280 million) (UNCTAD Bulletin No. 218, January 1986).

25. The aims of the international commodity agreements vary from one agreement to another. The principal objectives, however, are price and export earnings stabilization and long-term development. The latter comprises activities related to improved market access and supply reliability, increased diversification and industrialization, augmented competitiveness of national products *vis-à-vis* synthetics and substitutes, improved marketing, and distribution and transportation systems. Two agreements with development provisions, namely the Jute and the Tropical Timber Agreements, 1982 and 1983 respectively, have been concluded. International commodity agreements may have additional objectives, e.g. the increase of consumption, the prevention of unemployment or underemployment, and the alleviation of serious economic difficulties.

26. The following commodity agreements, adopted at various United Nations conferences under the auspices of UNCTAD, are in force. These agreements were prepared pursuant to the objectives adopted by UNCTAD in resolutions 93(IV) and 124(V) on the Integrated Programme for Commodities:

- International Natural Rubber Agreement, 1979 (TD/RUBBER/15/Rev.1, United Nations publication, Sales No. 80.II.D.5): The 1985 United Nations Conference on Natural Rubber was unable to complete negotiations on a new Agreement at its first session. The negotiations were adjourned on 8 May 1985 with a request to the Secretary-General of UNCTAD to make arrangements for reconvening the Conference. The negotiations are to be resumed in April 1986.
- International Cocoa Agreement, 1980 (TD/COCOA/6/7/Rev.1, *United Nations Treaty Series*, No. 15033, vol. 1023): The United Nations Cocoa Conference held four rounds of negotiations (May 1984, October-November 1984, February-March 1985 and February 1986) to replace the 1980 Agreement. The last session of this Conference was unable to reach a consensus on a new Agreement. The Conference has requested a resumption of negotiations in July 1986.
- Negotiations on a new Agreement to replace the Sixth International Tin Agreement, 1981 (TD/TIN.6/14/Rev.1, United Nations publication, Sales No. 82.II.D.16), which is due to remain in force until 30 June 1987, have been expected to start in the first half of 1986. (Note, however, that trading in tin was suspended in the international markets in October 1985 in consequence of which the status of the Agreement may be called into question.)



- International Tropical Timber Agreement, 1983 (TD/TIMBER/11/Rev.1, United Nations publication, Sales No. 84.II.D.5): This Agreement entered into force provisionally on 1 April 1985. It will remain in force until 31 May 1990, unless terminated before that date or extended for not more than two periods of two years each.
- International Sugar Agreement, 1984 (TD/SUGAR.10/11/Rev.1, United Nations publication, Sales No. 85.II.D.9): This replaces the 1977 Agreement. It entered into force provisionally on 1 January 1985. It will remain in force until 31 December 1986, unless terminated earlier or extended on a year-to-year basis.
- International Olive Oil Agreement, 1979 (TD/OLIVE OIL.7/7/Rev.1 United Nations publication, Sales No. 80.II.D.1): This Agreement entered into force provisionally on 1 January 1980 and conclusively on 1 January 1982. It had a basic duration of five years until 31 December 1984 but has been extended for a total of two years. It is now due to remain in force until 31 December 1986.
- International Agreement on Jute and Jute Products, 1982 (TD/JUTE/11/Rev.1, United Nations publication, Sales No. 83.II.D.3): It entered into force provisionally on 1 January 1984. It will remain in force until 8 January 1989, unless terminated before that date or extended for a period not exceeding two years.

27. The International Agreement on Jute and Jute Products, 1982, provides that the International Jute Organization (IJO) shall, to the maximum extent possible, rely upon and fully utilize the facilities, services and expertise of organizations such as FAO. In the period 1983–1985, FAO continued to extend support to the International Jute Organization, which was officially established in January 1984, through the identification of project proposals for research, development and cost reduction in jute agriculture and processing for implementation by the IJO.

#### **B. UNCTAD: complementary facility for commodity-related shortfalls in export earnings**

28. By resolution 157(VI) of 2 July 1983, UNCTAD requested its Secretary-General to convene, after consultation with interested Governments, a Group of Experts on the Compensatory Financing of Export Earnings Shortfalls. The Expert Group was convened and it prepared a report on "Compensatory financing of export earnings shortfalls" (TD/B/1029 and Add.1) which was submitted to the fourteenth special session of the Trade and Development Board, which took place between 10 and 14 June 1985. In that report, the Expert Group identified supply instability as a major cause of commodity export earnings' instability at the country level and considered that a new commodity compensatory financ-

ing facility must be created. The Group of Experts mentioned are expected to meet in June 1986.

29. Furthermore, the fourteenth special session suggested that a special session of the Trade and Development Board be convened in 1986 to decide upon the action to be taken as a follow-up to the fourteenth special session, including the possibility of convening a negotiating conference on an additional complementary facility.

30. Other recent studies carried out by UNCTAD are:

- "Compensatory financing of export earnings shortfalls" (TD/B/1029/Rev.1);
- *The Processing and Marketing of Tea: Areas for International Co-operation* (TD/B/C.1/PSC/28/Rev.1, United Nations publication, Sales No. E.84.II.D.10);
- *The Processing and Marketing of Copper: Areas for International Co-operation* (TD/B/C.1/PSC/30/Rev.1, United Nations publication, Sales No. E.84.II.D.24); and
- *The Processing Before Export of Cocoa: Areas for International Co-operation* (TD/B/C.1/PSC/18/Rev.1, United Nations publication, Sales No. E.84.II.D.16)

#### **C. Informal commodity arrangements**

##### *1. FAO: price arrangements for hard fibres*

31. At its eighteenth session in September 1983, the FAO Intergovernmental Group on Hard Fibres agreed to maintain unchanged the indicative price range for sisal and henequen that had been in force since 1980. It decided that the quota system should continue to be maintained in principle, but that the global and national quotas should remain suspended. In reviewing the informal arrangement for abaca, the Group agreed to maintain the current indicative range, in force since December 1979, and to keep inoperative the mechanism triggering automatic consultations for abaca.

32. The Group also decided to examine at future sessions the possibility of developing, within the framework of the existing informal arrangements for sisal and henequen, an appropriate formula for recommending indicative prices for sisal twines, including differentials between sisal and polypropylene harvest twines, and an associated system of supply management for sisal fibre and twine.

33. At its nineteenth session in December 1984, the Group agreed to reduce the indicative price range for the major African grade and to introduce a differential to Brazilian fibre. It was decided that the quota system should continue to be maintained in principle but that the global and national quotas should remain suspended. However, for the first time the Group, with the exception of two countries, agreed to recommend an indicative

price for sisal and henequen baler twine. In respect of abaca, the Group suspended price recommendations within the informal arrangements in view of the unsettled market situation.

#### 2. *FAO: price arrangements for jute and kenaf*

34. At its nineteenth session in October 1983, the FAO Intergovernmental Group on Jute, Kenaf and Allied Fibres recommended indicative prices for both jute and kenaf fibres. Indicative prices for jute, which had remained almost unchanged since 1978–1979, were increased in view of the diminished supply in prospect for the 1983–1984 season. For kenaf, indicative prices were retained at the previous year's level.

35. At its twentieth session in November 1984, the Group suspended the informal indicative price arrangements for jute and kenaf temporarily for the 1984–1985 season because of an unprecedented shortage of fibre and extremely high prices.

#### D. *CTC: processing and marketing of primary commodities*

36. The CTC and its units, working jointly with the regional commissions and with financial assistance from UNDP, have undertaken an interregional study of the involvement of transnational corporations in the production, processing and marketing of a number of primary commodities. A draft technical paper presenting the conclusions drawn from the various country and commodity case studies undertaken in earlier phases of the project has been prepared.

#### E. *ESCAP: guide on information sources for jute*

37. In August 1983, the ESCAP Trade Promotion Centre was requested by the Intergovernmental Consultation on Jute and Jute Products to compile a comprehensive *Guide to Selected Information Sources for Jute and Jute Products* to assist the jute-producing countries in the region in developing and promoting their jute industry and trade. The *Guide* is an inventory of basic information sources related to jute and jute products as well as a pointer to the information available through secondary sources. It is intended (a) to serve as a reference source for the government Ministries of the jute-producing countries and interested organizations and agencies and (b) to assist the Governments of the jute-producing countries in gaining a better understanding of the jute trade and in developing a systematic methodology to increase the export earnings of their farmers by gathering and analyzing data on jute production in order to formulate a pricing policy. The *Guide* contains background information and an operational frame designed to assist the ESCAP jute producing countries in setting up their country-level market information services for jute and jute products. The *Guide* was published by ESCAP in March 1985.

### III. Industrialization

#### A. *UNIDO: System of Consultations*

38. A report on "Trade and trade-related aspects of industrial collaboration at the enterprise level" (ID/B/348) was submitted to the Industrial Development Board—the governing body of UNIDO—at its nineteenth session as a follow-up to the *Ad Hoc* UNCTAD/UNIDO Group of Experts on Trade and Trade-related Aspects of Industrial Collaboration Arrangements.

39. In accordance with the recommendations of the Industrial Development Board, UNIDO has evolved a set of legal materials, including model contracts and clauses, guidelines and checklists for contractual arrangements, according to the requirements of each of the 13 industrial sectors served by the System of Consultations. A number of these are referred to in sections B and D below.

#### B. *UNIDO: model contracts and contractual arrangements*

##### 1. *Model contracts for the fertilizer industry*

40. In addition to two model contracts for the construction of fertilizer plants completed prior to 1983, namely the turnkey lump-sum contract and the cost-reimbursable contract, UNIDO has completed two additional model contracts, the semi-turnkey contract and the licensing and engineering services agreement. The last two model contracts were presented to the Fourth Consultation on the Fertilizer Industry in January 1984 and were reviewed by an international expert group in July of that year. At present the following draft versions of the model forms of contract are being revised and edited for publication:

(a) "UNIDO model form of turnkey lump-sum contract for the construction of a fertilizer plant including guidelines and technical annexures" (UNIDO/PC.25/Rev.1);

(b) "UNIDO model form of cost-reimbursable contract for the construction of a fertilizer plant including guidelines and technical annexures" (UNIDO/PC.26/Rev.1);

(c) "Second draft of the UNIDO model form of licensing and engineering services agreement for the construction of a fertilizer plant including guidelines and technical annexures" (UNIDO/PC.73);

(d) "UNIDO model form of semi-turnkey contract for the construction of a fertilizer plant including guidelines and technical annexures" (UNIDO/PC.74).

##### 2. *Contractual arrangements in the petrochemical sector*

41. In respect of the petrochemical sector, UNIDO has issued documents as follows:

(a) "UNIDO model form of agreement for licensing of patents and know-how in the petrochemical industry,

including annexures: an integrated commentary and alternative texts of some clauses" (UNIDO/PC.50/Rev.1). The final version of this document was presented to the Third Consultation on the Petrochemical Industry in December 1985;

(b) "Survey and analysis of joint-venture arrangements in the petrochemical industry" (ID/WG.448/4). This paper is based on the information supplied by over 50 joint-venture companies surveyed by UNIDO. The principal elements in joint-venture agreements are discussed in this paper, which was considered by the Third Consultation on the Petrochemical Industry.

42. UNIDO has also prepared terms of reference for "mini-models" of long-term co-operative arrangements in, *inter alia*, financing, marketing, training and long-term supply of raw materials and feedstock. However, only the terms of reference regarding access to technology have been expanded upon, namely in "Approaches to contractual agreements aimed at access to technology and to its improvements in the petrochemical industry with illustrative examples" (ID/WG.448/5).

### 3. *Contractual arrangements in the pharmaceutical sector*

43. The documents listed below were finalized by UNIDO in co-operation with the Third *Ad Hoc* Panel of Experts on Contractual Arrangements in April 1985 in the light of the comments and suggestions made at the Second Consultation on the Pharmaceutical Industry:

(a) "Items which could be incorporated in contractual arrangements for the transfer of technology for the manufacture of those bulk drugs/intermediates included in UNIDO's illustrative list" (ID/WG.393/1/Rev.2);

(b) "Items which could be included in licensing arrangements for the transfer of technology for the formulation of pharmaceutical dosage forms" (ID/WG.393/3/Rev.2);

(c) "Items which could be included in contractual arrangements for the setting-up of a plant for the production of bulk drugs (or intermediates) included in UNIDO's illustrative list" (ID/WG.393/4/Rev.2).

44. UNIDO is preparing new documents on:

(a) Items that could be included in contractual arrangements for the setting-up of turnkey plants for: (i) the production of pharmaceutical chemicals (bulk drugs) or intermediates included in the UNIDO illustrative list; and for (ii) the production of pharmaceutical formulations;

(b) Arrangements for technical assistance for the formulation of pharmaceutical forms;

(c) Areas not covered in the documents ID/WG.393/1, 3 and 4, Rev.2, referred to above.

The members of the Fourth *Ad Hoc* Panel of Experts are to supply UNIDO with their comments on the drafts of those documents. The drafts, as amended in the light

of those comments, will then be submitted to the Third Consultation on the Pharmaceutical Industry scheduled for March 1987.

### 4. *Contractual arrangements in the agricultural machinery sector*

45. UNIDO has prepared the following documents:

(a) "Issue paper No. III: Main items to be included in model contracts for the import, assembly and manufacture of agricultural equipment including training; model licensing agreement" (ID/WG.400/4);

(b) "Items to be included in model contracts for the import, assembly and manufacture of agricultural equipment including training; model licensing agreement" (ID/WG.400/2);

(c) "Guidelines to international contracts for the acquisition, assembly and manufacture of agricultural machinery and spare parts therefor" (ID/WG.443/1);

(d) "Comparison of sample clauses for contracts for the initial management of a factory for the assembly or manufacture of agricultural machinery and the rendering of technical assistance ancillary thereto" (ID/WG.443/2);

(e) "Comparison of sample clauses for contracts for the supply of spare parts for agricultural machinery" (ID/WG.443/3);

(f) "Comparison of sample clauses for contracts for the supply and installation of production equipment for the assembly and manufacture of agricultural machinery" (ID/WG.443/4);

(g) "Comparison of sample clauses for contracts for the transfer of know-how, grant of patent/trademark licenses, assignment of technical information and the rendering of technical services ancillary thereto for the manufacture of agricultural machinery" (ID/WG.443/5);

(h) "Comparison of sample clauses for contracts between clients and industrial architects for the design and supervision of the construction of works for the assembly or manufacture of agricultural machinery" (ID/WG.443/6);

(i) "Comparison of sample clauses for contracts for the supply of agricultural machinery" (ID/WG.443/7).

### 5. *Contractual arrangements in the food-processing sector*

46. In November 1981 UNIDO was asked to prepare a check-list of contractual elements that might be included in agreements in the food-processing industry to promote efficient co-operation between the contracting parties. As a first step towards the preparation of this check-list, a report on "Trends and issues in contractual arrangements in the food-processing industry. Information paper" (ID/WG.427/11) was prepared for the Second Consultation on the Food-processing Industry (October 1984). This paper, which deals with the practice of developing countries entering into contractual arrangements with

foreign partners in this sector, will serve as a basis for the formulation of a check-list directly applicable to this industry.

#### 6. *Contractual arrangements in the leather and leather-products sector*

47. The work initiated in this field by UNIDO in 1981 resulted in the preparation of two documents—a separate check-list each for the tanning industry and the footwear industry—since these subsectors pose individual problems in international co-operation. The check-list for the footwear sector was approved by the fifth session of the UNIDO Leather Panel, held at Vienna from 25 to 27 November 1981, while the one for the tanning sector was approved by the sixth session of that Panel, held at Vienna from 29 November to 1 December 1982. Both documents, i.e. “Check-list for contractual agreements in the footwear sector between enterprises from developed and developing countries. Background paper for issue No. 1” (ID/WG.411/1) and “Check-list for contractual agreements in the tanning sector between enterprises from developed and developing countries. Background paper for issue No. 1” (ID/WG.411/2), were submitted to the Third Consultation on the Leather and Leather-Products Industry which was held at Innsbruck from 16 to 20 April 1984.

#### C. *General conditions*

##### 1. *CMEA: general conditions governing the technical standards of maintenance of machines, equipment and other goods*

48. In January 1985 the CMEA Executive Committee approved the proposals, formulated by the CMEA Standing Commission on Foreign Trade, for the improvement of the General Principles for the supply of spare parts for machinery and equipment delivered in mutual trading among the CMEA member countries and the Socialist Federal Republic of Yugoslavia. The Executive Committee recommended to the CMEA member countries and to Yugoslavia that they should put into effect from 1 July 1985 the amendments and additions approved by the Committee to the General Principles.

##### 2. *FIDIC: standard conditions of contract for works of civil engineering construction*

49. A task committee comprising representatives of FIDIC and of the Confederation of International Contractors' Associations is currently preparing a fourth edition of the “Conditions of contract (international) for works of civil engineering construction” (the third edition was published in March 1977). Before the document is finally approved for publication by the Executive Committee of FIDIC, comments will be invited from the international funding institutions. Publication of the fourth edition is expected during the second half of 1986.

##### 3. *FIDIC: conditions of contract for electrical and mechanical works*

50. A committee comprising representatives of FIDIC and the European Association of Plant Manufacturers (ORGALIME) is currently engaged in reviewing the FIDIC “Conditions of contract (international) for electrical and mechanical works” (second edition, 1980) in preparation for the publication of a third edition in 1986.

##### 4. *FIDIC: international general rules of agreement between client and consulting engineer (IGRA)*

51. FIDIC commenced publication of standard conditions for client/consultant agreements in 1963. The documents currently in issue are those dealing with pre-investment studies (IGRA 1979 P.I.); design and supervision of construction of works (IGRA 1979 D&S); and project management (IGRA 1980 P.M.). FIDIC has appointed subcommittees to review each of these documents and to make recommendations regarding their amendment.

#### D. *Guides and guidelines*

##### 1. *ECE: draft Guide on Drawing Up International Contracts for Services Relating to Maintenance, Repair and Operation of Industrial and Other Works*

52. In July 1984 the ECE Group of Experts (twenty-fourth session) began the first reading of the draft Guide on Drawing Up International Contracts for Services Relating to Maintenance, Repair and Operation of Industrial and Other Works (TRADE/GE.1/R.32). At its twenty-sixth session in July 1985, the Group of Experts approved most of the articles dealing with maintenance contracts, these having been revised by the secretariat in the light of the comments made by the twenty-fifth session of the Group of Experts. The remaining paragraphs regarding maintenance contracts were approved at the twenty-seventh meeting in December 1985. The Expert Group also considered and approved the paragraphs of the Guide dealing with repair. The Group requested the secretariat to prepare a revised version of the Guide containing the changes and amendments already agreed and, to the extent that these apply to the text relating to operation contracts, to make changes in that latter part of the Guide. This revised document (TRADE/GE.L/R.32/Rev.4) will be before the twenty-eighth session of the Group of Experts in July 1986.

##### 2. *UNIDO: guidelines for the establishment of industrial joint ventures in developing countries*

53. The UNIDO “Guidelines for the establishment of industrial joint ventures in developing countries” (UNIDO/IS.361) were prepared in 1982. The following topics are dealt with in the Guidelines: the incorporation

of a company and its international structure, negotiating the management of a joint-venture company, negotiating the capital structure of the joint-venture company, and negotiating the transfer of know-how and technology-related services in the joint venture context. On the basis of this document revised guidelines are in preparation for specific issues relating to the acquisition of technology through joint ventures.

3. *UNCITRAL: draft Legal Guide on Drawing Up International Contracts for Construction of Industrial Works*

54. UNCITRAL considered the legal implications of the new international economic order during its twelfth, thirteenth and fourteenth sessions. At its fourteenth session (1981) the Commission decided that a legal guide that would identify the legal issues involved in contracts for the supply and construction of large industrial works and would suggest possible solutions to assist parties, particularly those from developing countries, in their negotiations, should be prepared.

55. This work was assigned to the UNCITRAL Working Group on the New International Economic Order. The Working Group considered clauses to be found in contracts for the supply and construction of large industrial works at its second and third sessions (1981 and 1982) and examined the draft chapters of the Legal Guide at its fourth to eighth sessions (between May 1983 and March 1986) (for the draft chapters see: A/CN.9/WG.V/WP.9/Add.3 and 4; A/CN.9/WG.V/WP.11, Add.1 and 3-8; A/CN.9/WG.V/WP.13/Add.1 and 3-6; A/CN.9/WG.V/WP.15, Add.1 and 2, 4-6, 9 and 10; and A/CN.9/WG.V/WP.17/Add.1-9).

56. It is expected that at its ninth session (1987) the Working Group will consider all the draft chapters of the Legal Guide as revised by the secretariat in the light of the comments by the Working Group. It is anticipated that the draft Legal Guide will be placed before the Commission for approval at its twentieth session (1987).

### E. Investment protection

1. *World Bank: Multilateral Investment Guarantee Agency (MIGA)*

57. In May 1984, the management of the World Bank presented to member Governments a concrete proposal for MIGA, and, in October 1984, the Bank submitted a first draft Convention for the establishment of such an Agency to member Governments of the Bank reflecting the comments received on the proposal. The draft Convention served as the basis for wide-ranging discussions held by the Bank with member Governments, business and professional associations and international

organizations. In the light of those discussions, a draft Convention was submitted to the Executive Directors of the Bank in March 1985; that draft was discussed in a Meeting of the Whole in June 1985. Many issues were resolved during the course of those discussions. In September 1985 the Bank approved plans to establish MIGA and it is anticipated that the agency will go into operation before the end of 1986. MIGA will be affiliated to the Bank but will be a separate entity. (See *The World Bank Annual Report 1985*, p. 52.)

58. The object of the MIGA proposal is to encourage the flow of resources to productive enterprises in the participating countries by guaranteeing investments emanating from other participating countries against non-commercial risks. Ancillary to this aim is the furnishing of information about investment opportunities and the giving of advice and technical assistance to interested members on measures useful to attract foreign investment.

59. In its operations, MIGA is expected to respond to the demand for protection that is not being adequately met at present by national investment guarantee schemes or by the private market. MIGA will complement these schemes and will co-operate with them through co-insurance and re-insurance. It will give special attention to guaranteeing investments from countries that do not have a national scheme and in host countries where a national scheme is either unable to operate or is already heavily exposed. It will, together with national schemes, co-insure large investments and will insure and co-insure multinationally financed investments. MIGA may be able to act as re-insurer of national schemes. MIGA will also co-operate with private political risk insurers, mainly by co-insuring large investments and re-insuring part of its portfolio with them.

60. In general terms, four broad categories of non-commercial risks are covered: (a) the transfer risk resulting from host government restrictions on conversion and transfer from local currency into another currency, (b) the risk of loss resulting from the action or inaction of the host Government depriving the foreign investor of substantial rights or reducing the benefits of the investment, (c) the risk of armed conflict and civil unrest, and (d) the repudiation of government contracts resulting in a denial of justice.

2. *AALCC: promotion and protection of investment*

61. At the twenty-first session of the AALCC (Jakarta, April 1980), the question of the promotion and protection of investments on a reciprocal basis was first discussed in the context of the promotion of co-operation in industry in the Asian-African region. The AALCC secretariat prepared a draft model bilateral agreement on investment protection which was considered by the Trade Law Subcommittee at its twenty-second session in May 1981. The report of that Subcommittee was reviewed by a ministerial meeting in Istanbul in September 1981.

62. Extensive consultations followed the Istanbul meeting and through these it became apparent that a uniform approach in the promotion and protection of investments resulting in the formulation of a single model bilateral treaty might not meet the situation. Rather, it was suggested that three different draft agreements should be prepared. Accordingly, the secretariat's study of November 1982 on this question suggested three draft model agreements:

(a) *Model A*: a draft of a bilateral agreement on a similar pattern as the agreements entered into between some of the countries of the region with industrialized States with certain changes and improvements, particularly in the matter of promotion of investments;

(b) *Model B*: a draft agreement whose provisions are somewhat more restrictive than Model A in the matter of the protection of investments and contemplate a greater degree of flexibility; and

(c) *Model C*: a draft agreement on the pattern of Model A but applicable only to certain classes of investments, as determined by the host country.

The texts of these models are to be found in "Promotion and protection of investments (Secretary-General's report)", Doc. No. AALCC XXIII/9.

63. During 1983 and early in 1984 the study was examined by an Expert Group. That Expert Group's recommendations in the form of three draft models were finalized in January-February 1984. The models were submitted to the Governments concerned for their observations and comments.

64. At its twenty-fourth session (February 1985), the Trade Law Subcommittee formally approved the three model agreements and adopted its final report on the topic. The model agreements were submitted to the member Governments so that they could be brought to the notice of the interested authorities and be of assistance to them in negotiating such agreements.

65. The other aspects of investment promotion and protection being considered by the AALCC are:

(a) The World Bank's draft Convention for a Multilateral Investment Guarantee Agency;

(b) The different investment incentives offered by member States; and

(c) The means by which the Secretary-General's good offices can be employed in assisting member Governments in promoting investment by, *inter alia*, arranging meetings between representatives of the member States and foreign investors.

### 3. ICSID: legislation published

66. ICSID has edited a series containing the legislation of 63 developing countries on investments, i.e. texts of the laws. It has also published the texts of some 230 treaties on bilateral investment promotion and protection between developed as well as developing countries.

### F. CMEA: multilateral production specialization and co-operation

67. In 1983 the CMEA Conference on Legal Questions approved the basic principles for the drafting, structure, content and fulfilment of clauses relating to inter-State obligations in the area of multilateral production specialization and co-operation between CMEA member countries. The intention is that these basic principles shall be applied by the countries at their discretion for the purpose of improving contractual practices and of providing for the more effective legal regulation of multilateral inter-State relations in connection with production specialization and co-operation.

68. In this same area, a practical guide is at present being prepared on the drafting of contracts, using the model principles, for individual types of international production co-operation schemes between the economic organizations of the CMEA member countries. This work is scheduled to be completed in 1986.

69. In that same year, 1983, the CMEA Conference on Legal Questions approved a report on the possible content of model agreements and contracts regulating co-operative relationships in the area of science, technology and production. On the basis of that report, the Conference is preparing a multilateral, inter-agency model agreement and the relevant civil law contracts on scientific, technical and production co-operation.

### G. AALCC: regional co-operation in the field of industry

70. A two-day ministerial meeting of the AALCC on regional co-operation in industry was held at Kuala Lumpur in December 1980 with the object of devising a possible framework for regional co-operation in the economic field, particularly in regard to industrialization. The important areas for such co-operation were identified at that meeting. A further ministerial meeting held at Istanbul in September 1981 recommended that medium- and small-scale projects, such as cement, fertilizer and building-material production plants, be brought within the framework of that co-operation. The need for an exchange of information in respect of industrial policies and plans for industrial development, as well as regarding the relevant laws and regulations concerning investments in the region, was emphasized. The preparation of general guidelines for co-operation in industrial projects and for the organization of training programmes in technical and managerial fields was recommended.

71. Some progress has been made in the matter of the exchange of information regarding laws and regulations in the field of industry, investment and training. Fifteen member Governments have furnished information, which has been duly circulated. The preparation of draft guidelines for joint-venture arrangements in the industrial sector has been commenced.

## H. Studies and meetings

### 1. CTC

72. CTC has continued its work of comparative analysis of industrial contracts in specific sectors and contracts related to specific types of activities. In these studies, the financial, economic, legal, institutional and operational aspects of such contracts are analysed, as are their structure and the formulation of specific provisions. The work is intended to aid officials from Governments and enterprises in developing countries in formulating their negotiating strategy in similar projects.

73. In 1984, CTC completed another study in this series entitled "Analysis of engineering consultancy contracts and technical services agreements" (ST/CTC/58). CTC intends to commence the analysis of contracts in other sectors of particular importance to developing countries, taking into account requests from Governments in regard to contractual arrangements.

### 2. UNCTAD

74. UNCTAD co-operated with UNDP on project RAF/83/006 which involved the preparation of documentation for the first Conference of Chambers of Commerce from African and Latin American Countries held from 20 to 25 October 1985 in the Canary Islands. This documentation included the draft outline of an agreement on a legal régime for bi-regional enterprises in Africa and Latin America and a compendium of existing draft bilateral conventions on trade and co-operation between selected developing countries.

### 3. FAO

75. The FAO Legal Office participated in and contributed to the FAO/UNCTC/CECAF Regional Training Workshop on Joint Ventures and other Commercial Arrangements in Fisheries convened at Casablanca, Morocco, from 8 to 17 November 1983. It also provided assistance to Cape Verde on joint ventures.

### 4. FIDIC

76. FIDIC has taken the initiative to arrange meetings, at which the construction industry, the insurance industry, lawyers specializing in construction contracts, bankers and consulting engineers are represented, in order to examine insurance procedures for major construction contracts and to recommend any revisions to such procedures. A core paper was issued by FIDIC in April 1985, and a meeting of those concerned was held at Munich on 21 June 1985.

## IV. Transnational Corporations

### A. CTC: draft Code of Conduct on Transnational Corporations

77. At its thirty-ninth session, the General Assembly (resolution 39/443 of 18 December 1984), decided to reconvene the special session of the Commission in June

1985. To facilitate work at that session, the Assembly requested CTC "...to prepare a report on the outstanding issues in the draft code of conduct [on transnational corporations], including, *inter alia*, the questions of international law and international obligations *vis-à-vis* national legislation...". The report was duly prepared and formed the basis of discussion at the reconvened special session of the Commission in June 1985. Among the issues discussed at that session were the applicability of international law/international obligations to the code of conduct and the acceptable formulation in this regard, specific norms relating to national jurisdiction over transnational corporations (TNCs), non-interference by TNCs in internal political affairs, national treatment to be accorded to TNCs, nationalization and compensation and procedures for the settlement of disputes between Governments and TNCs. The report of the Commission's special session, held in January 1986, will be considered by the twelfth session of the Commission meeting between 9 and 18 April 1986.

### B. CTC: international, regional and bilateral arrangements

78. CTC has continued its earlier work on international, regional and bilateral arrangements on matters relating to transnational corporations. This work has involved the examination of a number of facets of co-operation in this area: the efforts made by various organizations to formulate multilateral instruments for the regulation of the activities of transnational corporations; the initiatives of regional and subregional organizations to harmonize the policies of member countries relating to foreign direct investment and the activities of transnational corporations; and bilateral investment agreements. A technical paper entitled "Bilateral investment agreements" (ST/CTC/65) was finalized in 1984 for publication in 1985. Another technical paper on regional and international arrangements relating to foreign investment was to be finalized in 1985.

### C. CTC: studies

79. In the studies of industry prepared by CTC, an overall description and analysis of the role and impact of transnational corporations in trade in specific natural resources, manufacturing and service sectors is presented. Trends in the participation of transnational corporations in an industry against the background of the structure and characteristics of that industry are examined. In that context, market concentration, competitive structure, intra-firm relationships and the pattern of ownership and control are analysed, as are the investment, technology and marketing practices and policies of host and home countries towards firms in the industry in question. Also examined in the studies are technological changes and their impact on the structure of the industry, on the location of operations, on international competition and trade, on employment and on the future role of transnational corporations in the industry concerned in developing countries.

80. Efforts have been initiated to include, as an annex to each study, a profile of the main transnational corporations active in the industry concerned. Such a presentation should contribute to a better understanding of the industry and of the role of transnational corporations operating in it, and should be useful information for Governments in their endeavours to develop appropriate policies and to strengthen their negotiating capability with transnational corporations.

81. An addition to the existing collection of industry studies, *Transnational Corporations in the Pharmaceutical Industry of Developing Countries* was published in 1984 (United Nations publication, Sales No. E.84.11.A.10). Drafts of three further studies have been completed: "Transnational corporations in the international semiconductor industry" (ST/CTC/39), "Transnational corporations in the international construction and engineering industry" (ST/CTC/60); and "Transnational corporations in the man-made fibre, textile and clothing industries" (ST/CTC/63). In addition, an informal seminar was convened to review a preliminary draft report on the involvement of transnational corporations in the armaments industry and in the transfer of military technology.

82. *Transnational Corporations and International Trade: Selected Issues* was published in 1985 (United Nations publication, Sales No. E.85.11.A.4). This technical study seeks to review the issues of the role of transnational corporations in the exports of manufactures of developing countries, the import propensities of transnational corporations, the behaviour of intra-firm flows, the problem of transfer pricing and the impact of transnational corporations on the trade policies of their home countries.

83. Four other studies were to be completed in 1985 and published as technical papers, namely "Transnational corporations in biotechnology", "Transnational corporations in international data-processing services", "Transnational corporations in the international data-processing equipment industry" and "Transnational corporations and non-fuel minerals". In addition, studies of transnational corporations in the plastics industry and in the telecommunications industry have been initiated.

## V. Transfer of technology

### A. UNCTAD: proposed International Code of Conduct on the Transfer of Technology

84. The General Assembly, by resolution 32/188 of December 1977, convened the United Nations Conference on an International Code of Conduct on the Transfer of Technology to negotiate and adopt such a Code. This Conference has held six sessions since October 1978. The substantive provisions of the present text of the proposed Code as of 5 June 1985 (contained in document TD/CODE TOT/47) fall into two broad groups: those concerning the regulation of transfer of

technology transactions and of the conduct of the parties to them; and those relating to steps to be taken by Governments to meet their commitments to the Code.

85. The fifth session of the Conference, convened in pursuance of General Assembly resolution 37/210, met from 17 October to 4 November 1983. Negotiations on the issues outstanding in the draft Code took place on the basis, *inter alia*, of proposals that had been made by an Interim Committee of the Conference in 1982. Although agreement was reached during the session on virtually all of chapter 5 (responsibilities and obligations of parties), no solution could be found for the other main outstanding issues in chapter 4 (restrictive practices in transfer of technology transactions) and in chapter 9 (applicable law and settlement of disputes).

86. The sixth session of the Conference, convened in consequence of resolution 38/153, met at Geneva from 13 to 31 May 1985. Negotiations concentrated on the resolution of the main issues outstanding in chapters 4 and 9, as the other issues (definition of international transfer of technology transactions, formulation of obligation of confidentiality, international institutional machinery) would most probably have been quickly resolved. However, no satisfactory solution could be found to the issue of the treatment of restrictive practices between parent and subsidiary enterprises. The Conference adopted a decision requesting the General Assembly to take the measures necessary for further action, including the possibility of reconvening negotiations on the International Code of Conduct. The General Assembly, on 3 December 1985, requested the Secretary-General of UNCTAD and the President of the Conference to consult with regional groups and Governments on the question. The Secretary-General of UNCTAD is to report to the forty-first session of the General Assembly which will then decide on the action to be taken in the matter.

### B. UNCTAD: policies on the transfer, acquisition and development of technology

87. In response to resolution 20 (IV), adopted at the fourth session of the Committee on Transfer of Technology (December 1984), the UNCTAD secretariat prepared three reports, namely "Reports on UNCTAD activities in the development and transfer of technology: promotion and encouragement of technological innovation: policies and instruments for the promotion and encouragement of technological innovation", (TD/B/C.6/123) and two documents in the "Restructuring the Legal Environment" series, "Periodic report on policies, laws and regulations conducive to development, transfer and acquisition of technology", (TD/B/C.6/111 and Corr.1); and "Effects of legislation and regulations on transfer of technology: an analysis of the experience of Nigeria and Portugal", (TD/B/C.6/112).

88. Having considered these studies, the Committee at its fifth session requested the UNCTAD secretariat to



continue studies on national laws and regulations relating to the transfer, application and development of technology. By the same resolution, the Committee requested the secretariat, in co-operation with other institutions concerned, to continue its studies of policies and instruments for the promotion and encouragement of technological innovation in all countries, and particularly in developing countries. These studies will be considered at the Committee's sixth session, tentatively scheduled for 27 October to 7 November 1986.

### C. *UNIDO/ICPE: guarantee and warranty provisions in transfer of technology contracts*

89. A guide to the guarantee and warranty provisions in transfer of technology contracts, which has been elaborated by UNIDO and ICPE, is being finalized. This guide will take into consideration the developing country recipients' point of view. It will include draft individual guarantee and warranty clauses, reflecting the present legal situation and contractual practices, as well as the main problems and possible solutions.

### D. *UNIDO: Technological Information Exchange System (TIES)*

90. Within the framework of TIES and upon the request of the annual meetings of the Heads of Technology Transfer Registries, the following UNIDO documents have been issued to meet the needs in developing countries for guidance on the contractual arrangements in specific sectors where the transfer of technology to developing countries has been expanded considerably:

(a) "Licensing computer software. Basic considerations as to protection and licensing of computer software and its implications for developing countries" (ID/WG.383/3);

(b) "Contractual arrangements for the transfer of technology in the fast food industry" (ID/WG.405/2);

(c) "Contractual arrangements for the transfer of technology in the hotel industry" (ID/WG.405/1); and

(d) "Trends and issues in contractual arrangements in the food-processing industry" (ID/WG.429/6).

### E. *UNCITRAL*

91. As part of its report on current activities of international organizations related to the harmonization and unification of international trade law, the secretariat of UNCITRAL prepared a report on the activities of international organizations within the United Nations system relating to the legal aspects of technology transfer (A/CN.9/269).

## VI. *Industrial and intellectual property law*

### A. *Intellectual property activities*

#### 1. *WIPO*

92. During 1984, the International Bureau of WIPO continued to promote acceptance by States of the Convention Establishing the World Intellectual Property Organization 1967 (WIPO Convention) (WIPO publication number 251) and of the other treaties administered by WIPO. Discussions on such acceptance took place during WIPO missions to States, particularly missions for the purposes of development co-operation, and in other contacts with government representatives. Notes concerning the advantages of acceptance of particular treaties by particular countries were prepared and sent to the competent authorities of the countries concerned.

93. In 1984, Cyprus, New Zealand and Venezuela deposited their instruments of accession to the WIPO Convention, bringing the number of members of WIPO to 109. In addition, 15 States which have not yet become members of WIPO are party to one or more of the treaties administered by WIPO.

#### 2. *WIPO: activities of particular interest to developing countries*

94. WIPO's work in this area has as its objective the assisting of developing countries in the establishment or modernization of their industrial property systems in the areas of specialist training, creating or improving domestic legislation, creating or improving government institutions, stimulating domestic inventive activity, stimulating the acquisition of foreign patented technology, creating a corps of practitioners, and exploiting technological information contained in patent documents. In 1984 WIPO received 486 applications for training in industrial property.

95. WIPO continued to co-operate with Governments or groups of Governments of developing countries in the adoption of new laws and regulations or in the modernization of existing ones in the field of industrial property. WIPO also co-operated with government and regional institutions in the creation or modernization of industrial property institutions, including their patent documentation and information services.

96. A number of training courses and seminars on the development of the effective use of the industrial property system for the benefit of inventors, the industry and the commerce of developing countries were organized by WIPO.

#### 3. *UNCTAD*

97. UNCTAD continues to examine the economic, commercial and development aspects of the industrial property system, patents and trademarks. It is also contributing to the current revision of the Paris Convention for the Protection of Industrial Property (Act of

Stockholm, 1967) (WIPO publication number 201). At its fifth session in December 1984, the Committee on Transfer of Technology, by resolution 28 (V), invited the Secretary-General of UNCTAD, in consultation with regional groups, to convene, as appropriate, a meeting of the Group of Governmental Experts on the Economic, Commercial and Developmental Aspects of Industrial Property in the Transfer of Technology to Developing Countries.

#### 4. ICC: counterfeiting

98. ICC has established a Counterfeiting Intelligence Bureau. Its purpose is to investigate and seek to prevent the counterfeiting of trademarked goods, as well as of patents, copyrights and industrial designs and models. It also conducts seminars on this issue.

### B. Copyright and neighbouring rights

#### 1. WIPO: activities of particular interest to developing countries

99. The aim of WIPO's work in this area is to assist developing countries in the establishment or modernization of their copyright systems, in training specialists, in creating or modernizing domestic legislation and infrastructure for the administration of such legislation, in stimulating domestic creative activity, and in facilitating access to foreign works protected by copyright owned by foreigners. In 1984, WIPO received 123 applications for training in the fields of copyright and neighbouring rights from 53 developing countries.

#### 2. UNESCO: activities in the area of copyright and neighbouring rights

100. UNESCO's activities in the field of copyright and neighbouring rights comprise, *inter alia*, the application and promotion of international instruments on copyright and on the protection of performers, producers of phonograms and broadcasting organizations concluded under UNESCO's sponsorship and the extension of the geographical field of their application. Among these instruments, the most recent is the Multilateral Convention for the Avoidance of Double Taxation of Copyright Royalties 1979 (WIPO publication number 294).

#### 3. UNESCO/WIPO: joint international service for access by developing countries to works protected by copyright

101. Since 1976 some of the activities in WIPO's permanent programme have concerned fields already covered by the activity of the International Copyright Information Centre of UNESCO. This was particularly the case with regard to access to works of foreign origin. In order to lessen the duplication in their work a Joint International UNESCO/WIPO Service for Access by Developing Countries to Works Protected by Copyright with effect

from 1 January 1981 was established. A Joint UNESCO-WIPO Consultative Committee was also convened to advise the Directors-General of those two organizations on the preparation and implementation of the activities of the joint service.

102. The first ordinary session of the Consultative Committee was held at Paris in September 1981. Following the deliberations of that session, UNESCO and WIPO jointly convened a Working Group on Model Contracts in respect of co-publishing and commissioned works (November 1982). The Joint Consultative Committee held its second session at Geneva in July 1983 and considered the report on the activities of the Joint International UNESCO-WIPO Service since the first session of the Committee.

#### 4. UNESCO: creation of a Committee for International Copyright Funds (COFIDA)

103. The International Fund for the Promotion of Culture, an autonomous financial body under UNESCO, adopted at the April 1981 session of its Administrative Council the Rules of Procedure of the Committee for International Copyright Funds (COFIDA). COFIDA is a subsidiary organ of the Fund and provides, *inter alia*, total or partial financing for copyright royalties when a developing country encounters difficulties in paying for the reproduction, translation, adaptation, broadcast or communication to the public by any other means of works of foreign origin of an educational, scientific, technical, technological or cultural nature. The operations of COFIDA may take various forms, such as loans or technical assistance to developing countries for purposes related to access to protected works of foreign origin. A brochure entitled "Committee for International Copyright Funds" (WIPO/CCC/I/4, CP7-81/CONF.502/COL.3) explaining the aims, objectives, constitution and operation of the Fund was published by UNESCO in 1981.

### C. Guides and model contracts

#### 1. UNESCO: model contracts concerning copyright in printed and audio-visual works

104. In the context of its overall activities in the field of facilitating access by developing countries to protected works and to serve as a link between publishers and copyright holders in various countries, both developed and developing, UNESCO's International Copyright Information Centre has established model contracts, accompanied by comments and guidelines, for use by interested parties in the fields of publication and the granting of rights as follows:

(a) "Model contract for the publication of a reproduction of an edition of a work" and "Model contract for the publication of the translation of a work", both to be found in UNESCO 081;

(b) "Model contract for the licensing of rights in a work for the purpose of sound recording";

(c) "Model contract for the licensing of motion picture rights";

(d) "Guidelines for the preparation of contracts for translation, reproduction and other rights required by developing countries".

## 2. UNESCO/WIPO: model provisions for national laws on publishing contracts for literary works

105. UNESCO and WIPO jointly convened a Working Group on Model Provisions for National Laws on Publishing Contracts for Literary Works (Geneva, June 1984). The draft model provisions, as revised by the two secretariats in the light of the recommendations of the Working Group, were to be submitted to a committee of governmental experts in December 1985 for adoption.

## 3. WIPO: guides on industrial property and licensing

106. The WIPO *Guide on the Industrial Property Activities of Enterprises in Developing Countries* (WIPO publication number 659) has been issued as a sales publication. A revised edition of the WIPO *Directory of Associations of Inventors* (1984 edition) (WIPO publication number 622) and a brochure entitled "The problems encountered by inventors" (WIPO publication number 711) were published in May 1984.

107. A Group of Consultants on the Revision of the WIPO *Licensing Guide for Developing Countries* (WIPO publication number 620) met at Geneva in June 1984. The Group consisted of 14 persons either selected by the Director-General of WIPO or designated, upon his invitation, by Governments and international organizations. The meeting of the Group of Consultants discussed the *Guide* in detail and gave advice on how to revise and update it in preparation for a new edition.

## VII. International payments

### A. Documentary credits

#### 1. ICC

108. ICC introduced a revised version of its *Uniform Customs and Practice for Documentary Credits* (1983 Revision, ICC Document No. 400) with effect from 1 October 1984. These rules and guidelines can be applied to letter of credit operations.

109. The ICC Commission on Banking Technique and Practice has published the "Draft ICC publication on documentary credit forms" (Document No. 470/455), for adoption by the ICC Executive Board. The forms are intended for use by banks and credit applicants in documentary credit operations.

## 2. UNCITRAL

110. At its seventeenth session UNCITRAL commended the use of the 1983 revision of the Uniform Customs and Practice for Documentary Credits (UCP), as from 1 October 1984, in transactions involving the establishment of a documentary credit.

### B. UNCITRAL: draft Convention on International Bills of Exchange and International Promissory Notes

111. At its seventeenth session (1984) UNCITRAL had before it an analytical compilation of the comments by Governments and international organizations on the draft Convention on International Bills of Exchange and International Promissory Notes and the draft Convention on International Cheques and a note by the secretariat indicating the major controversial issues in the draft Conventions (A/CN.9/248, 249 and Add. 1). At that session the Commission put the work of revising the draft Convention on International Bills of Exchange and International Promissory Notes in the light of the discussions at the seventeenth session and the comments by Governments and international organizations into the hands of the Working Group of International Negotiable Instruments. Work on the draft Convention on International Cheques was postponed and a decision on future work in its regard will be taken after the work on the draft Convention on International Bills of Exchange and International Promissory Notes is completed.

112. The Working Group concluded its work on the revision of the draft Convention mentioned at its fourteenth session in December 1985 (see report of the session A/CN.9/273). The revised version of the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/274) will be considered by the nineteenth session of UNCITRAL (June-July 1986).

### C. Hague Conference on Private International Law: negotiable instruments

113. The Hague Conference is considering drafting conflict of laws rules on the law applicable to negotiable instruments. The following documents on this topic have been prepared: "Note on the law applicable to negotiable instruments" (prel. doc. No. 1) and "Note on the preparation of a convention on the law applicable to negotiable instruments" (prel. doc. No. 3). They were submitted to the Special Commission on General Matters and Policy of the Hague Conference in January 1984 and to the fifteenth session of the Conference in October 1984.

114. A report on this subject is being prepared; its timing will depend on the progress made in the work of

UNCITRAL. A final decision on whether to open the Conference to non-member States in order to discuss this topic remains to be made by the member States of the Conference.

#### **D. UNCITRAL: electronic funds transfers**

115. At its fifteenth session in 1982, UNCITRAL requested its secretariat to begin the preparation of a legal guide on electronic funds transfers in co-operation with the UNCITRAL Study Group on International Payments. Several chapters were submitted to the Commission at its seventeenth session in 1984 (A/CN.9/250 and Add. 1 to 4), and the remaining chapters were submitted to the Commission at its eighteenth session in 1985 (A/CN.9/266 and Add. 1 and 2).

116. The Commission, at its eighteenth session, requested the Secretary-General to transmit the legal guide on electronic funds transfers to Governments and interested international organizations in order to obtain their comments. It also requested the secretariat, in co-operation with the UNCITRAL Study Group on International Payments, to revise the draft legal guide in the light of the comments received from Governments and international organizations. The draft legal guide, revised in the light of the aforementioned comments, is being submitted to the nineteenth session of UNCITRAL, June-July 1986 (A/CN.9/278).

#### **E. CMEA: model principles for trade and payment**

117. The CMEA Executive Committee in 1984 approved the Individual Model Principles for Trade and Payment Agreements (Protocols), worked out by the CMEA Conference on Legal Questions, in order that the CMEA member countries might apply them as they see fit when concluding specific agreements (protocols) on trade and payment. These principles may also be appropriately incorporated into other agreements on economic and scientific-technical co-operation.

### **VIII. International transport**

#### **A. Transport by sea and related matters**

##### **1. UNCTAD: United Nations Conference on Conditions for Registration of Ships**

118. The United Nations Conference on Conditions for Registration of Ships was convened in 1985 pursuant to General Assembly resolutions 37/209 of 20 December 1982 and 39/213-A of 18 December 1984 in order to consider the adoption of an international agreement covering the conditions under which vessels should be accepted on national shipping registers. Pursuant to

General Assembly resolution 39/213-B of 12 April 1985, a further two-week session of the Conference was held between 8 and 19 July 1985, at the end of which a report containing a draft of an international agreement on conditions for the registration of ships was approved (TD/RS/CONF/19 and Add.1). The Conference met again from 20 January to 7 February 1986. On 8 February 1986, the Final Act of the Conference adopting the Convention was signed by representatives of 86 States ("Final Act of the United Nations Conference on Conditions for Registration of Ships", TD/RS/CONF/22). The Convention will be open for signature from 1 May 1986 to 30 April 1987. The Convention will enter into force when it has been ratified by 40 States representing 25 per cent of relevant gross registered tonnage.

##### **2. UNCTAD: Convention on a Code of Conduct for Liner Conferences**

119. The Convention on a Code of Conduct for Liner Conferences (TC/CODE/13/Add.1, United Nations publication, Sales No. 75.II.D.12) entered into force on 6 October 1983. Its fundamental objectives are: (a) to facilitate the orderly expansion of world sea-borne trade; (b) to stimulate the development of regular and efficient liner services adequate to the requirements of the trade concerned; and (c) to ensure a balance of interests between suppliers and users of liner shipping services. In addition, three basic principles are specified in the Convention: (a) that conference practices should not involve any discrimination against the shipowners, shippers or the foreign trade of any country; (b) that conferences should hold consultations with shippers' organizations, shippers' representatives and shippers on matters of common interest, with, upon request, the participation of appropriate authorities; and (c) that conferences should publish and make available to interested parties pertinent information about their activities.

120. In line with these objectives and principles, the Code deals with, *inter alia*, the relationships between member lines of conferences and principles for the participation by member lines in the trade carried by conferences. This it does by establishing equitable principles for the use of loyalty arrangements, as well as requirements that conferences may be compelled to hold consultations with shippers or their representative organizations on matters of concern to shippers, such as changes in freight rates, loyalty arrangements and the imposition of surcharges. The Code also contains provisions dealing with the establishment of pools and other types of trade-sharing arrangements in conferences. Furthermore, it regulates freight rate increases, promotional freight rates, surcharges and currency adjustment factors.

121. To ensure the smooth functioning of the Code, the machinery for a system of dispute settlement based on conciliation is established. The Code requires that a Review Conference be convened five years from the date on which the Convention comes into force in order to

reconsider the Convention, with particular regard to its implementation and in order to adopt any appropriate amendments. Before that Review Conference, any problems encountered with the implementation of the Convention will be considered by the Committee on Shipping of UNCTAD at its twelfth session (in November 1986).

122. As of November 1985, 40 countries had acceded to the Convention, two had approved it, one had accepted and five had given definitive signatures.

### 3. IMO: liability and compensation for oil pollution damage

123. The preparatory work on the revision of the International Convention on Civil Liability for Oil Pollution Damage 1969 (IMO sales number 77.16) and the International Convention for the Establishment of an International Fund for Compensation for Oil Pollution Damage 1971 (IMO sales number 72.10), carried out by the Legal Committee of IMO, culminated in the adoption of an amending Protocol to each of the two Conventions (LEG. 53.6) by a diplomatic conference convened under the auspices of IMO in May 1984 (see also 1976 Protocols, IMO sales number 77.05). The two 1984 Protocols' most important feature is the introduction of substantially higher limits of compensation for oil pollution damage as compared to the limits set out in the two Conventions. A new minimum liability for shipowners has been set at SDR 3 million, and the maximum compensation available to victims from the shipowner and the Fund will be initially SDR 135 million but will reach SDR 200 million when certain conditions are met. Another important change is the adoption of a simplified system for amending the various liability and compensation limits introduced by the two Protocols. The solution chosen is based to a considerable extent upon the provisions of the unit of account and the adjustment of the limit of liability adopted by UNCITRAL at its fifteenth session and recommended by the General Assembly for use in the preparation of future international conventions containing limitations of liability provisions or in revisions of existing ones (General Assembly resolution 37/107 of 16 December 1982). (For the text of the unit of account and limitation of liability provisions see "Report of the United Nations Commission on International Trade Law on the work of its seventeenth session", *Official Records of the General Assembly, Thirty-ninth Session, Supplement No. 17 (A.39/17)*).

124. The diplomatic conference referred to above also had before it a draft Convention on liability in connection with the carriage of noxious and hazardous substances by sea (LEG/CONF.6/3 and LEG.55.5). The conference, while recognizing the need for an international agreement on this question, concluded that it was not feasible in the time available to resolve the many complex issues and decided, accordingly, to refer the draft Convention back to IMO for further consideration. The Council and the Legal Committee of the IMO are currently examining the question of how best to proceed in this matter.

### 4. UNCTAD: charter-parties

125. The report by the UNCTAD secretariat entitled *Charter-parties* (United Nations publication, Sales No. E.74.II.D.12), was discussed by the Working Group on International Shipping Legislation at its fourth session (27 January to 7 February 1975). This document examines the principal clauses in voyage and time charter-parties and suggests, *inter alia*, that such clauses be standardized and that the introduction of mandatory international legislation on certain aspects of the liability of the shipowners and charterer be considered. In accordance with the work programme adopted at its eleventh session (decision 52(XI) of 30 November 1984), the UNCTAD Working Group on International Shipping Legislation will consider the additional studies that are now in progress in the UNCTAD secretariat and will decide what future action on the subject of charter-parties should be taken.

### 5. UNCTAD: marine insurance

126. The Committee on Shipping, at its tenth session in June 1982, gave priority to the subject of marine hull and cargo insurance in the work programme of the Working Group on International Shipping Legislation (resolution 49(X)). By the end of the ninth session of the Working Group, its subgroup of experts, established for the purpose of drawing up a set of standard model marine hull and cargo insurance clauses, had formulated two alternative composite texts for hull insurance. As for cargo insurance, three alternative sets of clauses had been drafted.

127. The UNCTAD secretariat prepared two reports for the tenth session (September 1984) of the Working Group, one entitled "Marine hull insurance: working paper to assist in the drawing up of a set of standard hull clauses" (TD/B/C.4/ISL/41), and the other on marine cargo insurance entitled "Marine cargo insurance: working paper to assist in the drawing up of a set of standard cargo clauses" (TD/B/C.4/ISL/42).

128. At that session of the Working Group, the subgroup completed the drafts of the model clauses both in respect of hull and of cargo insurance. On hull insurance, two alternative sets of clauses were formulated, one on an "all risks minus exception" basis and the other on a "named perils" basis, each containing provisions on basic coverage, general exclusions, period of coverage, duties of the assured, measure of indemnity, claims settlement and extended cover clause. On cargo insurance three sets of clauses have been drafted providing "all risks", "intermediate" and "restricted" coverage, respectively, and each including provisions on basic coverage, general exclusions, additional coverage, period of coverage, measure of indemnity, and insurable interests.

129. The Working Group adopted the texts of the model clauses on marine hull and cargo insurance subject to the corrections to them which were to be communi-

cated in writing to the UNCTAD secretariat and on the understanding that the corrected texts would be examined by the competent experts during the eleventh session (1984) of the Committee on Shipping. The final texts of the model clauses prepared by the Rapporteur of the Working Group on the basis of amendments proposed by various delegations and in consultation with insurance experts ("UNCTAD model clauses on marine hull and cargo insurance", TD/B/C.4/ISL/50) have been circulated to the member States of UNCTAD, drawing their attention to the amendments made by the Rapporteur and inviting them to provide comments thereon, if any. The Committee on Shipping at its twelfth session in November 1986 will consider a report of the comments received and will request the appropriate action of the Board.

#### 6. IMO: salvage

130. The question of salvage and assistance at sea was placed on the agenda of the Legal Committee of IMO in the wake of the *Amoco Cadiz* disaster. In 1984 the Committee began work on this issue, basing its deliberations on the text of a draft Convention prepared by the CMI which was designed to revise and replace the 1910 Convention on Salvage and Assistance at Sea. The revised draft text appears in document LEG 52/3 (see also the "Note by the secretariat" on the revised draft text LEG 54/INF.2).

131. In addition, the Committee is examining various public law aspects arising in connection with salvage, including a possible obligation of ship-masters to notify casualties to coastal States, and the need to grant powers to coastal States to intervene in salvage operations that pose hazards of environmental damage to their coastal and related interests.

#### 7. UNCTAD: maritime fraud

132. The UNCTAD secretariat prepared "International maritime legislation - future work: report by the UNCTAD secretariat" (TD/B/C.4/244), which reviewed the activities of other organizations relevant to the subject of maritime fraud, briefly analysed the nature of the problem and set out possible courses of action to suppress maritime fraud, for the tenth session of the Committee on Shipping. By resolution 49(X), adopted in 1982, the Committee established an *Ad Hoc* Intergovernmental Group to Consider Means of Combating All Aspects of Maritime Fraud, Including Piracy.

133. At its first session held from 6 to 17 February 1984, the *Ad Hoc* Intergovernmental Group had before it a report prepared by the UNCTAD secretariat entitled "Review and analysis of possible measures to minimize the occurrence of maritime fraud and piracy" (TD/B/C.4/AC.4/2). The *Ad Hoc* Intergovernmental Group requested the UNCTAD secretariat, in collaboration with the appropriate intergovernmental and non-govern-

mental organizations and the commercial parties concerned, to carry out studies to be submitted to the second session. Those studies were to focus on the feasibility of improving the effectiveness of the administrative and legal procedures of prosecuting authorities with regard to, *inter alia*, the jurisdiction of States and extradition, the formulation of a set of guidelines for the international banking community, the feasibility of a banking super-service scheme, minimum standards for shipping agents and the availability of shipping information ("Maritime fraud: piracy: the feasibility of improving the administrative and legal procedures of prosecuting authorities in cases of maritime fraud" (TD/B/C.4/AC.4/8), "Maritime fraud: preliminary report on the feasibility of a bank super-service" (TD/B/C.4/AC.4/7)).

134. In addition to the studies mentioned, the UNCTAD secretariat also prepared a report for the second session of the *Ad Hoc* Intergovernmental Group of various studies of the means of combating maritime fraud that have been undertaken by specialized international and commercial organizations, alone or in co-operation with UNCTAD. The second session of the *Ad Hoc* Intergovernmental Group met at Geneva from 23 October to 1 November 1985 (the report appears in TD/B/C.4/296-TD/B/C.4/AC.4/10). It requested the Trade and Development Board to authorize the carrying out of certain studies by the UNCTAD secretariat in preparation for the twelfth session of the Committee on Shipping to be held from 10 to 21 November 1986.

#### 8. UNCTAD/IMO/CMI: maritime liens and mortgages

135. The Committee on Shipping at its tenth session in 1982 decided to give priority to the subject of maritime liens and mortgages priority (resolution 49 (X)). "Analysis of progress in possible reforms in the existing international régime of maritime liens and mortgages" (TD/B/C.4/ISL/52 and Corr.1) was issued by the UNCTAD secretariat pursuant to that resolution and discussed by the Working Group on International Shipping Legislation at its tenth session.

136. The Working Group urged the UNCTAD secretariat to carry out a study of the economic aspects of maritime liens and mortgages and proposed that the International Convention for the Unification of Certain Rules relating to Maritime Liens and Mortgages 1976 (IMO/LEG 55/4) should be taken as the basis for future work and discussion.

137. Consultations between UNCTAD and IMO took place in order to decide how best the organizations could deal with the various aspects of the subject-matter without duplication. It has been agreed that IMO will undertake studies on those aspects of maritime mortgages that are essentially ship-related, such as the entry and the cancellation of mortgages on national shipping registers. IMO will also carry out studies on maritime liens, particularly in respect of the existing practices, including

the need and desirability of maintaining lien status for claims currently enjoying such status, the ranking of different maritime liens *inter se* and the possibility of extending lien status to other types of claims.

138. Draft revisions of the Conventions on maritime liens and mortgages and arrest were considered and adopted by the XXXIII International Conference of CMI held between 19 and 25 May 1985 at Lisbon. CMI has noted, however, that under the Agreement between IMO and UNCTAD a new method of dealing with maritime liens and mortgages and related subjects has been adopted by the two intergovernmental bodies. The two organizations, themselves, have expressly stated that they will take due and full account of the conclusions reached by CMI in their studies to determine the need for international legislation or other appropriate action and the scope of such action. Accordingly, the reports of CMI on the draft Conventions on maritime liens and mortgages and arrest were circulated to the participants of its Working Group on International Shipping Legislation by UNCTAD in October 1985 (the reports are contained in TD/B/C.4/ISL/L.79).

139. The UNCTAD Working Group on International Shipping Legislation, by a resolution adopted at its eleventh session in October 1985, proposed that the Trade and Development Board convene, jointly with IMO, an intergovernmental group of experts to examine the subject of maritime liens and mortgages. The UNCTAD Working Group has proposed that that examination of mortgages and liens include a review of the Conventions in their regard and related enforcement procedures such as arrest and the preparation of model laws or guidelines on maritime liens, mortgages and arrest. The intergovernmental group of experts should also consider the feasibility of an international registry of maritime liens and mortgages. The Legal Committee of IMO is reviewing this proposal. Its views and recommendations will be reported to the IMO Council for consideration and decision at the Council's fifty-sixth session to be held in June 1986.

#### 9. UNCTAD: maritime law

140. On 1 April 1982 the UNCTAD secretariat issued a "Draft outline of a model code for maritime legislation" that can be used as a guide by developing countries in elaborating their own national laws (TD/B/C.4/244, annex II). UNCTAD intends to develop those sections of the model code dealing with the economic and commercial aspects of shipping.

#### 10. UNCTAD: regional associations and joint ventures in the field of maritime transport

141. The UNCTAD secretariat is studying the feasibility of creating and strengthening regional associations of ports, shippers, shipowners and maritime authorities for the purpose of co-operating and harmonizing policies and practices. UNCTAD is also carrying out a study of the

feasibility of projects involving joint ventures or multinational shipping companies in the fields of shipping and port facilities in developing countries. These studies may ultimately result in the preparation of model rules for regional associations and joint ventures.

142. On 26 September 1984 UNCTAD issued the report "Draft programme of action for co-operation among developing countries in the area of shipping, ports and multimodal transport" (TD/B/C.4/273) (see also "Draft report of the *Ad Hoc* Intergovernmental Group of Port Experts on its session from 25 February to 5 March 1986", TD/B/C.4/AC.7/L.1 and Add.1)

#### 11. UNCTAD: treatment of foreign merchant vessels in ports

143. In response to the Committee on Shipping's request in that regard, made at its seventh session, the UNCTAD secretariat prepared a note in 1977 entitled "Economic co-operation in merchant shipping. Treatment of foreign vessels in ports" (TD/B/C.4/158). As a number of developments on some elements of the subject were under consideration in other international organizations, the note suggested that the Committee on Shipping might not wish to make a final decision at that stage as to whether there was a need to revise the 1923 Convention and Statute of the International Régime of Maritime Ports, or to prepare a new international convention on the treatment of foreign merchant vessels in ports. Subsequently, the Committee on Shipping by its resolution 49(X) adopted at the tenth session in 1982, requested that the UNCTAD secretariat submit a report regarding regional arrangements for the treatment of merchant vessels in ports. This was done and the report is entitled "Industrial maritime legislation. Treatment of merchant vessels in ports at the regional level" (TD/B/C.4/275). The report provides a summary of replies to the note verbale of the Secretary-General of UNCTAD requesting Governments to provide information on any arrangements which might be in force in their national ports, or on such arrangements in force in foreign ports, which affect vessels flying their national flag. The report makes reference to the Memorandum of Understanding on Port State Control, 1982, as elaborating the only such existing arrangement. Having considered that report the Committee on Shipping at its eleventh session in November 1984 requested the member States of UNCTAD to inform the secretariat of UNCTAD and the IMO of the consequences they had noted resulting from the Memorandum of Understanding.

#### 12. ECE: carriage of dangerous goods by inland waterway

144. The ECE is undertaking a revision of the European provisions concerning the international carriage of dangerous goods by inland waterway (ADN) so as to provide a basis for national and international regulations, and to bring those provisions into line with the regulations governing other modes of transport.

**B. ' Transport over land and related issues****1. OTIF: Convention concerning international transport by rail (COTIF)**

145. Participants at a diplomatic conference held at Berne between 15 and 17 February 1984 brought into force on 1 May 1985 the Convention concerning international transport by rail of 8 May 1980 (COTIF), together with its Protocol on the privileges and immunities of the Intergovernmental Organization for International Rail Transport (OTIF). The following were also introduced:

(a) Uniform rules concerning the international rail transport of passengers and luggage (CIV), appendix A, and

(b) Uniform rules concerning the international rail transport of goods (CIM), appendix B, including the following annexes:

*Annex I:* Rules concerning the international rail transport of dangerous goods (RID)

*Annex II:* Rules concerning international rail transport of personal wagons (RIP)

*Annex III:* Rules concerning international rail transport of containers (RICO)

*Annex IV:* Rules concerning international rail transport of express parcels. (RIEX)

146. COTIF and its appendices replace the 1970 International Convention Concerning the Carriage of Goods by Rail (CIM), and the 1970 International Convention Concerning the Carriage of Passengers and Luggage by Rail (CIV) and the additional Convention to CIV of 26 February 1966 relating to the liability of railways for death of and personal injury to passengers.

147. The members of the International Rail Transport Committee (CIT) include some 300 transport enterprises (rail transport, road transport and navigation) from 33 countries in Europe, the Near East, the Middle East and North Africa which are parties to COTIF. The task of CIT is to develop international railway transport law on the basis of COTIF and its appendices A and B, CIV and CIM respectively. The purpose of the CIT is also to provide for the uniform regulation of other issues concerning international rail transport law.

148. Envisaging the coming into force of COTIF, CIT prepared a set of uniform rules for the implementation of the Convention and its appendices A and B (CIV and CIM) for the use of transport enterprises. These rules consist of regulations binding the transport enterprises and their users and of agreements either regulating in a mandatory way the relationships among the transport enterprises or being only of an indicative character.

149. CIT is preparing a study concerning the legal requirements of a substitution of the rail consignment note by another instrument which would enable the use of automatic data processing.

**2. UNIDROIT: civil liability for damage caused by hazardous cargoes**

150. The UNIDROIT Committee of Governmental Experts for the preparation of uniform rules relating to liability and compensation for damage caused during the carriage over land of hazardous substances has held six sessions at Rome since 1981. The Committee decided to restrict the sphere of application of the future uniform rules to liability and compensation for damage caused during the carriage of hazardous substances by road, rail and inland navigation vessels and, in consequence, rejected a suggestion to also cover transmission of hazardous substances by pipelines. It has agreed, for the time being, not to endorse a proposal to broaden its terms of reference to cover liability for damage resulting from the carrying out of dangerous activities in general.

151. Various amendments have been made to the original draft and a series of alternative texts introduced into it. At its sixth session, held in October 1984, the Committee completed its second, and began its third reading of the preliminary draft Convention and also gave further consideration to the question of the list of substances to which the future Convention should apply and which should be annexed to it, in the light especially of the findings of a joint working group of technical and legal experts which met at Rome in March 1984. A revised version of the draft articles for a Convention was prepared in February 1985 (Study LV-DOCs. 61, 62 and 65).

152. With a view to seeking solutions to a number of problems in respect of which differences of opinion have emerged between the UNIDROIT Committee of Governmental Experts and the Inland Transport Committee of ECE, a meeting of experts drawn from the membership of the two committees was held in November 1985. A report of that meeting (Study LV-Doc. 64) will be before the UNIDROIT committee which will reconvene for its seventh session in May 1986. It is hoped that work within UNIDROIT on the prospective Convention will be completed either at that session or at one to be held later on in the year.

153. The Inland Transport Committee of ECE was involved in the initiation of this work and is currently participating in the elaboration of the draft Convention.

**C. ICAO: transport by air and other related matters**

154. At its twenty-fifth session the ICAO Legal Committee, which met at Montreal from 12 to 27 April 1983, reviewed the status of the instruments of the "Warsaw System" (Warsaw Convention 1929) relating to the international carriage of passengers, cargo and mail by air and adopted a decision urging States to ratify the Montreal Protocols of 1975. That session also reviewed the general work programme of ICAO in the legal field. This programme was subsequently approved by the ICAO



Council on 3 June 1983 and confirmed by the twenty-fourth session of the Assembly of ICAO that was held in September and October of 1983. One of the items in the programme was the proposed ICAO secretariat paper entitled "Study of the instruments of the Warsaw System".

155. The purpose of that study is to present an historical background to the item "Study of the status of the instruments of the 'Warsaw System'" in the general work programme of the Legal Committee, to describe briefly the characteristics of the different components of that system and also to outline the outstanding problems in the international carriage of passengers, baggage and cargo.

156. The Panel of Experts on the General Work Programme of the Legal Committee concluded that no further work should be done with respect to this item except that an exchange of information between countries should take place; the Council agreed with that approach. In view of that conclusion, it was suggested that a questionnaire be sent to the appropriate government bodies and international organizations to enable the twenty-sixth session of the Legal Committee, meeting in 1986, to arrange an appropriate exchange of information among States.

157. The questionnaire asked Governments for the reasons, if any, preventing them from becoming parties to the Guatemala City Protocol, 1971, the Additional Protocols Nos. 1, 2, and 3, 1975, and the Montreal Protocol No. 4, 1975. Governments were also asked whether, pending the implementation of those instruments, they had taken any unilateral steps (a) to adjust the limits of liability with respect to air passengers of national and/or foreign carriers and (b) to regulate the conversion of the "gold clause" into national currency. The questionnaire also requested information regarding the action that countries would support in order to remove any practical difficulties experienced with the instruments of the "Warsaw System". Finally, Governments were asked whether they saw a possibility of conflict between the instruments of the "Warsaw System" and the United Nations Convention on International Multimodal Transport of Goods, 1980, and, if so, what the solution to that conflict might be.

#### **D. UNCITRAL: liability of operators of transport terminals**

158. UNCITRAL is currently formulating uniform legal rules on the liability of operators of transport terminals. These rules will be designed to establish a uniform international legal régime governing the liability of terminal operators in respect of goods involved in international transport. They are intended to fill the gaps in the liability régimes left by international transport conventions governing the liability of carriers in respect of such goods. This work, which is based in part on a preliminary draft

Convention on Operators of Transport Terminals, adopted by UNIDROIT in 1983, has been assigned to the UNCITRAL Working Group on International Contract Practices.

#### **E. UNCTAD: rights and duties of container terminal operators**

159. The UNCTAD secretariat has prepared a study on this subject which will be presented to the twelfth session of the UNCTAD Committee on Shipping to be held from 10 to 16 November 1986.

#### **F. UNCTAD/UNCITRAL: promotion of the Multimodal Transport Convention and the Hamburg Rules**

160. With the collaboration of the secretariat of UNCITRAL, the UNCTAD secretariat is preparing a booklet on the United Nations Convention on International Multimodal Transport of Goods (1980) (TD/MT/CONF/16) ("Multimodal Convention"), elaborated by UNCTAD, and the United Nations Convention on the Carriage of Goods by Sea (1978) (A/CONF.89/13) ("Hamburg Rules"), elaborated by UNCITRAL. The booklet will be designed to promote more widespread international acceptance of those two Conventions by explaining their objectives, features and implications.

161. At the twenty-fifth session of AALCC, held from 3 to 10 February 1984, the Trade Law Sub-Committee of AALCC recommended that member States consider ratifying the Hamburg Rules. The Organization of American States, at its Third Interamerican Conference on Private International Law, held from 15 to 24 May 1984, also recommended that its member States ratify or accede to the Hamburg Rules.

162. By 1 February 1985, four States had become contracting parties to the Multimodal Convention and three States had signed it subject to ratification. Thirty States are required for the Convention to come into force. By 31 March 1986, 11 States had ratified or acceded to the Hamburg Rules, while 25 States had signed the Convention. Twenty parties are required for the Hamburg Rules to come into force.

163. In its resolution 40/71 on the report of UNCITRAL on the work of its eighteenth session, the United Nations General Assembly stressed the importance of bringing into effect the Conventions resulting from the work of UNCITRAL, including the Hamburg Rules.

#### **G. UNCTAD: Northern Corridor Transit Agreement**

164. This Agreement was signed by Burundi, Kenya, Rwanda and Uganda on 19 February 1985 and will come into force 31 days after its ratification by those four countries. The "Northern Corridor" is a term used to describe the transport infrastructure in East Africa that is

served by the port of Mombassa in Kenya and that also extends to Sudan and Zaire. It is a major transport system, linking the latter two countries as well as Burundi, Kenya, Rwanda and Uganda with the ocean. The Agreement enables the most effective route to be used for the surface transport of goods amongst the contracting parties. Under the Agreement, these latter grant each other the right of transit in order to facilitate the movement of goods through their respective territories and promise to provide the facilities necessary for traffic in transit among them.

## H. Container standards

### 1. UNCTAD

165. Having considered the reports of the *Ad Hoc* Intergovernmental Group on Container Standards for International Multimodal Transport (TD/B/AC.20/6 and TD/B/AC.20/10) and the proposals contained therein, the Trade and Development Board decided in March 1980 to remit to the Committee on Shipping the question of container standards and that regarding the possibility of drawing up an international agreement on those standards.

166. In response to a request made in that regard by the Committee on Shipping, the UNCTAD secretariat, in cooperation with IMO and ISO, prepared a note entitled "Review of developments in the standardization of containers and related activities" (TD/B/C.4/270 and Corr. I) which was submitted to the Committee on Shipping at its eleventh session (19 to 30 November 1984). In preparing the note the views of regional commissions and of several governmental and non-governmental organizations were also sought. Having considered that note, the Committee on Shipping requested the Secretary-General of UNCTAD to communicate to ISO the concern of many countries with regard to the proposed increase of the tonnage and the height of containers.

### 2. ISO

167. The ISO Committee on Freight Containers (TC 104) is studying the new features in the standardization requirements arising from the increase in the tonnage and height of containers.

## I. UNCTAD: freight forwarding

168. The UNCTAD secretariat has circulated a report examining freight forwarding operations and services, including applicable legal régimes, as they relate to the promotion of freight forwarding in developing countries (document UNCTAD/SHIP/193), and will continue to keep this area of growing activity under review particularly with regard to its legal aspects. UNCTAD is considering means of combating maritime fraud by the regulation of freight forwarders.

## J. CMI: non-negotiable transport documents

169. At its thirty-third International Conference, held from 19 to 25 May 1985, CMI decided to establish a subcommittee to study potential problems flowing from the arrival of cargo at its destination before the arrival of the relevant bill of lading and the use of non-negotiable documents, such as sea waybills, and new techniques such as electronic data processing or the creation of a central bill of lading registry. The subcommittee is to seek solutions to those problems, possibly through uniform rules or an international convention, taking into account, *inter alia*, the development of a paper-less system.

## IX. International arbitration<sup>a</sup>

### A. UNCITRAL

170. The UNCITRAL Working Group on International Commercial Practices prepared a draft model law on international commercial arbitration during its third, fourth, fifth, sixth and seventh sessions. At its seventeenth session (1984) UNCITRAL requested the Secretary-General to transmit the text of the draft model law to Governments and interested international organizations for their comments.

171. The Commission had before it at its eighteenth session (1985) a report prepared by the secretariat containing an analytical compilation of the comments received (A/CN.9/263 and Add.1-3) and a report of the Secretary-General consisting of a commentary on the draft text (A/CN.9/264). The Commission considered the text of the draft model law in detail and, on 21 June 1985, decided to adopt the Model Law on International Commercial Arbitration (for the terms of the text adopted, see "Report of the United Nations Commission on International Trade Law on the work of its eighteenth session", *Official Records of the General Assembly, Fortieth Session, Supplement No. 17 (A/40/17, annex I)*).

172. The General Assembly recommended in its resolution 40/72 of 11 December 1985, that "all States give due consideration to the Model Law on International Commercial Arbitration, in view of the desirability of uniformity of the law of arbitral procedures and the specific needs of international commercial arbitration practice".

### B. AALCC

#### 1. Consideration of UNCITRAL Model Law on International Commercial Arbitration

173. The AALCC Sub-Committee on International Trade Law Matters, at its twenty-fourth session held at Kathmandu (Nepal) in 1985, examined the draft text of a

<sup>a</sup>A fuller description of the work of international organizations in the area of arbitration can be found in "Co-ordination of work: activities of international organizations on certain aspects of arbitration: report of the Secretary-General" (A/CN.9/280).

model law on international commercial arbitration, as adopted by the UNCITRAL Working Group on International Contract Practices. At its seventh-fifth session held at Arusha (United Republic of Tanzania) in 1986, the Sub-Committee considered and recommended the use of the UNCITRAL Model Law on International Commercial Arbitration, as adopted by the Commission on 21 June 1985.

## 2. *Establishment of regional centres of arbitration in the Asian-African region*

174. The AALCC has established two Regional Arbitration Centres, one at Kuala Lumpur and one at Cairo, and has decided to establish further centres, one in Tehran, one in an East-African State and probably one in a West-African State. The rules of procedure applied by these centres in arbitrations held under their auspices are the UNCITRAL Arbitration Rules of 1976 as supplemented by internal or administrative rules of the Centres.

175. The AALCC has concluded agreements with the World Bank's ICSID for co-operation and assistance under which arbitration proceedings under the ICSID Convention can be held at either of these Regional Centres, if the parties so choose. Similarly, the proceedings in arbitrations under the auspices of either of these Centres can be held on the premises of ICSID, particularly that part of such proceedings involving the recording of evidence of witnesses. These arrangements have been made in order to ensure the prompt resolution of cases, to minimize arbitration costs and for the convenience of the parties.

176. The AALCC and its Kuala Lumpur Centre have also concluded a co-operation agreement with the Tokyo Maritime Arbitration Commission to provide specialized institutional facilities for the resolution of disputes arising out of international maritime contracts. Under this agreement it is possible, where the parties so agree, for that Commission to administer maritime arbitrations on behalf of the Kuala Lumpur Centre.

177. The Kuala Lumpur Centre has also concluded mutual co-operation agreements with the Korean Commercial Arbitration Board, the Indian Council of Arbitration, the Japan Commercial Arbitration Association and the Indonesian Commercial Arbitration Board. Each of these agreements carries the commitment to "co-operate in providing assistance in the enforcement of arbitral awards rendered in arbitral proceedings under the auspices of the Regional Centre or the national institution".

### C. CMEA

178. During the period 1983-1985 the CMEA Conference on Legal Questions continued its study into the practical application of the Convention on Settlement by Arbitration of Civil Law Disputes arising from Economic,

Scientific and Technical Co-operation (26 May 1972). The Conference also examined the use made by the CMEA member countries of the Uniform Rules for Arbitration Tribunals (1974). The intention is to prepare a report on the basis of this work on the application of the 1972 Arbitration Convention and on possible improvements to the 1974 Uniform Arbitration Rules to enable the Conference to agree upon the direction of further work.

### D. FIDIC/ICC

179. In collaboration with ICC and the European International Contractors, FIDIC has compiled lists of experts suitable for appointment as arbitrators in cases where technical expertise is required. These lists will be made available to parties in order to help them in their choice of arbitrators.

### E. Hague Conference on Private International Law

180. The Hague Conference is considering the possibility of extending the applicability of the 1970 Convention on the Taking of Evidence Abroad in Civil or Commercial Matters (Evidence Convention) to arbitration proceedings (see paragraph 233 below).

### F. ICC

181. The ICC Commission on International Arbitration, at its meetings held at Paris on 14 May 1985, 25 October 1985 and 13 March 1986, considered, *inter alia*, the following matters, most of which were being studied by special working parties:

- (a) Draft guidelines and model clauses for multi-party arbitration;
- (b) Establishment of an arbitral referee procedure;
- (c) Review of ICC Conciliation Rules; and
- (d) Study of practice of interim and partial awards and dissenting opinions.

182. ICC is preparing a second volume on arbitration laws to follow on the "Guide to Arbitration Law in Europe" (ICC publication No. 353). This second volume will cover the Far East and the Pacific and is expected to be published in 1986.

### G. ICCA

183. The ICCA continues to publish the *Yearbook Commercial Arbitration*. The *Yearbook*, which provides comprehensive and up-to-date world-wide information on commercial arbitration, entered its tenth volume in 1985. The contents of this volume include national reports on arbitration law and practice, national court decisions on the application of the New York Conven-

tion, 1958, arbitral awards from arbitral institutions and *ad hoc* arbitrations.

184. In 1983, the ICCA started its *Congress Series*, publishing the papers of the VIIth Congress, held at Hamburg from 7 to 11 June 1982, and having as its subject "New trends in the development of international commercial arbitration and the role of arbitral and other institutions". In 1984 the papers of ICCA's Interim Meeting on "UNCITRAL's project for a model law on international commercial arbitration", held at Lausanne from 9 to 12 May 1984, were published in *Congress Series No. 2*.

185. In 1984 ICCA launched the *International Handbook on Commercial Arbitration*, a loose-leaf series of national reports on arbitration law and practice, that updates and completes what is already published in the *Yearbook* by including the text of arbitration laws and other basic legal materials. The first issue of the *Handbook* and the two supplements to it published in 1984 cover reports on 20 countries, complete with relevant legal texts. Supplements to the *Handbook*, including updatings of existing basic work, will appear regularly each year until about 60 countries of interest to international commercial arbitration are covered.

186. Under the auspices of ICCA, the VIIIth International Arbitration Congress will be held in New York between 6 and 9 May 1986 and will discuss the following two themes: (a) comparative arbitration practices, and (b) public policy and arbitration. The papers of the meeting will be published by ICCA in *Congress Series No. 3*.

## X. Products liability: EEC

187. On 26 July 1985 the Council of Ministers of the European Communities adopted a directive on the approximation of the laws, regulations and administrative provisions of the member States relating to liability for defective products (OJ No. L 210, p. 29). This directive aims at removing distortions in the comparison of the competitiveness of products resulting from differences in national rules wherein the re-sale prices of a product are higher in those countries where the rules are stricter. It also seeks to eliminate certain barriers to the free movement of goods and to reinforce consumer protection.

## XI. Private international law

### A. EEC

188. The EEC Convention on the Law Applicable to Contractual Obligations 1980 (OJ No. L 266, 9.10.1980, p. 1) constitutes a logical complement to the Brussels Convention on Jurisdiction and Enforcement of Court Decisions in Civil and Commercial Matters 1968 (OJ No. L 304, 30.10.1978, p. 77). Having dealt with conflicts of

jurisdiction it was necessary to deal with conflicts in the applicable law in order to increase legal certainty within the EEC, to facilitate exchanges and to avoid "forum shopping". With this in mind the measures provided for facilitate the determination of the law applicable and seek to ensure that all the courts of EEC member States will apply the same law to identical cases between the same parties.

### B. Hague Conference on Private International Law

189. The fifteenth session of the Hague Conference, held at The Hague from 18 to 20 October 1984, decided to retain in the agenda for future work of the Conference the question of the law relating to conflict rules in respect of contractual obligations and to leave to the Secretary-General of the Conference the responsibility of deciding whether or not to convene a working group to explore the subject. The same session of the Hague Conference also decided to retain on the agenda for future work of the Conference the study in liaison with the international organizations concerned, in particular WIPO, of conflict rules for licensing and know-how agreements.

190. An exploratory study on the preparation of rules dealing with conflicts of laws occasioned by transfrontier data flows is under preparation by the Hague Conference. This study is to be undertaken in liaison with the international organizations concerned, in particular UNCITRAL. (See also paragraphs 115 and 116.)

### C. Hague Conference on Private International Law: international sale of goods

191. At its fourteenth session in October 1980, the Hague Conference on Private International Law (Hague Conference) decided to consider the revision of the 1955 Convention on the Law Applicable to International Sales of Goods. A report in this regard was published in September 1982. A first Special Commission meeting on the subject was held in December 1982. At the second meeting of the Special Commission, held in November 1983, the draft Convention on the Law Applicable to Contracts for the International Sale of Goods was adopted. The text of the draft Convention and an accompanying report were published in August 1984.

192. The fourteenth session of the Hague Conference had decided to invite the member States of UNCITRAL to participate in the preparatory work on this subject. Eighteen countries that were not members of the Hague Conference participated in the preparatory work. All States, including non-member States of the Hague Conference, were invited to participate in the diplomatic conference held at The Hague between 14 and 30 October 1985. Fifty-four States participated and eight States attended as observers. The Convention on the Law Applicable to Contracts for the International Sale of Goods, adopted by the final act of the conference on 30 October 1985, was opened for signature or accession at the closing ceremony.

## XII. Other topics of international trade law

### A. Agency

#### 1. UNIDROIT

193. The UNIDROIT diplomatic conference held at Geneva from 31 January to 17 February 1983, which adopted and opened to signature the Convention on Agency in the International Sale of Goods, requested UNIDROIT to "consider the possibility of elaborating rules on a global or regional level governing the relations between principal and agent in the international sale of goods".

194. Accordingly, the Governing Council instructed the secretariat to prepare a report on the possibility of elaborating rules governing the relations between principals and agents, in particular in the international sale of goods, based primarily on a study of existing national legislation and of attempts at harmonization and unification of laws at a universal and a regional level. A progress report on the study was submitted by the secretariat to the Governing Council at its sixty-third session (May 1984) in the light of which the Council decided to adjourn further discussion on this work on the international relations between principals and agents until a later session when it would be possible to assess developments in the field, in particular the outcome of the work by the EEC on a draft directive on commercial agency.

#### 2. EEC

195. The amended proposals for an EEC directive to co-ordinate the laws of the member States relating to commercial agents has, since April 1981, been the subject of discussions in the Council of Ministers by a group of government experts. The aim of the proposals is to harmonize the laws of the member States governing relations between traders and their commercial agents. At present agents enjoy different degrees of protection, depending on the member State involved. As a result, the cost of employing agents varies from one country to another. Harmonization should, to a large extent, remove the cost differences and should render conditions more competitive.

#### 3. ICC

196. The ICC has completed work on a practical business guide to the drafting of international commercial agency agreements (ICC publication No. 410) and has started to work on a companion guide to distributorship agreements.

### B. EEC: accounts of financial institutions

197. On 19 March 1981 the Commission of the European Communities sent the Council of Ministers the proposal for a directive concerning the annual accounts of banks and other financial institutions (OJ No. C 130, p.1).

198. In February 1982 the Economic and Social Committee of the Communities determined that credit institutions have a duty to provide their staff, customers, shareholders and the public at large with all relevant information concerning their activities. The Committee indicated that, although it opposed the proposed directive in the form it was presented, it would welcome specific rules on the annual accounts of banks and other financial establishments instead of additional rules relevant to banks simply being tacked on to the Fourth Directive (78/660/EEC, OJ No. L 222, p. 11) concerning the annual accounts of certain types of companies. On 6 July 1983 the European Parliament welcomed the proposed directive but requested that some amendments be made to it.

199. In May 1984 the Council of Ministers began its consideration of the amended proposal forwarded to it by the Commission (amended proposal of 14 March 1984, OJ C 83, p. 6.)

200. From the viewpoint of harmonization, the proposal for an EEC directive concerning the annual accounts of banks and other financial institutions will be an important complement to the Fourth Directive mentioned. The proposal adapts the provisions of the 1978 Fourth Directive to the particular characteristics of banks and other financial institutions. However, in order to prevent distortions in a comparison of competitiveness in the credit sector, it has been given a wider scope than the earlier directive, so as to include undertakings with a legal structure not covered by the latter.

201. At present credit institutions are not required to publish detailed balance-sheets and profit-and-loss accounts in all member States. Once the directive has been adopted, all banks and all other financial institutions doing business in the EEC will be obliged to publish comparable annual accounts. The proposal also contains such detailed provisions as apply specifically to the accounts of banks and other financial institutions.

### C. Bankruptcy

#### 1. EEC

202. The EEC draft Convention on Bankruptcy, Winding-up, Arrangements, Compositions and Similar Proceedings, was proposed in 1970 and completely renegotiated with the accession of new member States. This draft Convention was transmitted, in June 1980, by the Chairman of the Group of Governmental Experts, to the President of the Council of Ministers and, with a view to obtaining their opinions, to the Permanent Representatives of the member States and the President of the Commission. On 10 December 1981 the Commission communicated to the member States and to the Council its opinion in regard to this draft Convention. Since 1981 the draft Convention has been discussed in the Council by the Group of Governmental Experts.

## 2. Council of Europe

203. The Council of Europe Committee of Experts on Bankruptcy (CJ-DF) held an exchange of views and information on reforms being considered, undertaken or completed in the different member States. At its seventh meeting, from 7 to 10 May 1985, it also adopted a draft Convention and draft Explanatory Report on the exercise abroad of certain powers of a liquidator. The draft Convention provides, *inter alia*, that without the necessity of an enforcement procedure, a liquidator appointed in bankruptcy proceedings in one member State will be entitled to take measures for the disposal of a debtor's property in another member State. Another chapter of the draft Convention provides a system for informing creditors residing in another member State of the bankruptcy proceedings and for the submission of their claims against the bankrupt.

204. This draft was examined by the Committee on Legal Co-operation (CD-CJ) at its meeting in December 1985. The draft was referred back to the Committee of Experts to be redrafted in the light of the discussion in the CD-CJ.

205. The Council of Europe Committee of Experts on Bankruptcy (CJ-DF) has now been given the following terms of reference:

(a) To attempt to harmonize some fundamental principles of member States' laws relating to bankruptcy and other proceedings with the purpose of rehabilitating the debtor and in such a way as to take into account the concepts of bankruptcy/liquidation and bankruptcy/rehabilitation; and

(b) To endeavour to solve the problems arising at an international level when bankruptcy proceedings are instituted in one member State whereas some creditors and assets of the debtor are in the territories of other States.

### D. Council of Europe: creditors

206. The Council of Europe Committee of Experts on the Rights of Creditors has completed its work by adopting a draft Convention on the Reservation of Ownership Clause, the main portions of which relate to the recognition and enforcement of that clause so long as it complies with the Convention's rules in its regard. The draft has been sent to the European Committee on Legal Co-operation for consideration before being sent to the Committee of Ministers for final adoption.

### E. CMEA: combines

207. During 1983-1984 the CMEA Conference on Legal Questions prepared a report on the legal issues involved in the development of direct links between the

combines, enterprises and other economic organizations of the CMEA member countries. This report also deals with the establishment and operation of international economic organizations on the territory of these countries for the purpose of the further expansion of co-operation and direct ties within the CMEA. In this connection, work proceeded during 1985 on a comparative study of the provisions in effect in these countries for the regulation of the establishment and operation of direct links between economic organizations.

### F. EEC: companies

#### *Directives and proposed Directives*

208. During and after 1983, the EEC issued the following Directives or proposed Directives relating to companies:

(a) Amended proposal for a Fifth Directive of 19 August 1983 (OJ C 240, p. 2) concerning the structure of public limited companies, the powers and obligations of their organs and employee participation;

(b) Seventh Directive of 13 June 1983 (83/349/EEC) (Adopted OJ L 193, p. 1) on parent undertakings of groups comprising either a public limited company or a private limited company and relating to consolidated accounts;

(c) Eighth Directive of 10 April 1984 (84/253/EEC) (Adopted O.J. L 126, p. 20) on the approval of persons responsible for carrying out the statutory audits of accounting documents;

(d) Proposal for a Tenth Directive of 8 January 1985 (OJ C 23, p. 11) concerning cross-border mergers of public limited companies;

(e) Draft of a proposed Ninth Directive on public limited companies relating to the links between undertakings. Technical preparatory work has been carried out by the Commission's departments, but the Commission itself has not yet made a decision on the matter. The current draft was sent to Governments, industry and trade unions at the end of 1984 in order to enable them to communicate their reactions to the Commission.

#### *International mergers of public limited liability companies*

209. A preliminary draft European agreement on international mergers of public limited liability companies prepared by a group of experts was presented to the Council of Ministers of the European Communities and the Governments of member States in 1973. Progress on the draft Convention, the technical aspects of which have been completed, is blocked because of problems relating mainly to employee participation. The draft Convention aims at making mergers between companies established under the laws of different States possible. The transactions covered by the Convention are mergers by takeover and by formation of a new company.

*European company statute*

210. A regulation establishing a statute for a European company has been proposed. Such a statute would create a legal structure, available throughout the EEC, which would permit undertakings to establish themselves or re-organize their businesses at a European level under one umbrella of legislation rather than to continue to rely on different national systems operating side by side.

211. A proposal for a regulation on a statute for a European company revised in the light of the opinions of the Economic and Social Committee and the European Parliament was submitted by the Commission to the Council on 13 May 1975 (Bull. EC 4. 1975). The first reading of the proposal has nearly been completed by an *ad hoc* group in Council. Only titles V (employee representation), VI (annual accounts) and VII (groups) still remain to be examined.

*Groups of companies*

212. Some of the issues which it is proposed to resolve in an EEC Directive on this question are: harmonization of municipal rules relating to groups of companies, extension of company law rules to holding-subsidiary relations, notification and publication of shareholdings, reciprocal holdings, subordination of a single company's interests to the interests of a group, and minority and creditor protection in dependent group companies.

213. A working group of governmental experts finished its discussions on this subject early in 1974. The Commission has not yet made any proposal to the Council but the latest draft was transmitted to Governments at the end of 1984 for their information.

*European Economic Interest Grouping (EEIG) (formerly European co-operation grouping).*

214. This is a new legal concept under EEC law intended to foster co-operation between individuals and companies of all sizes from the various member States while observing the rules for competition. The purpose of the new concept is to allow EEC individuals and companies to combine part of their activities or some of their functions so as to enhance the results of their own economic activity. The Grouping is therefore designed as an economic entity separate from its members and living independently but not itself in a dedicated quest for profits. It both amplifies and complements the activity of its members.

215. The purpose of the Regulation is to provide a means whereby undertakings (particularly small- and medium-sized ones) can co-operate across frontiers without being hindered by the territorial limits of national legal systems. The Grouping is intended to be a flexible legal instrument based on a contractual relationship of limited duration, for use by individuals and companies alike. The Regulation establishing such a Grouping prohibits it from aiming for profit as such, but if profit

happens to emerge, this will be taxed on the account of the members. The Grouping is vested with full legal capacity so as to enable it to participate to the full in the economic life of the EEC.

216. The Regulation on forming a European Economic Interest Grouping follows on the proposal concerning the statute for the European company (see paragraph 208 above). The concepts complement each other: the Grouping being primarily intended to facilitate provisional alliances based on joint interests and made through very flexible procedures which can be adapted swiftly to developments in economic conditions, while the European company is intended to bring together much closer groupings, usually irrevocably.

217. On 12 April 1978 the Commission presented to the Council a proposed Regulation amended in the light of the opinions of the Economic and Social Committee and the European Parliament given in respect of a similar, earlier proposal for setting up what was then termed a "European Co-operation Grouping". This proposal has now become the "European Economic Interest Grouping (EEIG) Regulation 1985" (OJ L 199, 25.7.1985, p. 1).

**G. ICC: code of practice for on-demand guarantees**

218. The ICC is studying the desirability of a standard international code of practice for on-demand guarantees.

**H. UNEP: consumer protection**

219. By its decision 12/14, section II, of 28 May 1984, the Governing Council of UNEP expressed its satisfaction at the results of the first session of the *Ad Hoc* Working Group of Experts for the Exchange of Information on Potentially Harmful Chemicals (in particular Pesticides) in International Trade (26 to 30 March 1984) and requested the Executive Director to continue the work initiated by the Group and to take all appropriate steps to expedite the preparation of the guidelines and principles elaborated by the Group with a view to their early adoption by the Governing Council.

220. The second session of the Working Group was accordingly convened at Rome from 28 January to 1 February 1985. The Working Group revised the draft guidelines and considered the implementation of the provisional notification scheme for banned and severely restricted chemicals (see "Report of the Working Group on the Work of its Second Session", UNEP/WG/112/5).

221. The Working Group also considered the following issues: information on the basic data required for the assessment of the hazards to man and the environment, the conditions for the safe use of certain chemicals and various definitions used in the draft guidelines, i.e. "chemical", "pesticide", "potentially harmful chemical", "banned or severely restricted", "trade" and "export", "re-export" and "import".

**I. ILO: employment and labour**

222. At the seventieth session of the International Labour Conference (June 1984), a recommendation was adopted containing a section on "International economic co-operation and employment". The recommendation concerns employment policies relating to, *inter alia*, population, employment of youth and disadvantaged groups and persons, technology, small undertakings, regional development, public investment and special public works programmes and international economic co-operation and employment.

223. The following industrial meetings of ILO held in 1983 and 1984 adopted conclusions touching on international trade questions:

(a) Eleventh session of Metal Trades Committees ("Effect to be given to the conclusions and resolutions of the committee", GB.226/IA/2/1);

(b) Fourth Tripartite Technical Meeting for Mines other than Coal Mines ("Effect to be given to the conclusions and resolutions of the meeting", GB.226/IA/4/2);

(c) First Session of the Food and Drink Industries Committee ("Effect to be given to the conclusions and resolutions of the committee", GB.230/IA/5/7).

224. The ILO's Joint Maritime Commission met in September 1984 and adopted a resolution dealing with the carrying of radioactive nuclear cargoes (report of the twenty-fourth session of the Committee, GB.228/7/8). A tripartite Preparatory Technical Maritime Conference will meet in May 1986 to prepare for a Maritime Session of the International Labour Conference scheduled for 1987. The Conference is likely to adopt conventions or recommendations on the following subjects:

(a) Social security protection for seafarers including those serving in ships flying flags other than those of their own country;

(b) Health protection and medical care for seafarers;

(c) Revision of the Repatriation of Seamen Convention, 1926 (No. 23); and of the Repatriation (Ships Masters and Apprentices) Recommendation, 1926 (No. 27);

(d) Seafarers welfare at sea and in port.

In addition, proposals on the subject of health and safety in construction work are to be considered by the International Labour Conference in 1987.

225. The ILO is preparing a "Code of Practice and Occupational Safety and Health and Working Conditions Specifications in the Transfer of Technology to Developing Countries". A draft of this Code of Practice is to be submitted to a meeting of experts in October 1986.

**J. UNEP: environmentally sound management of hazardous wastes**

226. The *Ad Hoc* Working Group of Experts on the Environmentally Sound Management of Hazardous Wastes, established pursuant to UNEP Governing Council decision 10/24 of 31 May 1982 to consider guidelines and principles on the subject, held its first session at Munich from 28 February to 5 March, 1984. By its decision of 28 May 1984, the Governing Council expressed satisfaction with the results of the first session of the Working Group and requested the Executive Director to continue the work so initiated, in accordance with the recommendations submitted by the Working Group, and to take all necessary measures to expedite the preparation of the guidelines and principles elaborated by the Working Group. The Working Group met three times and at its last meeting in December 1985 it adopted its final report (UNEP/WG.122/3) which comprises, *inter alia*, the text of the guidelines prepared and adopted by it.

**K. UNCTAD: Export Credit Guarantee Facility**

227. The question of establishing an International Export Credit Guarantee Facility (ECGF) to give support to developing countries' exports has been extensively discussed within UNCTAD. At its eighth session the UNCTAD Committee on Invisibles and Financing related to Trade (CIFT) dealt with both policy and technical issues relating to the establishment of a Facility. In its resolution 15 (VIII) of 3 November 1978 and Decision 17 (IX) of 11 July 1980, the Committee requested the secretariat, in consultation with member States and international institutions, and with the assistance of financial experts, to formulate the detailed operational characteristics of a Facility. The secretariat prepared a study on "The operational features of an international export credit guarantee facility" (TD/B/AC.33/2 and Corr. 1) which was considered by an expert group meeting in January 1982 (the report of the Intergovernmental Group of Experts is reproduced in TD/B/889). The Committee at its tenth session in February/March 1983 considered this study as well as the report "Evaluation of the operational features of an export credit guarantee facility" (TD/B/C.3/183/Add.1, 2, 2 Corr. 1, 3, and 3 Corr. 1). The Conference at its sixth session in June-July 1983 considered this question and decided to remit it to the Trade and Development Board in order that the latter might finalize its consideration of the issue. In the event, it was suggested at the Trade and Development Board's thirteenth session (2 to 6 April 1984) that the decision on the proposal for the establishment of an international export credit guarantee facility should be taken by the Committee on Invisibles and Financing Related to Trade.

**L. UNIDROIT: factoring**

228. The preliminary draft of uniform rules on certain aspects of international factoring was approved by the UNIDROIT study group on factoring contracts at the



close of its third session in April, 1982. The Governing Council adopted at its sixty-second session (May 1983) the text of the draft uniform rules as prepared by the study group and instructed the secretariat to communicate that text and the accompanying explanatory report (Study LVIII- Doc. 16) to Governments for their observations with a view to deciding on the next steps to be taken. On the basis of the observations received, the Council decided at its sixty-third session in May 1984 to set up a committee to review certain aspects of international factoring. The first session of the committee took place at Rome, in March 1985, and was attended by representatives from more than 20 States and by observers from a number of international organizations. A revised text of the draft, together with an updated commentary thereon (Study LVIII-Doc. 20) was circulated to Governments in order to obtain their observations on the documents. A summary of these observations will be circulated before the second session of the committee meeting from 21 to 24 April 1986.

#### **M. UNIDROIT: acquisition of corporeal moveables**

229. The UNIDROIT draft Uniform Law on the Acquisition in Good Faith of Corporeal Moveables (LUAB) was the subject of a detailed discussion by the Governing Council at its sixty-first session (April 1982) at which time continuing interest in the draft was expressed. At its sixty-second session (May 1983), the Governing Council decided to retain the subject on its work programme for the triennium 1984-1986 and to take a decision concerning a review of the provisions of the 1974 draft of the Uniform Law at its 1984 session, in the light of information regarding developments in certain aspects of the problem in UNESCO and in the Council of Europe and of the general climate of government opinion regarding the unification of the law of international sales as reflected by acceptance of the existing conventions in that field. At its sixty-third session the Governing Council authorized the secretariat to accept a proposal by UNESCO that UNIDROIT prepare a study focusing on the acquisition of cultural property which should take into account the draft Uniform Law on the Acquisition in Good Faith of Corporeal Moveables and the 1970 UNESCO Convention on the Means of Prohibiting and Preventing the Illicit Import, Export and Transfer of Ownership of Cultural Property.

230. At its sixty-fourth session held in May 1985, the Governing Council considered the study, on the basis of which it authorized the UNIDROIT secretariat to respond favourably to any future request by UNESCO for a study supplementing that first one. The Council postponed, however, any decision as to whether or not UNIDROIT should at some time in the future become involved in drafting a new instrument to supplement the 1970 UNESCO Convention.

#### **N. Council of Europe: insider trading**

231. The Committee on Legal Co-operation (CD-CJ) established a Committee of Experts on Insider Trading

for the purpose of studying the problems of insider trading with a view to drafting a convention providing for specific international assistance which would cover the administrative, civil, criminal, and, if necessary and appropriate, private international law, aspects. This Committee on Insider Trading started its work in May 1985.

232. Concern in this area has been aroused by the prospect that the principles of equal opportunity and trust in firms, upon which principles the stock market is founded, may be undermined by transactions by insiders attempting to use privileged information not publicly known in order to make profits or avoid losses. Such practices are contrary to the interests of the firms and their shareholders and shake the confidence of prospective investors. This has already prompted some member States of the Council of Europe to take preventative or punitive measures of a criminal, civil or administrative nature. Others have not done so either because it is inexpedient considering the circumstances of the stock exchange or because they are still considering appropriate measures. As a result, insiders can conduct their transactions from countries where this is not punishable through the agency of banks or "straw men". The question is to identify means of thwarting such transactions.

#### **O. Hague Conference on Private International Law: international judicial and administrative co-operation**

233. The fourteenth session of the Hague Conference authorized its Secretary-General to convoke at regular intervals special commissions to study the practical operation of conventions and recommendations in matters of judicial and administrative co-operation, and, where necessary, to propose recommendations in these areas. The fifteenth session instructed the Secretary-General to convene a Special Commission on the operation of the 1970 Hague Convention on the Taking of Evidence Abroad in Civil or Commercial Matters (Evidence Convention). More particularly, the fifteenth session also decided:

(a) To entrust this Special Commission with the task of proceeding to an exchange of views on the possibility of international co-operation relating to the taking of evidence in fields connected to competition law;

(b) To request this Special Commission to obtain an exchange of views on the possibility of using the 1970 Convention for the Taking of Evidence Abroad in the context of arbitral proceedings, while instructing the Secretary-General to gather any useful information from international organizations or bodies specialized in the field of arbitration.

234. A preliminary document for the Special Commission meeting on the Evidence Convention was issued in March 1985. The Special Commission meeting on the operation of the Evidence Convention was held at The Hague from 28 to 31 May 1985.

235. *A Practical Handbook on the Operation of the Hague Convention of 15 November 1965 on the Service Abroad of Judicial and Extrajudicial Documents in Civil or Commercial Matters* (Hague Convention on Private International Law ISBN 90 6215 073), in loose-leaf form, was published early in 1983. A similar handbook on the operation of the Convention on the Taking of Evidence Abroad was published in 1984, entitled *Practical Handbook on the Operation of the Hague Convention of 18 March 1970 on the Taking of Evidence Abroad in Civil or Commercial Matters* (ISBN 90 6215 112 4).

#### **P. Hague Conference on Private International Law: jurisdiction**

236. The Hague Conference, at its fifteenth session (1984), invited the Permanent Bureau to undertake exploratory studies on the desirability of revising the 1965 Hague Convention on the Choice of Court, in particular to assure the recognition and enforcement of decisions.

#### **Q. UNIDROIT: leasing**

237. The preliminary draft of uniform rules on international leasing was considered by the UNIDROIT Governing Council at its sixtieth session (April 1981). The Council decided that, given the novelty of leasing, it would be preferable to delay the transmission of the text to a committee of government experts for the elaboration of a final text until such time as the preliminary draft had been given maximum exposure among practitioners. Accordingly symposia were organized in New York (May 1981) and at Zürich (November 1981) to which an audience of bankers, businessmen and lawyers having expertise in international leasing were invited. Both symposia provoked much constructive criticism of the preliminary draft, as too did the First World Leasing Convention, held at Hong Kong in January 1983.

238. The various proposals for amendment of the draft made at the three meetings were considered by the Chairman of the study group convened to draft the uniform rules and by the secretariat. A revised text, taking account of those proposed amendments, was submitted to the study group which, at its fourth session in March 1984, approved the text of the preliminary draft uniform rules on international financial leasing. That text was then adopted by the Governing Council at its sixty-fourth session in May 1984 (C.D. 63. Concls. 4). The Council also decided to set up a Committee of Government Experts for the preparation of a draft Convention on international financial leasing. The first session of the Committee took place at Rome on March 1985. A revised text of the draft, together with an updated commentary thereon, was circulated to Governments with a request for observations (those observations appear in Study LIX-Doc. 26). A second session of the Committee of Governmental Experts in April 1986 will consider these observations and the final draft provisions drawn up by the UNIDROIT secretariat (Study LIX-Doc. 27).

#### **R. ITC: legal aspects of foreign trade**

239. Under the ITC subprogramme "Legal aspects of foreign trade", work in this field started in May 1983, with the preparation of a guide on "Legal aspects of foreign trade - How governmental trade-promotion agencies and business organizations can assist exporters and importers". This guide, financed by UNDP, has been published.

240. The aim of the new ITC subprogramme is to improve the capacity of both government and private trade promotion organizations as advisers to exporters and importers on legal aspects of foreign trade. As this subprogramme is currently in its early stages, it is anticipated that research and development will continue to be an important element of its activities, with the specific aim of producing training and information materials, as follows:

(a) Preparation of sets of specific profiles for individual countries about legal aspects of foreign trade, comprising both developing and developed countries;

(b) Collection, analysis and dissemination of information on legislation, standard contracts and related general conditions governing trade transactions between developing and developed countries, as well as between developing countries. The dissemination of such material to governmental trade promotion and business organizations may be done through a new ITC series of notes on legal aspects of foreign trade;

(c) The advisory services and direct training on export matters for trade promotion and business organizations to be provided will be directed towards the organization of a legal service and training of those responsible for the provision of legal advisory services to exporters and importers.

#### **S. Restrictive business practices**

##### **1. UNCTAD: Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices**

241. The General Assembly, by its resolution 35/63 of 5 December 1980, adopted the Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices. The resolution also called for a United Nations Conference to review all aspects of the Set to be convened in 1985. As charged by the Set, the Intergovernmental Group of Experts on Restrictive Business Practices acted as a preparatory body for the Review Conference. The Group considered a number of proposals for the improvement and further development of the Set of Principles and Rules and identified the following elements for further consideration by the Conference: (a) the legal nature of the Set, (b) the establishment of a Special Committee to replace the Intergovernmental Group of Experts, (c) the implementation of technical assistance, as set out in paragraphs 6 and 7 of section F of the Set, (d) the framework for multilateral consultations

in accordance with paragraph 3(a) of section G and paragraph 4 of section C of the Set, and (e) the further Review Conference in 1990. The Group also approved the provisional agenda and rules of procedure for the Conference. The Conference met in November 1985 but was unable to reach agreement. The Conference decided to transmit its report (TD/RBP/CONF.2/8) together with the proposals made by regional groups (annexes II, III and IV to the above-mentioned report) to the General Assembly. The Conference requested the General Assembly to decide, in the light of the information transmitted to it, whether to convene a resumed session of the Conference. The General Assembly, by resolution 40/192 of 17 December 1985, invited the Secretary-General of UNCTAD and the President of the Conference to review all aspects of the Set to undertake consultations with regional groups and Governments on the reconvening of the Conference and to report thereon to the General Assembly at the earliest opportunity.

242. The Intergovernmental Group of Experts has reviewed the implementation and application of the Set and repeatedly expressed concern about the continued resort to restrictive business practices adversely affecting international trade, particularly the trade and development of developing countries, and has called upon all States to implement the Principles and Rules. The Group has expressed regret that the necessary action has not been taken to implement the technical assistance, advisory and training programmes on restrictive business practices, as agreed in section F, paragraph 6 of the Set, and has invited States to consider taking the issue up at the General Assembly. International organizations and financing programmes have been urged to provide the necessary resources, and States have been invited to make voluntary contributions to this effect.

243. The studies and reports prepared by the UNCTAD secretariat in this area include:

(a) "Studies on restrictive business practices related to the provisions of the Set of Principles and Rules: Collusive tendering" (TD/B/RBP/12/Rev.1);

(b) "Restrictive business practices in the services sector by consulting firms and other enterprises in relation to the design and manufacture of plant and equipment: note by the UNCTAD secretariat" (TD/B/RBP/19);

(c) "Tied purchasing: study by the UNCTAD secretariat" (TD/B/RBP/18);

(d) "Consideration of the revised draft of a model law or laws on restrictive business practices" (TD/B/RBP/15/Rev.1 and Corr.1-2);

(e) The Annual Reports for 1982 and 1983-1984 on legislation and other instruments in developed and developing countries for the control of restrictive business practices (TD/B/RBP/11 and 29, respectively).

In addition, the secretariat has circulated quarterly Restrictive Business Practices Information Notes, issues 1 to 15 (TD/B/RBP/INF. series) with a view to keeping

Governments and other international bodies or persons informed of recent major developments in the area of restrictive business practices. At its third session, the Intergovernmental Group of Experts examined the revised draft of the model law referred to above and requested the secretariat to continue work in this area and to proceed with the preparation of a handbook on restrictive business practices legislation, which should contain descriptions supplied by States of their relevant legislation and of court and other decisions.

## 2. ICC

244. The ICC is preparing a business guide on the subject of restrictive business practices.

### T. GATT: technical barriers to trade

245. The GATT Agreement on Technical Barriers to Trade (TBT/W/67/Rev.1), more commonly known as the "Standards Code", entered into force on 1 January 1980. It was designed to ensure that procedures and systems related to standards, certification and testing of products do not act as unnecessary barriers to trade. Some 37 contracting parties have either accepted or signed the Code. By the end of 1984, some 1100 individual notifications by participating countries of measures and regulations had been notified to GATT.

246. During that year, the Committee on Technical Barriers to Trade discussed and adopted a number of recommendations on the application of the Agreement and on procedures for the conduct of its work. The Committee heard representations by regional standards bodies; namely, the European Committee for Electrotechnical Standardization, the Pacific Area Standards Congress and the European Conference of Postal and Telecommunications Administrations.

247. The Committee met on a number of occasions to investigate a complaint concerning procedures for type approval of heating radiators and electrical medical equipment. The third meeting of persons responsible for information exchange took place in 1985. An information meeting was also held with developing country signatories and non-signatories with a view to enabling developing country signatories to make fuller use of the Agreement and to facilitate acceptance by other developing countries.

## XIII. Facilitation of international Trade

### A. Harmonization and facilitation of administrative procedures relating to goods and documents

#### 1. ECE/ECLAC: harmonization of frontier control of goods

248. Accession to and implementation of the 1982 International Convention on the Harmonization of Fron-

tier Controls of Goods (ECE/TRANS/55), which was adopted by the ECE Inland Transport Committee at its thirty-third special session in October 1982, was subject to further promotion. In 1984, 12 ECE member countries and the EEC signed the Convention and two ECE countries have transmitted instruments of approval and accession. Although the Convention is not yet in force, the ECE Group of Experts on Customs Questions Affecting Transport, which elaborated the Convention, has been considering concrete ways and means to implement its provisions, in particular regarding facilitation measures concerning the international transport of perishable foodstuffs and the international transport of goods carried by rail. To that end it is proposed to supplement the Convention by additional protocols.

249. Pursuant to an ECE Resolution concerning technical assistance measures for the implementation of the International Convention on the Harmonization of Frontier Controls of Goods, ECA, ESCAP and ECLAC have taken measures to promote accession to the Convention.

250. At the twelfth Meeting of Ministers of Public Works and Transport of the Southern Cone Countries (Asunción, from 18 to 22 October 1982) the question of delays in passing frontiers was discussed and an agreement was adopted requesting ECLAC to co-operate with the countries in studying the International Convention on the Harmonization of Frontier Control of Goods. In response to this request ECLAC has undertaken the preparation of various studies which seek to highlight, *inter alia*, the difficulties encountered by carriers at frontier crossing points and measures which might be taken to reduce or eliminate these difficulties. As a result of these efforts a growing number of Latin American countries have become aware of the need to harmonize their frontier crossing requirements.

## 2. ECE/ECLAC: customs

251. The ECE Group of Experts on Customs Questions Affecting Transport has continued its work related to the application and updating of various international customs conventions. The Customs Convention on the International Transport of Goods under Cover of TIR Carnets (TIR Convention) 1975 (ECE/TRANS/17 Amend. 4) was modified in 1983 and 1984 by two amendments concerning technical and administrative provisions. The Customs Convention on the Temporary Importation of Private Road Vehicles 1954 (United Nations, *Treaty Series*, vol. 282, p. 249) and the Customs Convention on the Temporary Importation of Commercial Road Vehicles 1956 (United Nations, *Treaty Series*, vol. 327, p. 123) are under consideration for a major revision.

252. The CCC participated in work on customs transit and, having undertaken similar work in the past, resumed consideration of this question at the same time as the ECE and adopted a resolution on the matter as did the Inland Transport Committee of ECE at its forty-fourth session in February 1983.

253. ECLAC has been promoting the application of an international customs transit system such as the TIR Convention (1975) for Latin America. In November 1982 ALADI and ECLAC began to promote the signing of a limited-scope agreement, under the ALADI Montevideo Treaty of 1980, between Argentina, Brazil, Chile, Paraguay and Uruguay concerning adoption of the TIR Convention (1975). A draft agreement was drawn up and discussions were held with the customs authorities of those countries. Following the discussions, a meeting of representatives from the above countries, as well as those from ALADI and ECLAC, was held during 1984 to consider the draft agreement. At that meeting the agreement was accepted by Brazil, Chile, Paraguay and Uruguay, while Argentina indicated the need to complete certain studies related thereto.

## B. Facilitation of international trade procedures

### 1. ECE: Uniform Rules for Communications Agreements (UNCA)

254. Since 1977 work has been continuing within the framework of the ECE Working Party on Facilitation of International Trade Procedures in the study of the problems of a legal nature likely to arise with the replacement of traditional procedures (based on the physical transmission of paper documents) by the exchange of data through ADP and teletransmission.

255. In view of the increasing urgency of the problem, the Rapporteurs on legal questions suggested that, pending progress on legislative solutions at an international level, it might be advisable to develop interim solutions to some of the legal issues in the automatic transfer of trade data. One such solution would be the preparation of a set of uniform rules for communication agreements to which the parties involved in trade data interchange could voluntarily and explicitly agree to be bound. Binding agreements of that sort were admissible in application of the universal principle of the autonomy of the will of the parties in the absence of mandatory provisions.

256. In March 1985 the Rapporteurs on legal questions submitted a draft proposal for Uniform Rules for Communication Agreements (UNCA) (ICC Publication No. 374/2) to the ECE Group of Experts No. 1: Data Elements and Automatic Data Interchange, which agreed to propose to the Working Party that UNCITRAL, CCC, ICC, OECD and other interested organizations be invited to participate actively in the development of the UNCA in an appropriate forum. This view was endorsed by the Working Party at its twenty-first session (March 1985). The ICC convened a committee to consider the preparation of a final text of UNCA. The committee held its first meeting from 16 to 17 January 1986 and further meetings are to be held in May and November 1986.

2. *ECE/UNCTAD: Trade Data Elements Directory (UNTDED) and Trade Data Interchange Directory (UNTDID)*

257. The ECE Working Party on Facilitation of International Trade Procedures is continuing its work on the development and maintenance of UNTDED (TD/B/FAL/INF.79) and UNTDID (TD/B/FAL/INF.77) which propound a set of standards for the exchange of international trade data. The "Guidelines for trade data interchange developed within the United Nations Economic Commission for Europe", which form Part 4 of UNTDID, are being revised to enable them to frame a United Nations Recommendation.

3. *ECE: notification of laws and regulations concerning foreign trade and changes therein (MUNOSYST)*

258. The ECE Committee on the Development of Trade is continuing its work aimed at assessing whether the creation of a multilateral system for the notification of laws and regulations concerning foreign trade and changes therein would be practicable and desirable. Taking into account the ever increasing number of trade information systems available either through government initiative or on a commercial basis, the Committee has decided, before proceeding further with its feasibility study, to ascertain the views of the business community regarding the relevance or need of such a project for trade activities and its potential commercial viability.

4. *ECE: PAYTERMS – abbreviations of terms of payment*

259. In September 1983, the ECE Working Party on Facilitation of International Trade Procedures reviewed the position regarding the preparation of further coded representations for the elements constituting the standard terms of payment. It was agreed to revert to this matter when more practical experience in applying these PAYTERMS (comprised in Recommendation 17 adopted by the ECE Working Party on Facilitation of International Trade Procedures (1980 and 1982) and ECE/TRADE/142) has been gained in several countries.

5. *ICC: INCOTERMS – abbreviations of trade terms*

260. The ICC is considering whether more detailed cost units should be added to INCOTERMS (ICC Publication No. 350), an internationally applied set of trade terms for export transactions. Consideration is also being given to the desirability of revising other provisions of the INCOTERMS, particularly in the light of the increased use of electronic communications techniques.

6. *IMO: harmonization of term "documentary requirements"*

261. The Facilitation Committee of IMO at its fifteenth session returned to the question of whether the term "documentary requirements" which appears in a number of articles of the International Convention on Facilitation of International Maritime Traffic 1965 (as amended) (IMO sales number 78.10) covered automatic data processing. The Committee concluded that it would be desirable to provide a harmonized interpretation of the term "documentary requirements" to the effect that the term should be understood to include information not only conveyed on paper but also by way of any other medium that was acceptable to the party concerned. The Council of IMO has approved this harmonized interpretation.

### C. *Studies on trade facilitation*

#### 1. *ICC*

262. The ICC Commission on Computing, Telecommunications and Information Policies and its Working Parties on Telecommunications and Transborder Data Flows, have recently published documents on the following subjects:

- "The liberalization of telecommunication services – needs and limits";
- "An international programme for homologation/certification of equipment attached to telecommunication networks";
- "Privacy legislation, data protection and legal persons";
- "International private leased circuits: the business user's view";
- "Information flows – an international business perspective";
- "ISDN – a future universal telecommunications network: a business user's view";
- "Protection of information in electronic systems – operational; guidelines";
- "Protection of information in electronic systems – management introduction".

#### 2. *LAIA*

263. A regional action programme within the framework of LAIA to facilitate international trade was issued by the general secretariat of LAIA in the form of a study dated 3 March 1983 entitled "The facilitation of international trade" (ALADI/SEC/Estudio 6). The document ALADI/SEC/di 85, issued by the general secretariat on 19 May 1983, describes the studies and activities for facilitating trade and transport which were carried out in 1983.

**D. UNCITRAL: automatic data processing**

264. UNCITRAL, at its eighteenth session in 1985, as part of its work on the subject of the legal implications of automatic data processing in the flow of international trade, received the report prepared by the secretariat on the legal value of computer records (A/CN.9/265). After discussions of the report the Commission adopted a recommendation urging Governments to review legal requirements and rules which inhibit the use of the new technology in trade and advocating that international organizations revise and elaborate legal texts related to

trade in the light of the recommendation to Governments (see "Report of the United Nations Commission on International Trade Law on the work of its eighteenth session" (1985), *Official Records of the General Assembly, Fortieth Session, Supplement No. 17 (A/40/17)*, paragraphs 354-360).

265. A report of the legal implications of automatic data processing, including information regarding the work of international organizations in this area (A/CN.9/279) is being submitted to the nineteenth session of UNCITRAL (16 June-11 July 1986).

## VII. STATUS OF CONVENTIONS

Note by the secretariat (A/CN.9/283)

[Original: English]

1. At its thirteenth session the Commission decided that it would consider, at each of its sessions, the status of conventions that were the outcome of work carried out by it.<sup>a</sup>

2. The present note is submitted pursuant to that decision. The annex hereto sets forth the state of signatures, ratifications and accessions as of 12 May 1986 to the following conventions: Convention on the Limitation

Period in the International Sale of Goods (New York, 1974); Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980); United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg); United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980); and Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958). The latter convention, which has not emanated from the work of the Commission, has been included because of the close interest of the Commission in it, particularly in connection with the Commission's work in the field of international commercial arbitration.

<sup>a</sup>Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 163.

### ANNEX

#### 1. *Convention on the Limitation Period in the International Sale of Goods (New York, 1974)*

<i>State</i>	<i>Signature</i>	<i>Ratification</i>	<i>Accession</i>
Argentina			9 October 1981
Brazil	14 June 1974		
Bulgaria	24 February 1975		
Byelorussian SSR	14 June 1974		
Costa Rica	30 August 1974		
Czechoslovakia	29 August 1975	26 May 1977	
Dominican Republic			23 December 1977
Egypt			6 December 1982*
German Democratic Republic	14 June 1974		
Ghana	5 December 1974	7 October 1975	
Hungary	14 June 1974	16 June 1983	
Mongolia	14 June 1974		
Nicaragua	13 May 1975		
Norway <sup>1</sup>	11 December 1975	20 March 1980	
Poland	14 June 1974		
Ukrainian SSR	14 June 1974		
USSR	14 June 1974		
Yugoslavia			27 November 1978

Signatures only: 10; ratifications: 4; accessions: 4  
Ratifications and accessions necessary to come into force: 10

\*By virtue of accession to the Protocol Amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980) (art. VIII(2) of the Protocol).

#### *Declaration*

<sup>1</sup>Upon signing the Convention Norway declared that, in accordance with article 34, the Convention would not govern contracts of sale where the seller and the buyer both had their relevant places of business within the territories of the Nordic States (i.e. Denmark, Finland, Iceland, Norway and Sweden).

**2. Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980)**

<i>State</i>	<i>Accession</i>
Argentina	19 July 1983
Egypt	6 December 1982
Hungary	16 June 1983

Having received the required number of accessions (2), the Protocol will come into force between acceding States when the Convention comes into force.

**3. United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg)**

<i>State</i>	<i>Signature</i>	<i>Ratification</i>	<i>Accession</i>
Austria	30 April 1979		
Barbados			2 February 1981
Brazil	31 March 1978		
Chile	31 March 1978	9 July 1982	
Czechoslovakia <sup>1</sup>	6 March 1979		
Denmark	18 April 1979		
Ecuador	31 March 1978		
Egypt	31 March 1978	23 April 1979	
Finland	18 April 1979		
France	18 April 1979		
Germany, Federal Republic of	31 March 1978		
Ghana	31 March 1978		
Holy See	31 March 1978		
Hungary	23 April 1979	5 July 1984	
Lebanon			4 April 1983
Madagascar	31 March 1978		
Mexico	31 March 1978		
Morocco			12 June 1981
Norway	18 April 1979		
Pakistan	8 March 1979		
Panama	31 March 1978		
Philippines	14 June 1978		
Portugal	31 March 1978		
Romania			7 January 1982
Senegal	31 March 1978	17 March 1986	
Sierra Leone	15 August 1978		
Singapore	31 March 1978		
Sweden	18 April 1979		
Tunisia			15 September 1980
Uganda			6 July 1979
United Republic of Tanzania			24 July 1979
United States of America	30 April 1979		
Venezuela	31 March 1978		
Zaire	19 April 1979		

Signatures only: 23; ratifications: 4; accessions: 7

Ratifications and accessions necessary to come into force: 20

*Declaration*

<sup>1</sup>Upon signing the Convention the Czechoslovak Socialist Republic declared, in accordance with article 26, a formula for converting the amounts of liability referred to in paragraph 2 of that article into the Czechoslovak currency and the amount of the limits of liability to be applied in the territory of the Czechoslovak Socialist Republic as expressed in the Czechoslovak currency.



**4. United Nations Convention on Contracts for the International Sale of Goods, Vienna (1980)**

<i>State</i>	<i>Signature</i>	<i>Ratification</i>	<i>Accession</i>
Argentina <sup>3</sup>			19 July 1983
Austria	11 April 1980		
Chile	11 April 1980		
China	30 September 1981		
Czechoslovakia	1 September 1981		
Denmark <sup>1</sup>	26 May 1981		
Egypt			6 December 1982
Finland <sup>1</sup>	26 May 1981		
France	27 August 1981	6 August 1982	
German Democratic Republic	13 August 1981		
Germany, Federal Republic of	26 May 1981		
Ghana	11 April 1980		
Hungary <sup>2,3</sup>	11 April 1980	16 June 1983	
Italy	30 September 1981		
Lesotho	18 June 1981	18 June 1981	
Netherlands	29 May 1981		
Norway <sup>1</sup>	26 May 1981		
Poland	28 September 1981		
Singapore	11 April 1980		
Sweden <sup>1</sup>	26 May 1981		
Syrian Arab Republic			19 October 1982
United States of America	31 August 1981		
Venezuela	28 September 1981		
Yugoslavia	11 April 1980	27 March 1985	

Signatures only: 17; ratifications: 4; accessions: 3

Ratifications and accessions necessary to come into force: 10

*Declarations and reservations*

<sup>1</sup>Upon signing the Convention the Governments of Denmark, Finland, Norway and Sweden declared, in accordance with article 92(I), that they would not be bound by Part II of the Convention (Formation of the Contract).

<sup>2</sup>Upon ratifying the Convention the Government of Hungary declared that it considered the General Conditions of Delivery of Goods between Organizations of the Member Countries of the Council for Mutual Economic Assistance to be subject to the provisions of article 90 of the Convention.

<sup>3</sup>Upon ratifying the Convention the Governments of Argentina and Hungary stated, in accordance with articles 12 and 96 of the Convention, that any provision of article 11, article 29 or Part II of the Convention that allows a contract of sale or its modification or termination by agreement or any offer, acceptance or other indication of intention to be made in any form other than in writing, does not apply where any party has his place of business in their respective States.

**5. Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958)**

<i>State</i>	<i>Signature</i>	<i>Ratification</i>	<i>Accession</i>
Argentina	26 August 1958		
Australia			6 March 1975
Austria <sup>2</sup>			2 May 1961
Belgium <sup>2</sup>	10 June 1958	18 August 1975	
Benin			16 May 1974
Botswana <sup>1,2</sup>			20 December 1971
Bulgaria <sup>2,3</sup>	17 December 1958	10 October 1961	
Byelorussian SSR <sup>2,3</sup>	29 December 1958	15 November 1960	
Canada <sup>1,6</sup>			12 May 1986
Central African Republic <sup>1,2</sup>			15 October 1962
Chile			4 September 1975
Colombia			25 September 1979
Costa Rica	10 June 1958		

<i>State</i>	<i>Signature</i>	<i>Ratification</i>	<i>Accession</i>
Cuba <sup>1 2 3</sup>			
Cyprus <sup>1 2</sup>			30 December 1974
Czechoslovakia <sup>2 3</sup>	3 October 1958	10 July 1959	29 December 1980
Democratic Kampuchea			5 January 1960
Denmark <sup>1 2</sup>			22 December 1972
Djibouti			14 June 1983
Ecuador <sup>1 2</sup>	17 December 1958	3 January 1962	
Egypt			9 March 1959
El Salvador	10 June 1958		
Finland	29 December 1958	19 January 1962	
France <sup>1 2</sup>	25 November 1958	26 June 1959	
German Democratic Republic <sup>1 2 3</sup>			20 February 1975
Germany, Federal Republic of <sup>2</sup>	10 June 1958	30 June 1961	
Ghana			9 April 1968
Greece <sup>1 2</sup>			16 July 1962
Guatemala <sup>1 2</sup>			21 March 1984
Haiti			5 December 1983
Holy See <sup>1 2</sup>			14 May 1975
Hungary <sup>1 2</sup>			5 March 1962
India <sup>1 2</sup>	10 June 1958	13 July 1960	
Indonesia <sup>1 2</sup>			7 October 1981
Ireland <sup>2</sup>			12 May 1981
Israel	10 June 1958	5 January 1959	
Italy			31 January 1969
Japan <sup>2</sup>			20 June 1961
Jordan	10 June 1958	15 November 1979	
Kuwait <sup>2</sup>			28 April 1978
Luxembourg <sup>2</sup>	11 November 1958	9 September 1983	
Madagascar <sup>1 2</sup>			16 July 1962
Malaysia <sup>1 2</sup>			5 November 1985
Mexico			14 April 1971
Monaco <sup>1 2</sup>	31 December 1958	2 June 1982	
Morocco <sup>2</sup>			12 February 1959
Netherlands <sup>2</sup>	10 June 1958	24 April 1964	
New Zealand <sup>2</sup>			6 January 1983
Niger			14 October 1964
Nigeria <sup>1 2</sup>			17 March 1970
Norway <sup>2 4</sup>			14 March 1961
Pakistan	30 December 1958		
Panama			10 October 1984
Philippines <sup>1 2</sup>	10 June 1958	6 July 1967	
Poland <sup>1 2</sup>	10 June 1958	3 October 1961	
Republic of Korea <sup>1 2</sup>			8 February 1973
Romania <sup>1 2 3</sup>			13 September 1961
San Marino			17 May 1979
South Africa			3 May 1976
Spain			12 May 1977
Sri Lanka	30 December 1958	9 April 1962	
Sweden	23 December 1958	28 January 1972	
Switzerland <sup>2</sup>	29 December 1958	1 June 1965	
Syrian Arab Republic			9 March 1959
Thailand			21 December 1959
Trinidad and Tobago <sup>1 2</sup>			14 February 1966
Tunisia <sup>1 2</sup>			17 July 1967
Ukrainian SSR <sup>2 3</sup>	29 December 1958	10 October 1960	
USSR <sup>2 3</sup>	29 December 1958	24 August 1960	
United Kingdom <sup>2</sup>			24 September 1975
United Republic of Tanzania <sup>2</sup>			13 October 1964
United States of America <sup>1 2</sup>			30 September 1970
Uruguay			30 March 1983
Yugoslavia <sup>1 2 5</sup>			26 February 1982

Signatures only: 4; ratifications: 21; accessions: 49  
Entered into force: 7 June 1959

*Declarations and reservations*

(Excludes territorial declarations and certain other reservations and declarations of a political nature)

<sup>1</sup>The Convention will apply only to differences arising out of legal relationships whether contractual or not which are considered as commercial under the national law.

<sup>2</sup>The Convention will apply to recognition and enforcement of awards made in the territory of another contracting State.

<sup>3</sup>With regard to awards made in the territory of non-contracting States, the Convention will apply only to the extent to which those States grant reciprocal treatment.

<sup>4</sup>The Convention will not apply to differences where the subject matter of the proceedings is immovable property situated in the State, or a right in or to such property.

<sup>5</sup>The Convention will apply only to those arbitral awards which were adopted after the coming into effect of the Convention.

<sup>6</sup>With respect to the Province of Alberta, the Government of Canada will apply the Convention only to the recognition and enforcement of awards made in the territory of another contracting State.

## VIII. TRAINING AND ASSISTANCE

### Report of the Secretary-General (A/CN.9/282)

[Original: English]

1. At the eighteenth session of the Commission<sup>1</sup> there was general agreement that the sponsorship of symposia and seminars on international trade law should be continued and strengthened. It was noted that such symposia and seminars were of great value to young lawyers and government officials from developing countries.

2. By its resolution 40/71 of 11 December 1985 on the report of the Commission on the work of its eighteenth session, the General Assembly reaffirmed the importance, in particular for developing countries, of the work of the Commission concerned with training and assistance in the field of international trade law. It also reaffirmed the desirability for the Commission to sponsor symposia and seminars, in particular those organized on a regional basis, to promote training and assistance in the field of international trade law. The General Assembly also expressed its appreciation to those Governments, regional organizations and institutions that had collaborated with the secretariat in organizing regional symposia and seminars, and invited Governments, international organizations and institutions to assist the secretariat in financing and organizing symposia and seminars, in particular in developing countries. The General Assembly also invited Governments, relevant United Nations organs, organizations, institutions and individuals to make voluntary contributions which might be utilized to enable nationals of developing countries to participate in symposia and seminars.

3. The main activities undertaken in this field since the date of the report on training and assistance presented to the eighteenth session of the Commission (A/CN.9/270) are set forth below in the chronological order in which they have occurred.

4. A regional seminar on international trade law and foreign trade (22–23 April 1985, Bogotá Colombia) was organized by the Chamber of Commerce of Bogotá and the UNCITRAL secretariat, with the support of the secretariat of the Organization of American States. The seminar was attended by practising lawyers, law teachers and businessmen from countries of the Andean region. The subjects discussed were UNCITRAL's role in Latin America, the United Nations Convention on the Carriage

of Goods by Sea, 1978 (Hamburg), the Convention on the Limitation Period in the International Sale of Goods (New York, 1974), the United Nations Convention on Contracts for the International Sale of Goods, (Vienna, 1980) (hereinafter referred to as the Vienna Sales Convention), the UNCITRAL Arbitration Rules and the UNCITRAL Conciliation Rules, the UNCITRAL Model Law on International Commercial Arbitration (hereinafter referred to as the UNCITRAL Model Law) and the UNCITRAL draft Legal Guide on Drawing Up International Contracts for the Construction of Industrial Works.

5. The UNCITRAL secretariat participated in a seminar entitled "International Arbitration Rules—Diversity of Choice" (17 May 1985, London) organized by the Chartered Institute of Arbitrators, London. The seminar was attended by lawyers, arbitrators and businessmen, mainly from the United Kingdom. There were also some participants from Continental Europe. Amongst the rules presented and discussed were the UNCITRAL Arbitration Rules and the UNCITRAL Conciliation Rules.

6. The UNCITRAL secretariat participated in an expert group meeting (9–13 September 1985, Vienna) organized by the United Nations Industrial Development Organization (UNIDO) for the purpose of drafting guidelines for the import, assembly and manufacture of agricultural machinery. The objective of the meeting was to prepare guidelines which would assist entities from developing countries in concluding contracts for the import, assembly and manufacture of agricultural machinery. Experts from all the regions attended the meeting.

7. The UNCITRAL secretariat participated in the annual meeting of the International Council of Hide, Skin and Leather Traders' Associations (11–13 September 1985, Cannes, France). At that meeting of about 40 national delegations of the Council from the various regions of the world, the following texts were among the topics discussed: the UNCITRAL Model Law and the Vienna Sales Convention.

8. The UNCITRAL secretariat participated in the "Pacific Rim Conferences on International Commercial Arbitration", (19–21 September 1985, Auckland, New Zealand; 24 September 1985, Sydney, Australia; 28 September 1985, Hong Kong) organized by the Chartered Institute of Arbitrators, London, and, as regards

<sup>1</sup>Report of the United Nations Commission on International Trade Law on the work of its eighteenth session, *Official Records of the General Assembly, Fortieth Session, Supplement No. 17 (A/40/17)*, paras. 366–367.

the conference in Hong Kong, co-sponsored by the International Bar Association. These conferences were attended by lawyers from the countries in which the conferences were held, and by many lawyers from various other countries in the Far Eastern region. The UNCITRAL Model Law was a main topic at all three conferences.

9. The UNCITRAL secretariat participated in a seminar on trade law and in consultations on existing and future legislation on trade law (7–9 October 1985, Beijing, China) organized by the China Council for the Promotion of International Trade. The topics included the Vienna Sales Convention, the UNCITRAL Conciliation Rules and the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, New York, 1958.

10. The UNCITRAL secretariat participated in a conference on international commercial arbitration (14–16 October 1985, Quebec, Canada) organized by Laval University. The conference was attended by lawyers from Canada, the United States of America and Western Europe. One of the main topics discussed was the UNCITRAL Model Law.

11. The UNCITRAL secretariat participated in an international trade law seminar (17 October 1985, Ottawa, Canada) organized by the Department of Justice, Canada. Information was given to participants on the activities of UNCITRAL relating, in particular, to automatic data processing and the legal value of computer records.

12. The UNCITRAL secretariat participated in a seminar on the methods of settlement of commercial disputes (28–29 October 1985, Radenci, Yugoslavia) organized by the Chamber of Commerce of the Socialist Republic of Slovenia. Among the subjects discussed were the UNCITRAL Arbitration Rules, the UNCITRAL Conciliation Rules and the UNCITRAL Model Law.

13. The UNCITRAL secretariat participated in a conference entitled "UNCITRAL Model Law—The Immediate Impact" (29 November 1985, London) organized by the Chartered Institute of Arbitrators, London. The participants were mainly from the United Kingdom. However, there were also some participants from jurisdictions (e.g. Canada, Hong Kong) where adoption of the UNCITRAL Model Law was under active consideration.

14. A regional seminar on international commercial arbitration (20–22 January 1986, Cairo) was organized by the Asian-African Legal Consultative Committee (AALCC) and the Cairo Centre for International Commercial Arbitration, with the co-operation of the UNCITRAL secretariat. The subjects discussed included the facilities and activities of the Cairo Centre for International Commercial Arbitration, the UNCITRAL Arbitration Rules and the UNCITRAL Model Law. The seminar was very widely attended by lawyers and businessmen from the countries of the Middle East.

15. The UNCITRAL secretariat participated in meetings of a drafting committee of the Uniform Law Conference (5–8 February 1986, Ottawa, Canada) and of the British Columbia Task Force (10–11 February 1986, Vancouver, Canada). These meetings were convened to consider the possible implementation of the UNCITRAL Model Law.

16. The UNCITRAL secretariat participated in a working party on liquidated damages and penalty clauses (7 February 1986, Paris) established by the International Chamber of Commerce (ICC). The working party is preparing a legal guide on the drafting of liquidated damages and penalty clauses which may be included in international commercial contracts.

17. The UNCITRAL secretariat participated in a seminar entitled "International Commercial Arbitration—The UNCITRAL Model Law" (10–14 March 1986, Dubrovnik, Yugoslavia) organized by the Inter-University Centre of Postgraduate Studies, Dubrovnik, Yugoslavia. The main topic for discussion was the UNCITRAL Model Law, but other topics in international commercial arbitration were also discussed. The seminar was attended by postgraduate students, research assistants and young corporate counsel from Eastern and Western Europe.

18. The UNCITRAL secretariat participated in a seminar entitled "Paperless Trading and the Law in the European Economic Community" (17–18 March 1986, Brussels) organized by the European Committee (Comité Européen) Lex Informatica Mercatoriaque (CELM). The seminar was attended by approximately 100 lawyers and technicians from the countries of the European Communities. Among the subjects discussed was the implementation of UNCITRAL's recommendation at its eighteenth session on the legal value of computer records.<sup>2</sup>

19. The UNCITRAL secretariat assisted in the instruction involved in the segment devoted to arbitration of a "Development Lawyers Course" (19–21 March 1986, Rome) organized by the International Development Law Institute, Rome. The course was attended by lawyers from developing countries, in particular from Africa. These lawyers included legal advisers to Governments, governmental entities and financial organizations. The UNCITRAL Arbitration Rules, the UNCITRAL Conciliation Rules, and the UNCITRAL Model Law were discussed.

20. The UNCITRAL secretariat participated in a seminar (1 April 1986, Vienna) on UNCITRAL activities, in particular in the field of arbitration, organized by the Federal Chamber of Commerce, Austria. There were participants from countries of Eastern and Western Europe.

21. On some occasions other than those mentioned in the preceding paragraphs, the UNCITRAL secretariat addressed gatherings of lawyers in order to promote the

<sup>2</sup>*Ibid*, para. 360.

work of the Commission. The secretariat also contributed articles to legal periodicals on various aspects of the Commission's work. The secretariat intends to keep in touch with Governments and organizations with a view to collaborating with them in organizing symposia and seminars.

22. Since the eighteenth session of the Commission, four interns received training with the UNCITRAL

secretariat, and were associated with on-going projects of the Commission.

23. The UNCITRAL secretariat thanks the organizers of the conferences, seminars and meetings mentioned above for inviting the secretariat to participate in the conferences, seminars and meetings. On most occasions the expenses of the secretariat in participating were met in whole or in part by the organizers.

# I. DRAFT CONVENTION ON INTERNATIONAL BILLS OF EXCHANGE AND INTERNATIONAL PROMISSORY NOTES

(as revised by the United Nations Commission on International Trade Law at its nineteenth session, New York, 23 June-11 July 1986<sup>a</sup>)

## Chapter I. Sphere of application and form of the instrument

### Article 1

(1) This Convention applies to international bills of exchange and to international promissory notes.

(2) An international bill of exchange is a written instrument with the heading "International bill of exchange (Convention of ...)" which:

(a) Contains, in the text thereof, the words "international bill of exchange (Convention of ...)";

(b) Contains an unconditional order whereby the drawer directs the drawee to pay a definite sum of money to the payee or to his order;

(c) Is payable on demand or at a definite time;

(d) Is dated;

(e) Specifies at least two of the following places and indicates that any two so specified are situated in different States:

(i) The place where the bill is drawn;

(ii) The place indicated next to the signature of the drawer;

(iii) The place indicated next to the name of the drawee;

(iv) The place indicated next to the name of the payee;

(v) The place of payment;

(f) Is signed by the drawer.

(3) An international promissory note is a written instrument with the heading "International promissory note (Convention of ...)" which:

(a) Contains, in the text thereof, the words "international promissory note (Convention of ...)";

(b) Contains an unconditional promise whereby the maker undertakes to pay a definite sum of money to the payee or to his order;

(c) Is payable on demand or at a definite time;

(d) Is dated;

(e) Specifies at least two of the following places and indicates that any two so specified are situated in different States:

(i) The place where the note is made;

(ii) The place indicated next to the signature of the maker;

(iii) The place indicated next to the name of the payee;

(iv) The place of payment;

(f) Is signed by the maker.

(4) Proof that the statements referred to in paragraph (2)(e) or (3)(e) of this article are incorrect does not affect the application of this Convention.

(5) This Convention does not apply to cheques.

### Article 2

This Convention shall apply without regard to whether the places indicated on an international bill of exchange or on an international promissory note pursuant to paragraph (2)(e) or (3)(e) of article 1 are situated in Contracting States.

## Chapter II. Interpretation

### Section 1. General provisions

#### Article 3

In the interpretation of this Convention, regard is to be had to its international character, the need to promote uniformity in its application and the observance of good faith in international transactions.

#### Article 4

In this Convention:

(1) "Bill" means an international bill of exchange governed by this Convention;

(2) "Note" means an international promissory note governed by this Convention;

(3) "Instrument" means a bill or a note;

(4) "Drawee" means the person on whom a bill is drawn but who has not accepted it;

<sup>a</sup>For lack of time, the Commission did not consider certain drafting proposals made by the Drafting Group with respect to articles 38(1), 40(1), 41, 48, 66, 72(1), 73(2) and 80(I)(c), which have been incorporated in this text.

- (5) "Payee" means the person in whose favour the drawer directs payment to be made or to whom the maker promises to pay;
- (6) "Holder" means a person in possession of an instrument in accordance with article 14;
- (7) "Protected holder" means the holder of an instrument which, when he took it, was complete or, if an incomplete instrument within the meaning of article 11(1), was completed in accordance with authority given, provided that, when he became a holder:
- (a) He was without knowledge of a claim to or defence upon the instrument referred to in article 25, other than in paragraph (1)(c)(ii) thereof, or of the fact that it was dishonoured by non-acceptance or non-payment; and
- (b) The time-limit provided by article 51 for presentment of that instrument for payment had not expired;
- (8) "Party" means any person who has signed an instrument as drawer, maker, acceptor, endorser or guarantor;
- (9) "Maturity" means the date of payment referred to in article 8;
- (10) "Signature" means a handwritten signature, or a facsimile thereof, or any other means of effecting the equivalent authentication, and "forged signature" includes a signature by the wrongful or unauthorized use of such means;
- (11) "Money" or "currency" includes a monetary unit of account which is established by an intergovernmental institution or by agreement between two or more States, provided that this Convention shall apply without prejudice to the rules of the intergovernmental institution or to the stipulations of the agreement.

#### Article 5

For the purposes of this Convention, a person is considered to have knowledge of a fact if he has actual knowledge of that fact or could not have been unaware of its existence.

### Section 2. Interpretation of formal requirements

#### Article 6

The sum payable by an instrument is deemed to be a definite sum although the instrument states that it is to be paid:

- (a) With interest;
- (b) By instalments at successive dates;
- (c) By instalments at successive dates with the stipulation on the instrument that upon default in payment of any instalment the unpaid balance becomes due;
- (d) According to a rate of exchange indicated on the instrument or to be determined as directed by the instrument; or
- (e) In a currency other than the currency in which the amount of the instrument is expressed.

#### Article 7

- (1) If there is a discrepancy between the amount of the instrument expressed in words and the amount expressed in

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

- (2) If the amount of the instrument is expressed in a currency having the same description as that of at least one other State than the State where payment is to be made as indicated on the instrument and the specified currency is not identified as the currency of any particular State, the currency is to be considered as the currency of the State where payment is to be made.

- (3) If any instrument states that it is to be paid with interest, without specifying the date from which interest is to run, interest runs from the date of the instrument.

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

- (5) A rate at which interest is to be paid may be expressed either as a definite rate or as a variable rate. For a variable rate to qualify for this purpose, it must vary in relation to one or more reference rates of interest in accordance with provisions stipulated in the instrument and each such reference rate must be published or otherwise available to the public and not subject, directly or indirectly, to unilateral determination by any person who, at the time the bill is drawn or the note is made, is named in the instrument as payee, drawee, or actual or prospective party or other holder.

- (6) Where the rate at which interest is to be paid is expressed as a variable rate, it may be stipulated expressly on the instrument that such rate shall not be less than or exceed a specified rate of interest, or that the variations are otherwise limited.

- (7) If a variable rate does not qualify under paragraph (5) of this article or for any reason it is not possible to determine the numerical value of the variable rate for any period, interest shall be payable for the relevant period at the rate calculated in accordance with article 66(2).

#### Article 8

- (1) An instrument is deemed to be payable on demand:

- (a) If it states that it is payable at sight or on demand or on presentment or if it contains words of similar import; or
- (b) If no time for payment is expressed.

- (2) An instrument payable at a definite time which is accepted or endorsed or guaranteed after maturity is an instrument payable on demand as regards the acceptor, the endorser or the guarantor.

- (3) An instrument is deemed to be payable at a definite time if it states that it is payable:

- (a) On a stated date or at a fixed period after a stated date or at a fixed period after the date of the instrument; or
- (b) At a fixed period after sight; or
- (c) By instalments at successive dates; or
- (d) By instalments at successive dates with the stipulation on the instrument that upon default in payment of any instalment the unpaid balance becomes due.



(4) The time of payment of an instrument payable at a fixed period after date is determined by reference to the date of the instrument.

(5) The maturity of a bill payable at a fixed period after sight is determined by the date of the acceptance.

(6) The maturity of an instrument payable on demand is the date on which the instrument is presented for payment.

(7) The maturity of a note payable at a fixed period after sight is determined by the date of the visa signed by the maker on the note or, if signature is refused, from the date of presentment.

(8) Where an instrument is drawn, or made, payable at one or more months after a stated date or after the date of the instrument or after sight, the instrument matures on the corresponding date of the month when payment must be made. If there is no corresponding date, the instrument matures on the last day of that month.

#### Article 9

(1) A bill may:

- (a) Be drawn upon two or more drawees;
- (b) Be drawn by two or more drawers;
- (c) Be payable to two or more payees.

(2) A note may:

- (a) Be made by two or more makers;
- (b) Be payable to two or more payees.

(3) If an instrument is payable to two or more payees in the alternative, it is payable to any one of them and any one of them in possession of the instrument may exercise the rights of a holder. In any other case the instrument is payable to all of them and the rights of a holder can only be exercised by all of them.

#### Article 10

A bill may:

- (a) Be drawn by the drawer on himself;
- (b) Be drawn payable to his order.

### Section 3. Completion of an incomplete instrument

#### Article 11

(1) An incomplete instrument which satisfies the requirements set out in subparagraphs (a) and (f) of paragraph (2) or (a) and (f) of paragraph (3) of article 1 but which lacks other elements pertaining to one or more of the requirements set out in paragraph (2) or (3) of article 1 may be completed and the instrument so completed is effective as a bill or a note.

(2) When such an instrument is completed without authority or otherwise than in accordance with the authority given:

- (a) A party who signed the instrument before the completion may invoke such lack of authority as a defence against a holder who had knowledge of such lack of authority when he became a holder;
- (b) A party who signed the instrument after the completion is liable according to the terms of the instrument so completed.

## Chapter III. Transfer

#### Article 12

An instrument is transferred:

- (a) By endorsement and delivery of the instrument by the endorser to the endorsee; or
- (b) By mere delivery of the instrument if the last endorsement is in blank.

#### Article 13

(1) An endorsement must be written on the instrument or on a slip affixed thereto ("*allonge*"). It must be signed.

(2) An endorsement may be:

- (a) In blank, that is, by a signature alone or by a signature accompanied by a statement to the effect that the instrument is payable to a person in possession thereof;
- (b) Special, by a signature accompanied by an indication of the person to whom the instrument is payable.

#### Article 14

(1) A person is a holder if he is:

- (a) The payee in possession of the instrument; or
- (b) In possession of an instrument which has been endorsed to him, or on which the last endorsement is in blank, and on which there appears an uninterrupted series of endorsements, even if any of the endorsements was forged or was signed by an agent without authority.

(2) When an endorsement in blank is followed by another endorsement, the person who signed this last endorsement is deemed to be an endorsee by the endorsement in blank.

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

#### Article 15

The holder of an instrument on which the last endorsement is in blank may:

- (a) Further endorse the instrument either in blank or to a specified person; or
- (b) Convert the blank endorsement into a special endorsement by indicating therein that the instrument is payable to himself or to some other specified person; or
- (c) Transfer the instrument in accordance with paragraph (b) of article 12.

#### Article 16

(1) When the drawer or the maker has inserted in the instrument such words as "not negotiable", "not transferable", "not to order", "pay (X) only", or words of similar import, the instrument may not be transferred except for purposes of collection, and any endorsement, even if it does not contain words authorizing the endorsee to collect the instrument, is deemed to be an endorsement for collection.

(2) When an endorsement contains the words "not negotiable", "not transferable", "not to order", "pay (X) only", or words of similar import, the instrument may not be transferred further except for purposes of collection, and any subsequent endorsement, even if it does not contain words authorizing the endorsee to collect the instrument, is deemed to be an endorsement for collection.

#### Article 17

- (1) An endorsement must be unconditional.
- (2) A conditional endorsement transfers the instrument whether or not the condition is fulfilled. The condition is deemed not to have been written as to parties and transferees subsequent to the endorsee.

#### Article 18

An endorsement in respect of a part of the sum due under the instrument is ineffective as an endorsement.

#### Article 19

When there are two or more endorsements, it is presumed, unless the contrary is established, that each endorsement was made in the order in which it appears on the instrument.

#### Article 20

(1) When an endorsement contains the words "for collection", "for deposit", "value in collection", "by procuration", "pay any bank", or words of similar import, authorizing the endorsee to collect the instrument (endorsement for collection), the endorsee:

- (a) May only endorse the instrument for purposes of collection;
- (b) May exercise all the rights arising out of the instrument;
- (c) Is subject to all claims and defences which may be set up against the endorser.

(2) The endorser for collection is not liable upon the instrument to any subsequent holder.

#### Article 21

The holder of an instrument may transfer it to a prior party or the drawee in accordance with article 12; nevertheless, in the case where the transferee was a prior holder of the instrument, no endorsement is required and any endorsement which would prevent him from qualifying as a holder may be struck out.

#### Article 22

An instrument may be transferred in accordance with article 12 after maturity, except by the drawee, the acceptor or the maker.

#### Article 23

(1) If an endorsement is forged, the person whose endorsement is forged or any party who signed the instrument before the forgery has the right to recover compensation for any damage that he may have suffered because of the forgery against:

- (a) The forger;
- (b) The person to whom the instrument was directly transferred by the forger;
- (c) A party or the drawee who paid the instrument to the forger directly or through one or more endorsees for collection.

(2) However, an endorsee for collection shall not be liable under paragraph (1) if at the time at which:

- (a) He pays the principal or advises the principal of the receipt of the proceeds of the instrument, or
- (b) He receives the proceeds of the instrument,

whichever comes later, he is without knowledge of the forgery, provided that such absence of knowledge is not due to his negligence.

(3) Also, a party or the drawee who pays an instrument shall not be liable under paragraph (1) if, at the time he paid the instrument, he was without knowledge of the forgery, provided that such absence of knowledge was not due to his negligence.

(4) Except as against the forger, the damages recoverable under paragraph (1) may not exceed the amount referred to in article 66 or 67.

#### Article 23 bis

(1) If an endorsement is made by an agent without authority or power to bind his principal in the matter, the principal or any party who signed the instrument before such endorsement has the right to recover compensation for any damage that he may have suffered because of such endorsement against:

- (a) The agent;
- (b) The person to whom the instrument was directly transferred by the agent;
- (c) A party or the drawee who paid the instrument to the agent directly or through one or more endorsees for collection.

(2) However, an endorsee for collection shall not be liable under paragraph (1) if at the time at which:

- (a) He pays the principal or advises the principal of the receipt of the proceeds of the instrument, or
- (b) He receives the proceeds of the instrument,

whichever comes later, he is without knowledge that the endorsement does not bind the principal, provided that such absence of knowledge is not due to his negligence.

(3) Also, a party or the drawee who pays an instrument shall not be liable under paragraph (1) if, at the time he paid the instrument, he was without knowledge that the endorsement did not bind the principal, provided that such absence of knowledge was not due to his negligence.

(4) Except as against the agent, the damages recoverable under paragraph (1) may not exceed the amount referred to in article 66 or 67.

**Chapter IV. Rights and liabilities****Section 1. The rights of a holder and of a protected holder***Article 24*

- (1) The holder of an instrument has all the rights conferred on him by this Convention against the parties to the instrument.
- (2) The holder is entitled to transfer the instrument in accordance with article 12.

*Article 25*

- (1) A party may set up against a holder who is not a protected holder:
- (a) Any defence available under this Convention;
- (b) Except as provided in paragraph (3) of this article, any defence based on the underlying transaction between himself and the drawer or between himself and the party subsequent to himself or arising from the circumstances as a result of which he became a party;
- (c) Any defence resulting from:
- (i) The underlying transaction between himself and the holder;
- (ii) Any other transaction between himself and the holder that would be available as a defence against contractual liability;
- (d) Any defence based on incapacity of such party to incur liability on the instrument or on the fact that such party signed without knowledge that his signature made him a party to the instrument, provided that such absence of knowledge was not due to his negligence.

(2) Except as provided in paragraph (3) of this article, the rights to an instrument of a holder who is not a protected holder are subject to any valid claim to the instrument on the part of any person.

(3) A holder who is not a protected holder is subject to a defence under paragraph (1)(b) or to a claim under paragraph (2) of this article only if he took the instrument with knowledge of such defence or claim or if he obtained the instrument by fraud or theft or participated at any time in a fraud or theft concerning it. However, a holder who takes the instrument after the expiration of the time-limit for presentment for payment is subject to any claim to or defence upon the instrument to which his transferor is subject.

(4) A party may not raise as a defence against a holder who is not a protected holder the fact that a third person has a claim to the instrument unless:

- (a) Such third person asserted a valid claim to the instrument; or
- (b) Such holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery.

*Article 26*

- (1) A party may not set up against a protected holder any defence except:
- (a) Defences under articles 29(1), 30, 31(1), 32(3), 49, 53, 59 and 80 of this Convention;

(b) Defences based on the underlying transaction between himself and such holder or arising from any fraudulent act on the part of such holder in obtaining the signature on the instrument of that party;

(c) Defences based on the incapacity of such party to incur liability on the instrument or on the fact that such party signed without knowledge that his signature made him a party to the instrument, provided that such absence of knowledge was not due to his negligence.

(2) The rights to an instrument of a protected holder are not subject to any claim to the instrument on the part of any person, except a valid claim arising from the underlying transaction between himself and the person by whom the claim is raised or arising from any fraudulent act on the part of such holder in obtaining the signature on the instrument of that person.

*Article 27*

- (1) The transfer of an instrument by a protected holder vests in any subsequent holder the rights to and upon the instrument which the protected holder had.
- (2) Such rights are not vested in a subsequent holder if:
- (a) He participated in a transaction which gives rise to a claim to, or a defence upon, the instrument;
- (b) He has previously been a holder, but not a protected holder.

*Article 28*

Every holder is presumed to be a protected holder unless the contrary is proved.

**Section 2. The liability of the parties****A. General provisions***Article 29*

- (1) Subject to the provisions of articles 30 and 32, a person is not liable on an instrument unless he signs it.
- (2) A person who signs an instrument in a name which is not his own is liable as if he had signed it in his own name.

*Article 30*

A forged signature on an instrument does not impose any liability thereon on the person whose signature was forged. Nevertheless, where such person has accepted to be bound by the forged signature or represented that the signature was his own, he is liable as if he had signed the instrument himself.

*Article 31*

- (1) If an instrument has been materially altered:
- (a) Parties who have signed the instrument subsequent to the material alteration are liable thereon according to the terms of the altered text;
- (b) Parties who have signed the instrument before the material alteration are liable thereon according to the terms of the original text. Nevertheless a party who has himself made, authorized, or assented to, the material alteration is liable on the instrument according to the terms of the altered text.

- (2) Failing proof to the contrary, a signature is deemed to have been placed on the instrument after the material alteration.
- (3) Any alteration is material which modifies the written undertaking on the instrument of any party in any respect.

#### Article 32

- (1) An instrument may be signed by an agent.
- (2) The signature of an agent placed by him on an instrument with the authority of his principal and showing on the instrument that he is signing in a representative capacity for that named principal, or the signature of a principal placed on the instrument by an agent with his authority, imposes liability on the principal and not on the agent.
- (3) A signature placed on an instrument by a person as agent but without authority to sign or exceeding his authority, or by an agent with authority to sign but not showing on the instrument that he is signing in a representative capacity for a named person, or showing on the instrument that he is signing in a representative capacity but not naming the person whom he represents, imposes liability thereon on the person signing and not on the person whom he purports to represent.
- (4) The question whether a signature was placed on the instrument in a representative capacity may be determined only by reference to what appears on the instrument.
- (5) A person who is liable pursuant to paragraph (3) and who pays the instrument has the same rights as the person for whom he purported to act would have had if that person had paid the instrument.

#### Article 33

The order to pay contained in a bill does not of itself operate as an assignment to the payee of funds made available for payment by the drawer with the drawee.

### B. The drawer

#### Article 34

- (1) The drawer engages that upon dishonour of the bill by non-acceptance or non-payment, and upon any necessary protest, he will pay to the holder, or to any endorser or any endorser's guarantor who pays the bill in accordance with article 66, the amount of the bill, and any interest and expenses which may be recovered under article 66 or 67.
- (2) The drawer may exclude or limit his own liability for acceptance or for payment by an express stipulation on the bill. Such stipulation has effect only with respect to the drawer. A stipulation excluding or limiting liability for payment is operative only if another party is or becomes liable on the bill.

### C. The maker

#### Article 35

- (1) The maker engages that he will pay to the holder, or to any endorser or any endorser's guarantor who pays the note in accordance with article 66, the amount of the note in accordance

with the terms of that note, and any interest and expenses which may be recovered under article 66 or 67.

- (2) The maker may not exclude or limit his own liability by a stipulation on the note. Any such stipulation is without effect.

### D. The drawee and the acceptor

#### Article 36

- (1) The drawee is not liable on a bill until he accepts it.
- (2) The acceptor engages that he will pay to the holder, or to any party who pays the bill in accordance with article 66, the amount of the bill in accordance with the terms of his acceptance, and any interest and expenses which may be recovered under article 66 or 67.

#### Article 37

An acceptance must be written on the bill and may be effected:

- (a) By the signature of the drawee accompanied by the word "accepted" or by words of similar import; or
- (b) By the signature alone of the drawee.

#### Article 38

- (1) An incomplete instrument which satisfies the requirements set out in article 1(2)(a) may be accepted by the drawee before it has been signed by the drawer, or while otherwise incomplete. In such case, article 11 shall apply accordingly to completion by the drawer or another person.
- (2) A bill may be accepted before, at or after maturity, or after it has been dishonoured by non-acceptance or non-payment.
- (3) When a bill drawn payable at a fixed period after sight, or a bill which must be presented for acceptance before a specified date, is accepted, the acceptor must indicate the date of his acceptance; failing such indication by the acceptor, the drawer or the holder may insert the date of acceptance.
- (4) If a bill drawn payable at a fixed period after sight is dishonoured by non-acceptance and the drawee subsequently accepts it, the holder is entitled to have the acceptance dated as of the date on which the bill was dishonoured.

#### Article 39

- (1) An acceptance must be unqualified. An acceptance is qualified if it is conditional or varies the terms of the bill.
- (2) If the drawee stipulates on the bill that his acceptance is subject to qualification:
- (a) He is nevertheless bound according to the terms of his qualified acceptance;
- (b) The bill is dishonoured by non-acceptance.
- (3) An acceptance relating to only a part of the amount of the bill is a qualified acceptance. If the holder takes such an acceptance, the bill is dishonoured by non-acceptance only as to the remaining part.

(4) An acceptance indicating that payment will be made at a particular address or by a particular agent is not a qualified acceptance, provided that:

- (a) The place in which payment is to be made is not changed;
- (b) The bill is not drawn payable by another agent.

#### E. The endorser

##### Article 40

(1) The endorser engages that upon dishonour of the instrument by non-acceptance or non-payment, and upon any necessary protest, he will pay to the holder, or to any subsequent endorser or such endorser's guarantor who pays the instrument in accordance with article 66, the amount of the instrument, and any interest and expenses which may be recovered under article 66 or 67.

(2) The endorser may exclude or limit his own liability by an express stipulation on the instrument. Such stipulation has effect only with respect to that endorser.

#### F. The transferor by endorsement or by mere delivery

##### Article 41

(1) Unless otherwise agreed, a person who transfers an instrument, by endorsement and delivery or by mere delivery, represents to the holder to whom he transfers the instrument that:

- (a) The instrument does not bear any forged or unauthorized signature;
- (b) The instrument has not been materially altered;
- (c) At the time of transfer, he has no knowledge of any fact which would impair the right of the transferee to payment of the instrument against the acceptor or, in the case of an unaccepted bill, the drawer, or against the maker of a note.

(2) Liability of the transferor under paragraph (1) is incurred only if the transferee took the instrument without knowledge of the matter giving rise to such liability.

(3) Where the transferor is liable under paragraph (1), the transferee may recover, even before maturity, the amount paid by him to the transferor, plus interest calculated in accordance with article 66, against return of the instrument.

#### G. The guarantor

##### Article 42

(1) Payment of an instrument, whether or not it has been accepted, may be guaranteed, as to the whole or part of its amount, for the account of a party or the drawee. A guarantee may be given by any person who may or may not already be a party.

(2) A guarantee must be written on the instrument or on a slip affixed thereto ("*allonge*").

(3) A guarantee is expressed by the words "guaranteed", "*aval*", "*good as aval*" or words of similar import, accompanied by the signature of the guarantor.

(4) A guarantee may be effected by a signature alone. Unless the content otherwise requires:

- (a) A signature alone on the front of the instrument, other than that of the drawer or the drawee, is a guarantee;
- (b) The signature alone of the drawee on the front of the instrument is an acceptance; and
- (c) A signature alone on the back of the instrument other than that of the drawee is an endorsement.

(5) A guarantor may specify the person for whom he has become guarantor. In the absence of such specification, the person for whom he has become guarantor is the acceptor or the drawee in the case of a bill, and the maker in the case of a note.

(6) A guarantor may not raise as a defence to his liability the fact that he signed the instrument before it was signed by the person for whose account he is a guarantor, or while the instrument was incomplete.

##### Article 43

(1) A guarantor is liable on the instrument to the same extent as the party for whom he has become guarantor, unless the guarantor has stipulated otherwise on the instrument.

(2) If the person for whom he has become guarantor is the drawee, the guarantor undertakes to pay the bill at maturity.

##### Article 44

(1) Payment of an instrument by the guarantor in accordance with article 68 discharges the party for whom he became guarantor of his liability on the instrument to the extent of the amount paid.

(2) The guarantor who pays the instrument has rights thereon against the party for whom he became guarantor and against parties who are liable thereon to that party.

### Chapter V. Presentment, dishonour by non-acceptance or non-payment, and recourse

#### Section 1. Presentment for acceptance and dishonour by non-acceptance

##### Article 45

(1) A bill may be presented for acceptance.

(2) A bill must be presented for acceptance:

- (a) When the drawer has stipulated on the bill that it must be presented for acceptance;
- (b) When the bill is drawn payable at a fixed period after sight; or
- (c) When the bill is drawn payable elsewhere than at the residence or place of business of the drawee, except where such a bill is payable on demand.

*Article 46*

(1) The drawer may stipulate on the bill that it must not be presented for acceptance before a specified date or before the occurrence of a specified event. Except where a bill must be presented for acceptance under article 45(2), the drawer may stipulate that it must not be presented for acceptance.

(2) If a bill is presented for acceptance notwithstanding a stipulation permitted under paragraph (1) and acceptance is refused, the drawer, the endorser, and their guarantors are not liable for dishonour by non-acceptance.

(3) If the drawee accepts a bill notwithstanding a stipulation that it must not be presented for acceptance, the acceptance is effective.

*Article 47*

A bill is duly presented for acceptance if it is presented in accordance with the following rules:

(a) The holder must present the bill to the drawee on a business day at a reasonable hour;

(b) A bill drawn upon two or more drawees may be presented to any one of them, unless the bill clearly indicates otherwise;

(c) Presentment for acceptance may be made to a person or authority other than the drawee if that person or authority is entitled under the applicable law to accept the bill;

(d) If a bill is drawn payable on a fixed date, presentment for acceptance must be made before or on the date of maturity;

(e) A bill drawn payable on demand or at a fixed period after sight must be presented for acceptance within one year of its date;

(f) A bill in which the drawer has stated a date or time-limit for presentment for acceptance must be presented on the stated date or within the stated time-limit.

*Article 48*

(1) Delay in making a necessary presentment for acceptance within the time-limit stated within the bill is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of the delay ceases to operate, presentment must be made with reasonable diligence.

(2) A necessary or optional presentment for acceptance is dispensed with if the drawee is dead or has no longer the power freely to deal with his assets by reason of his insolvency, or is a fictitious person or a person not having capacity to incur liability on the instrument as an acceptor, or if the drawee is a corporation, partnership, association or other legal entity which has ceased to exist.

(3) When a necessary presentment for acceptance cannot be effected within the time-limit prescribed in subparagraph (d) or (e) of article 47 due to circumstances which are beyond the control of the holder and which he could neither avoid nor overcome, the necessary presentment for acceptance is dispensed with.

*Article 49*

If a bill which must be presented for acceptance is not so presented, the drawer, the endorsers and their guarantors are not liable on the bill.

*Article 50*

(1) A bill is considered to be dishonoured by non-acceptance:

(a) When the drawee, upon due presentment, expressly refuses to accept the bill or acceptance cannot be obtained with reasonable diligence or when the holder cannot obtain the acceptance to which he is entitled under this Convention;

(b) If presentment for acceptance is dispensed with pursuant to article 48, unless the bill is in fact accepted.

(2) If a bill is dishonoured by non-acceptance the holder may:

(a) Subject to the provisions of article 55, exercise an immediate right of recourse against the drawer, the endorsers and their guarantors;

(b) Exercise an immediate right of recourse against the guarantor of the drawee.

**Section 2. Presentment for payment and dishonour by non-payment***Article 51*

An instrument is duly presented for payment if it is presented in accordance with the following rules:

(a) The holder must present the instrument to the drawee or to the acceptor or to the maker on a business day at a reasonable hour;

(b) A bill drawn upon or accepted by two or more drawees, or a note signed by two or more makers, may be presented to any one of them, unless the instrument clearly indicates otherwise;

(c) If the drawee or the acceptor or the maker is dead, presentment must be made to the persons who under the applicable law are his heirs or the persons entitled to administer his estate;

(d) Presentment for payment may be made to a person or authority other than the drawee, the acceptor or the maker if that person or authority is entitled under the applicable law to pay the instrument;

(e) An instrument which is not payable on demand must be presented for payment on the date of maturity or on the business day which follows;

(f) An instrument which is payable on demand must be presented for payment within one year of its date;

(g) An instrument must be presented for payment:

(i) At the place of payment specified on the instrument; or

(ii) If no place of payment is specified, at the address of the drawee or the acceptor or the maker indicated on the instrument; or

(iii) If no place of payment is specified and the address of the drawee or the acceptor or the maker is not indicated, at the principal place of business or habitual residence of the drawee or the acceptor or the maker;

(h) An instrument which is presented at a clearing-house is duly presented for payment if the law of the place where the clearing-house is located or the rules or customs of that clearing-house so provide.

*Article 52*

(1) Delay in making presentment for payment is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, presentment must be made with reasonable diligence.

(2) Presentment for payment is dispensed with:

(a) If the drawer, an endorser or guarantor has expressly waived presentment; such waiver:

- (i) If made on the instrument by the drawer, binds any subsequent party and benefits any holder;
- (ii) If made on the instrument by a party other than the drawer, binds only that party but benefits any holder;
- (iii) If made outside the instrument, binds only the party making it and benefits only a holder in whose favour it was made;

(b) If an instrument is not payable on demand, and the cause of delay in making presentment continues to operate beyond 30 days after maturity;

(c) If an instrument is payable on demand, and the cause of delay continues to operate beyond 30 days after the expiration of the time-limit for presentment for payment;

(d) If the drawee, the maker or the acceptor has no longer the power freely to deal with his assets by reason of his insolvency, or is a fictitious person or a person not having capacity to make payment, or if the drawee, the maker or the acceptor is a corporation, partnership, association or other legal entity which has ceased to exist;

(e) If there is no place at which the instrument must be presented in accordance with article 51(g).

(3) Presentment for payment is also dispensed with as regards a bill, if the bill has been protested for dishonour by non-acceptance.

*Article 53*

(1) If a bill is not duly presented for payment, the drawer, the endorsers and their guarantors are not liable thereon.

(2) If a note is not duly presented for payment, the endorsers and their guarantors are not liable thereon.

(3) Failure to present an instrument for payment does not discharge the acceptor or the maker or their guarantors or the guarantor of the drawee of liability thereon.

*Article 54*

(1) An instrument is considered to be dishonoured by non-payment:

(a) When payment is refused upon due presentment or when the holder cannot obtain the payment to which he is entitled under this Convention;

(b) If presentment for payment is dispensed with pursuant to article 52(2) and the instrument is unpaid at maturity.

(2) If a bill is dishonoured by non-payment, the holder may, subject to the provisions of article 55, exercise a right of recourse against the drawer, the endorsers and their guarantors.

(3) If a note is dishonoured by non-payment, the holder may, subject to the provisions of article 55, exercise a right of recourse against the endorsers and their guarantors.

**Section 3. Recourse***A. Protest**Article 55*

If an instrument has been dishonoured by non-acceptance or by non-payment, the holder may exercise a right of recourse only after the instrument has been duly protested for dishonour in accordance with the provisions of articles 56 to 58.

*Article 56*

(1) A protest is a statement of dishonour drawn up at the place where the instrument has been dishonoured and signed and dated by a person authorized in that respect by the law of that place. The statement must specify:

- (a) The person at whose request the instrument is protested;
- (b) The place of protest; and
- (c) The demand made and the answer given, if any, or the fact that the drawee or the acceptor or the maker could not be found.

(2) A protest may be made:

- (a) On the instrument itself or on a slip affixed thereto ("allonge"); or
- (b) As a separate document, in which case it must clearly identify the instrument that has been dishonoured.

(3) Unless the instrument stipulates that protest must be made, a protest may be replaced by a declaration written on the instrument and signed and dated by the drawee or the acceptor or the maker, or, in the case of an instrument domiciled with a named person for payment, by that named person; the declaration must be to the effect that acceptance or payment is refused.

(4) A declaration made in accordance with paragraph (3) is deemed to be a protest for the purpose of this Convention.

*Article 57*

(1) Protest for dishonour of a bill by non-acceptance must be made on the day on which the bill is dishonoured or on one of the two business days which follow.

(2) Protest for dishonour of an instrument by non-payment must be made on the day on which the instrument is dishonoured or on one of the two business days which follow.

*Article 58*

(1) Delay in protesting an instrument for dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, protest must be made with reasonable diligence.

(2) Protest for dishonour by non-acceptance or by non-payment is dispensed with:

- (a) If the drawer, an endorser or guarantor has expressly waived protest; such waiver:

- (i) If made on the instrument by the drawer, binds any subsequent party and benefits any holder;
  - (ii) If made on the instrument by a party other than the drawer, binds only that party but benefits any holder;
  - (iii) If made outside the instrument, binds only the party making it and benefits only a holder in whose favour it was made;
- (b) If the cause of delay under paragraph (1) in making protest continues to operate beyond 30 days after the date of dishonour;
- (c) As regards the drawer of a bill, if the drawer and the drawee or the acceptor are the same person;
- (d) If presentment for acceptance or for payment is dispensed with in accordance with article 48 or 52(2).

#### Article 59

- (1) If a bill which must be protested for non-acceptance or for non-payment is not duly protested, the drawer, the endorsers and their guarantors are not liable thereon.
- (2) If a note which must be protested for non-payment is not duly protested, the endorsers and their guarantors are not liable thereon.
- (3) Failure to protest an instrument does not discharge the acceptor or the maker or their guarantors or the guarantor of the drawee of liability thereon.

### B. Notice of dishonour

#### Article 60

- (1) The holder, upon dishonour of a bill by non-acceptance or by non-payment, must give notice of such dishonour to the drawer, the endorsers and their guarantors.
- (2) The holder, upon dishonour of a note by non-payment, must give notice of such dishonour to the endorsers and their guarantors.
- (3) An endorser or a guarantor who receives notice must give notice of dishonour to the party immediately preceding him and liable on the instrument.
- (4) Notice of dishonour operates for the benefit of any party who has a right of recourse on the instrument against the party notified.

#### Article 61

- (1) Notice of dishonour may be given in any form whatever and in any terms which identify the instrument and state that it has been dishonoured. The return of the dishonoured instrument is sufficient notice, provided it is accompanied by a statement indicating that it has been dishonoured.
- (2) Notice of dishonour is duly given if it is communicated or sent to the party to be notified by means appropriate in the circumstances, whether or not it is received by that party.
- (3) The burden of proving that notice has been duly given rests upon the person who is required to give such notice.

#### Article 62

Notice of dishonour must be given within the two business days which follow:

- (a) The day of protest or, if protest is dispensed with, the day of dishonour; or
- (b) The receipt of notice given by another party.

#### Article 63

(1) Delay in giving notice of dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

(2) Notice of dishonour is dispensed with:

- (a) If after the exercise of reasonable diligence notice cannot be given;
- (b) If the drawer, an endorser or guarantor has expressly waived notice of dishonour, such waiver:
  - (i) If made on the instrument by the drawer, binds any subsequent party and benefits any holder;
  - (ii) If made on the instrument by a party other than the drawer, binds only that party but benefits any holder;
  - (iii) If made outside the instrument, binds only the party making it and benefits only a holder in whose favour it was made;
- (c) As regards the drawer of the bill, if the drawer and the drawee or the acceptor are the same person.

#### Article 64

Failure to give notice of dishonour renders a person who is required to give such notice under article 60 to a party who is entitled to receive such notice liable for any damages which that party may suffer from such failure, provided that such damages do not exceed the amount referred to in article 66 or 67.

### Section 4. Amount payable

#### Article 65

The holder may exercise his rights on the instrument against any one party, or several or all parties, liable thereon and is not obliged to observe the order in which the parties have become bound.

#### Article 66

- (1) The holder may recover from any party liable:
  - (a) At maturity: the amount of the instrument with interest, if interest has been stipulated for;
  - (b) After maturity:
    - (i) The amount of the instrument with interest, if interest has been stipulated for, to the date of maturity;
    - (ii) If interest has been stipulated to be paid after maturity, interest at the rate stipulated, or in the absence of such stipulation, interest at the rate specified in paragraph (2), calculated from the date of presentment on the sum specified in paragraph (1)(b)(i);
    - (iii) Any expenses of protest and of the notices given by him;



## (c) Before maturity:

- (i) The amount of the bill with interest, if interest has been stipulated for, to the date of payment, subject to a discount from the date of payment to the date of maturity, calculated in accordance with paragraph (3);
- (ii) Any expenses of protest and of the notices given by him.

(2) The rate of interest shall be the rate that would be recoverable in legal proceedings taken in the jurisdiction where the instrument is payable.

(3) Nothing in paragraph (2) prevents a court from awarding damages or compensation for additional loss caused to the holder by reason of delay in payment.

(4) The discount shall be at the official rate (discount rate) or other similar appropriate rate effective on the date when recourse is exercised at the place where the holder has his principal place of business, or if he does not have a place of business his habitual residence, or, if there is no such rate, then at such rate as is reasonable in the circumstances.

*Article 67*

A party who pays an instrument in accordance with article 66 may recover from the parties liable to him:

- (a) The entire sum which he was obliged to pay in accordance with article 66 and has paid;
- (b) Interest on that sum at the rate specified in article 66, paragraph (2), from the date on which he made payment;
- (c) Any expenses of the notices given by him.

**Chapter VI. Discharge****Section 1. Discharge by payment***Article 68*

(1) A party is discharged of liability on the instrument when he pays the holder, or a party subsequent to himself who has paid the instrument and is in possession thereof, the amount due pursuant to article 66 or 67:

- (a) At or after maturity; or
- (b) Before maturity, upon dishonour by non-acceptance.

(2) Payment before maturity other than under paragraph (1)(b) of this article does not discharge the party making the payment of his liability on the instrument except in respect of the person to whom payment was made.

(3) A party is not discharged of liability if he pays a holder who is not a protected holder and knows at the time of payment that a third person has asserted a valid claim to the instrument or that the holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery.

(4) (a) A person receiving payment of an instrument must, unless agreed otherwise, deliver:

- (i) To the drawee making such payment, the instrument;
- (ii) To any other person making such payment, the instrument, a receipted account, and any protest.

(b) In the case of an instrument payable by instalments at successive dates, the drawee or a party making a payment, other than payment of the last instalment, may require that mention of such payment be made on the instrument and that a receipt therefor be given to him.

(c) If an instrument payable by instalments at successive dates is dishonoured by non-acceptance or non-payment as to any of its instalments and a party, upon dishonour, pays the instalment, the holder who receives such payment must give the party a certified copy of the instrument and any necessary authenticated protest in order to enable such party to exercise a right on the instrument.

(d) The person from whom payment is demanded may withhold payment if the person demanding payment does not deliver the instrument to him. Withholding payment in these circumstances does not constitute dishonour by non-payment under article 54.

(e) If payment is made but the person paying, other than the drawee, fails to obtain the instrument, such person is discharged but the discharge cannot be set up as a defence against a protected holder.

*Article 69*

(1) The holder is not obliged to take partial payment.

(2) If the holder who is offered partial payment does not take it, the instrument is dishonoured by non-payment.

(3) If the holder takes partial payment from the drawee, the guarantor of the drawee, or the acceptor or the maker:

- (a) The guarantor of the drawee, or the acceptor or the maker is discharged of his liability on the instrument to the extent of the amount paid; and
- (b) The instrument is to be considered as dishonoured by non-payment as to the amount unpaid.

(4) If the holder takes partial payment from a party to the instrument other than the acceptor or the maker or the guarantor of the drawee:

- (a) The party making payment is discharged of his liability on the instrument to the extent of the amount paid; and
- (b) The holder must give such party a certified copy of the instrument and any necessary authenticated protest in order to enable such party to exercise a right on the instrument.

(5) The drawee or a party making partial payment may require that mention of such payment be made on the instrument and that a receipt therefor be given to him.

(6) If the balance is paid, the person who receives it and who is in possession of the instrument must deliver to the payer the receipted instrument and any authenticated protest.

*Article 70*

(1) The holder may refuse to take payment in a place other than the place where the instrument was presented for payment in accordance with article 51.

(2) If in such case payment is not made in the place where the instrument was presented for payment in accordance with article 51, the instrument is considered as dishonoured by non-payment.

## Article 71

- (1) An instrument must be paid in the currency in which the amount of the instrument is expressed.
- (2) When the amount of an instrument is expressed in a monetary unit of account within the meaning of article 4(11) and the monetary unit of account is transferable between the person making payment and the person receiving it, then, unless the instrument specifies a currency of payment, payment shall be made by transfer of the monetary unit of account. If the monetary unit of account is not transferable between those persons, payment shall be made in the currency specified in the instrument or, if no such currency is specified, in the currency of the place of payment.
- (3) The drawer or the maker may indicate on the instrument that it must be paid in a specified currency other than the currency in which the amount of the instrument is expressed. In that case:
- (a) The instrument must be paid in the currency so specified;
  - (b) The amount payable is to be calculated according to the rate of exchange indicated on the instrument. Failing such indication, the amount payable is to be calculated according to the rate of exchange for sight drafts (or, if there is no such rate, according to the appropriate established rate of exchange) on the date of maturity:
    - (i) Ruling at the place where the instrument must be presented for payment in accordance with article 51(g), if the specified currency is that of that place (local currency); or
    - (ii) If the specified currency is not that of that place, according to the usages of the place where the instrument must be presented for payment in accordance with article 51(g);
  - (c) If such an instrument is dishonoured by non-acceptance, the amount payable is to be calculated:
    - (i) If the rate of exchange is indicated on the instrument, according to that rate;
    - (ii) If no rate of exchange is indicated on the instrument, at the option of the holder, according to the rate of exchange ruling on the date of dishonour or on the date of actual payment;
  - (d) If such an instrument is dishonoured by non-payment, the amount payable is to be calculated:
    - (i) If the rate of exchange is indicated on the instrument, according to that rate;
    - (ii) If no rate of exchange is indicated on the instrument, at the option of the holder, according to the rate of exchange ruling on the date of maturity or on the date of actual payment.
- (4) Nothing in this article prevents a court from awarding damages for loss caused to the holder by reason of fluctuations in rates of exchange if such loss is caused by dishonour for non-acceptance or non-payment.
- (5) The rate of exchange ruling at a certain date is the rate of exchange ruling, at the option of the holder, at the place where the instrument must be presented for payment in accordance with article 51(g) or at the place of actual payment.

## Article 72

- (1) Nothing in this Convention prevents a Contracting State from enforcing exchange control regulations applicable in its territory and its provisions relating to the protection of its currency, including regulations which it is bound to apply by virtue of international agreements to which it is a party.
- (2) (a) If, by virtue of the application of paragraph (1) of this article, an instrument drawn in a currency which is not that of the place of payment must be paid in local currency, the amount payable is to be calculated according to the rate of exchange for sight drafts (or, if there is no such rate, according to the appropriate established rate of exchange) on the date of presentment ruling at the place where the instrument must be presented for payment in accordance with article 51(g).
- (b) (i) If such an instrument is dishonoured by non-acceptance, the amount payable is to be calculated, at the option of the holder, at the rate of exchange ruling on the date of dishonour, or on the date of actual payment.
- (ii) If such an instrument is dishonoured by non-payment, the amount is to be calculated, at the option of the holder, according to the rate of exchange ruling on the date of presentment or on the date of actual payment.
- (iii) Paragraphs (3) and (4) of article 71 are applicable where appropriate.

## Section 2. Discharge of a prior party

## Article 73

- (1) When a party is discharged wholly or partly of his liability on the instrument, any party who has a right on the instrument against him is discharged to the same extent.
- (2) Payment by the drawee of the whole or a part of the amount of a bill to the holder, or to any party who has paid the bill in accordance with article 66, discharges all parties of their liability to the same extent, except where the drawee pays a holder who is not a protected holder and knows at the time of payment that a third person has asserted a valid claim to the instrument or that the holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery.

## Chapter VII. Lost instruments

## Article 74

- (1) When an instrument is lost, whether by destruction, theft or otherwise, the person who lost the instrument has, subject to the provisions of paragraph (2) of this article, the same right to payment which he would have had if he had been in possession of the instrument. The party from whom payment is claimed cannot set up as a defence against liability on the instrument the fact that the person claiming payment is not in possession thereof.
- (2)(a) The person claiming payment of a lost instrument must state in writing to the party from whom he claims payment:

- (i) The elements of the lost instrument pertaining to the requirements set forth in article 1(2) or 1(3); for this purpose the person claiming payment of the lost instrument may present to that party a copy of that instrument;
  - (ii) The facts showing that, if he had been in possession of the instrument, he would have had a right to payment from the party from whom payment is claimed;
  - (iii) The facts which prevent production of the instrument.
- (b) The party from whom payment of a lost instrument is claimed may require the person claiming payment to give security in order to indemnify him for any loss which he may suffer by reason of the subsequent payment of the lost instrument.
- (c) The nature of the security and its terms are to be determined by agreement between the person claiming payment and the party from whom payment is claimed. Failing such an agreement, the court may determine whether security is called for and, if so, the nature of the security and its terms.
- (d) If the security cannot be given, the court may order the party from whom payment is claimed to deposit the amount of the lost instrument, and any interest and expenses which may be claimed under article 66 or 67, with the court or any other competent authority or institution, and may determine the duration of such deposit. Such deposit is to be considered as payment to the person claiming payment.

#### Article 75

- (1) A party who has paid a lost instrument and to whom the instrument is subsequently presented for payment by another person must notify the person to whom he paid of such presentment.
- (2) Such notification must be given on the day the instrument is presented or on one of the two business days which follow and must state the name of the person presenting the instrument and the date and place of presentment.
- (3) Failure to notify renders the party who has paid the lost instrument liable for any damages which the person whom he paid may suffer from such failure, provided that the damages do not exceed the amount referred to in article 66 or 67.
- (4) Delay in giving notice is excused when the delay is caused by circumstances which are beyond the control of the person who has paid the lost instrument and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.
- (5) Notice is dispensed with when the cause of delay in giving notice continues to operate beyond 30 days after the last date on which it should have been given.

#### Article 76

- (1) A party who has paid a lost instrument in accordance with the provisions of article 74 and who is subsequently required to, and does, pay the instrument, or who, by reason of the loss of

the instrument, then loses his right to recover from any party liable to him, has the right:

- (a) If security was given, to realize the security; or
- (b) If the amount was deposited with the court or other competent authority or institution, to reclaim the amount so deposited.

- (2) The person who has given security in accordance with the provisions of paragraph (2)(b) of article 74 is entitled to obtain release of the security when the party for whose benefit the security was given is no longer at risk to suffer loss because of the fact that the instrument is lost.

#### Article 77

A person claiming payment of a lost instrument duly effects protest for dishonour by non-payment by the use of a written statement that satisfies the requirements of article 74, paragraph (2)(a).

#### Article 78

A person receiving payment of a lost instrument in accordance with article 74 must deliver to the party paying the written statement required under article 74, paragraph (2)(a), receipted by him and any protest and a receipted account.

#### Article 79

- (1) A party who has paid a lost instrument in accordance with article 74 has the same rights which he would have had if he had been in possession of the instrument.
- (2) Such party may exercise his rights only if he is in possession of the receipted written statement referred to in article 78.

### Chapter VIII. Limitation (prescription)

#### Article 80

- (1) A right of action arising on an instrument may no longer be exercised after four years have elapsed:
  - (a) Against the maker, or his guarantor, of a note payable on demand, from the date of the note;
  - (b) Against the acceptor or the maker or their guarantor of an instrument payable at a definite time, from the date of maturity;
  - (c) Against the acceptor of a bill payable on demand, from the date on which it was accepted, or, if no such date is shown, from the date of the instrument;
  - (d) Against the drawer or an endorser or their guarantor, from the date of protest for dishonour by non-acceptance or non-payment or, where protest is dispensed with, from the date of dishonour.
- (2) If a party has paid the instrument in accordance with article 66 or 67 within one year before the expiration of the period referred to in paragraph (1) of this article, such party may exercise his right of action against a party liable to him within one year from the date on which he paid the instrument.

## II. SUMMARY RECORDS OF THE UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW FOR MEETINGS DEVOTED TO THE DRAFT CONVENTION ON INTERNATIONAL BILLS OF EXCHANGE AND INTERNATIONAL PROMISSORY NOTES<sup>a</sup>

Summary record of the 335th meeting  
Monday, 23 June 1986, 10.30 a.m.

[A/CN.9/SR.335]

*Temporary Chairman:* Mr. FLEISCHHAUER  
(Under-Secretary-General, The Legal Counsel)

*Chairman:* Mr. KARTHA (India)

*Chairman of the Committee of the Whole entrusted with studying the draft Convention on International Bills of Exchange and International Promissory Notes:* Mr. VIS (Netherlands)

*The meeting was called to order at 11 a.m.*

### Opening of the session

1. The TEMPORARY CHAIRMAN said that it had been necessary to reduce by one week the length of the session of the United Nations Commission on International Trade Law (UNCITRAL) in order to cope with the extremely serious financial situation of the United Nations caused by the failure of some Member States to pay their contributions to the United Nations regular budget and the late payment of contributions by others. In addition, there would be a considerable reduction in the United Nations documentation issued prior to the session, during the session and after it. Furthermore, as a result of the absolute freeze on hiring, two posts in the staffing table of the International Trade Law Branch which had been about to be filled would remain vacant, and new vacancies would occur as some of the currently serving staff members left the Branch.

2. UNCITRAL now had less time than expected for consideration of the main item on the agenda, namely, the draft Convention on International Bills of Exchange and International Promissory Notes; it was particularly regrettable that that should occur when, according to the opinion expressed by the Working Group on International Negotiable Instruments in its report (A/CN.9/273), the review of the draft Convention at the Commission's current session should have been the final consideration of the full text prior to its adoption as a convention. UNCITRAL must decide whether it was necessary to have a thorough examination of the articles of the draft Convention at a diplomatic conference or at an extension of the session of

UNCITRAL, or whether it would suffice—and perhaps be even preferable—to proceed to its adoption, perhaps in the context of the General Assembly and the Sixth Committee.

3. There were other important items on the agenda for the current session. In the field of international payments, another draft was about to be completed: that was the draft Legal Guide on Electronic Funds Transfers, prepared by the secretariat in collaboration with the Study Group on International Payments. As indicated in the Secretary-General's report on that item (A/CN.9/278), the comments submitted by Governments and international organizations on the Legal Guide were, without exception, extremely favourable. The annex to the report contained suggestions for proposed modifications to the Legal Guide. The Commission might wish to proceed to the adoption of the Legal Guide and to request that it should be published in an appropriate form. Its adoption and publication would constitute an important achievement for UNCITRAL and a valuable contribution in the search for harmonious solutions to the various existing legal questions in that important and contemporary sphere. The Commission might wish to decide whether it should now begin the preparation of uniform rules and, if so, what form they should take. The secretariat had included in the report certain considerations and suggestions in that regard.

4. The Working Group on the New International Economic Order had completed its consideration of all the chapters of the draft Legal Guide on Drawing Up International Contracts for Construction of Industrial Works (A/CN.9/276). The secretariat was now revising those chapters with a view to implementing the decisions of the Working Group. It was the Working Group's intention to complete the draft Legal Guide at its next session, to be held in March or April 1987, which would enable UNCITRAL to consider and adopt the Legal Guide at its next annual session.

5. Since the Working Group on the New International Economic Order would soon conclude the work entrusted to it, the Commission might wish to consider possible items for future work. The secretariat had prepared a note (A/CN.9/277) in which four items of possible interest were examined and some suggestions were made for their consideration by UNCITRAL.

6. There were two other spheres, both of which were included in the important item of co-ordination of work, which the

<sup>a</sup>The summary records contained in this volume include the corrections requested by the delegations and such editorial changes as were considered necessary.

Commission might wish to consider in relation to future work. The first concerned the legal aspects of automatic data processing, on which UNCITRAL had a detailed report (A/CN.9/279) containing a description of the work carried out, an analytical summary and a number of conclusions. The second involved international commercial arbitration, which had been a priority item of the Commission from the outset, and was a field in which the Commission had achieved a number of successes, such as the UNCITRAL Arbitration Rules and the Model Law on International Commercial Arbitration. The Commission had before it a report (A/CN.9/280) which contained information on the activities carried out by other organizations, and which might help it in deciding whether some of the six aspects referred to in the report deserved further study.

7. Two more documents merited special mention. The 1986 report on the current activities of international organizations related to the harmonization and unification of international trade law (A/CN.9/281) was of impressive quality and scope and constituted an extremely useful and informative document. Judging from the report of the Working Group on International Contract Practices concerning the work carried out at its ninth session (A/CN.9/275), satisfying progress had been made in formulating uniform rules on the liability of operators of transport terminals.

*The meeting was suspended at 11.20 a.m. and resumed at 11.45 a.m.*

#### **Election of officers**

8. The TEMPORARY CHAIRMAN announced that the Group of Asian States had proposed the candidature of Mr. Kartha (India) for the office of Chairman of the Commission.

9. *Mr. Kartha (India) was elected Chairman by acclamation.*

10. *Mr. Kartha (India) took the Chair.*

11. Mr. GOH (Singapore) nominated Mr. Vis (Netherlands) for the office of Chairman of the Committee of the Whole entrusted with studying the draft Convention on International Bills of Exchange and International Promissory Notes.

12. Mrs. ADEBANJO (Nigeria) supported the nomination.

13. *Mr. Vis (Netherlands) was elected Chairman of the Committee of the Whole entrusted with studying the draft Convention on International Bills of Exchange and International Promissory Notes.*

#### **Adoption of the agenda (A/CN.9/272)**

14. Mr. SZASZ (Hungary) asked for a clarification on the repercussions of the shortening of the session on the provisional agenda and the tentative schedule of meetings (A/CN.9/272).

15. Mr. BERGSTEN (Secretary of the Commission) said that there would be no modification whatsoever of the agenda. With respect to the schedule of meetings, the reduction of the length of the session from four to three weeks meant that less time would have to be given to the main task before the Commission in 1986: consideration of the draft Convention on International Bills of Exchange and International Promissory Notes. Instead

of 14 working days for the study of that item, as anticipated in document A/CN.9/272, the Commission would have only 9 working days, up to 3 July inclusive. On the other hand, there would be no substantial change in the schedule of meetings for the last week; 7–9 July would be devoted to the study of the other items and 10 and 11 July to the preparation and adoption of the report of the Commission. Nevertheless, even though the Commission would conclude, during the first two weeks of the session, its substantive consideration of the draft Convention on International Bills of Exchange and International Promissory Notes, it would perhaps have to conclude the drafting changes in that text in the first days of the last week.

16. *The agenda was adopted.*

#### **International payments**

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/261, A/CN.9/273, A/CN.9/274, A/CN.9/285 and A/39/17)*

17. The CHAIRMAN suggested that, in view of the highly technical nature of the discussion on the draft Convention on International Bills of Exchange and International Promissory Notes, the meeting should be chaired by the Chairman of the Committee of the Whole.

18. *It was so decided.*

19. Mr. VIS (Chairman of the Committee of the Whole entrusted with studying the draft Convention on International Bills of Exchange and International Promissory Notes) said that in view of the circumstances the adoption of the Convention would not be an easy task. It would be necessary to shorten the deliberations on the various provisions of the draft, endeavouring, nevertheless, to ensure that the Commission maintained its usual good standard of work. He believed that the best way of proceeding would be to study the work carried out by the Working Group on International Negotiable Instruments at its two most recent sessions.

20. The main document before the Commission was the draft Convention on International Bills of Exchange and International Promissory Notes (A/CN.9/274). It was a consolidated text which had incorporated the decisions adopted by the Commission at its seventeenth session and the amendments proposed by the Working Group. In addition to that document, there were the two reports of the Working Group on the work done at its thirteenth and fourteenth sessions (A/CN.9/261 and A/CN.9/273, respectively), the 1981 commentary on the draft Convention (A/CN.9/213) and the report of the Commission on its seventeenth session, when it had first examined the draft (A/39/17).

21. The first question to be studied was that of forged endorsements (article 23 of the draft Convention). As would be seen, that was one of the fundamental questions which divided the systems of common law and civil law. The current wording of article 23 represented a compromise solution between the two systems. Under civil law, the forged endorsement did not prevent the endorsee from being a holder. The risk of loss as a result of a forgery fell ultimately on the person who had been dispossessed of the instrument, through either loss or theft—in other words, the person whose endorsement had been forged.

On the other hand, under the common-law system, the forged endorsement prevented the endorsee from being a holder. In that case, the risk of loss fell on the person who had obtained the instrument from the forger of the endorsement, unless the forger could be found. Draft article 23 satisfied both criteria in that, on the one hand, it laid down that the forged endorsement did not prevent the endorsee from being a holder, and, on the other hand, assigned the risk of loss to the person who had received the instrument from the hands of the forger. That compromise solution had been present in the draft Convention from the beginning and had been the view accepted by the Working Group and by the Commission.

22. It should be pointed out that article 14(1)(b) of the draft Convention granted the status of holder to the person in possession of an instrument which had been endorsed to him, or on which the last endorsement was in blank, and on which there appeared an uninterrupted series of endorsements, even if any of them was forged. Under that provision, the forged endorsement did not prevent a person from being a holder, and for that reason it would be necessary to bear that provision in mind in interpreting article 23.

23. Article 23 provided that the person whose endorsement was forged had the right to recover compensation for any damage that he might have suffered because of the forgery against, in the first place, the forger and, secondly, the person to whom the instrument had been directly transferred by the forger (para. (1)(a) and (b)). There had never been any disagreement on that point.

24. On the other hand, the person whose endorsement was forged also had the right to recover compensation from the party or the drawee who had paid the instrument directly to the forger (para. (1)(c)). Thus, the drawer, the maker, the acceptor and the drawee could be held liable for the damage suffered by the person whose endorsement had been forged. That was a new element that had arisen during the Commission's discussions in 1984. In other words, if a person forged the signature of the holder of a bill of exchange and made it payable to himself, and then presented it to the drawee or to the acceptor for payment, those last two were liable for damages if they paid the forger.

25. Mr. SPANOGLE (United States of America) said that, in his opinion, the problem lay in knowing what had been meant by the expression "paid ... directly". Since, in article 23(2), in practice, the bank which made the collection was exempt from liability, banking circles in his country had indicated that it must be made clear that the person referred to in article 23(1)(c) included the person who paid through a series of banks which acted as intermediaries for the collection. The wording of subparagraph (c) could be amended to reflect that interpretation.

26. Mr. VIS (Chairman of the Committee of the Whole) offered an example as clarification of what had been said: "A" forged the endorsement of the holder and endorsed the instrument to himself; the instrument was paid to "A", but through a collecting bank to which "A" endorsed the instrument for collection; the bank presented the instrument to the drawee, and the latter paid the bank. According to his interpretation, it was the wish of the United States representative that "A" should continue to be held liable and that the collecting bank too would be liable.

27. Mr. SPANOGLE (United States of America) said that, from his viewpoint, the rules for the collecting bank were clearly established in article 23(2), and that it was hardly likely that that bank would be held liable. It was not, therefore, necessary to refer to that situation in connection with paragraph (1)(c).

28. Mr. VIS (Chairman of the Committee of the Whole) asked whether the drawee who had paid the collecting bank was liable. After all, he had paid the forger not directly, but through a collecting bank. At first sight, it seemed sensible that he should be held liable in that case.

29. Mr. SPANOGLE (United States of America) said that he had always interpreted subparagraph (c) to mean that direct payment referred to the payment to the forger, even though it had been made through a bank.

30. Mr. VIS (Chairman of the Committee of the Whole) said that, according to a literal interpretation, the payment that was made through a collecting bank was not a direct payment made by the drawee to the forger. It was therefore necessary to clarify in that case whether the payee whose endorsement had been forged would have, in any event, the right to recourse against the drawee who had paid, in accordance with article 23.

31. Mr. CRAWFORD (Canada) said he wondered how the proposal by the United States representative could be reconciled with the practice of United States banks requiring that endorsements must be guaranteed prior to payment of instruments presented to them through banks in other countries.

32. Mr. SPANOGLE (United States of America) said that, although that was done in practice, there was no law requiring it. The problem was that, if the forgery were discovered after payment of the instrument that had been collected through a bank, the person whose signature had been forged literally had no one from whom he could claim, unless he had some recourse against the drawee. Article 23(2) contained a list of conditions which, in practice, discharged collecting banks of liability. If the losing party was to be compensated, there would have to be someone against whom a claim could be asserted. In a case where the forger had presented the document to the bank, the drawee was the only party against whom a claim could be made.

33. Mrs. PIAGGI de VANOSI (Argentina) said that it was her understanding that, if a bank had been an endorsee for collection of the forged instrument, the bank was liable under paragraph (1)(b). If, on the other hand, a collecting bank had not been involved, the drawee was liable under paragraph (1)(c).

34. Mr. VIS (Chairman of the Committee of the Whole) indicated that, since paragraph (2) excluded the collecting bank from paragraph (1)(b), the payee whose endorsement had been forged would have no recourse against the collecting bank that had taken the instrument from the forger. Paragraph (2) provided separately for such cases. However, if no collecting bank had been involved, it would mean that the forger had been paid directly, in which case the payee would have the right to claim compensation from the drawee who had paid the instrument. In his opinion, the United States representative was referring to cases in which the forger deposited the instrument in a bank for collection and the bank obtained payment in favour of the forger. That did not constitute direct payment to the forger,

according to a literal interpretation of paragraph (1)(c). The issue was to determine whether, even in that case, the drawee who had paid the forger through a collecting bank was also accountable to the payee whose endorsement had been forged. He believed that the United States representative had been correct in pointing out that the paragraph, as worded, did not make that clear. In any case, it should be kept in mind that, according to paragraph (3), the liability of the drawee who had made payment depended upon his knowledge of the forgery.

35. Mrs. PIAGGI de VANOSI (Argentina) proposed that the word "directly" should be deleted from article 23(1)(c).

36. Mr. SPANOGLE (United States of America) said that that would resolve the problem, but it could create others.

37. Mr. VIS (Chairman of the Committee of the Whole) said that, if he heard no objection, he would consider that the Committee had accepted the United States proposal to make the drawee also liable even if he had paid the forger not directly, but rather through a collecting bank or several collecting banks. If that were indeed the case, he proposed that the representatives of the United States and Argentina should draft a provision that would appropriately reflect the decision taken.

38. *It was so decided.*

39. Mr. VIS (Chairman of the Committee of the Whole) invited the Committee to examine the wording "or any party who signed the instrument before the forgery", contained in article 23(1). That provision meant that only parties who had signed before the forgery, such as the drawer, could suffer damage. On the other hand, the payee whose endorsement had been forged could, of course, not be held liable, since he had not signed the instrument.

40. Mr. BRANDT (German Democratic Republic) said that the right to recover compensation provided for in article 23 was justified, but the number of persons entitled to receive it should be limited, as had been established in the Working Group on International Negotiable Instruments.

41. Mr. GUEST (United Kingdom) expressed reservations about the relationship between article 23(1)(c) and article 68(3), in which two different situations were considered, for the first referred to the right to recover compensation and the second to the discharge of liability.

42. Mr. VIS (Chairman of the Committee of the Whole) said it seemed that the underlying idea in the draft Convention was that the drawee or acceptor should not pay if he had knowledge of the forgery. If he did pay, he could be liable to the person whose signature had been forged, and the payment would not discharge the acceptor of liability, which was reasonable. If the payee's signature was forged and the acceptor had knowledge of the forgery, the rule was that he should not pay. If he did pay, the acceptor was liable to the payee, who still had recourse to the acceptor because the payment had not discharged him of liability. In that context, there was apparently no conflict between the two articles.

43. Mr. GUEST (United Kingdom) said that situations could arise in which the two articles would conflict. For example, if the

acceptor's absence of knowledge had been due to his negligence, he was protected under article 68(3), which made no mention of negligence, but he might be liable under article 23. However, if he had not known that the holder had forged the signature of the payee, but merely that the signature had been forged, the acceptor would not be liable under article 68. He would be, however, under article 23.

44. Mr. DUCHECK (Austria) said that the word "knows" in article 68(3) should be considered in relation to the negligence implied in article 5.

45. Mr. GUEST (United Kingdom) said that, in using the words "or could not have been unaware of its existence" in article 5, the Working Group had not meant to imply negligence alone.

46. Mr. VASSEUR (France) said that, if the term "knowledge" in article 5 was to be consistent with that term as used in articles 23 and 23 *bis*, the expression "provided that such absence of knowledge was not due to his negligence" would have to be deleted from paragraph 2 of articles 23 and 23 *bis*.

47. Mrs. PIAGGI de VANOSI (Argentina) said that, in her opinion, the word "knowledge" in articles 23 and 23 *bis* was similar to the wording "or could not have been unaware of its existence" in article 5. Both expressions referred to the "objective good faith" in the law on negotiable instruments, and the articles did not contradict one another.

48. Mr. VIS (Chairman of the Committee of the Whole) noted that the wording of article 23 seemed to refine the concept of "knowledge" in article 5. The two concepts could be harmonized in order to facilitate comprehension of those articles, and to that end, he believed that the French proposal was appropriate.

49. Mr. GANTEN (observer for the Federal Republic of Germany) said that it was difficult at that stage—before article 5 had been examined—to establish a final version of article 23. He believed that the concept of "knowledge" differed in articles 5 and 23, respectively, even though the difference might not be very important. If article 5 was amended to include the concept contained in articles 23 and 23 *bis*, it would be easier to formulate articles 23 and 23 *bis* later on. If the current wording of article 5 was retained, he would have reservations about the wording of articles 23 and 23 *bis*.

50. Mr. VAN SANDIK (observer, International Bar Association) said that first the wording of article 5 should be studied, and then the wording of article 23, since the concept of "knowledge" was presenting problems. In that regard, he supported the French proposal.

51. Mr. VIS (Chairman of the Committee of the Whole) said that, since at that point no decision could be made on the contents of article 23, it would be useful to analyse the term "knowledge", which also appeared in other articles of the Draft Convention, when examining article 5.

Summary record of the 336th meeting  
Monday, 23 June 1986, 3 p.m.

[A/CN.9/SR.336]

Chairman: Mr. KARTHA (India)

Chairman of the Committee of the Whole:  
Mr. VIS (Netherlands)

The meeting was called to order at 3.05 p.m.

**International payments (continued)**

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes* (continued) (A/CN.9/273, A/CN.9/274 and A/CN.9/285)

Article 23

1. Mr. VIS (Chairman of the Committee of the Whole), referring to the text of the draft Convention contained in document A/CN.9/274, said that agreement had been reached on the proposal of the representative of the United States to add to paragraph (1)(c) of article 23 the words "or to the forger through one or more endorsees for collection". If he heard no objection, he would take it that the Commission adopted paragraph (1), as amended.

2. *It was so decided.*

3. Mr. VASSEUR (France), referring to paragraph (2), suggested that the phrase "provided that such absence of knowledge was not due to his negligence" should be replaced by the phrase "within the meaning of article 5".

4. Mr. VIS (Chairman of the Committee of the Whole) said that the Commission had decided to resume discussion of the question of knowledge when it took up article 5. If he heard no objection, he would take it that the Commission adopted paragraph (2), pending future discussion of that question.

5. *It was so decided.*

6. Mr. VIS (Chairman of the Committee of the Whole) said that, under paragraph (3), a party, maker, acceptor or drawee who paid an instrument directly to the forger or to the forger through one or more endorsees for collection was not liable if he was without knowledge of the forgery. If he heard no objection, he would take it that, apart from the additional wording following the term "knowledge" to be discussed at a later meeting, the principle of making the liability dependent on knowledge was acceptable.

7. *It was so decided.*

8. Mr. VIS (Chairman of the Committee of the Whole) asked whether some members of the Commission still objected to the reference to article 66 or 67 in paragraph (4).

9. Mr. VASSEUR (France) said that articles 66 and 67 did not stipulate the means for determining the amount of damages. The reference to those articles therefore appeared to be somewhat meaningless.

10. Mr. VIS (Chairman of the Committee of the Whole) said that those articles established a ceiling on damages. If he heard

no other objections, he would take it that the Commission adopted paragraph (4) as it stood.

11. *It was so decided.*

Article 23 bis

12. Mr. VIS (Chairman of the Committee of the Whole) said that, since the provisions of article 23 bis were parallel to those of article 23, the question had arisen as to whether to combine them in one article, thereby equating the term "forgery" with the term "endorsement made by an agent without authority". However, some of the members had expressed a preference for having two separate articles. He asked whether the members agreed to the provisions of article 23 bis, on the understanding that the change just made in article 23(1)(c) would also be made in article 23 bis (1)(c).

13. Mr. ANGELICI (Italy) said that his delegation could not agree to the equation of forged instruments with endorsements by an agent without authority. In the latter case, the transferee would have the much more difficult tasks not only of determining the fact of the forgery but also of researching the entire legal situation, which could be very complex. For example, in Italy it was difficult to establish whether the agent who had authority in general also had the authority to deal with a bill of exchange. It therefore seemed inappropriate to impose, in such case, a risk on the purchaser of the instrument. Eventually, a possible compromise would be to establish fault liability. However, if the rule imposed strict liability on the transferee, his delegation could not agree with the proposal.

14. Mr. VIS (Chairman of the Committee of the Whole) asked whether there were any delegations which shared the concerns of the Italian delegation.

15. Mr. VAN SANDICK (observer, International Bar Association) said that the point just made by the representative of Italy had also been made by the Italian rapporteur who had presented one of the 11 reports from various jurisdictions.

16. Mr. VIS (Chairman of the Committee of the Whole) said that there did not seem to be any further support for the view expressed by the representative of Italy. However, it would be noted in the report.

17. He then read out a letter from the Acting Director-General of the Department of Legislation of Norway addressed to the Secretary of the Commission, in which the Norwegian Government proposed the following wording for article 23 bis (3): "Also, any person against whom compensation is sought other than the agent shall not be liable under paragraph (1), if, etc.". The Norwegian Government had commented that the person to whom the instrument was directly transferred by the unauthorized agent should not be liable towards the purported principal under paragraph (1) of article 23 bis unless he had or ought to have had knowledge of the lack of authority. The risk of loss should not be transferred from the purported principal to the endorsee in good faith. Since in most cases the transferee was in good faith, there would exist some kind of relationship between the purported principal and the unauthorized agent. Thus, it seemed more equitable and better public policy to let the purported principal and not the transferee in good faith bear



the risk of unauthorized transfers by someone purporting to have authority as an agent. The solution in such cases, therefore, should not be exactly the same as that in article 23(3) regarding forged endorsements.

18. Consideration of that proposal would be postponed until the secretariat had prepared copies of the letter for distribution to the members.

#### Article 4

19. Mr. VIS (Chairman of the Committee of the Whole) read out the new text of article 4(7) as adopted by the Working Group. The Working Group had redrafted paragraph (7) in accordance with the general feeling expressed in the Commission two years previously that if an incomplete instrument was completed in accordance with the authority given, the holder would become a protected holder at the time of completion. If that consensus still held, the Commission would adopt paragraph (7) of article 4 in so far as it related to an incomplete instrument. The rest would remain as it stood. He noted that the Working Group had also deleted the words "the instrument must be regular on its face".

20. If he heard no objection, he would take it that the Commission agreed to the new definition of a protected holder.

21. *It was so decided.*

22. Mr. ANGELICI (Italy) said that article 4 needed to be brought into line with article 11. In the case of an incomplete instrument, the sole problem was that which arose from the non-observance of the agreement of completion. In all other respects, there was no reason to make a difference between a complete and an incomplete instrument. If that reasoning was correct, he did not see why the status of the protected holder must depend on the fact that the instrument was subsequently completed in accordance with the agreement of completion. The difference between a complete and an incomplete instrument must be understood in the light of the extent of the protection of the holder, not the protection itself. It was therefore preferable to delete the new words referring to an incomplete instrument included in article 4 by the Working Group.

23. On the other hand, his delegation supported the Working Group's proposal to delete the requirement that the instrument must be regular, because such a requirement would be too ambiguous. If the instrument was irregular, there were only two possibilities: that the irregularity was so important as to deprive the instrument of its validity, with the result that there was no problem with regard to the protection of the holder, or that the instrument was valid notwithstanding the irregularity. In the latter case, the problem of protection arose only if the irregularity implied knowledge of the claim or defence.

24. Mr. VIS (Chairman of the Committee of the Whole) asked how it would then be determined whether someone who completed an instrument was a holder or a protected holder.

25. Mr. ANGELICI (Italy) said that the protected holder was defined by the requirements stipulated in subparagraphs (a) and (b) of paragraph (7) of article 4. The problem of completion was entirely resolved by article 11.

26. Mr. VIS (Chairman of the Committee of the Whole) said he took it that the representative of Italy did not disagree with

the view expressed in the current wording of article 4(7) that the holder could be described as a protected holder even if the instrument was not a negotiable instrument under the Convention when it was originally taken by the holder.

27. Mr. ANGELICI (Italy) said that the Chairman's interpretation was correct. There might be a problem if the instrument was completed subsequently by another person as a result of a later circulation of the instrument.

28. Mr. CRAWFORD (observer for Canada) said that it was unclear whether the representative of Italy was suggesting that it should be impossible to become a protected holder of an incomplete instrument, or whether he was merely proposing a drafting change to clarify the relationship between article 4(7) and article 11.

29. Mr. VIS (Chairman of the Committee of the Whole) said his understanding was that no substantive question was involved; the representative of Italy did recognize that a person who received an incomplete instrument and then completed it in accordance with the authority given could be a protected holder.

30. Mr. ANGELICI (Italy) said that confusion was created when the notion of the protected holder was made to depend on the notion of completion in accordance with authority.

31. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that her interpretation of the article was that the reference to article 11 was indispensable, because what was involved was the requirement that the instrument must be completed. In the absence of such requirement, she would agree that article 4 should not refer to article 11. In the new text, however, the holder could be protected if he had received an incomplete instrument, in other words, when some prerequisite had not in fact been met, it being understood that the instrument had subsequently been completed in accordance with the agreement. It was necessary to clarify who would be completing the instrument. Perhaps it could be indicated that the instrument was to be completed by the holder. He could become a protected holder if he met the other requirements, but only when he himself had completed the instrument in accordance with the agreement.

32. Mr. VIS (Chairman of the Committee of the Whole) said that the person in question was receiving an incomplete, and therefore non-negotiable instrument. He was at that time not considered to be a holder because he did not have a negotiable instrument. He did, however, have authority to complete it, and if he did so in accordance with the authority given by the drawer or maker, he might qualify as a protected holder, provided he complied with the other requirements for protected holder status.

33. Mr. VASSEUR (France) said that he did not recall whether it had been decided at Vienna to make reference in article 4(7) to the authority given. He feared that the person who received an instrument would be obliged to ask for justification for the authority given to the person who appeared to have completed the instrument. It might be preferable to return to the original wording, which stated that the term "protected holder" meant the holder of an instrument which appeared to be complete and regular when he became the holder of it. A person receiving an instrument, then, would not necessarily have to worry about the possible authority in the possession of the

person who held the instrument before he did. An international instrument should not constrain the person receiving the instrument to verify the authority of the previous holder of the instrument in order for him to become a protected holder.

34. Mr. VIS (Chairman of the Committee of the Whole) said that, in general, the person who completed the instrument was the same person who had received authority to do so. Verification by that person therefore seemed unnecessary. Subsequent holders could, of course, become protected holders. It was the intention of the Convention that there should be no need for subsequent transferees to verify whether the instrument was completed in accordance with the authority given. Even where it was not so completed, the transferee could be a protected holder. There seemed to be a misunderstanding of the exact field of application of the definition of a protected holder. It basically dealt only with the person who completed an incomplete instrument, and it answered the question "Can that person become a protected holder?" affirmatively, provided that, *inter alia*, he completed it in accordance with the authority given.

35. Mr. VASSEUR (France) said that he was concerned as to whether, if a person received an incomplete instrument, he had to verify the authority of the person who transferred that instrument to him in order to become a protected holder. In his view, such a person did not have that obligation if the instrument had appeared to be regular and complete when received. However, article 4(7) did not meet that concern, because under that article, when a person received an instrument, he was required to request a justification of the authority of the person who transferred the instrument to him.

36. Mr. VIS (Chairman of the Committee of the Whole) said that the drawer or maker who transferred an incomplete instrument to another person presumably was giving him authority to complete the instrument.

37. Mr. VASSEUR (France) said that another situation frequently encountered in practice was that in which the drawer gave an instrument to a banker who himself transferred the instrument to another banker. If the instrument was completed by the first banker, it was not clear whether the second banker was required to consider whether the first banker had had the authority to complete it. Article 4(7) did not really answer the question which arose in that situation.

38. Mr. VIS (Chairman of the Committee of the Whole) said he thought that only the case of the first banker was covered in article 4(7). The second banker did not need to be concerned with the question.

39. Mr. VASSEUR (France) said that he was not sure whether article 4(7) took account of the situation he had presented. He inquired whether the second banker should be concerned about the authority which might have been given to the first banker by the drawer.

40. Mr. VIS (Chairman of the Committee of the Whole) said that that question had been dealt with in paragraph 22 of the report of the Working Group on International Negotiable Instruments on the work of its fourteenth session (A/CN.9/273).

41. Mr. GUEST (United Kingdom) said that he had no difficulties with the situation presented by the representative of France. It was clear from the English text that, if a person took a

complete instrument, provided that he had satisfied the other conditions, he was a protected holder. In the example given by the representative of France, the second banker had taken a complete instrument and he was, therefore, protected.

42. Mr. VIS (Chairman of the Committee of the Whole) asked whether the French text would be clearer if the words "*par lui*" were inserted in article 4(7) after the words "*a été complété*".

43. Mr. VASSEUR (France) said that the addition proposed by the Chairman should appear in all texts.

44. Mr. VIS (Chairman of the Committee of the Whole) said that the Commission would make the proposed addition to article 4(7) in all texts.

45. Mr. GRIFFITH (Australia) said his delegation had understood that the Working Group at its fourteenth session had decided to delete the words "by him" in all texts for the reasons indicated in paragraph 22 of document A/CN.9/273.

46. Mr. VIS (Chairman of the Committee of the Whole) said that that had been the case, but that the deletion had given rise to difficulties of interpretation.

47. Mr. GRIFFITH (Australia) said that to restore the words "by him" would, reintroduce the difficulty which the Working Group had sought to eliminate.

48. Mr. VIS (Chairman of the Committee of the Whole) said that the Working Group had deleted the words "by him" because the instrument might be completed by a person acting under the authority of the person in possession of the incomplete instrument.

49. Mr. SPANOGLE (United States of America) said that his preference was to maintain the English text exactly the way it was, without the words "by him".

50. Mr. VIS (Chairman of the Committee of the Whole) said that, if the delegations which used the French language considered that the words "*par lui*" should be reinserted, the Commission must accept that view.

51. Mr. DUCHEK (Austria) said that his delegation preferred that all texts should remain consistent. The words "by him" must be added in all languages, since the addition of those words to the French text only might give rise to different interpretations when the French text was used. He did not know how frequently the situation arose in which there was one person who was the holder of an instrument and another person who, acting under the authority of the first person, completed that instrument. The frequency with which such a situation arose should determine whether the words "by him" were included in all texts.

52. Mr. SPANOGLE (United States of America) asked whether the problem in the French text could be solved by the insertion, in article 4(7), after the words "was completed", of the words "after he took it". That would make it quite clear that the person who took a complete instrument would not have to worry about the authority given for its completion.

53. Mr. VIS (Chairman of the Committee of the Whole) said that perhaps it would be better to restore the words "by him", on the ground that the Working Group's reasons for deleting them

might not be of any practical significance. The Working Group seemed to have had in mind the case of a person holding the instrument who gave it to someone who filled in the name of the payee.

54. Mr. SPANOGLE (United States of America) said that he favoured the insertion of the words "after he took it". He had in mind the case in which an escrow agent in possession of an instrument was to enter figures on it when the details of the transaction were fully known. That person might not be the holder, and the name of the payee might already be known and on the instrument.

55. Mr. VASSEUR (France) said that the addition proposed by the representative of the United States was not very clear. He preferred the insertion, in article 4(7), after the words "*a été complété*", of the words "*par lui ou sous son autorité*", since that would take account of the completion of the instrument by a person delegated by the holder.

56. Mr. GRIFFITH (Australia) said that, frequently in such cases, the holder could not be referred to in English by the words "him" or "her" but by "it". The introduction of personal pronouns would therefore give rise to uncertainty and difficulties in the English text. His delegation accepted the French proposal to use the words "under his authority", but its first preference was to leave the text as it was.

57. Mr. VIS (Chairman of the Committee of the Whole) said he took it that the Commission was in agreement with regard to the substance of article 4(7). He suggested that the question of the appropriate wording should be left to a drafting group or to the representative of France and those representatives who did not agree with his proposal.

58. *It was so decided.*

#### Article 25

59. Mr. VIS (Chairman of the Committee of the Whole) said that, at its 1984 session, the Commission had made drastic changes in article 25. The previous text had basically followed the common-law system, and had corresponded to the dual concept of holder and protected holder. However, there had been opposition to such an approach on the grounds that a person should not be subject to a claim or defence of which he had no previous knowledge. Under common law, knowledge of one defence let in all other defences, whether a person knew about them or not. At the 1984 session, the Commission had reached the general consensus that there might be merit in the civil-law approach. However, if the holder had obtained the instrument by fraud or participated in a fraud, he was subject to all defences, as was the case under common law. That solution had been fully endorsed in the Working Group by both civil and common law representatives.

60. He took it that the Commission agreed to paragraphs (1), (2) and (2 *bis*).

61. Speaking as the representative of the Netherlands, he said that he had difficulty in understanding the word "asserted" in paragraph (3)(a). He was not sure whether it was enough for the payee to go to the drawer and assert a claim, or whether the payee must bring an action against the holder, accusing him of stealing an instrument.

62. Mr. GRIFFITH (Australia) said that his delegation had difficulty with the association of the words "asserted" "valid" and "claim". He could not imagine a case in which it could be said that a valid claim had been asserted, unless proceedings had been instituted and a final judgement had been received. The word "valid" should therefore be deleted from paragraph (3)(a) and from similar provisions. His delegation was prepared to accept an interpretation according to which the institution of proceedings would not be required.

63. Mr. VIS (Chairman of the Committee of the Whole) agreed that the word "valid" should perhaps be deleted. The question of validity had to be left to the courts.

64. Mr. CRAWFORD (observer for Canada) inquired whether the draft was not merely indicating that if the subsequent judicial review showed that the third person had assisted a valid claim, the person who had ignored the claim at the time it had been asserted would have done so at his peril. If the claim was not valid, the *ius tertii* was irrelevant.

65. Mr. VIS (Chairman of the Committee of the Whole) said that a difficulty would arise in cases where a payment had been demanded from the acceptor of a bill of exchange and, at the moment payment was demanded, there had been a claim to the instrument. For example, the payee might tell the acceptor not to pay because the instrument had been stolen from him. The text of the draft stated that the acceptor did not have to pay if the third person, the payee, had asserted a valid claim. However, the acceptor could require proof of the validity of such claim.

66. Mr. CRAWFORD (observer for Canada) said that the rule applied only where the holder was not a protected holder.

67. Mr. VIS (Chairman of the Committee of the Whole) agreed that that was the case. However, in the example which he had cited, the acceptor would have to ask whether the drawer was indeed a thief, and ascertain whether the third person had a valid claim. Those were the practical difficulties involved. Other systems which had the *ius tertii* rule did not proceed in that manner.

68. Mr. ABASCAL (Mexico) said that he had no problem with the Spanish text, since it suggested that the third person would take his claim to court if it was important to determine its validity. The text provided two advantages: first, the third person would institute court proceedings only if he believed that he had the right to assert a claim; second, the acceptor would have reason to believe that the claim was valid because he would have received notification of the court proceedings.

69. Mr. DELFINO-CAZET (Uruguay) said that he agreed in principle with the Chairman of the Committee of the Whole, but did not agree with the representative of Mexico because he could not find any specific reference in the Spanish text to the situation to which that representative had referred. In his view, there would be no substantive change in paragraph (3)(a) if the word "valid" was deleted.

70. Mr. MAEDA (Japan) said that the problem could be solved by the inclusion of a reference to article 68(3). He supported the retention of the word "valid".

71. Mr. VIS (Chairman of the Committee of the Whole) said that there still remained the problem of interpreting what was a "valid claim".

72. Mr. VASSEUR (France) said that the recognition of the validity of the third person's claim would not necessarily result from a court decision; it could also result from an amicable agreement. He therefore proposed that the words "recognized as such" should be inserted in paragraph (3)(a) after the word "claim".

73. Mr. VAN SANDICK (observer, International Bar Association) said that the practising lawyers of the Association had unanimously agreed that paragraph (3)(a) referred to court proceedings. The word "valid" seemed to mean that the matter would remain pending until a court ruling on the issue was received.

*The meeting was suspended at 4.35 p.m. and resumed at 4.55 p.m.*

74. Mr. VIS (Chairman of the Committee of the Whole) said it was clear that a number of members had difficulty with the use of the word "valid" in article 25(3)(a). He suggested that the matter should be dealt with by a drafting group. There was also the question of whether payment of an instrument to a thief by a maker or acceptor acting in good faith and without knowledge of the theft constituted a discharge of liability. Article 68 provided the answer to that question.

75. Mr. SPANOGLE (United States of America) said he had difficulty with the insertion of paragraph (2 bis) as a separate paragraph of article 25. The style and clarity of the article as a whole would be enhanced if the substance of paragraph (2 bis) were included in paragraph (2) and in paragraph (1)(b).

76. Mr. VIS (Chairman of the Committee of the Whole) said that while the suggestion was a sensible one, it had to do with a drafting change and did not require further discussion at the present stage.

77. Mr. SPANOGLE (United States of America) said that paragraph (3)(b) allowed defences that related to theft or forgery to be raised, while paragraph (2 bis) made no reference to theft or forgery. The draft Convention should provide for a defence to be raised on the basis of theft and forgery, which were as reprehensible as fraud and should be referred to in paragraph (2 bis).

78. Mr. GRIFFITH (Australia), Mr. MAEDA (Japan) and Mr. CRAWFORD (observer for Canada) supported the United States proposal.

79. Mr. VIS (Chairman of the Committee of the Whole) said that if he heard no objections, he would take it that the Commission agreed to include references to theft and forgery in paragraph (2 bis).

80. *It was so decided.*

81. Mr. VIS (Chairman of the Committee of the Whole) suggested that, in view of the several proposals for drafting changes, a drafting group should be established, and that the secretariat should hold consultations on its composition by the following day.

82. *It was so decided.*

#### Article 26

83. Mr. VIS (Chairman of the Committee of the Whole) drew attention to the fact that a reference to article 59 had been added to paragraph (1)(a). Paragraph (1)(b) was still open to discussion.

84. One question raised by article 26 was whether a holder who had acted fraudulently to obtain a signature could be deemed a protected holder. A second question was how far should one go in allowing defences between immediate parties where the holder was a protected holder. Should the draft Convention allow only defences that arose from transactions between such parties which had given rise to the issuance or transfer of an instrument, or should it also allow other defences derived from unrelated transactions? He wished to invite comments on those questions.

85. Mr. BRANDT (German Democratic Republic) said that the defences for refusal to pay a protected holder should be restricted in order to shift the balance in favour of the creditor. His delegation's position was based on the function of the bill of exchange as an international negotiable instrument. The legal consequences of all relations existing outside of the bill of exchange must be clearly understood by all the parties concerned. His delegation was therefore not in favour of increasing the possibilities of defences, and would prefer the version of article 26 given in document A/CN.9/274.

86. Mr. GRIFFITH (Australia) and Mrs. PIAGGI de VANOSI (Argentina) supported the position of the German Democratic Republic.

87. Mr. VASSEUR (France) said that the use of the word "opération" instead of "transaction" in paragraph (1)(b) of the French text would be more appropriate. He wished to know whether the term referred to the transaction which gave rise to the issuance of the instrument or whether it referred to any other transactions by the parties.

88. Mr. VIS (Chairman of the Committee of the Whole) said that the first supposition was correct.

89. Mr. VASSEUR (France) said that, while that solution was possible, the objection could be raised that the drawer of an instrument could be a creditor of the holder. Would it then be proper for the drawer to raise his indebtedness as a defence against the holder?

90. Mr. VIS (Chairman of the Committee of the Whole) said that the underlying issue was that of the defence to liability. That difficult question had been debated for several years, and the Working Group on International Negotiable Instruments had decided that it should be resolved by domestic legislation. Different approaches were adopted by the domestic legislation of individual countries, and the Working Group had merely provided that where a protected holder and a liable party were the immediate parties, then any defence arising from an underlying transaction could be raised against the protected holder.

91. Mrs. PIAGGI de VANOSI (Argentina) said that she endorsed the views expressed by the representative of France on the use of the term "transaction" in the French text. The same applied in the case of the Spanish term "transacción".

92. Mr. VASSEUR (France) suggested that article 26(1)(b) should begin with the words "defences based on the transaction underlying the instrument".

93. Mr. DUCHEK (Austria), supported by Mr. GANTEN (observer for the Federal Republic of Germany), said that he would interpret the term "underlying transaction" as also covering agreements related to such a transaction. If that was the Commission's view, it must be reflected in the report.

94. Furthermore, in cases where national law was applicable, the draft Convention must contain an express statement to that effect.

95. Mr. GUEST (United Kingdom) said that he endorsed the statement made by the representative of Austria. Conversely, of course, it would not be consistent with any common-law jurisdiction to say, in cases where under national law the defence based on the underlying transaction would not be available, that that defence would not be available. A common-law jurisdiction would have to admit the defence under article 26(1)(b).

96. It was clear that a person who had committed a fraudulent act in obtaining the signature on the instrument of another party could indeed be a protected holder. For example, a person might acquire the instrument as payee of a promissory note, as protected holder, and subsequently seek a guarantee on that instrument and use fraud in obtaining the signature of the guarantor.

97. Mr. VIS (Chairman of the Committee of the Whole) said that if the example quoted by the representative of the United Kingdom was the only exception, it would probably not arise in the context of article 26. In that example, the protected holder would be the person guaranteed and the party would be the guarantor.

98. Mr. GUEST (United Kingdom) said that he disagreed with the view just expressed by the Chairman of the Committee of the Whole. If a promisor made a promissory note in favour of a payee, the payee was a holder. The payee took the note, under conditions that made him a protected holder. He then sought a guarantor of the liability of the maker of the note. The guarantor was a party because he had signed the instrument.

99. Mr. VIS (Chairman of the Committee of the Whole), speaking as the representative of the Netherlands, said that

under the law of negotiable instruments, most systems dealt with immediate parties. The case under consideration also concerned immediate parties—a protected holder who had dealt with the party liable and who was an immediate party together with the party liable. In such situations, the question of the protected holder or holder in due course was not really of great importance. Basically, the principle of negotiability applied in cases where remote parties were involved.

100. Most legal systems would make the protected holder who was an immediate party vulnerable. The Commission would therefore not be taking an extraordinary step in making the protected holder vulnerable.

101. He fully shared the concerns voiced by the representative of Austria, but the question was how the problem under consideration was to be dealt with. The Commission should not further protect the protected holder.

102. Mr. GRIFFITH (Australia) said that the issue under consideration was of great importance. Under the common-law system, a *bona fide* holder, who in the case under consideration was regarded as equivalent to a protected holder, was, save in exceptional circumstances, entitled to treat a bill of exchange as cash, on maturity. In any action on the bill and matters relating to counter-claims arising out of particular transactions or other transactions that were not regarded as a defence, the rule was first to pay up on the bill of exchange and then to pursue claims. That was one of the fundamental advantages of bills of exchange, including international bills of exchange.

103. Mr. VIS (Chairman of the Committee of the Whole), responding to a point raised by the representative of the United States of America, said that the statement made by the representative of Austria concerned defences, not counter-claims, cross-claims or set-offs.

104. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that her delegation objected to the current wording of article 26, which constituted a direct departure from the principle on which the article had originally been based. The principle in question was that it was extremely important to set forth a list of the defences that could be used by the protected holder, without making any reference to any other defences that might be available under national legislation.

*The meeting rose at 6 p.m.*

### Summary record of the 337th meeting Tuesday, 24 June 1986, 10 a.m.

[A/CN.9/SR.337]

*Chairman:* Mr. KARTHA (India)

*Chairman of the Committee of the Whole:*  
Mr. VIS (Netherlands)

*The meeting was called to order at 10.10 a.m.*

#### International payments (continued)

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes* (continued) (A/CN.9/273, A/CN.9/274 and A/CN.9/285)

*Articles 4(7) and 25 to 28 (continued)*

1. Mr. CHAFIK (Egypt) said that the amendments to the draft Convention on International Bills of Exchange and International Promissory Notes proposed by the Working Group on International Negotiable Instruments, while they improved the text, related only to secondary issues and did not address the major objections which had surfaced at the Commission's seventeenth session. For example, the criterion of internationality, which was considered by many members to be too narrowly defined, had been completely overlooked. With reference to the distinction between a protected holder and a holder, and the defences which could be set up against each of them, the Working Group had ignored the objections raised to the effect

that the concept was alien to national legislations and exchange law practice, and had simply made a drafting change in article 4(7). Lastly, although the Working Group had resolved some of the difficulties caused by having treated the drawer originally as a guarantor and not as the principal debtor, it had not gone far enough, since the drawer should remain the principal debtor until the drawee had accepted the instrument. The signature of the drawee alone should enable the drawer to act as a guarantor, since it was the drawee that held the funds and thus constituted the most effective guarantee of payment.

2. The text was also weighed down by unnecessary references; for example, article 26(1)(a) mentioned eight other articles of the draft Convention. In the view of his delegation, the draft Convention required further revision before it would be ready for adoption.

3. Mr. VIS (Chairman of the Committee of the Whole) said that the question at issue in article 26(1)(b) was simply that of liability on an instrument and whether any defence existed against such liability. It seemed that the text as it stood was not completely clear, and he invited proposals for its amendment.

4. The CHAIRMAN, speaking as the representative of India, said that article 26(1)(b) was an exception to the general rule that the protected holder took the instrument free from defences and claims of prior parties. In the view of his delegation, the Convention should not specify which law was applicable to such cases, since a determination could be made only by considering the transaction and the intent of the parties. Accordingly, his delegation supported the wording of the article as it stood.

5. Mr. GUEST (United Kingdom) said that article 26(1)(b) was of considerable importance to many common law systems. His delegation would have preferred it not to have been possible to raise any defence, even one based on the underlying transaction. However, the text represented a compromise between two opposing views, and he trusted that it would be adopted as it stood.

6. Mr. VASSEUR (France) said that article 26(1)(b) was not satisfactory; it should be made clear exactly which defences might be set up. The French text of the article should be amended to read "*Les exceptions fondées sur l'opération sous-jacente à l'effet ...*".

7. Mrs. PIAGGI de VANUSSI (Argentina) agreed that the article, as worded, was ambiguous. She proposed the amendment of the Spanish version of the text to read: "... *basadas en la relación subyacente ...*".

8. Mr. VIS (Chairman of the Committee of the Whole) said that the proposed amendments could be dealt with in a drafting group.

9. Mr. DUCHEK (Austria) said that it was not clear what the position was with regard to set-offs and local law. Under some legal systems, set-offs constituted substantive rather than procedural law and were, in fact, considered defences. It might be preferable in the view of some delegations for set-offs, where applicable, to complement the defences available under the draft Convention. However, other delegations wished the list contained in the draft Convention to be exhaustive and for local defences to be excluded. So the question arose whether countries which considered set-offs to be substantive law could use them as a defence in addition to those defences provided for in the draft Convention.

10. The wording used in article 25(1)(c) was much broader than that in article 26(1)(b). The wording of the latter article should be aligned with the wording of article 25(1)(c), since both dealt with relations between a party and a holder.

11. Mr. VIS (Chairman of the Committee of the Whole), referring to article 26(1)(b), said that, although set-offs were a defence under some legal systems, that was certainly not the case under others. It appeared that the text as it now stood would be acceptable to common-law and some other countries. It seemed to him that such remedial actions as counter-claims or set-offs would remain in place; the draft Convention would not abolish them. The Commission should concentrate its debate on liability on the instrument and what defences were available.

12. Mr. DUCHEK (Austria) said that his delegation could support that interpretation, provided that the Commission's report stated that matters such as set-offs, together with other obligations, were not dealt with in the article in question. It would then be clear that there was scope for national law to apply. It should be noted that the Working Group on International Negotiable Instruments had stated (A/CN.9/273, para. 20) that article 25(1)(c) should be in accord with article 26(1)(b), a view which his delegation endorsed.

13. Mr. MAEDA (Japan) said that his delegation supported the suggestion made by the secretariat in document A/CN.9/WG.IV/WP.30 concerning article 26(1)(b). There was no need to distinguish between holders who were protected and those who were not. The present wording of articles 25(1)(c) and 26(1)(b) was the product of lengthy negotiation. It did not seem advisable to his delegation to leave the matter to national law.

14. Mr. SPANOGLE (United States of America) recalled that originally articles 25(1)(c) and 26(1)(b) had had the same wording. A compromise formulation, however, had been agreed upon for article 26(1)(b) in order to accommodate the special treatment of the protected holder under some common-law systems. Nevertheless, under all systems a non-protected holder was subject to all defences that could be raised as to a transaction between that holder and the immediate party. That being the case, it was better to keep the existing text of article 25(1)(c) as being representative of the current law of the majority, rather than changing it unnecessarily for the sake of internal consistency.

15. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that she supported the United States view. Austria was proposing not simply a drafting change but a substantial change of approach.

16. With regard to the document referred to by the representative of Japan, the secretariat had indeed made a proposal for a drafting change; but since article 26(1)(b) was not being amended, there was no need to amend article 25(1)(c).

17. Mr. GRIFFITH (Australia) and Mrs. PIAGGI de VANUSSI (Argentina) said that they agreed with the United States representative.

18. Mr. GUEST (United Kingdom) said that he agreed with the representatives of the United States and the Soviet Union.

19. Mr. DUCHEK (Austria) pointed out that his suggestion represented also the view of the Working Group expressed in its report. While article 26(1)(b) allowed a party to set up defences

against a protected holder based only on the underlying transaction, a holder, on the other hand, could not become a protected holder if he had knowledge of defences to contractual liability based on a transaction other than the underlying transaction. He himself did not see why the holder's knowledge of other matters should be of consequence to his relation to the party. Obviously, the defences intended in article 25(1)(c) were set-offs. Furthermore, although the Commission had decided earlier that set-offs were not covered by article 26 and although the language of articles 25(1)(c) and 26(1)(b) was different, the reference in the latter was also clearly to set-offs. There had been much theoretical discussion, but no examples given of any real differences between the issues dealt with in the two articles. If the majority wished to maintain a distinction, however, he would not object.

20. Mr. CRAWFORD (observer for Canada) said that the Convention must be acceptable to the banking community. If a bank took care to preserve its position as a protected holder, it was only fair that it should be subject to a narrower range of potential defences, of delaying or defeating conditions, even in its relations with immediate parties. The arguments of the representative of Austria had more force in the case of a non-protected holder. However, the Convention had to strike a proper balance between the various issues and, in his view, the text as it stood had achieved the right balance.

21. Mr. VIS (Chairman of the Committee of the Whole) said that he would take it, if he heard no objection, that the Commission wished to retain the current text of articles 25(1)(c) and 26(1)(b) and to refer the amendments to the drafting group.

22. He would also take it, if he heard no objection, that the Commission wished to adopt articles 26(1)(c), 26(2), 27(1), 27(2) and 28.

23. *It was so decided.*

24. Mr. HERRMANN (International Trade Law Branch) noted that the Working Group, in its deliberations on the articles dealing with the holder and the protected holder, had considered that the current formulation of article 4(7) was probably too broad in its requirement that a protected holder should have no knowledge of any defences under article 25. The Working Group had felt that a holder could become a protected holder if he had knowledge only of defences arising from a transaction between himself and the immediate party other than the underlying transaction, and that article 4(7)(a) should therefore require only a lack of knowledge of defences under article 25(1)(a), (b) and (d) and of defences arising from the underlying transaction between himself and the immediate party.

25. Mr. GUEST (United Kingdom) said that he agreed. If, for instance, a maker asserted a previous claim against a payee in whose favour he had made a promissory note, it would not be sensible to deprive that payee of his status as a protected holder under the Convention.

26. Mr. SPANOGLE (United States of America) agreed that notice of defences arising from other transactions not involved in the instrument should not disqualify one as a protected holder. He believed, however, that it would be going too far to eliminate any reference to article 25(1)(c). Some reference should be retained in article 4(7) to knowledge of defects in the transaction

between the party and the person from whom the holder took the instrument, which knowledge should disqualify the holder from becoming a protected holder.

27. Mr. VIS (Chairman of the Committee of the Whole) said that the United States representative had introduced an interesting refinement. If, for instance, in an underlying transaction consisting of a sale of goods, A issued a note to a payee who transferred it to B and B noticed that the goods were defective, that knowledge would prevent B from becoming a protected holder. On the other hand, if the payee in that same transaction had a debt with A on a loan which had nothing to do with the note, and B had knowledge of that loan, that would not prevent B from becoming a protected holder.

28. Mr. GUEST (United Kingdom) considered that a holder who had knowledge of a defect in an underlying transaction was still a protected holder but could raise a defence under article 26(1)(b) even though he was a protected holder.

29. Mr. MAEDA (Japan) said that he agreed with the distinction made by the United States representative. He also agreed with the formulation in paragraph 6 of document A/CN.9/WG.IV/WP.30.

30. Mr. VASSEUR (France) saw no difference between the two examples given by the Chairman of the Committee of the Whole: the holder in both cases was a protected holder.

31. Mr. VIS (Chairman of the Committee of the Whole) remarked that if, as the representative of France maintained, knowledge of a defect did not disqualify a holder from becoming a protected holder, that would go against a long-standing consensus in the Commission.

32. At any rate, he believed that there was general agreement that article 4(7), in its reference to all defences mentioned in article 25(1), went too far. The issue with regard to article 4(7) was whether a holder's knowledge of a transaction with a remote party affected his status as a protected holder.

33. Mr. SPANOGLE (United States of America) wondered whether his point was perhaps already covered in article 25(1)(b) by the formulation "arising from the circumstances as a result of which he became a party". If so, he would not insist and would accept the proposed amendment. He asked what in fact was covered by article 25(1)(c) but not by article 25(1)(b).

34. He shared some of the concerns raised earlier by the representatives of France and Egypt. It might be better not to include a cross-reference in article 4(7), but simply to state what was meant even at the risk of repetition.

35. Mr. GUEST (United Kingdom) observed that initially the debate had centred on whether the reference in article 25(1)(c) to a defence based on any transaction was perhaps too wide. The United States delegation had thus raised a point regarding the situation of a holder who had knowledge of a defence based on an underlying transaction. The Chairman of the Committee of the Whole had introduced a different question relating to article 25(1)(b), regarding knowledge of defences between other parties: that was a different matter which needed to be discussed separately.

*The meeting was suspended at 11.30 a.m. and resumed at noon.*

36. Mr. VIS (Chairman of the Committee of the Whole) said there appeared to be general agreement that a holder who had knowledge of a defence based on an underlying transaction was not a protected holder. However, if the transaction on which the defence was based was an unrelated transaction, the question whether the holder was protected or not was immaterial, since article 26 would apply, as the representative of the United Kingdom had pointed out. The distinction would matter only in so far as the shelter rule (article 27) was applied in the case of subsequent holders.

37. Mr. CRAWFORD (observer for Canada) questioned whether a defence based on an unrelated transaction between a holder and a drawer constituted a defence to contractual liability, as referred to in article 25(1)(c).

38. Mr. VIS (Chairman of the Committee of the Whole) noted that article 4(7)(a) defined a protected holder as one who "without knowledge of a claim to or defence upon the instrument"; however, rather than defining any such defences, the article merely made a reference to article 25. He believed it would be more useful for article 4(7)(a) to identify clearly those defences or claims.

39. Mr. GUEST (United Kingdom) agreed that the distinction as to whether or not a holder was protected might make a difference in the case of the application of the shelter rule if article 25(1)(c) were deleted from the text of the draft Convention. He cited as an example a case in which party A issued a note made payable to party B; if, on taking possession of the note, party B knew of a defence based on the underlying transaction, B would nevertheless continue to be a protected holder. If B then transferred the instrument to a third party, that party would also qualify under the shelter rule as a protected holder, subject to the limitations set out in article 27(2).

40. Mr. CHAFIK (Egypt) said that the question required a great deal of reflection. He proposed that the matter should be considered by a small working group, which would then submit a clearly worded proposal on the subject for discussion by the Commission.

41. Mr. VIS (Chairman of the Committee of the Whole) endorsed the proposal made by the representative of Egypt and suggested that a small working group composed of the representatives of Egypt, France, Japan, Mexico, Nigeria and the United Kingdom and the observer for Canada should be established to redraft article 4(7) with a view to formulating a specific definition of defences that would replace the reference to article 25.

42. *It was so decided.*

#### *Article 41*

43. Mr. VIS (Chairman of the Committee of the Whole) explained that the article dealt with the liability of a party (transferee) who acquired an instrument by mere delivery rather than by endorsement and delivery. Since the transferor of the instrument would not have endorsed it, he would not, under a general rule of negotiable instruments law, have any liability on that instrument. However, most legal systems recognized that a transferor by mere delivery did in fact have liability in certain cases. The way in which such cases of liability were dealt with depended on the legal system in question, a situation which

could give rise to a high degree of uncertainty. Consequently, it had been deemed necessary for the draft Convention to contain a specific provision for dealing with such cases.

44. The draft text of article 41 had been acceptable to countries from both the common-law and civil-law systems. Once the text had been formulated, the drafting group responsible for it had concluded that the same rules should apply to a transferor by endorsement, so as to ensure that one mode of transfer did not entail greater liability than the other.

45. Mr. VASSEUR (France) said that he was in favour of article 41 as currently worded. However, he suggested that, in order to make it clear that the article applied to all transfers, whether by endorsement or mere delivery, the words "even by mere delivery" should be inserted in the first line of article 41 after the word "instrument".

46. Mr. BRANDT (German Democratic Republic) said that he was in favour of article 41 and of the proposed amendment.

47. Mr. DRUEY (Observer for Switzerland) likewise supported the French amendment. He suggested that article 41 should be given a separate heading as it was not covered by the one preceding article 40.

48. Mr. VIS (Chairman of the Committee of the Whole) said that that was a matter for the drafting group.

49. If he heard no objection, he would take it that the Commission wished to adopt article 41.

50. *It was so decided.*

#### *Article 5*

51. Mr. GRIFFITH (Australia) said that article 5 as currently drafted was tautological. His delegation would prefer to delete the final phrase.

52. Mr. VASSEUR (France) agreed.

53. Mr. GUEST (United Kingdom) said that he would have some difficulty with such a proposal. The aim of the Working Group had been to cover situations in which, even if a person did not have actual knowledge of a fact, he did have knowledge of circumstances from which he should have inferred the particular fact, had he not deliberately ignored it.

54. Mrs. PIAGGI de VANUSSI (Argentina), Mr. GANTEN (observer for the Federal Republic of Germany), Mr. MAEDA (Japan), Mr. PISEK (Czechoslovakia), Mrs. ADEBANJO (Nigeria) and Mr. DELFINO-CAZET (Uruguay) said that they too were in favour of leaving article 5 as it stood.

55. Miss PULIDO (observer for Venezuela) said that the article should state in more objective terms what constituted knowledge of a fact.

56. Mr. SPANOGLE (United States of America) supported the article as currently worded. The last phrase did add something, for it covered the doctrine of wilful ignorance. The existing formulation gave the courts an opportunity to examine the circumstances under which a transaction had taken place. Moreover, it was one that had been used in other conventions prepared by the Commission.



57. The CHAIRMAN, speaking as the representative of India, supported the present formulation of article 5, which reflected the wording used in previous conventions prepared by the Commission.

58. Mr. ILLESCAS ORTIZ (Spain) pointed out that the last phrase of article 5 established a presumption, which it should be possible to disprove in a court of law. Accordingly, he suggested that the words "unless proved otherwise" should be added at the end of the article.

59. Mr. VAN SANDICK (International Bar Association) said that some comments submitted to the Association were not entirely supportive of the wording of article 5. In actual practice the article might not operate exactly as the Commission expected. One comment had noted that it was not clear from article 5 whether "knowledge" meant knowledge of facts (which

would give rise to a claim or defence) or knowledge that those facts as a matter of law amounted to a claim or defence. The defences outlined in article 25 would vary considerably depending on the law governing a particular contract or the circumstances giving rise to a defence. It might be very difficult to prove knowledge of the existence of a defence, as opposed to the existence of the fact giving rise to a defence. Where international transactions were involved, it might be necessary to show that a holder was aware of the legal consequences of certain facts under foreign laws. The author of the comment was not aware of any system that presumed knowledge of foreign laws and he therefore felt that the article should make it clear that "knowledge" meant knowledge of the facts giving rise to a defence and not of the legal consequences of such facts. .

*The meeting rose at 1 p.m.*

### Summary record of the 338th meeting Tuesday, 24 June 1986, 3 p.m.

[A/CN.9/SR.338]

*The meeting was called to order at 3.10 p.m.*

#### Co-ordination of work

1. Mr. SEN (Secretary-General, Asian-African Legal Consultative Committee) recalled that the Commission's establishment in 1968 had proved particularly welcome to developing nations in their quest for the development of international trade norms that were suited to the needs of the changing structure of the international community in the years following decolonization. Such nations had felt that existing international trade law was a product of, and unduly benefited, the developed Western world and that developed and developing countries must pool their expertise in order to arrive at a more just solution.

2. The Asian-African Legal Consultative Committee had thus been very happy to respond to the call for co-operation addressed to it by the Commission's Chairman in 1969, following which the active participation of the Commission's secretariat had helped to establish a close working relationship between the two bodies. Subsequently, at its 1970 session at Accra, the Committee had established an open-ended standing sub-committee on international trade law with the task of preparing model contracts for commodity sales transactions, an item then pending consideration by the Commission and of particular interest to developing countries, exporters of agricultural produce, minerals and other raw materials. Three model contracts developed at successive sessions of the Committee with the active participation of the Commission's secretariat had finally been adopted in 1976 and published a year later as documents of the Economic and Social Council.

3. Another topic on which the Committee had worked closely with the UNCITRAL secretariat was international commercial arbitration. The impetus for the Committee's work had been provided by the report of the Commission's Special Rapporteur, who had envisaged the possibility of establishing regional and national institutions in the third world to handle international arbitration, with a view to promoting wider acceptance of arbitration as a means of settling commercial disputes. The

Committee had first discussed that possibility in 1974 and, at its Baghdad session in 1977, had decided to establish two regional arbitration centres, the functions of which included promoting the Arbitration Rules adopted by the Commission in 1976. The UNCITRAL secretariat had been closely associated with the establishment of the regional centres, ensuring that, in arbitrations administered by them, the UNCITRAL Arbitration Rules, adapted to suit the needs of institutional arbitration, were applied. The Committee had thus been the first organization to promote the UNCITRAL Rules, even before the General Assembly had recommended their adoption.

4. In 1977, following consideration of the Committee's recommendations for possible amendments to the 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards, the Commission had decided to undertake the preparation of a model law on arbitration. The model law had finally been adopted at the Commission's eighteenth session and was sure to assist many developing countries in establishing a legal framework for the conduct of arbitrations within their territories; it was thus bound to have a significant impact on the growth of national institutions capable of handling the settlement of disputes between parties under different jurisdictions. The Committee, at its 1986 session, had recommended that its member Governments consider the model law.

5. The UNCITRAL secretariat had also been represented at various seminars on commercial arbitration held over the years under the Committee's auspices and had sponsored jointly with the Committee seminars on arbitration and other aspects of trade law. The two bodies had also co-operated actively with regard to shipping and industrial contracts and the Commission's project on the latter had in fact been undertaken at the Committee's suggestion.

6. Apart from the close links which existed between the two bodies at working level, he believed that their co-operation had helped many developing countries to play a wider role in the work of UNCITRAL itself. Since the Committee considered the Commission's report at each of its annual sessions, it helped place special emphasis on the Commission's work, and the notes

on UNCITRAL's work which it prepared for Sixth Committee debates helped its member States to participate more effectively in discussions on the Commission's report.

7. In the face of harsh economic and political realities, the idea of establishing a new international economic order no longer evoked the enthusiasm and zeal to reform and restructure the world economy that it once had. The quiet and steady work of bodies such as UNCITRAL would help to bring about that new order in practical terms, however, and the Committee was grateful therefore to the Commission for fostering and strengthening the close working relationship that existed between their two bodies.

#### International payments (continued)

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes* (continued) (A/CN.9/273, A/CN.9/274 and A/CN.9/285)

Articles 5, 23, 23 bis, 25 and 26

8. Mr. VIS (Chairman of the Committee of the Whole) recalled that, at its previous meeting, the Commission had considered the definition of knowledge given in draft article 5 as it appeared in document A/CN.9/274. The vast majority of members had taken the view that, while the definition was not totally satisfactory, it could be retained. If he heard no objection, he would take it that the Commission decided to adopt draft article 5 as it appeared in document A/CN.9/274.

9. *It was so decided.*

10. Mr. VIS (Chairman of the Committee of the Whole) pointed out that the concept of "knowledge" was used in several articles of the draft Convention, in some cases with the qualifying phrase "provided that such absence of knowledge was not due to his negligence" and in some cases without. The Commission should now determine whether the use of that qualifying phrase was in fact justified in the instances in which it was used. The Commission might start by considering the use of that phrase in draft articles 23(2) and 26(1)(c) and ask itself whether in fact the simple definition of knowledge given in article 5 would not be adequate.

11. Mr. SPANOGLE (United States of America) explained with regard to draft article 26(1)(c) that it was a traditional argument of the defence in cases of fraud that the party concerned had signed an instrument without knowing that his signature would make him a party to it. However, there was an opposing argument that the party should have read what he had signed. The definition in article 5 did not cover that eventuality, for draft article 26 implied that parties had an obligation to seek out information before signing an instrument.

12. Mr. ABASCAL (Mexico) said that in Mexico the concept of fault or negligence was covered by the term "*culpa*". The term "*negligencia*" did not mean anything under Mexican law. The concept of "*negligencia*" would therefore have to be clarified in Mexico and other civil-law countries.

13. Mr. VASSEUR (France) commented that, while the United States representative had explained the purpose of the qualifying phrase perfectly, he believed that an international legal text should not seek to over-refine concepts. That could

give rise to ambiguities when the Convention must instead establish very clear concepts. The Convention might not cover every single eventuality, but it was up to the law courts of each country to interpret it in each case. Once the concept of "knowledge" had been defined in article 5, it must not be qualified in subsequent articles. In any case, two different concepts were involved in the present instance: draft article 23(3) first stated that a party or drawee who paid a forged instrument was not liable under the Convention if, at the time he paid the instrument, he was without knowledge of the forgery. The second concept, namely that such absence of knowledge must not be due to his negligence, was governed by common law and should not come within the purview of the draft Convention. All references to negligence should therefore be deleted from the draft.

14. Mr. GUEST (United Kingdom) pointed out that the Commission could not take a blanket decision on all the instances in which the possibility of negligence was invoked in the draft Convention. Each specific instance must be considered in order to determine whether or not it was appropriate to include the reference to fault or negligence. In that connection, he wished to point out to the representative of France that not all common-law systems might be adequate to address cases of negligence.

15. Concerning the reference to negligence in draft article 26(1)(c), and also in draft article 25(1)(d), he agreed with the United States representative that the party signing an instrument must take the necessary care to check its contents. If the reference to negligence in article 26(1)(c) was deleted, he was quite sure that the provisions of article 26 would simply not be applied in the United Kingdom. It was also very doubtful whether common law would remedy the results of such negligence in his country. He would therefore prefer to retain the reference to negligence while recognizing that, if the concept was unintelligible in other legal systems, it would have to be reformulated.

16. Mr. MAEDA (Japan) supported the arguments put forward by the representatives of the United States and the United Kingdom. The issues raised in draft articles 25(1)(d) and 26(1)(c) were issues of real defence and the scope of the concept of real defence should not be too broad. The reference to negligence should therefore be retained.

17. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) recalled that when the Working Group had drafted articles 25 and 26, the reference to negligence had been included to show that those articles covered real lack of knowledge and that the defence argument of ignorance could not be invoked unjustifiably. The clarification provided by the United States representative bore out that interpretation. Articles 25 and 26 referred to real lack of knowledge and not simply to lack of knowledge as defined in article 5.

18. Mrs. PIAGGI de VANOSI (Argentina) said that the reference to negligence in articles 25 and 26 should not be deleted, because a distinction should be drawn between absence of knowledge as defined in article 5, which was an objective concept, and negligence, which was more subjective in meaning.

19. Mr. VIS (Chairman of the Committee of the Whole) asked whether all the members were convinced that there were valid reasons to retain the current text.

20. Mr. GANTEN (observer for the Federal Republic of Germany) said that his delegation supported the text only in so far as articles 25 and 26 were concerned.
21. Mr. VASSEUR (France) said that, in the interest of consistency, article 5 must be modified to redefine the concept of knowledge.
22. Mr. GANTEN (observer for the the Federal Republic of Germany) said that, in order to meet France's objection, the phrase "unless stated otherwise in this Convention" could be added to article 5. In other words, where there was no reference to negligence, the definition of knowledge in article 5 would stand.
23. Mr. CRAWFORD (observer for Canada) said there were 11 references to "knowledge" in the draft Convention, 6 of which were linked with the concept of negligence. The Working Group had had valid policy reasons for linking the concept of knowledge to absence of fault for some purposes and not for others.
24. Mr. VASSEUR (France) said that if the draft Convention referred to exceptions to the definition contained in article 5, that definition no longer held.
25. Mr. VAN SANDICK (observer, International Bar Association) said that, if knowledge was defined in article 5, it should have the same meaning throughout the draft Convention. However, that definition did not work in all situations. He would welcome some clarification on the standards used to measure negligence by the courts, in particular as they related to subjective and objective negligence.
26. Mr. DRUEY (observer for Switzerland) said that he shared France's view. A reservation should not be made in article 5. On the other hand, the use of the concept of negligence in articles 23, 25 and 26 demonstrated the narrowness of the definition of knowledge contained in article 5. That concept therefore required further elucidation.
27. Mr. ANGELICI (Italy) said that he saw two possibilities: either to delete article 5 and clarify in each article the relevant concept of knowledge, or to follow France's suggestion and make an effort to unify the concept of knowledge. In his view the first possibility was preferable.
28. Mr. SPANOGLA (United States of America) said that he supported Switzerland's position. The English version of the draft Convention set up two separate conditions: one related to the definition of knowledge and the other related to negligence, there being no necessary overlap between the two. He would be interested to hear more from the civil-law countries about their difficulties with the concept of negligence.
29. Mr. VIS (Chairman of the Committee of the Whole) said that there appeared to be a general consensus that the definition contained in article 5 was inadequate in the context of the defences referred to in articles 25 and 26. He asked whether, in article 23(2), there was a similar justification for modifying the concept of knowledge contained in article 5.
30. Mr. SPANOGLA (United States of America) gave an example from United States traditional banking usage in which a payee was able to evade the rule that cash must not be paid out over the counter from a corporate account by, for example, opening an account and then drawing cash from that account. A bank might in fact handle such an instrument without knowing that anything was wrong, but it would be violating the traditional practice.
31. Mr. VIS (Chairman of the Committee of the Whole) asked whether article 5 would not apply in that case.
32. Mr. SPANOGLA (United States of America) said that the payee might say that he had permission for the transaction. However, the bank had a duty of care, and it would expect to bear the risk of not handling the instrument properly. Failure to follow the normal banking practices would be considered negligence. He therefore felt that the negligence requirement must be retained in articles 23 and 23 *bis*.
33. Mr. GUEST (United Kingdom) said that the success or failure of the draft Convention would depend to a large extent on its acceptance by the bankers of various countries. The question was what duty a banker had when collecting a note. He might have no duty, and therefore no liability; he might be liable only if he collected an instrument to which there was no title; he might be liable only in the absence of knowledge under the extended concept of article 5; or, as the representative of the United States had said, ordinary banking practices might have to be examined to see whether the bank had been negligent.
34. The proposed draft fell somewhere in the middle of that spectrum. It might not appeal to bankers in countries where the liability of the collecting banker was minimal. However, in a country like the United States, there might be strong pressure to retain the concept of negligence. A political solution might therefore have to be adopted in order to ensure that the draft would not be too unacceptable to any banking community.
35. Mr. VASSEUR (France) said that he supported the views of the representative of the United States because French banks were taking a cautious approach to the draft Convention, and there had even been some pressure on the Government not to sign or ratify it. Under French law, a collecting bank which paid a note on which the signature appeared to be in order could not be held liable. If articles 23 and 23 *bis* were interpreted as increasing the banks' liability, their reservations might turn into outright hostility towards the draft Convention. He felt, therefore, that the meaning of negligence must be clarified.
36. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that the text of article 23 had been the result of a compromise reached with great difficulty. The previous text had created even more difficulties for civil-law countries. Under the current text, the bank would be negligent if it paid an instrument after receiving notification that the instrument had been stolen or had fallen into the hands of a dishonest holder. That would be the case even where the notification had not reached the person in the bank who was authorized to act upon it, in other words, even if the bank did not "know" that the instrument was in the hands of a swindler.
37. Articles 25 and 26 referred to an actual absence of knowledge, which was not the same as that defined in article 5. Such an absence of knowledge might be taken into account in a defence if it had been caused by negligence. Thus article 5 must be retained, first, because it arose from article 4 and was

needed in order to define a protected holder, and second, because its deletion would make it necessary to amend the other articles under discussion.

*The meeting was suspended at 4.40 p.m. and resumed at 5.10 p.m.*

38. Mr. VIS (Chairman of the Committee of the Whole) said that there were different interpretations of article 5, in particular as a result of the addition of the words "or could not have been unaware of its existence". Some delegations seemed to feel that those words contained elements of negligence which courts could take into account in determining whether or not a person had knowledge of a fact.

39. Mr. MAEDA (Japan) said that the word "negligence" should be retained in paragraphs (2) and (3) of article 23. In article 5, the words "could not have been aware of its existence" referred to one aspect of knowledge, and should not be construed as implying negligence. Article 5 should therefore remain without change.

40. Mr. GANTEN (observer for the Federal Republic of Germany) said that his delegation preferred to delete the words "provided that such absence of knowledge was not due to his negligence" in paragraphs (2) and (3) of article 23.

41. Mr. ILLESCAS ORTIZ (Spain) said that the question being discussed had both a formal and a substantive aspect. The formal aspect presented problems not because of knowledge, but rather because of the absence of knowledge of certain circumstances. The Commission was discussing the absence of knowledge on the part of one of the persons involved in a transaction relating to a negotiable instrument. Moreover, apart from the absence of knowledge, there was also absence of knowledge due to negligence. Perhaps article 5 should contain a second paragraph defining absence of knowledge due to negligence. In that way, the Commission would do justice to Cartesian logic and, at the same time, it would make the concept of negligence more precise.

42. With regard to substance, the consequences of the absence of knowledge due to negligence were completely different in the four cases contained in articles 23, 23 *bis*, 25 and 26. In articles 25 and 26, the retention of the concept of absence of knowledge due to negligence strengthened the negotiable instrument and decreased the number of defences. On the other hand, in article 23, the retention of the concept of absence of knowledge through negligence meant that banks might be subject to increased liability under certain systems of civil law. Perhaps the Commission should include a definition of absence of knowledge due to negligence and decide later whether to retain that term in articles 23, 23 *bis*, 25 and 26. The Commission should also consider the consequences of retaining the text in its current form.

43. Mr. VIS (Chairman of the Committee of the Whole) said that he was not in a position to draw a conclusion. He wished to refer briefly to the other articles in which the concept of knowledge was relevant, namely articles 4(7), 11(2)(a), 41(1)(c), 41(2) and 68(3).

44. With regard to article 4(7), article 5 in its current form would be applicable, and he took it that the Commission accepted the concept of knowledge as defined in article 5.

45. Mr. VASSEUR (France) said that, in article 4(7), the word "knowledge" referred to the knowledge of the protected holder, and it was clear that that provision should be consistent with article 26, which referred to the protected holder.

46. Mr. VIS (Chairman of the Committee of the Whole) said that, in article 4(7), the reference was to the holder who was without knowledge, and that was one of the elements of protected-holder status.

47. He referred briefly to articles 11(2)(a), 41(1)(c), 41(2) and 68(3). It was his impression that the Commission agreed that article 5 in its current form was applicable to all of those articles.

48. The Commission was left with a few instances in which absence of knowledge contained the element of negligence, namely in articles 23, 23 *bis*, 25 and 26. He took it that the Commission wished to retain the concept of negligence in those articles, and to refer the question of the deviation from article 5, which had been raised by the representative of France, to a drafting group.

#### *Article 1*

49. Mr. CHAFIK (Egypt) said that the substantive issue in article 1(2) was the criteria for determining when a bill of exchange or promissory note became international. In his view, a bill of exchange was drawn up within a national framework, in which case article 1(2) would not apply. However, when that bill of exchange was endorsed or guaranteed in another country, an international element entered into the life of that bill of exchange. He wondered why such an instrument was not subject to article 1(2); once it was established in an international way, it remained international. The Working Group had not dealt with that question.

50. Mr. VIS (Chairman of the Committee of the Whole) said that when the Commission had just taken up the question of negotiable instruments, it had requested the secretariat to consider ways in which the question could be approached. One of the proposals advanced had been that the existence of an international element in the use of an international negotiable instrument should be one criterion for the application of the uniform rules on bills of exchange and promissory notes. The Commission had subsequently decided that a new international instrument was required. It was against that background that article 1 of the draft Convention on International Bills of Exchange and International Promissory Notes had been introduced in order to define the international instrument to be governed by the Geneva Uniform Law. Consequently, instruments drawn under national law and endorsed in a foreign country were not covered by the draft Convention. The international element mentioned in article 1(2)(a) of the draft Convention was the formal requisite of a negotiable instrument.

51. Mr. CHAFIK (Egypt) said that in the current draft Convention the notion of internationality was too narrowly defined. However, it was too late to seek to extend its scope of application.

52. Mr. GUEST (United Kingdom) said that, at its previous session, the Working Group on International Negotiable Instruments had amended article 1 of the draft Convention in such a way as to require the words "international bill of exchange" to be included in both the heading and the text of an international bill of exchange. A preference had been expressed to him by

certain banks for the use of the words "international bill of exchange" in the heading only. While he did not feel very strongly about the matter, he wondered whether the use of the words in the heading alone would not indeed suffice.

53. Mr. VIS (Chairman of the Committee of the Whole) said that the reason for the approach adopted was that it was possible to alter an international bill of exchange by inserting the words "international bill of exchange" at the top of the instrument; hence the need for those words to appear in the very text of the instrument.

54. Mr. GUEST (United Kingdom) said that he was satisfied with that explanation.

55. Mr. GANTEN (observer for the Federal Republic of Germany) said that it must be made very clear that an international bill of exchange was indeed international. He had been urged to try to convince the Commission that the heading on international bills of exchange should be in the same language all over the world. While acknowledging that it would be difficult for a United Nations convention to advocate the use of a single language, he was mindful of the problems faced by bankers and other persons who dealt with international bills of exchange. English should be chosen as that common language since it was the language most widely used in international banking circles. He therefore proposed that the text of the draft Convention should provide for the use of the English language on the heading of international bills of exchange.

56. Mr. CHAFIK (Egypt) said that the implementation of that proposal would lead to a conflict of languages. He wished to propose instead that a colour, such as the colour of the United Nations flag, should be used as a means of identification.

57. Mr. VIS (Chairman of the Committee of the Whole) said that he did not think that the Commission should pursue the proposal made by the observer for the Federal Republic of Germany, since it was unlikely to receive full support.

58. Mr. PELICHET (observer, Hague Conference on Private International Law) recalled that at the previous session of the Working Group he had proposed a restructuring of article 1 of the draft Convention. That proposal (A/CN.9/273, para. 61) had been motivated by the lack of internal logic in the structure of the current draft article, which unfortunately combined two quite separate elements. Article 1(2) referred to elements concerning the implementation of the draft Convention itself, as well as to elements concerning the validity of an instrument when the draft Convention came into force. It was essential to draw a distinction between those two elements. Moreover, the entire structure of the draft Convention was based on an autonomy of will which operated at two levels. At the international level, it related to conflicts of law, while, at a second level, a person wishing to draw an instrument under the draft Convention was able to choose a certain legal system under which he had a further choice between a new system and an existing system. It was generally understood that the draft Convention would set up an optional system and was not designed to replace existing national systems. Article 1 of the current draft Convention did not clearly bring out that element of choice. That was why he had proposed the words: "This Convention applies to an international bill of exchange when the instrument contains the words 'International Bill of Exchange'". Such a wording would clearly establish the prerequisite for the application of the future convention.

*The meeting rose at 6 p.m.*

### Summary record of the 339th meeting Wednesday, 25 June 1986, 10 a.m.

[A/CN.9/SR.339]

*Chairman:* Mr. KARTHA (India)

*Chairman of the Committee of the Whole:*  
Mr. VIS (Netherlands)

*The meeting was called to order at 10.10 a.m.*

#### International payments (continued)

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes* (continued) (A/CN.9/273, A/CN.9/274 and A/CN.9/285)

#### Articles 1 and 2

1. Mr. KIM (observer for the Republic of Korea) supported the proposal made at the previous meeting by the observer for the Hague Conference on Private International Law that a distinction should be made in article 1 between the requirements necessary to ensure the validity of an instrument and the requirements necessary to ensure the applicability of the draft Convention.

2. Mrs. VILUS (Yugoslavia) likewise supported the proposal, which would, however, involve restructuring the entire article. In addition, she felt that a distinction should be made between those elements listed in article 1(2)(e) which were essential in order for a bill of exchange to be considered valid and those which were not essential. The current wording implied that all five elements were essential; that would discourage the easy circulation of international negotiable instruments. Under the 1930 Geneva Convention in order to be considered valid an instrument had to indicate only the place where it was drawn and the place of payment.

3. Mr. LEAES (Brazil), referring to the report of the Commission on the work of its seventeenth session (A/39/17, para. 19), asked whether a study had been made to determine whether countries that had ratified the 1930 and 1931 Geneva Conventions could ratify the proposed draft Conventions without violating their obligations under the former Conventions and, if so, what the findings had been.

4. Concerning the international elements, he said that article 1 should state clearly what were the minimum formal requirements in order for an instrument to be considered an international bill of exchange governed by the draft Convention. In his view, the requirement stated in the introductory sentence to

article 1, paragraphs (2) and (3), was unnecessary. It was quite sufficient if the words "international bill of exchange (convention of ...)" or "international promissory note (convention of ...)" appeared in the text of the instrument concerned.

5. He, too, agreed with the proposal made by the observer for the Hague Conference.

6. Mr. PISEK (Czechoslovakia) said that he saw no reason to change the existing text of article 1.

7. Mr. CHAFIK (Egypt) reiterated that the concept of internationality outlined in the draft Convention was both too broad and too narrow. It was too broad in that it could apply to instruments which should really fall under national law. For example, if a businessman residing in Lebanon were to draw, while passing through Egypt, an instrument for a debt in Lebanon, payable in Lebanon, such an instrument would attract the application of the draft Convention even though properly it belonged under national law. At the same time, the draft Convention was too narrow since it took into account only the place where an instrument was drawn and the place of payment. There were, however, other elements that could be taken into consideration. For example, should an instrument drawn in Lebanon, payable in Lebanon, but endorsed in Egypt to an Egyptian bank be considered as falling under national law?

8. Mr. VIS (Chairman of the Committee of the Whole) pointed out that article 1(4), which provided that proof that the statements referred to in paragraph (2)(e) or (3)(e) were incorrect did not affect the application of the Convention, enabled the drawer to choose whether the instrument should fall under domestic law or under the Convention.

9. Mr. GUEST (United Kingdom) said that article 1 of the 1930 Geneva Convention required, as a condition for the validity of an instrument, that a bill of exchange should state the place at which payment was to be made and the date and place of issue. He did not believe that it had ever been the Commission's intention that an instrument should embody all five elements listed in article 1(2)(e); only two of the five elements were required.

10. The proposal of the representative of Egypt to expand the scope of application of the draft Convention by including the place of endorsement among the elements of article 1(2)(e) might increase the problems that might arise if a dispute in regard to an instrument to which the Convention applied arose in a non-Contracting State.

11. Mr. VIS (Chairman of the Committee of the Whole) asked the representative of Egypt whether he was proposing that a bill drawn under national law in the Netherlands, for example, and payable in Egypt could be made international simply by virtue of being endorsed in Egypt.

12. Mr. VENKATRAMIAH (India) said that he could not agree to the proposal to divide article 1 into two, since that might create problems of interpretation in national courts and might destroy the uniformity that the draft Convention was intended to promote. He could agree to the proposal made by the representative of Egypt to broaden the scope of the draft Convention, provided that that did not create problems.

13. Mr. CRAWFORD (observer for Canada) suggested that, in order to meet the concern expressed by the representa-

tive of Yugoslavia, the Commission might consider amending article 1(2)(e) slightly to make it clear that only two of the places needed to be indicated and to be situated in different States.

14. Referring to the model forms of instruments contained in the note by the secretariat (A/CN.9/285), he suggested that the words "address of payee" and "address of drawee" should be inserted instead of "place of payee" and "place of drawee" respectively. Second, he suggested that it should be made clear that provision of that information was optional.

15. Mr. VIS (Chairman of the Committee of the Whole) recalled that the word used in the original form had, in fact, been "address". It would be necessary to ascertain why the Working Group had made the change.

16. Speaking as representative of the Netherlands, he said that he could agree to the text of article 1 either as currently drafted or, as the observer for the Hague Conference had suggested, amended to distinguish clearly between the requirements necessary to make an instrument a bill of exchange, and the requirements necessary to give an instrument the international character that would attract the application of the draft convention.

17. Mrs. PIAGGI DE VANOSI (Argentina), Mr. BURNS (Australia), Mr. CRAWFORD (observer for Canada), Mr. MAEDA (Japan), Mr. ABASCAL (Mexico), Mrs. ADEBANJO (Nigeria), Mr. DELFINO CAZET (Uruguay), Mrs. KAZAKOVA (Union of Soviet Socialist Republics) and Mr. SPANOGLE (United States of America) said that they were in favour of the existing text.

18. Mr. VIS (Chairman of the Committee of the Whole) said that he would therefore conclude that the proposal from the Hague Conference on Private International Law had not gained sufficient support in the Commission; however, it would appear in the records of the preparatory work for the Convention.

19. Mr. CHAFIK (Egypt) said that the criterion of internationality in article 1 must be changed completely: in the case of an instrument that was national, national law would be applicable, but as soon as it became international in nature, the Convention would apply.

20. Mr. VIS (Chairman of the Committee of the Whole) said that the question had been considered by the Working Group and that there had been difficulties with almost all ways of broadening the concept of internationality.

21. Turning to the question of including a definition of "writing" in the draft Convention, he recalled that at the Commission's seventeenth session a number of representatives had felt that such a definition was necessary since instruments were not usually handwritten but often took the form of, for instance, telexes, telegrams or data communications. The Working Group, however, had taken the view that the draft Convention should not include a definition of writing.

22. Mr. ABASCAL (Mexico) said that the draft Convention appeared to apply only to instruments consisting of a single page, judging by the reference to an "allonge" in article 13. It seemed that a written instrument consisting of several pages would not be covered by the Convention unless all the pages

were signed and identified. That point must be made clear in the text.

23. Mr. VIS (Chairman of the Committee of the Whole) said that he felt that instruments consisting of several pages were covered by the draft Convention.

24. Mr. GANTEN (observer for the Federal Republic of Germany) said that instruments consisting of several pages should not pose a problem as long as the pages were fixed together to form one instrument.

25. It was not necessary to include a definition of writing in the draft convention. The existing text, referring simply to a "written instrument", was sufficient and left room for interpretation; problems would arise if an attempt was made to include a definition.

26. Mr. DRUEY (observer for Switzerland) said that, in the light of the reference to an "*allonge*" in article 13, it appeared that a written instrument should essentially consist of one page. If instruments consisting of more than one page were to be covered by the draft Convention, that should be specifically stated.

27. Mr. VIS (Chairman of the Committee of the Whole) said that the concept of an "*allonge*" appeared in other laws on negotiable instruments, such as the Bills of Exchange Act, 1882 of the United Kingdom, the Uniform Commercial Code (United States of America) and the Geneva Uniform Law on Bills of Exchange and Promissory Notes. Instruments consisting of more than one page, particularly promissory notes, did exist.

28. Mr. BRANDT (German Democratic Republic) said that his delegation felt that there was no need for a definition of writing, since there were no such definitions in national laws on bills of exchange. International practice would have to establish what "writing" was in the light of all possible technical developments.

29. Mr. DELFINO-CAZET (Uruguay) said that it was not usual for writing to be defined under national law; the Working Group's position was appropriate, since it left open the possibility of expanding the traditional concept of writing to include modern means of communication by electronic and other means.

30. Mr. BURNS (Australia) said that his delegation did not feel that a definition of writing was needed, and believed that the question should be left to be determined by the courts. The commentary (A/CN.9/213, p. 13) made it clear that the term "written" would include any mode of representing or reproducing words in visible form. Australian legislation on the subject did contain a definition of writing, but that definition was inclusive, and the courts were left to define writing on a case-by-case basis. Any attempt to define writing would lead to difficulties.

31. Mr. VIS (Chairman of the Committee of the Whole) said that if it was the general view that there should be no definition of writing in the draft Convention, the text would remain as it stood.

32. Turning to article 1(5), he said that the paragraph had been included to make it clear that in common-law countries the draft Convention did not apply to cheques.

33. If there was no objection to that paragraph, he would take it that article 1 was adopted, subject to drafting changes to be submitted by the delegations of Canada and Yugoslavia.

34. *It was so decided.*

*The meeting was suspended at 11.25 a.m. and resumed at 11.55 a.m.*

35. Mr. VIS (Chairman of the Committee of the Whole) recalled that the Working Group had referred back to the Commission the controversial issues relating to article 2 of the draft Convention, as discussed in paragraph 69 of its report (A/CN.9/273).

36. Mr. PELICHET (observer, Hague Conference on Private International Law) said that the new draft Convention would conflict with the Geneva Convention for the Settlement of Certain Conflicts of Laws in Connection with Bills of Exchange and Promissory Notes as well as with the conflict-of-laws systems of the common-law countries or with instruments such as the Bills of Exchange Act or the Uniform Commercial Code, none of which recognized party autonomy. The Hague Conference, which was awaiting with interest the completion of the Commission's work on the draft Convention, had decided to consider whether the Geneva Convention on conflicts of laws should be revised in order to bring all operations relating to negotiable instruments under one law and also to allow party autonomy. His own view was that such a revision was needed to allow full scope to the Commission's draft Convention.

37. The difficulties raised by article 2 went beyond the problem of conflict of laws to a problem of territoriality, because the text allowed parties who had no links to a contracting State to negotiate instruments. In the most absurd instance, it would be possible for a drawer in a non-contracting State to draw a bill on a drawee in a non-contracting State. Article 2 was a legal aberration and would not work. He had suggested in the Working Group that at least two of the places mentioned in article 1(2)(e) should be situated in Contracting States, preferably the places where the instrument was drawn and paid, in order for an instrument to be covered by the Convention.

38. Mr. VIS (Chairman of the Committee of the Whole) gave an example of an instrument involving three States: a bill was drawn in Nigeria (which had ratified the Convention) on a drawee in the Netherlands (which had also ratified the Convention) in favour of a payee in Egypt (which had not ratified the Convention); the payee discounted it with a Cairo bank, which presented it for payment to the drawee in the Netherlands, who dishonoured it. The Cairo bank had a right of recourse against either the drawer in Nigeria (a Contracting State) or the payee in Egypt (a non-Contracting State). According to article 2, the liability of the payee was governed by the draft Convention. He supposed, however, that an Egyptian court might decide to apply its own rules on conflict of laws.

39. Mr. PELICHET (observer, Hague Conference on Private International Law) said that the Committee Chairman's example related strictly to a conflict of laws. If the Geneva Convention were revised, then the Egyptian judge could apply the Convention.

40. Mr. VIS (Chairman of the Committee of the Whole), returning to his earlier example, postulated a situation in which

the drawer in Nigeria (a Contracting State), wishing to invoke the Convention, drew on a drawee in the Netherlands (a non-Contracting State), who as drawee had no liability. There would be no problem if the drawee paid or if he dishonoured; the bank in Cairo would either take action against the drawer in Nigeria (where the Convention would apply) or against the payee in Egypt. He wondered why the observer for the Hague Conference was so concerned about the place of payment.

41. Mr. PELICHET (observer, Hague Conference on International Private Law) said that, although the place of payment was indeed most often the problem, it was not the only difficulty. He had therefore suggested that two of the places mentioned in article 1(2)(e) should be situated in Contracting States. As article 2 now stood, there could be a situation in which none of the places concerned was situated in a Contracting State. In the example given by the Committee Chairman, he did not see how the drawee in the Netherlands could possibly accept to pay, under the existing system.

42. Mr. VASSEUR (France) strongly supported the position of the observer for the Hague Conference regarding article 2. French banks were extremely concerned about article 2, which it was felt would lead to much uncertainty. In the second situation described by the Committee Chairman, there was in fact a problem with regard to the drawee, the problem of the defences available. The place of payment was crucial because there it would be determined whether a drawee had the right to refuse to pay or was obliged to pay. Article 2, on the other hand, declared that the Convention was applicable regardless of whether the place indicated on an instrument was situated in a contracting State.

43. Dealing with the issue of applicability, the 1980 United Nations Convention on Contracts for the International Sale of Goods was much less categorical in article 1; perhaps its provisions could be transposed to article 2 of the draft Convention.

44. Mr. SPANOGLE (United States of America) said that he himself had been convinced in the Working Group by the validity of the point made by the observer for the Hague Conference. However, at a meeting of United States bankers which he had attended, it had been said that the existing text of article 2 should be retained. The bankers had not been especially concerned about uncertainties as to the application of the Convention in cases which might or might not come before the courts of non-Contracting States. What they wanted was certainty in the day-to-day handling of paper in the banks themselves. The banks did not want to have to check constantly changing lists of parties to a Convention, and in any case regarded rules on conflict of laws as amorphous.

45. Mr. VIS (Chairman of the Committee of the Whole) remarked that what United States bankers might want would not, in any case, affect the Netherlands or other civil-law countries, which generally did not recognize autonomy of parties to negotiable instruments. A financier from the Netherlands fell under the law of the Netherlands and could not place himself under the Convention. United States bankers might want to think that the liability of a Netherlands drawee was a Convention liability, but in fact it was a liability under the law of the Netherlands. The certainty that satisfied them would thus be illusory.

46. Mrs. PIAGGI de VANOSI (Argentina) shared the concern of the Chairman of the Committee of the Whole. Argentina too did not recognize party autonomy. Article 2 as it stood would create enormous difficulties in implementing the Convention with regard to non-Contracting States and she believed that it should be amended.

47. Mr. DUCHEK (Austria) said that article 2, as currently worded, seemed to imply that the rules set out in the draft Convention were applicable in all cases. As he interpreted the article, however, the draft Convention would actually be applied on the basis of the national legislation of Contracting States, even though the text failed to indicate just how such national legislation was to be applied. That omission might create some legal uncertainty, but that uncertainty would not be much greater than that which currently existed under the rules set out in the Geneva Convention on conflicts of law.

48. Mr. GUEST (United Kingdom) said that the proposal made by the observer for the Hague Conference on Private International Law to require that both the place where an instrument was drawn or made and the place of payment should be situated in a Contracting State would not obviate all existing difficulties, particularly in the case of an international instrument involving several parties. Specifying one of those places as the point of linkage in article 2 might allay the fears of those who felt that the article was too "imperialistic" and uncertain. However, requiring that both places be situated in Contracting States might give pause to Governments that were considering ratifying the Convention in its early stages, when the number of non-Contracting States would exceed the number of Contracting States. He therefore was of the view that the current wording might best be left untouched.

49. He did not believe that any real analogies could be drawn between the draft Convention and the Convention on Contracts for the International Sale of Goods, since the latter involved only two parties—buyer and seller—while an international bill of exchange or promissory note might involve numerous parties.

50. Mr. ANGELICI (Italy) said that, as more and more requirements were imposed for international bills of exchange, increasingly difficult conflict-of-laws problems would arise. Furthermore, the draft Convention was intended to provide an alternative to domestic rules. He therefore saw no need for a linkage between the use of an international instrument and a Contracting State. Such a requirement might lead to a high degree of uncertainty and introduce the need to verify the status *vis-à-vis* the Convention of all the parties concerned.

51. Mr. VIS (Chairman of the Committee of the Whole) said that article 2 was addressed to States which had become parties to the Convention; given that, for such States, the Convention would always apply, the law of those States was not concerned with the effect of the Convention in a non-Contracting State. He agreed that article 2 was not clearly worded, but stressed that it was intended to mean that a Contracting State was obligated to apply the rules contained in the draft Convention.

52. Mr. MUOZ (observer, Latin American Banking Federation) said that the current discussion regarding article 2 was irrelevant. In practice, banks or holders of international instruments were interested in knowing only whether the Convention was applicable in the places where they operated. He therefore believed that the text of the article should not be changed.



53. Mr. CHAFIK (Egypt) said it was obvious that the wording of article 2 was somewhat unclear. He therefore proposed that the beginning of the article should be reworded to read: "When, in conformity with the rules of conflicts of laws, this Convention is applicable, it applies without regard to ...".

54. Mr. DUCHEK (Austria) suggested that article 2 placed the draft Convention in conflict with the Geneva Conventions. According to the Convention on conflicts of laws, the law applicable in the case of an international instrument was that of the country in which it had been signed. If the Geneva Conventions were not modified in any way, the draft Convention could not overrule their effect for States that were parties to them.

55. Mr. PELICHET (observer, Hague Conference on Private International Law) replied that if article 2 of the draft Convention contradicted the Geneva Convention of conflicts of laws and the Uniform Law on Bills of Exchange and Promissory Notes, States which had ratified the latter instruments might not be able to ratify the draft Convention.

56. Mr. QADER (observer for Bangladesh) said that, in his view, article 2 did not conflict with the provisions of any other conventions. Likewise, he saw no need to seek different interpretations of conflict-of-laws rules. Draft article 2 did not create any third-party liability; rather, it conferred a right. Some slight rewording might make the meaning clearer.

57. Mr. GUEST (United Kingdom) said it was his understanding of article 2 that, if proceedings were to be instituted in

connection with an international instrument in a forum of a State which had ratified the Convention, then the Convention would apply, regardless of the conflict-of-laws rules in effect in that State. If the article was interpreted to mean that the conflict-of-laws rules of the forum of a Contracting State governed the application of the Convention, then the wording of the article must be given serious consideration.

58. Mr. VIS (Chairman of the Committee of the Whole) concurred with the representative of the United Kingdom in his interpretation of article 2. He did not believe that the text should refer to conflict-of-laws rules, since that was not the intent of the article. However, as there appeared to be some confusion regarding the existing text, he suggested that it should be referred to the Drafting Group for further consideration.

59. Mr. CRAWFORD (observer for Canada) said he assumed that any State which ratified the draft Convention would assume responsibility for aligning its domestic law with the provisions of the Convention. However, he wondered whether States parties to the Geneva Conventions could in fact do so, or whether a revision of the Geneva Conventions would be required for that purpose.

60. Mr. VIS (Chairman of the Committee of the Whole) said he thought that that question could be settled only by the States parties to the Geneva Conventions.

*The meeting rose at 1.05 p.m.*

### Summary record of the 340th meeting Wednesday, 25 June 1986, 3.00 p.m.

[A/CN.9/SR.340]

*Chairman:* Mr. KARTHA (India)

*Chairman of the Committee of the Whole:*  
Mr. VIS (Netherlands)

*The meeting was called to order at 3.15 p.m.*

#### International payments (continued)

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes* (continued) (A/CN.9/273, A/CN.9/274 and A/CN.9/285)

1. Mr. VIS (Chairman of the Committee of the Whole) invited the Commission to resume consideration of the draft Convention contained in document A/CN.9/274.

*Articles 25 and 27*

2. Mr. MAEDA (Japan) said that, in a hypothetical sales transaction between two parties, A and B, in which A made a note in favour of B for the delivery of goods, A would have the defence of non-performance against B if B failed to deliver the said goods. If a third party, C, took the note after the expiration of the time-limit for its presentment for payment, without knowledge of the defence, the question was whether A could set

up against C the same defence as against B based on the underlying transaction between A and B. Article 25 (2 *bis*) provided that C would not be subject to that defence. In such a case, however, article 4(7)(b) would become meaningless. He therefore proposed the addition of the following text to paragraph (2 *bis*) of article 25: "except that a holder who takes the instrument after the expiration of the time-limit for presentment for payment is subject to any claim to or any defence upon the instrument to which his transferor is subject".

3. Mr. VIS (Chairman of the Committee of the Whole) asked whether members shared the concern expressed by the representative of Japan.

4. Mr. GRIFFITH (Australia) said that he was satisfied with the current construction of article 25 since it further strengthened the obligation to pay a bill of exchange. A holder would in due course be able to obtain payment while the person to whom the bill was originally issued could not because of the defences provided under article 25(1).

5. Mr. VASSEUR (France) said that he supported the representative of Australia. The principle established under the Geneva Uniform Law on International Bills of Exchange and International Promissory Notes was that, except in special circumstances, the endorsement of an instrument after maturity produced the same effect as endorsement prior to maturity. Since article 25 (2 *bis*) did not contradict that principle, he was in favour of retaining it in its current form.

6. Mr. ANGELICI (Italy) said that after maturity, an instrument should retain its negotiability. He therefore supported the Japanese position.

7. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that she had always been concerned about the provision in the draft Convention under which it was possible to make free use of bills of exchange even after their maturity. Article 25 of the draft Convention failed to make any distinction based upon whether the holder received the instrument before or after its maturity.

8. Under article 4(7)(b), a protected holder must have received the instrument before the expiration of the time-limit provided by article 51 for presentment of that instrument. A subsequent holder, under article 27, was also a protected holder even though he received the instrument after its maturity. No national legislation included such a provision, and she was not in favour of its inclusion in the draft Convention. Article 4(7)(b) should operate clearly in all situations, and article 27 should not enable a holder to use a bill of exchange which he had received after its expiration.

9. Mr. CRAWFORD (observer for Canada), supporting the Japanese proposal, said that the aim of the draft Convention should not be to encourage traffic in overdue bills. Failure to change article 25 (2 bis) could lead to serious dislocations in other sections of the draft Convention.

10. Mr. SPANOGLE (United States of America) said that he supported the Japanese proposal for resolving the difficulty in the current draft.

11. Mr. GUEST (United Kingdom) said that a person who took a bill after its maturity should not be a protected holder. Article 25 (2 bis) should therefore be amended along the lines of the Japanese proposal.

12. Mr. VASSEUR (France) said that he could not understand why the maturity of an instrument should cause it to lose its negotiability. Endorsement of an instrument was a simplified form of transfer. The element of maturity merely served to establish the obligation to present an instrument for payment and had nothing to do with the possibility of transferring that instrument through endorsement. He would not, however, insist on retaining the current text.

13. Mr. VIS (Chairman of the Committee of the Whole) said that under article 53, failure to present a bill for payment by the due date resulted in the discharge of the drawer, endorser or guarantor. The real question was whether the transferee of the payee who had failed to present the instrument for payment should have better rights than the payee, although he was only a holder. Moreover, why should a drawer, who had been discharged because of failure to present the instrument for payment by the due date, be liable to a person who had taken the instrument after its maturity?

14. Mr. GUEST (United Kingdom) said that it was not the intention of the draft Convention to prohibit the negotiation of bills after their maturity. A bill of exchange continued to be fully negotiable and transferable after its maturity. The transferee, however, took such a bill subject to any defects which could be raised against the title of the transferor. The reasoning of the Chairman of the Committee of the Whole concerning the discharge of the other parties was quite convincing. The

Japanese proposal simply meant that a person who took a bill of exchange after its maturity accepted the risk that certain defences could be set up against the transferor.

15. Mr. GRIFFITH (Australia) said that he would not insist on the retention of the current text.

16. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that, with regard to the "shelter" rule, she wished to propose that a separate paragraph should be added to article 27 to the effect that a holder who took an instrument from a protected holder after its maturity would not himself be a protected holder.

17. Mr. VIS (Chairman of the Committee of the Whole) said that article 27 did not provide that a holder became a protected holder if he received an instrument from a protected holder. He merely had the rights of the transferor. If that transferor did not present the instrument for payment in due time, he would lose his rights to payment from certain other parties liable. The "shelter" rule would, in such cases, not help the transferee.

18. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that under article 27 a protected holder did not lose his status but remained protected *vis-à-vis* the maker of the instrument. It was important to make it clear that the status of a protected holder would not be maintained if an instrument was transferred after its maturity.

19. Mr. VIS (Chairman of the Committee of the Whole) said that article 27 merely provided that the transfer of an instrument by a protected holder vested in any subsequent holder the rights to and upon the instrument which the protected holder had. The rights of the transferee should therefore be determined with reference to the rights of the transferor.

20. Mr. SPANOGLE (United States of America) said that it was important to look at the differences between the limits placed on the holder under article 25 (2 bis) and under article 27. Article 25 (2 bis) sought to protect the transferee who received an instrument with certain types of knowledge, but who could still exercise certain types of rights. Article 27 was designed to protect the rights of the transferor in order to permit him to market his instrument. There were times when a transferor would wish to market his instrument after its maturity. The holder of an instrument might have a high opportunity cost resulting from the delay in payment. The aim was not to protect the transferee but to enhance the negotiability of the instrument and to protect the transferor. The current text was therefore adequate.

21. Mr. GUEST (United Kingdom) observed that there were two questions at issue. First, there was the question of substance raised by the Soviet representative in connection with article 25 (2 bis), namely that, in the example quoted by Japan, if A made out a note to B representing a contract for the sale of goods, B was a protected holder at the time he received the note. If a dispute arose subsequently between A and B concerning the quality of the goods, A would have a defence against B. If B, as a protected holder, transferred the note to C after its maturity and C did not know of the existence of the dispute, would C be entitled to protected status under the "shelter" rule? It seemed to follow from the logic of other provisions of the draft Convention that C should not enjoy protected status and should be open to the possibility of a defence.

22. The second question concerned article 27. In his view, article 27 did not confer protected status on C but simply transferred to him the rights, however encumbered, which B had to and upon the instrument. Article 27 therefore did not distinguish between transactions involving bills before maturity and bills after maturity.

23. Mr. MAEDA (Japan) agreed with the United Kingdom representative's interpretation of article 27. It was irrelevant whether B and C were protected holders: if B was subject to a defence from A then C should also be.

24. Mr. VIS (Chairman of the Committee of the Whole) observed that the Japanese proposal concerning article 25 (2 *bis*) applied where C was the holder but was not protected because he had received the instrument after maturity. However, he stood in the shoes of B and was therefore subject to defences from A if B was subject to them.

25. Mr. ILLESCAS ORTIZ (Spain) observed that, if protected status could not be granted to C after maturity of the instrument, the most reasonable solution would be to state that principle in general terms in article 27. Otherwise, there would be a conflict between article 25 (2 *bis*) and article 27.

26. Mr. VIS (Chairman of the Committee of the Whole) said that, unlike the Soviet representative, he believed that under article 4(7) C could not be a protected holder if he received an instrument from B, who was a protected holder, after maturity. In such cases, however, C could enforce his rights against A under the "shelter" rule. Since no consensus had as yet emerged, he suggested that informal consultations should be conducted on the issue. In the mean time, if he heard no objection, he would take it that the Commission adopted the Japanese amendment to article 25 (2 *bis*).

27. *It was so decided.*

### Article 3

28. Mr. VIS (Chairman of the Committee of the Whole) recalled that the Working Group had proposed the addition of the phrase "and the observance of good faith in international transactions" at the end of article 3. If he heard no objection he would take it that the Commission agreed to make that addition.

29. *It was so decided.*

30. Mr. ANGELICI (Italy) said that his delegation had reservations concerning the addition to article 3. In its view, the concept of good faith had meaning for the parties to a contract but not for the judge called in to settle claims. Adding a reference to good faith could create problems by allowing a far more flexible interpretation of the Convention than was warranted.

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

31. Mr. VIS (Chairman of the Committee of the Whole) referred the Commission to paragraphs 76 to 86 of document A/CN.9/273, which summarized the Working Group's discussions on article 4(10) and article (X).

32. Mr. CHAFIK (Egypt) pointed out that, in defining "signature", article 4(10) made no reference to handwritten signatures. It should be made clear that handwritten signatures were included.

33. Mr. GANTEN (observer for the Federal Republic of Germany) reiterated that it was very difficult for his delegation to accept means other than handwritten signatures as signatures on international bills of exchange and promissory notes. Allowing other means of signature did not enhance the negotiability of instruments and would create numerous difficulties. If most members of the Commission were in favour of retaining article 4(10), a provision along the lines of article (X) must also be included.

34. Mr. ABASCAL (Mexico) observed that the definition of signature should also include illegible signatures, which were rife in Mexico at least, especially since article 29(2) ruled that a person signing an instrument in a name other than his own was liable as if he had signed it in his own name.

35. Mr. BRANDT (German Democratic Republic) observed that allowing contracting States to enter reservations to the Convention would create numerous difficulties in dealing with international commercial instruments. Reservations were inappropriate in the present instance, and article (X) should therefore be deleted.

36. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) agreed with the representative of the German Democratic Republic. The problem of defining signature, with or without reservations, had been under discussion for several years. The legal consequences of allowing reservations had been given particular attention, and the conclusion had been that the consequences of such reservations were not very clear. It was therefore in the interest of the adoption and proper implementation of the Convention, rather than of individual countries, to delete article (X).

37. Mrs. PIAGGI de VANOSI (Argentina) said that she could see no point in retaining article 4(10). The definition it gave could only create problems, and her delegation would therefore prefer its deletion.

38. Mr. SAMI (Iraq) observed that the question of signatures was one of the most important issues raised by the Convention and one that also touched on domestic law. Several forms of signature might be applicable in one country but not in another. For instance, because of illiteracy, some countries accepted a thumb-print as a signature. Accordingly, that was an issue that could be resolved only under domestic law. Being international in scope, the draft Convention must limit itself to defining the concept of signature and then allow each country to decide which forms of signature it would accept. The 1930 Geneva Convention had not defined the concept of signature and had left it to individual States to determine the various forms acceptable to them. Article (X) was extremely important therefore. Furthermore, article 4(10) should state that "signature" meant a handwritten signature but could also include the other means of signature listed.

39. Mr. PISEK (Czechoslovakia) said that his delegation had originally favoured article 4(10) because it opened the way to new techniques. Now, however, it realized that the definition was unacceptable to many countries and created the need for possible reservations. Since the implications of such reservations could not be predicted, it would be preferable to dispense with article 4(10) altogether and to leave the matter up to individual countries to decide.

40. Mr. KIM (observer for the Republic of Korea) agreed that article 4(10) should be deleted. No other international instrument contained a definition of signature, and such a definition, if retained, could conflict with domestic laws.

41. Mr. GUEST (United Kingdom) observed that a national of one State initiating an instrument which was to be subject to the Convention must know what forms of signature were acceptable in other contracting States. Problems had arisen in the United Kingdom concerning the acceptability or otherwise of stamps or facsimiles, and some countries might not recognize them. Article 4(10) should therefore be retained in order to keep pace with technological developments. While article (X) created problems for his delegation and he would prefer to see it deleted, his delegation would not oppose its retention if some countries attached importance to it. If the whole question of signatures was simply eliminated, the doubts that would remain regarding the validity of certain forms of signature would render the entire Convention ineffective.

42. Mr. DELFINO-CAZET (Uruguay) said that, in principle, he would be in favour of deleting article 4(10) in the interest of the smooth functioning of the future Convention. Since other definitions, such as that of "drawer", had been omitted from article 4, the definition of signature might also be eliminated without problem. However, if the members felt that the term needed to be defined, he agreed with the representative of Egypt that it should be clearly established in the definition that a signature must be handwritten. In his own country, for example, signatures were unacceptable if they were not handwritten.

43. Mr. SPANOGLE (United States of America) said that article 4(10) should be retained in its current wording; otherwise, banks which had been in the habit of accepting instruments signed by mechanical means would no longer be able to do so. Moreover, it was often safer and more feasible to rely on signatures by mechanical means. The same would apply to instances where an instrument was transmitted by telex or other electronic means. A reasonable solution to the problem of countries whose domestic law prohibited signatures other than handwritten ones had been made available in article (X).

*The meeting was suspended at 4.45 p.m. and resumed at 5.15 p.m.*

44. Mr. VASSEUR (France) said that the records of the meetings held in preparation for the 1930 Geneva Convention contained a very broad definition of a signature as being any material sign whatsoever which served, according to the usage of the country, to identify the signer on papers and bills. Although in 1961 the French *Cour de cassation* had ruled that a signature must be handwritten, French legislators had subsequently modified that definition to include means of signature other than handwritten ones. His delegation therefore felt very strongly that article 4(10) should be retained. Instead of listing the various forms of mechanical means of signature, however, it would be preferable to use a general term such as "any non-handwritten means". As to the use of electronic means referred to by the representative of the United States, he felt that the use of such means implied the elimination of paper altogether, whereas in France the term "bills of exchange" by definition required the use of paper. The means of signature referred to in article 4(10) must therefore include only mechanical means, not electronic means. As to article (X), although he would prefer that it should be omitted, he would not oppose it.

45. Mr. ILLESCAS ORTIZ (Spain) said that his delegation associated itself with the view that article 4(10) should be retained. The article merely listed a non-restrictive series of acceptable means of signature; it did not define the term itself. Moreover, he felt that in order to avoid problems arising from illegible signatures, article 1(2)(e)(v), stipulating that the place of payment should be shown on a bill of exchange or promissory note, should also include the name of the person who signed the bill or note. His delegation was opposed to the inclusion of article (X) because it might present a risk to the proper functioning of the Convention, in view of the variation in legislation from country to country.

46. His delegation did not share France's reservation concerning electronic means. Such means did not preclude the use of paper; for example, a bill or promissory note could be stamped by electronic means.

47. Mrs. VILUS (Yugoslavia) said that her delegation had no objection to retaining article 4(10); however, article (X) should be deleted because, if the place at which the bill had been signed was not apparent from the instrument, the reservation might not provide adequate protection to a contracting State whose legislation required a handwritten signature or, in fact, to other parties dealing with a State which had made such a reservation.

48. Mrs. ADEBANJO (Nigeria) said that article 4(10) should be retained together with article (X) because, without article (X), there was a possibility of forgery of signature by stamp or other means.

49. Mr. LIU Benku (China) said his delegation believed that article 4(10) should remain in its current form, since that would be in the interest both of countries which used handwritten signatures and of those which used other means. In China, for example, stamps were widely used. China was not opposed to making a specific reference to handwritten signatures, if that was the wish of some delegations.

50. Mr. VAN SANDICK (observer, International Bar Association) said that, among his associates, only one, who represented Switzerland, had reported that there was a legal requirement that a handwritten signature should be affixed to an international bill of exchange. Article (X) would make it possible for Switzerland to accede to the Convention. However, if article (X) was adopted, the Convention would lose the advantage of clarity. In the banking industry, there was a requirement that the implications of documents should be easily recognized. It was impossible for a bank clerk to check not only whether a convention existed but also whether a country had made a reservation at the time it had acceded to it. The possibility of making such a reservation would detract from the Convention.

51. Mr. GOH (Singapore) said that his delegation preferred the text of article 4(10) and article (X), as drafted by the Working Group.

52. Mr. KOCH (Sweden) said that his delegation was in favour of retaining article 4(10) and would also accept the retention of article (X).

53. Mr. GRIFFITH (Australia) said that his delegation would prefer to retain article 4(10) without article (X). If the Commission decided to retain article (X), that article should

contain a provision that the international bill of exchange should state the place where the bill was signed, so that it would be possible to determine from the face of the bill that it had originated in a country which had made the reservation provided for in article (X). According to the definition of an international bill of exchange as contained in article 1(2), it would seem that it was not essential to state the place where such a bill was signed. Once one went beyond the straightforward definition contained in article 4(10), which was entirely appropriate for a convention intended to enter into force in the late 1990s, it seemed to be very backward-looking to contemplate a fixed position regarding the development of methods of affixing acceptable signatures.

54. His delegation's first preference, then, was to retain article 4(10). Its second preference was to have as simple a formulation as possible, if it was the wish of some delegations to delete all definitions. Its third preference was to include article (X) and to require that the face of the bill should contain a clear indication of the place where it was signed.

55. Mr. GLATZ (Hungary) said that his delegation was in favour of the texts of article 4(10) and article (X) as drafted.

56. Mr. SPANOGLE (United States of America) said that he was not satisfied with the wording of article (X), since an instrument issued in a country which had ratified the Convention but had not made the reservation provided for in that article could be received by another country party to the Convention which had made that reservation and which could therefore refuse to accept a bill of exchange or promissory note on the grounds that it had not been properly signed. The retention of article (X) as drafted therefore introduced an element of great uncertainty. The Commission should accompany article (X) with a provision which would indicate which kinds of signature might be subjected to extra scrutiny.

57. Mr. DUCHEK (Austria) said that his delegation was in favour of retaining the text of article 4(10) as drafted and of deleting article (X) since it gave rise to many difficult questions. For example, a Contracting State which had made the reservation provided for in article (X) could declare that an international bill of exchange which did not contain a handwritten signature was unacceptable. He inquired whether States which did not make that reservation were obliged to consider any signature other than a handwritten signature as invalid. If that was not the case, a signature could be accepted as valid by one Contracting State and as invalid by another.

58. Mr. DRUEY (observer for Switzerland) said that Switzerland was not the only country which required that an international negotiable instrument should contain a handwritten signature. He believed that the same requirement applied in the Federal Republic of Germany. His Government was in favour of a provision which complied as far as possible with Swiss practice. He was not certain that article (X) did so, for it failed to provide a simple procedure for evaluating the authenticity of signatures on bills of exchange. The idea of having stricter requirements regarding signatures originating in a country which had made the reservation provided for in article (X) did not serve the purpose. He was not sure that article 4 (10), even without article (X), would provide much security in the matter of signatures.

59. Apart from the problem of the means of affixing signatures, the text of article 4(10) provided no information as to what a signature actually was. Was it something which imitated a

handwritten signature? Could it be typed? That matter was relatively simple in the case of natural persons but, in the case of firms and corporations, there were very different standards in various countries. Since there were so many cases in which it would be necessary to rely on local law, there should be a conflict-of-law rule which applied very generally to the validity of signatures.

60. Mr. VIS (Chairman of the Committee of the Whole) said that article 4(10) did not oblige Contracting States to adopt the practice of affixing signatures by mechanical means. It simply obliged a country to recognize signatures affixed by such means to bills of exchange originating in other countries.

61. Mr. GANTEN (observer for the Federal Republic of Germany) said that his country would recognize a signature affixed in accordance with the practice of a Contracting State which had not made the reservation provided for in article (X). The only problem would be that the person or bank dealing with a bill of exchange bearing a non-handwritten signature might have doubts about whether the bill had been signed. For example, a bank clerk might not readily identify perforations on a bill of exchange as a signature.

62. Mr. MAEDA (Japan) said that his delegation was in favour of retaining article 4(10). Although Japan believed that article (X) would pose an obstacle to the smooth negotiation of bills of exchange, it was prepared to accept the retention of that article in a spirit of compromise. However, if retained, article (X) should make clear what would be the legal consequences when a signature was affixed by mechanical means in a Contracting State which had made the reservation provided for in article (X). Japan believed that the person who signed an instrument of that kind did not bear liability on the instrument, and that an uninterrupted series of endorsements was not destroyed by the fact that a signature made by mechanical means was included on the face of the instrument. Article 41(1)(c) would apply when that kind of signature was made by the drawer, maker or acceptor.

63. Mr. VIS (Chairman of the Committee of the Whole) said that, although he personally felt that the adoption of article 4(10) was fraught with dangers and hidden problems, there were six States which had insisted on its adoption, and their views must be taken into account. The overwhelming majority of delegations wished to retain article 4(10) subject to the amendment proposed by the representative of Egypt, which had already been adopted. Since it would not be feasible to include a provision regarding the legal effects of the article, he suggested that the Commission should adopt article 4(10) as amended and article (X) as drafted.

64. Mr. CRAWFORD (observer for Canada) suggested that those States which were concerned that certain unacceptable practices might develop if unchecked by article (X) should refer to article 30. Countries which did not recognize certain kinds of signature on international bills of exchange should retain their right not to accept such instruments.

65. Mr. GRIFFITH (Australia) said that article (X) should state specifically whether the reservation pertained to the country where the signature was placed on the instrument or to the country where the instrument with that signature on it was first delivered. His delegation believed that what was significant was the place where the instrument was just delivered with the

signature on it. It might happen that the signature had been made in one country and the effective endorsement and delivery of the instrument had taken place in another. For the purposes of the reservation provided for in article (X), the country in which the signature was placed on the instrument or in which the instrument was delivered should be indicated on the face of the instrument.

66. Mr. VIS (Chairman of the Committee of the Whole) said he took it that the Commission wished to retain article 4(10). A small working group would be set up at the next meeting to consider the proposal made by the representative of Australia with regard to article (X).

*The meeting rose at 6 p.m.*

**Summary record of the 341st meeting  
Thursday, 26 June 1986, 10 a.m.**

[A/CN.9/SR.341]

*Chairman:* Mr. KARTHA (India)

*Chairman of the Committee of the Whole:*  
Mr. VIS (Netherlands)

*The meeting was called to order at 10.15 a.m.*

**International payments (continued)**

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes* (continued) (A/CN.9/273, A/CN.9/274 and A/CN.9/285)

*Articles 4(10) and (X) (continued)*

1. Mr. GRIFFITH (Australia) said that most members of the Commission appeared to support the inclusion of article (X). At the 340th meeting, his delegation had proposed that the text of that article should be amended; however, on reflection, he had concluded that the proposed amendments would in fact create further complications. Consequently, the original text should be retained.

2. Mr. VIS (Chairman of the Committee of the Whole) pointed out that, although a sizeable minority believed that article (X) should be retained, that view did not predominate among Commission members. However, there was clearly strong support for article 4 (10). He therefore suggested that, as a compromise, article (X) should also be retained.

3. *It was so decided.*

*Articles 4(11) and 71 (1 bis)*

4. Mr. VIS (Chairman of the Committee of the Whole) drew attention to paragraphs 87 to 92 of document A/CN.9/273, concerning the Working Group's efforts to define the terms "money" and "currency".

5. Mr. EFFROS (observer, International Monetary Fund) said that article 4(11) made it possible for international instruments to be expressed in terms of a monetary unit of account. That provision would contribute significantly to the Convention's utility by affirming the negotiability of instruments so denominated. However, as the Convention was not intended to supersede the rules of intergovernmental institutions or agreements between States establishing monetary units of account, the International Monetary Fund (IMF) had decided, after thorough consideration, to propose a proviso to article 4(11) which would read: "provided that this Convention shall apply

without prejudice to the rules of an intergovernmental institution or to the stipulations of an agreement between two or more States relating to a monetary unit of account established by such institution or agreement".

6. By way of illustration, he explained that the special drawing right (SDR), was a monetary unit of account established by IMF for the use of its member Governments. IMF had also established rules to govern transfers of SDRs between Governments entitled to do so, regulating such matters as the calculation of exchange rates and value dates of SDR transactions. Those were the rules which the Convention could not supersede. If the proviso was not included, it was conceivable that ambiguities might arise, particularly in the interpretation of article 71(2)(b), which dealt with the rates of exchange applicable to bills and notes expressed in monetary units of account. The proposed addition would ensure that, in the case of transfers of SDRs between IMF member Governments, IMF rules, and not those of the Convention, would prevail.

7. Mr. GRIFFITH (Australia) said that the proviso seemed somewhat superfluous. It was highly unlikely that the ambiguous situation described by the observer for IMF would occur. He therefore favoured the original, simpler text of article 4(11).

8. Mr. VIS (Chairman of the Committee of the Whole) asked the observer for IMF whether international instruments denominated in a unit of account such as the SDR could be used by States that were not members of the Fund.

9. Mr. EFFROS (observer, International Monetary Fund) explained that, while the SDR had been created for the purposes of the Fund and its member Governments, it had acquired a broader applicability. Like other monetary units of account created for government purposes, such as the European Currency Unit (ECU), it was now widely used by private parties in their transactions. The Convention would confer negotiability on instruments made by private parties and denominated in such units of account, which might become significant in commercial transactions. It should be noted that the private parties involved could not themselves hold SDRs: only IMF member Governments were entitled to do so. That did not preclude the denomination of instruments in SDRs by private parties; however, if payable to a private party, such instruments would be payable in currency.

10. Mr. FELSENFELD (United States of America) agreed with the representative of Australia that confusion regarding the application of the Convention to instruments denominated in monetary units of account was unlikely to arise. However, he believed that the IMF proviso should be incorporated in the text of the draft Convention in order to make that point clear.

11. Mr. PISEK (Czechoslovakia) said his delegation had always favoured the inclusion in the draft Convention of a clause that would provide for the issue of a bill or a note in an artificial currency, since such a provision would be consistent with practice in his country. The provision was not intended to interfere with the rules of IMF or other institutions. He therefore had no objection to the inclusion of the IMF proviso.
12. Mrs. BUURE-HAGGLUND (observer for Finland) suggested that, as there seemed to be agreement that the Convention was not intended to supersede the agreements referred to in the proviso, the observer for IMF might consider it sufficient if the matter was dealt with in the report of the Commission rather than in the text of the draft Convention itself.
13. Mr. GANTEN (observer for the Federal Republic of Germany) agreed with the remarks made by the observer for Finland. He failed to see why article 4(11) should be burdened with a proviso, since the current wording clearly conveyed the intent of the draft Convention. However, he was not strongly opposed to the inclusion of the proviso.
14. Mr. VIS (Chairman of the Committee of the Whole) asked the observer for IMF whether the proviso was not also addressed to courts which might be confronted with a situation in which they were obliged to enforce the exchange-control regulations of other countries.
15. Mr. EFFROS (observer, International Monetary Fund) said he believed that the situation to which the Committee Chairman was referring was addressed in article 72 of the draft Convention. However, under certain admittedly rare circumstances, the proviso might apply while article 72 did not. The proviso would be intended for the information of courts called upon to interpret the draft Convention and would ensure that, before a court issued its interpretation, it understood fully that the provisions of the Convention were not designed to supersede the rules of an international institution.
16. Mr. GUEST (United Kingdom), supported by Mr. CRAWFORD (observer for Canada), observed that, since most members of the Commission were dealing with a relatively unfamiliar area, it was difficult to express a concrete opinion in the matter. Under the circumstances, he preferred to rely on the opinion of IMF and was thus prepared to accept the proviso.
17. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said she was not opposed to including the IMF proviso in the text of article 4(11). At present it did no harm, and it might in the future present advantages not only for SDRs, but for transferable roubles as well.
18. Mrs. ADEBANJO (Nigeria) maintained that, while the proviso did not contradict article 4(11), it merely reiterated the latter portion of the existing text.
19. Mr. VIS (Chairman of the Committee of the Whole), responding to a question from Mr. GANTEN (observer for the Federal Republic of Germany), said that he interpreted article 71 (1 *bis*) to mean that, if an instrument was denominated in a unit of account, as a general rule it must be paid in the currency of the place of payment. Notwithstanding that general rule, if the unit of account was transferable between the party making payment and the party receiving payment, there was no obligation to make payment in a specific currency.
20. Mr. EFFROS (observer, International Monetary Fund) said that, if a unit of account was in fact transferable between two parties (in the case of IMF that would mean two Governments which were participants in the SDRs) and if the instrument did not specify the currency of payment, it would be possible for the instrument to be both denominated and payable in the unit of account. However, in the case of instruments between parties which could not in fact hold a particular unit of account, the only alternative would be payment in a particular currency (either the one indicated on the instrument or one determined according to art. 71). In the latter case, the instrument could be denominated only in a unit of account but would be payable in a national currency.
21. Mr. CRAWFORD (observer for Canada) said he was not sure that parties which could make payment by transfer of a unit of account were free to choose to make payment in a national currency. The phrase "However, this provision does not apply" in the second sentence of article 71 (1 *bis*) was ambiguous and must be clarified.
22. Mr. BERGSTEN (Secretary of the Commission), recalling that the secretariat had been asked what would be the consequences of the change in the definition of money or currency adopted by the Working Group on International Negotiable Instruments at its fourteenth session, drew attention to paragraph 4 of the note by the secretariat (A/CN.9/285).
23. Mr. VIS (Chairman of the Committee of the Whole) suggested that article 4(11) should be adopted, together with the proviso suggested by the observer for the International Monetary Fund. The various additional suggestions relating to article 4 and article 71 (1 *bis*), including the matters raised by the Secretary, should be referred to a drafting group.
24. *It was so decided.*
- Article 6(b) and (c)*
25. Mr. VIS (Chairman of the Committee of the Whole) recalled that, although a number of representatives from civil-law countries had objected to article 6(b) and (c), which provided the possibility for an instrument to be paid by instalments at successive dates, it had become clear that it would not be desirable to abolish the practice since it was well established in other countries.
26. Mrs. BUURE-HAGGLUND (observer for Finland) and Mr. VASSEUR (France) said that, although they represented civil-law countries, the banks in their countries were very much in favour of article 6(c) which, they believed, would help them in practice.
27. Mr. ANGELICI (Italy) said that, in cases where an instrument had to be paid by instalments, it would be possible to draw up several instruments each payable on the date on which the instalment was due. However, the purpose of a single instrument payable by instalments appeared to be to make it possible to add an acceleration clause. Such a clause made the position of a debtor more difficult, and he doubted whether article 6(c) would be acceptable to those delegations which represented debtor countries. He reserved his position on that issue.
28. Mr. VIS (Chairman of the Committee of the Whole), responding to a query from Mrs. ADEBANJO (Nigeria), said

that article 6(c) did not mean that the balance automatically became due if a debtor defaulted on any instalment. It merely indicated that under the Convention it was possible for a borrower to agree to an instrument containing an acceleration clause. Inclusion of such a clause was a matter for the creditor and debtor to decide.

29. Mr. SAMI (Iraq) said that he would have great difficulty in agreeing to article 6, which contained rules that could conflict with the nature of an instrument. Moreover, the article would make it very difficult to calculate the interest rate to be applied and would violate the principle of equality of the signatories, placing great responsibility on the debtor and obligating him to pay all future instalments.

30. Mr. VIS (Chairman of the Committee of the Whole) said that article 6(c) did not impose anything on anyone. It merely provided for the possibility of including an acceleration clause in an instrument. If the debtor did not wish to agree to such a clause, he did not have to sign the instrument.

31. Mr. CHAFIK (Egypt) said that, while current Egyptian law did not permit the drawing of instruments payable by instalments, the law was out of step with current commercial practice. In fact, people circumvented the law by drawing up several bills at one time, payable at successive dates. Accordingly, he favoured article 6 as it stood.

32. Mr. ILLESCAS ORTIZ (Spain) said that, although current Spanish legislation did not allow the type of stipulation envisaged in article 6(c), he had no difficulty in supporting it.

33. Mr. DELFINO-CAZET (Uruguay) said that he too favoured retaining article 6 as it stood.

34. Mrs. VILUS (Yugoslavia) said that article 6 was far superior to the corresponding articles of the 1930 and 1931 Geneva Conventions (of which her Government was a signatory); those Conventions did not correspond to modern commercial practice. She strongly supported article 6.

35. Mr. VIS (Chairman of the Committee of the Whole) said that it appeared that the Commission was prepared to adopt article 6(b) and (c). The dissenting comments made by the representatives of Iraq and Italy would be reflected in the Commission's report.

*The meeting was suspended at 11.30 a.m. and resumed at noon.*

#### *Floating interest rates*

36. Mr. VIS (Chairman of the Committee of the Whole) recalled that the topic of floating interest rates had first been raised in the Commission at its seventeenth session; the question had been referred to the Working Group, and a summary of its deliberations appeared in document A/CN.9/273, paragraphs 93 to 97. Instruments with floating rates had come into being over the past few years because of fluctuations in interest rates, but under current law they were not usually negotiable because they violated the requirement that the sum payable by the instrument be a definite sum. There was little doubt that, if the Commission included a provision on floating interest rates in the Convention, the Convention would gain considerably in importance.

37. Mr. ABASCAL (Mexico) said that it was undeniable that an instrument with a floating interest rate did not involve a definite sum. However, in order to contribute to a consensus, his delegation could support a provision on floating interest rates, on condition that, when a floating rate was agreed upon, reasonable units were established. Thus, in the light of the circumstances in each case, the parties to an instrument would negotiate a clause determining maximum and minimum rates, in accordance with their needs.

38. If, as was suggested in paragraph 9 of document A/CN.9/285, either the holder or the person liable on an instrument should have the right to declare the instrument immediately due, the instrument was made conditional, in violation of a long-standing tradition in the law of negotiable instruments. That provision undermined the autonomy of the parties: if one party declared the instrument immediately due, the other party would have to renegotiate the instrument under very unfavourable circumstances. If such a provision was to be included in the Convention, it was even more vital for instruments with floating interest rates to be subject to reasonable maximum and minimum limits.

39. Mr. BRANDT (German Democratic Republic) said that his delegation felt that international financial transactions required the inclusion in the draft Convention of a provision allowing instruments with floating interest rates, even though it did not believe that such a provision was needed for the floating-rate notes which were being issued in large numbers in the international financial market, since they were of a special nature. It expected that floating interest rates would be used mainly in credit agreements in which the parties to the transaction needed a special form of security.

40. Mr. SAMI (Iraq) said that his delegation did not agree with the principle of floating interest rates. If an interest rate was not fixed, the debtor did not know his obligations and could not calculate the amount that he would have to pay. Moreover, the rate was likely to be in the interest of the creditor rather than the debtor. Floating rates were also harmful to the interests of developing countries, suffering from the current high interest rates and the costs of debt servicing, and were inconsistent with the principles of the new international economic order that the Commission must strive to promote by devising provisions to ensure equality between the parties entering into financial dealings. Thus, his delegation opposed the inclusion in the draft Convention of a provision concerned with floating interest rates. However, if a majority of members of the Commission supported the principle, he felt that a ceiling would have to be imposed on such rates.

41. The CHAIRMAN, speaking as the representative of India, said that his delegation felt that a provision permitting floating interest rates was likely to introduce an element of uncertainty into the Convention. Under many legal systems, the sum of money to be paid on a bill of exchange or promissory note had to be fixed. That requirement was incorporated in article 1(2) and (3) of the draft Convention and was essential for the validity of a negotiable instrument. A provision permitting floating interest rates could cause irreparable damage to the circulation of an instrument and could be to the detriment of the debtor. Moreover, there was no indication in the report of the Working Group that bills of exchange with floating interest rates were in vogue in many countries. Many financial institutions in India had responded unfavourably to the idea of including the provision.



42. Mrs. BUURE-HAGGLUND (observer for Finland) said that the report of the Working Group (A/CN.9/273) rightly pointed out, in respect of the uncertainty inherent in a variable rate of interest, that the real cause of uncertainty lay in the economic situation with its fluctuating rates of interest and of currency exchange. Bills and notes with floating interest rates had developed in practice because they provided economic certainty. Her delegation supported the view that the Convention must be made attractive to banking circles, so that they would use the types of bills of exchange and promissory notes covered by it. The Convention would not impose the use of floating rates on any debtor, but merely allow the possibility of drawing instruments with floating rates. Thus her delegation was strongly in favour of the provision permitting floating interest rates. Banking circles in Finland believed that such a provision would make it easier to circulate bills of exchange and promissory notes. It would be preferable not to impose maximum and minimum limits on floating rates.
43. Mr. SPANOGLE (United States of America) said that many notes with floating interest rates were in use in international trade, even though there was no national law allowing such notes to be negotiable. Difficulties in accepting floating rates sometimes arose from the perception that the movement was only upwards, although over the past three years interest rates had been falling. If the Convention was to have a real impact on world trade and the use of negotiable instruments, floating interest rates must be included within its purview. If the conditions were made too onerous, the notes would not be negotiable under any national law or under the Convention.
44. His delegation did not support the idea of placing ceilings on floating interest rates. If such ceilings were imposed, notes would simply not be brought within the purview of the Convention. In national law, there were no ceilings on business loans, although there were sometimes ceilings for consumer loans, and the Convention would be concerned primarily with business transactions. It was also necessary to bear in mind the likely future evolution of the world financial market. He felt that the definition of interest rates in document A/CN.9/285 was too narrow. In a substantial number of floating-rate notes, the rate varied according to a commodity index, such as the price of oil, and such notes were designed largely to benefit the debtors. A provision on floating rates should be included, and there should be no ceiling.
45. Mrs. PIAGGI de VANOSI (Argentina), noting that certainty and security were basic to the negotiability of instruments, said that article 7(4) of the draft Convention precluded the issue of instruments with floating interest rates, and that such rates would violate the whole concept of the definite sum as an essential element of an instrument from the time of issue. Inclusion of the floating-interest-rate clause in the draft Convention might encourage the use of instruments with floating rates. In most developing debtor countries like her own, the general expectation was that interest rates would continue to rise, and consequently such instruments were not viewed with favour. Argentina believed that they should not be sanctioned under the draft Convention.
46. Mr. BRANDT (German Democratic Republic) said that, although he was not enthusiastic about the provision, he could see no legal objection to the inclusion of a text as drafted in document A/CN.9/285, paragraph 8. Although instruments with floating interest rates were more complicated, and consequently less negotiable and appealing, there nevertheless seemed to be a commercial need for them and the draft Convention would be more acceptable if it covered them.
47. Mr. OSAKA (Nigeria) concurred with the statements of the representatives of Iraq and India. He suggested that Libor rates could be used as a peg for the interest rate, rather than a less stable floating rate.
48. Mr. CRAWFORD (observer for Canada) remarked that, in article 6(d), the draft Convention already contemplated referring the parties to sources of information about exchange rates. The floating-interest-rate clause should be seen in that light, as an extension of a principle already accepted.
49. There was no such thing as an open Libor rate, since the rates were determined only for fixed periods, usually ranging from 30 to 90 days. Not much circulation of an instrument could be expected within such fixed periods; not many holders would want to wait so long for their interest, nor would they want the inconvenience of having to go back to the issuer for interest at regular periods.
50. The floating-interest-rate provision was significant mainly for the immediate parties to an instrument, although it might exceptionally be conducive to the transfer of those instruments to others. In money markets, in fact, it might lead to the development of instruments specially designed for transfer, accompanied by other, severable instruments for the payment of the interest portion, similar to coupons attached to bonds.
51. As the United States representative had pointed out, inclusion of the provision would simply facilitate and regulate an existing practice. Regarding the setting of a ceiling, he had understood the representative of Mexico to mean that the parties should be allowed to set a maximum rate if they wished, not that the draft Convention should stipulate a maximum rate. Stipulation of a maximum rate in the Convention would be contrary to all the reasons for including the provision in the first place, and would not be a good way to achieve certainty.
52. Mr. VASSEUR (France) said that, in view of the growing practice of using instruments with floating interest rates, a provision on that subject would make the draft Convention particularly attractive, certainly to French banks. He was therefore strongly in favour of the provision, which would not necessarily be to the advantage of creditors. The current decline in interest rates was, in fact, to the debtors' advantage.
53. The floating-interest-rate clause was tied to the provisions of article 6 regarding instalments at successive dates, since new rates of interest would be calculated each time a successive instalment came due. As far as terminology was concerned, he himself preferred the term "variable" to "floating".
54. If a ceiling was set on rates, a floor would also have to be set; but he was opposed to both. The Commission's task would be to determine the conditions under which rates could be set.
55. Mr. PISEK (Czechoslovakia) said that he was not opposed to the inclusion of a floating-interest-rate clause in the draft Convention but doubted it would have much influence on actual market conditions. In Czechoslovakia's experience, floating interest rates were not used in the sale or purchase of goods but rather in the financial market, in transactions between banks. Even there, he doubted that bills or notes with floating rates would circulate much, because it was not usual for creditor

banks to negotiate the claims they had on debtor banks. Such instruments would be used more as legal means of security regarding debtor banks.

56. Mr. GUEST (United Kingdom) said that United Kingdom banks regarded the floating-interest-rate provision as one of the most progressive and imaginative proposals, and he believed that the incorporation of the clause in the draft Convention was very important for its success. Others had pointed out that the existence of variable rates was inescapable and that the existence of at least promissory notes with variable rates was also a fact. The negotiability of such instruments was the main issue. The Czechoslovak representative had made a valid distinction between sales credit and finance credit, and certainly such instruments would have their major impact in financial transactions.

57. He believed that it was impossible for the draft Convention to legislate either a ceiling or a floor on variable interest rates for any given moment. It would be feasible, however, to draft a provision leaving it open to the parties to set such limits. He therefore proposed the addition of the following separate clause:

“Where the rate at which interest is to be paid is expressed as a variable rate, it may be stipulated that such rate shall not be less than or exceed a specified rate of interest.”

That would enable the parties, in the exercise of their autonomy, to stipulate either a floor or a ceiling, as they often did in promissory notes.

*The meeting rose at 1.05 p.m.*

**Summary record of the 342nd meeting  
Thursday, 26 June 1986, 3 p.m.**

[A/CN.9/SR.342]

*Chairman:* Mr. KARTHA (India)

*Chairman of the Committee of the Whole:*  
Mr. VIS (Netherlands)

*The meeting was called to order at 3.15 p.m.*

**International payments (continued)**

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes (continued)* (A/CN.9/273, A/CN.9/274 and A/CN.9/285)

*Articles 6 and 7*

1. Mr. ABASCAL (Mexico) said that his statement on floating interest rates at the previous meeting had been misunderstood. He had not raised an economic issue but rather a legal one. A law or a contract was useful if it created certainty, while uncertainty gave rise to conflicts in law and in contracts which ultimately had to be referred to a law court. A provision which contradicted logic and practice could only create problems, and he had therefore proposed a solution which allowed for the possibility of floating interest rates while also creating certainty. He had not proposed that there should be a ceiling and a floor on interest rate fluctuations, but simply that, if the parties to a contract used a floating rate, they must agree on a reasonable maximum and minimum limit on fluctuations.

2. Mr. MAEDA (Japan) supported the inclusion in the Convention of a provision allowing for floating interest rates, in order to meet a practical need. He also supported the United Kingdom proposal, since it would help to ensure that the Convention was adopted by as many countries as possible.

3. Mr. GRIFFITH (Australia) said that the question of floating interest rates was vitally important to the future of the Convention. He endorsed fully the statements by the representatives of Canada, Finland, France, the United Kingdom and the United States, and also the United Kingdom proposal. He did

not believe that the Convention should include a requirement that a ceiling and a floor should be imposed on interest rate fluctuations; rather it should be left to the parties to a contract to decide on such limits. Including a provision on floating interest rates was in line with current banking practice and would also assist trading countries, particularly developing countries, by making the conclusion of long-term contracts more feasible. Such a provision would make it possible to reflect changing market conditions in such contracts, to the mutual advantage of both parties, while a fixed interest rate would not.

4. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) observed that the question of floating interest rates was very important for the Convention. Her delegation therefore supported the inclusion of a provision on floating rates in article 6. The United Kingdom proposal could also help to dispel the misgivings of certain delegations.

5. Mr. CHAFIK (Egypt) said that, in Egypt, the practice of including a floating interest rate clause was well established in banking operations, especially for short-term credits and deposits. It did not apply to commercial bills, however, since the law required that the exact amount of such bills be specified. The usual practice was to add the interest to the principal in such cases. If a floating interest rate clause was allowed in the Convention, it would be introduced into the practice with regard to commercial bills in his country. His delegation would therefore support the inclusion of such a clause. Unlike the representative of Iraq, he did not believe that such a clause might lend itself to abuse since interest rates fluctuated according to the market and could benefit either debtor or creditor. There must be a ceiling on such fluctuations, however, and his delegation could therefore support either the Mexican or the United Kingdom proposal in that regard.

6. Mr. ILLESCAS ORTIZ (Spain) supported the proposal to include a floating interest rate clause, but observed that such a clause should be accompanied by a provision for a ceiling and a floor on fluctuations. He therefore supported the Mexican and United Kingdom proposals.

7. Mr. KOCH (Sweden) said that banking circles in his country favoured the use of floating interest rates. A provision to that

effect was therefore vital to the Convention's viability. It would be unwise not to include such a provision, but it would be equally unwise to introduce mandatory limits on fluctuations. The provision adopted should provide the possibility for the parties to a contract to agree on such limits. He therefore supported the United Kingdom proposal.

8. Mr. GLATZ (Hungary) agreed that the Convention should include the possibility of floating interest rates.

9. Mr. TITTI (observer for Cameroon) noted that the question of floating interest rates was extremely important because, like exchange rate fluctuations, interest rate fluctuations affected the burden of the debt service and could prevent debtors from fulfilling the terms of a contract through no fault of their own. A provision allowing floating interest rates could distort agreements between States and, given the possibility of non-compliance, might create reluctance to ratify the Convention, particularly among developing countries. His delegation would therefore be in favour of imposing a ceiling and a floor on such fluctuations in order to ensure that developing countries did not experience undue problems in meeting their obligations as a result of rising interest rates.

10. Mr. DUCHEK (Austria) supported the inclusion of a floating interest rate provision in the Convention since that was in line with existing international trade practice. He wished to point out, however, that floating rates were not necessarily to the detriment of debtors alone, but could also hurt creditors. He therefore supported the United Kingdom proposal for a ceiling and a floor on fluctuations, to be agreed to by the parties to individual contracts.

11. Mr. McCARTHY (Cuba) said that Cuba would prefer not to have a clause on floating interest rates at all. However, since the intention was to make the Convention more acceptable to a greater number of countries, his delegation could support Mexican and the United Kingdom proposals.

12. Mr. SAMI (Iraq) asked what was the precise difference between Mexican and the United Kingdom proposals.

13. Mr. ABASCAL (Mexico) explained that, under his proposal, the Convention would simply include a floating interest rate clause and not seek to establish a maximum and minimum limit on fluctuations. However, when the parties to a contract agreed on floating rates, they would have to impose reasonable limits on fluctuations in the rate. Such limits would not necessarily be maximum or minimum rates and would be left to the discretion of the contract parties.

14. Mr. VIS (Chairman of the Committee of the Whole) observed that the overwhelming majority of members of the Commission were in favour of a provision allowing for floating interest rates in the Convention. At the same time, a number of concerns had been expressed: first, the question had been raised whether a sum payable with a variable interest rate was a definite sum. As the observer for Canada had pointed out, however, the Convention already provided that once the rate of interest was fixed it was determined on the date of payment. Some delegations had called for a ceiling on fluctuations for fear that individual debtors or developing countries as a whole might have to face intolerable interest rates. The majority of members seemed to support a provision along the lines proposed by Mexico and the United Kingdom, and he suggested that the

Mexican and United Kingdom delegations pool their efforts to arrive at an acceptable wording. The representative of Iraq had expressed the fear that fluctuations in the interest rate might be subject to the will of the creditor. The Working Group's deliberations on that problem at the seventeenth session were reflected in paragraph 96 of document A/CN.9/273.

15. If he heard no objection therefore, he would take it that the Commission decided to include a floating interest rate provision in the Convention and to proceed to discuss the mechanics of such a provision, with a view to determining what outside source should be referred to in order to establish the interest rate applicable in each contract.

16. *It was so decided.*

17. Mr. SPANOGLE (United States of America) said that his delegation would like to retain the formulation given in paragraph 5 of document A/CN.9/285, on which it commended the secretariat, reformulated as follows:

"The rate at which interest is paid may be expressed either as a definite rate or as a variable rate. For a variable rate to qualify for this purpose, it must vary in accordance with provisions stipulated in the instrument and those provisions must refer to one or more indices, or sources, that are both publicly available, in the place of payment specified on the instrument during the term of the instrument, and not subject to unilateral variation by the payee."

That formulation could then be followed by the provision to be worked out jointly by Mexico and the United Kingdom. The reference to indices rather than interest rates was motivated by the fact that there were already floating rate instruments which used commodity indices as a reference; that trend was likely to grow. Such a practice was also likely to find favour among debtor countries. The new formulation also specified clearly that information on interest rates should be publicly available at the time and place of payment. Finally, the substitution of the term "unilateral variation" for "control" was motivated by the ambiguity of the term "control". That term could imply the ability to influence market rates, but "variation" was a more precise term.

18. Mr. VIS (Chairman of the Committee of the Whole) invited the Commission to consider the question of the use of indices to express interest rates. Debtor countries might wish to use their own commodity prices as indices. He doubted whether American bankers would consider that such indices were publicly available.

19. Mr. VASSEUR (France) said that he was in favour of the provision permitting floating interest rates. He supported the United States proposal that the Convention should make provision for reference to one or more indices; such indices or sources should not be subject to unilateral variation by the payee. He would be grateful, however, for further clarification of the meaning of the expression "publicly available".

20. Mr. CRAWFORD (observer for Canada) said that, while the United States proposal sought to improve the text of the draft Convention, he had difficulty with its omission of a reference to interest rates. Careful drafting would be required if such rates were tied to commodity prices. Moreover, he had doubts as to whether the rate of interest should be publicly available on a continuous basis during the term of the instru-

ment. Finally, the Convention would not be protecting the parties to instruments against all risks if it guarded only against interventions by payees. It was possible that payees might act through, or in collaboration with, other parties.

21. Mr. GUEST (United Kingdom) said that he had some difficulty with the United States proposal that interest rates could be expressed by reference to indices. The Commission had already taken a step forward in permitting variable interest rates, and should not proceed beyond that point. The application of interest rates based on commodity prices would require the use of complicated formulas. On the whole, he would prefer to be more conservative and retain the existing text.

22. Mr. VASSEUR (France), supporting the United States proposal, said that French banking circles were of the view that no limits should be placed on the choice of indices.

23. Mr. GANTEN (observer for the Federal Republic of Germany) said that he was not in favour of a reference to indices and other sources, and would prefer a reference to interest rates alone. It was perhaps a question of terminology since the term "interest rates" could cover indices and other sources.

24. Mr. SAMI (Iraq) said that he was in favour of retaining the text of the proposed paragraph (5) contained in paragraph 5 of document A/CN.9/285.

25. Mr. TITTI (observer for Cameroon) said that a reference to price indices in the developed countries would not take into account the interests of developing countries. If the text proposed by the secretariat were used, the developing countries might find it possible to ratify the Convention.

26. Mr. VIS (Chairman of the Committee of the Whole) said that the indices might also be the prices of commodities produced by the debtor countries.

27. Mr. QADER (observer for Bangladesh) said that he supported the text drafted by the secretariat. The square brackets in that text, however, should be removed.

28. Mr. VENKATRAMIAH (India) said that he was in favour of the text proposed by the secretariat.

29. Mr. VIS (Chairman of the Committee of the Whole) asked whether, in the light of the discussion, the representatives of France and the United States of America would be willing to withdraw their proposed amendment.

30. Mr. SPANOGLE (United States of America) and Mr. VASSEUR (France) agreed to withdraw the proposed amendment.

31. *The new paragraph (5) of article 7, as contained in paragraph 5 of document A/CN.9/285, was adopted.*

32. Mr. VIS (Chairman of the Committee of the Whole) invited the Commission to consider the requirement that the rates of interest should be publicly available. What did "publicly available" mean, and where and when must the rates be publicly available?

33. Mr. BERGSTEN (Secretary of the Commission) said that the secretariat had followed the instructions of the Working

Group in drafting the text under consideration. Square brackets had been placed around the words "that are both publicly available and not subject to the control of the payee" because the Study Group had had difficulties with the idea expressed therein. There had been no clear definition of the meaning of "publicly available". In the context of the London inter-bank offered rate (Libor), for example, there was no fixed rate. A further difficulty was whether a reference rate obtained by telephoning a bank should be considered a publicly available rate. Those difficulties needed to be addressed by the Commission itself.

34. Mr. CHAFIK (Egypt) sought clarification of the meaning of the word "control". In what sense could a payee have control?

35. Mr. BERGSTEN (Secretary of the Commission) said that the Working Group had requested the inclusion of that provision in the draft text.

36. Mr. CRAWFORD (observer for Canada) said that the Commission was faced with a choice of strategies. It could either add words to define more rigorously the freedom of the parties, or, on the basis of article 6 (d) of the draft Convention, it could express interest rates in terms of exchange rates, which were already publicly available.

37. Mr. VASSEUR (France) said that exchange rates could not be compared with interest rates since exchange rates were officially published while interest rates were not.

38. Mr. CRAWFORD (observer for Canada) said that there were always more rates of exchange than the particular rate of exchange announced on a given day. While he did not think that the two sets of rates were identical, they might usefully be treated as similar under the draft Convention.

39. Mr. QADER (observer for Bangladesh) sought clarification of the meaning of the words "publicly available" and "control".

40. Mr. VIS (Chairman of the Committee of the Whole) said that the Working Group had been mandated by the Commission to prepare a draft which reflected the concerns of the developing countries. If interest rates were publicly available, they would be removed from the control of the creditors.

41. Mr. QADER (observer for Bangladesh) said that he was in favour of the use of the expression "publicly available" in the current text.

42. Mr. SPANOGLE (United States of America) said that there had been a similar difficulty in the United States with respect to consumer loans. His Government had imposed a requirement that interest rates for mortgages and floating loan rates should be publicly available. Bankers with whom he had had discussions had had no difficulty in understanding the concept of publicly available rates. In his view, it was a straightforward way of protecting debtors.

43. Mr. VASSEUR (France) said that, while banks in the United States might not have had difficulties with the expression "publicly available", he could not say the same for French banks. French banking circles were not familiar with Libor, for example. There were various other offered rates in use among small groups of banks in Paris. Often such rates were not

publicly announced. He did not think that the Commission would be solving the problem if it merely provided for the rates of interest to be "publicly announced".

44. Mr. VIS (Chairman of the Committee of the Whole) pointed out that the English text (A/CN.9/285, para. 5), used the expression "publicly available", which was different from "publicly announced". The misapprehension might have arisen from an error in translation.

45. Mr. ILLESCAS ORTIZ (Spain) said that, in the Spanish version of paragraph (5), "*conocimiento público*" signified the general publication of the reference rate. It seemed that there was some contradiction between the freedom given to the parties to establish interest rates and the limitations placed on that freedom by having those rates "publicly available and not subject to the control of the payee". In a case where the parties concerned set a variable interest rate which was not known to the public and the maturity date arrived, how would it be possible to establish the amount to be claimed? His delegation preferred to delete the words in square brackets.

46. Mr. CRAWFORD (observer for Canada) said that the matter should be left with the parties concerned. There were not very many provisions in the draft Convention which provided protection for the parties against the freedom of contract. For example, there was nothing in the draft which said that the instrument would not bind the debtor who undertook more debt than he could cope with. With regard to the public availability of the reference rate or the freedom from influence, the Commission was faced with the problem of how to intervene to protect a party from making an improvident bargain. He suggested that the first sentence of paragraph (5) should be retained and that the second sentence should be modelled on article 6(d) of the draft Convention and should read: "For a variable rate of interest to qualify for this purpose, the method of variation must be indicated in the instrument or determinable as directed by the instrument". That wording would provide for readily ascertainable certainty.

*The meeting was suspended at 4.40 p.m. and resumed at 5.10 p.m.*

47. Mr. ABASCAL (Mexico) said that his delegation was in favour of deleting the square brackets and retaining the text as proposed by the secretariat.

48. Mr. VASSEUR (France) said that, since the Commission would never be able to clarify the meaning of "publicly available", he was in favour of deleting both the square brackets and the words contained within them. The parties concerned should by themselves determine the method of calculating interest rates.

49. Mr. VIS (Chairman of the Committee of the Whole) said that he could not agree with the representative of France. Paragraph 93 of document A/CN.9/273 stated that the Working Group had considered the proposal regarding instruments with floating interest rates but had added the following qualification: "It shall be required that any adjustments to the original stated rate relate directly to the movement of an index which is both publicly disclosed and not subject to the control of interested persons, in particular, the payee." Unless the Commission decided to reject the agreement reached by the Working Group, he felt bound by the directives of the Commission to continue to

seek a solution with regard to the text contained in square brackets in paragraph (5).

50. Mr. TITTI (observer for Cameroon) said that the reference to one or more other rates of interest which were both publicly available and not subject to the control of the payee presented a number of problems. For example, if one of the payees was involved in the setting of variable rates, it was clear that the rate might be affected. He wondered whether it was advisable to accept the idea of variable interest rates together with the idea of one or more other rates, in particular rates which might be controlled by the payee.

51. Mr. SAMI (Iraq) said that the words contained in square brackets in paragraph (5) had been the result of a long debate in which the developing countries had expressed their concerns regarding the principle of floating or variable interest rates. The text had been drawn up in order to provide some controls or guarantees which could reassure the debtor in the commercial transaction. His delegation was therefore in favour of retaining the text and deleting the square brackets.

52. Mr. SPANOGLE (United States of America) said that he was in favour of deleting the square brackets and retaining the text, or at least the concepts of the text, contained therein.

53. Mr. VIS (Chairman of the Committee of the Whole) said that the concerns expressed by delegations with regard to the text contained in square brackets in paragraph (5) could be referred to a small drafting group.

54. Mr. GRIFFITH (Australia) said that his delegation supported the French proposal to delete both the square brackets and the text which they contained. However, it would accept the decision of the Working Group if there was general agreement to do so.

55. Mr. VIS (Chairman of the Committee of the Whole) said that he wished to maintain the consensus with regard to the general principle that the Convention should include a provision on variable interest rates. A number of developing countries had agreed to the consensus on the understanding that the safeguards contained within square brackets in paragraph (5) would be included in the Convention.

56. Mr. VASSEUR (France) said that he would not object to retaining the text contained in square brackets, provided that certain modifications were made.

57. Mr. VIS (Chairman of the Committee of the Whole) said that the words "publicly available" would be referred to a drafting group. There remained the question of control. In the secretariat's draft of paragraph (5), "control" referred to the payee only. However, the maker, guarantors or endorsers of an instrument might also be involved.

58. Mr. CHAFIK (Egypt) said that the Commission should clarify the meaning and scope of "control".

59. Mr. VIS (Chairman of the Committee of the Whole) said that if a person took out a 10-year loan for \$1 million from a Manhattan bank at a variable rate of interest which was the commercial lending rate of that bank, the loan would be under the control of the payee. In other words, the lending institution could influence the rate of interest, and that was something the Commission wished to avoid.

60. Mr. CHAFIK (Egypt) asked whether what was meant was pressure rather than control.

61. Mr. VIS (Chairman of the Committee of the Whole) said that it was control, because the institution itself set the rate.

62. Mr. SPANOGLE (United States of America) said that his suggestion had been to use "unilateral variation" instead of "control" because there was some ambiguity about the concept of control. There was, however, a justifiable fear on the part of the debtor of abuse if the payee could unilaterally set the rate, although there might not be such a great risk as long as the rule applied to the entire group of lenders of a certain type. He pointed out that there was a difference between the prime rate set by a lender and the use of Libor because, in the latter case, the rate was the product of negotiations among several banks. The underlying rationale had been to approve the use of indices based upon LIBOR, United States treasury bills, or the discount rate, but to disapprove the use of the prime rate of the lender. All that could be done at present was to establish a principle rather than write an entire volume of regulations. Therefore, something similar to the language in square brackets should be used.

63. Mr. NADER (Mexico) said he understood that the words between square brackets were an attempt to avoid having one interested party define the scope of the obligations of one or more parties to the instrument. He therefore suggested that the words between brackets should read: "that are both publicly available and are not subject to the unilateral determination of any of the parties to the instrument or of its payee."

64. Mr. CRAWFORD (observer for Canada) proposed that, after the words "it must vary in accordance with provisions stipulated in the instrument", the following words should be added: "provided that, if such provisions refer to one or more reference rates of interest, each such reference rate must be published or otherwise made freely available to the public from a disinterested person not party to the instrument, and either (1) not subject to the direct or indirect influence or control of any party to the instrument acting alone or together with any other person, or (2) established in a public market in bank deposits in which no party to the instrument exerts exceptional influence". The second provision was necessary because the conduct of every participant in a market influenced the rates established in that market. However, if the conduct of a party did not exceed simple participation, it should be ignored. If no public market in bank deposits was being referred to, the requirements of the definition in the Convention would not be met by a rate that was subject to the direct or indirect influence or control of any party to the instrument acting alone or together with another person.

65. Mr. GUEST (United Kingdom) said that he had changed his mind and would support the United States proposal of the term "unilateral variation", which was simpler than such terms as "direct and indirect control".

66. Mr. VIS (Chairman of the Committee of the Whole) said that there seemed to be agreement on retaining certain basic concepts. He suggested that the United States and Canadian proposals and any other observations should be referred to a drafting group to be made up of the representatives of Bangladesh, Canada, Egypt, the German Democratic Republic, Mexico, the United Kingdom and the United States of America.

67. *It was so decided.*

68. Mr. VIS (Chairman of the Committee of the Whole) invited the Commission to turn its attention to the paragraphs of the report of the secretariat (A/CN.9/285) relating to floating interest rates.

69. Mr. BERGSTEN (Secretary of the Commission) said that, in discussing the drafting of article 7(5), the secretariat had foreseen two potential difficulties. If any requirements were stipulated for the major variable interest rate provisions, there was a possibility that the provisions adopted by parties would not meet those requirements. As a result, article 7(4) would apply, and there would be no interest. Second, even if the parties had drafted provisions which met the requirements of paragraph (5), they might be unable to apply them because they had referred to a reference rate which did not exist, or which had existed at the time of issue of the instrument but no longer did. The secretariat had therefore proposed, in paragraph 8 of document A/CN.9/285, a draft article (6), which provided that, if a variable rate did not qualify or if it was not possible to determine the numerical value of the variable rate for any period, interest would be payable for the relevant period at the rate specified in article 66(2).

70. Mr. MAEDA (Japan) said that article 66(2) should be replaced by article 66(3). According to article 66(1)(b)(ii), interest was to be paid at the rate specified in paragraph (2), calculated from the date of presentment on the sum specified in paragraph (1)(b)(i). It was clear that the interest rate referred to in article 66(2) was that which should be paid if the party or drawee refused to pay interest when the holder presented the bill for payment. On the contrary, the proposed article 7(6) concerned the rate of interest which should be paid before the instrument was presented for payment. It was therefore not appropriate to refer to article 66(2) for the purpose of reducing the consequences arising out of the invalidity of the floating rate provision.

71. Mr. VIS (Chairman of the Committee of the Whole) said the only problem was that paragraph (3) of article 66 referred to a rate which applied before maturity, whereas the time under discussion was the period of maturity proper. While he understood the Japanese representative's objection to paragraph (2), he believed that the same objection should apply to paragraph (3). Perhaps another reference would have to be made in article 7(6), if others agreed with that view.

72. Mr. BERGSTEN (Secretary of the Commission) said that it had been clear to the secretariat that the rate referred to in article 66(2) was not an appropriate one. The problem was that the parties might have contracted for a variable rate and that there would be no way of reconstructing that rate. Therefore, it had been concluded that rather than saying that no interest at all was payable, as would be the case under article 7(4), the concern should be to provide a reference point for such a rate. Paragraphs (2) and (3) of article 66 were the only current provisions of the draft Convention which might be used. The secretariat had suggested paragraph (2), knowing that the rate that would result would be fixed rather than variable and would not be the rate which normally would have resulted.

73. As a result, in paragraph 9 of document A/CN.9/285, a solution had been suggested without a specific text. Where proposed article 7(6) was to be applied, either the holder or the person liable on the instrument should have the right to declare

the instrument immediately due and payable by notice to the other party. In other words, since the applicable interest rate would differ from what the parties presumably would have anticipated, either party could accelerate the payment.

74. Mr. VIS (Chairman of the Committee of the Whole) said that the problem would have to be referred to a drafting group. He sensed that there was agreement on the policy underlying the secretariat's proposal.

75. Mr. BERGSTEN (Secretary of the Commission) said that, in the discussion of article 66(2), the secretariat had also noted a relatively minor problem, which had been described in paragraph 12 of document A/CN.9/285. In order to solve the problem that arose where there existed two or more official rates, the secretariat had suggested a minor redrafting of article 66(2).

*The meeting rose at 6 p.m.*

**Summary record of the 343rd meeting  
Friday, 27 June 1986, 10 a.m.**

[A/CN.9/SR.343]

*Chairman:* Mr. KARTHA (India)

*Chairman of the Committee of the Whole:*  
Mr. VIS (Netherlands)

*The meeting was called to order at 10.15 a.m.*

**International payments (continued)**

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes* (continued) (A/CN.9/273, A/CN.9/274 and A/CN.9/285)

*Article 11*

1. Mr. VIS (Chairman of the Committee of the Whole) said that he would take it, if he heard no objection, that the Commission wished to adopt the text of article 11 as revised in document A/CN.9/274.

2. It was so decided.

*Articles 16 and 20(3)*

3. Mr. VIS (Chairman of the Committee of the Whole) observed that the Working Group had thought it advisable to revise the draft Convention so as to separate two situations: one in which the issuer of an instrument made it non-transferable (covered in the existing text of article 16) and one in which the endorser wrote a restrictive endorsement (covered in the new paragraph 20(3)).

4. Mr. ANGELICI (Italy) said that there should be an indication in the text that the negotiability of an instrument depended solely on the intention of the drawer or maker and that therefore a restrictive clause inserted by another person, such as the endorser, could determine the position and liability only of that person. He therefore proposed the addition of a provision in article 20(3) to the effect that a restrictive endorsement limited the liability only of the endorser for the subsequent circulation of the instrument. That would reflect the view reported by the Working Group in document A/CN.9/273, paragraph 105, that the instrument should remain transferable but the endorser would not be liable to any subsequent transferee except his immediate endorsee.

5. Mr. VIS (Chairman of the Committee of the Whole) observed that, if the endorser was not liable to parties subse-

quent to his endorsee, the status of such subsequent endorsees was ambiguous. The Working Group had rejected the approach being suggested by the representative of Italy, which had been essentially the Geneva solution.

6. Mr. BRANDT (German Democratic Republic) said that he supported the prevailing view in the Working Group that article 16 should be taken literally and should exclude further transfer, and therefore felt that article 20 (3) should be maintained as it stood.

7. Mr. SAMI (Iraq) said that he thought article 20(3) was redundant when considered in conjunction with article 16. Article 16 was very clear: it specified an exception to the general rule that commercial paper should be negotiable. Any such exception should be dealt with entirely within article 16, regardless of which party imposed the restriction. Article 16 could be amended to include the words "or the endorser" after the words "When the drawer or the maker"; article 20(3) could then be deleted.

8. Mr. VIS (Chairman of the Committee of the Whole) said that the proposal of the representative of Iraq would revert to the original text, to which a number of representatives had objected because they had felt that it confused different situations.

9. Mr. MACCARONE (observer, European Banking Federation) said that the difference between the two situations described in articles 16 and 20(3) lay in the word "further" in the latter. When an instrument was drawn up from the outset with a restrictive clause, it was a non-negotiable instrument; when a restrictive clause was inserted by an endorser, the instrument had until that moment been a negotiable instrument in all respects.

10. Mr. DUCHEK (Austria) recalled that in the Working Group the main criticism of the previous text of article 16 had been directed at the formulation "the transferee does not become a holder except for purposes of collection", rather than at the idea of a single article covering the two situations.

11. He himself was inclined to support the suggestion of the representative of Iraq. Article 16 alone was misleading, since only later was there any reference to the possibility of the imposition of a restriction by an endorser. Obviously, in the second situation, a negotiable instrument became non-negotiable, but the text left no room for misunderstanding.

12. Mr. GUEST (United Kingdom) observed that, in its revision of the text, the Working Group had been following a

decision by the Commission, as reported in document A/39/17, paragraph 73. He would prefer to keep the text as redrafted by the Working Group.

13. Mr. DRUEY (observer for Switzerland) said that, as paragraph 73 of the Commission's 1984 report indicated, the Commission had expressed doubts about the formulation of article 16 rather than taken a decision to redraft it. He himself leaned towards the position of the representatives of Iraq and Austria. All restrictions on transfer should be dealt with the first time the subject was taken up, namely, in article 16.

14. Mr. SPANOGLE (United States of America) supported the comments made by the observer for the European Banking Federation and the United Kingdom representative. The original draft of article 16 had been confusing because it had not been clear whether the insertion of a restrictive clause by an endorser would affect the transferability of an instrument from the beginning of its journey through international trade or only after the instrument's transfer to the endorsee. He therefore supported the revised draft.

15. Mr. VASSEUR (France) said that he saw an advantage to keeping the two situations now covered by articles 16 and 20(3) separate, but also understood the concerns of the representatives of Austria and Iraq. Perhaps the solution would be to put the provision now comprising article 20(3) in article 16.

16. Mr. DRUEY (observer for Switzerland) supported the proposal of the representative of France.

17. Mr. CHAFIK (Egypt) said that he was concerned about another aspect of the situation covered in article 20(3). He wondered whether a rule or a rebuttable or irrebuttable presumption applied to the relationship between an endorser and his endorsee or between the endorser and any third party. If a presumption applied and if, despite the restrictive clause introduced by the endorser, his endorsee transferred the instrument further with a non-restrictive endorsement to a third party, was that further endorsement an endorsement for collection or for transfer?

18. Mr. MACCARONE (observer, European Banking Federation) said that the representative of Egypt had raised an important point: there was no indication in the text as to the effect of an endorsement that was contrary to the provisions of articles 16 and 20(3). A provision could be added to the effect that an endorsement in any form was always an endorsement for collection since the instrument, from the time the restrictive clause was inserted, had become non-negotiable; or to the effect that any endorsement other than the endorsement for collection was null and void and not capable of transferring the instrument in any way, even for collection.

19. Mr. VIS (Chairman of the Committee of the Whole) observed that, in the case where A, the payee of an instrument, endorsed it restrictively to B, and B then further transferred it to C, the representative of Egypt had asked what was the legal effect of the first transaction on the relation of A to B and of the second transaction on the relation of A to C. He himself thought that A was fully liable to B, or to his collecting agent, but not to C.

20. Mr. GUEST (United Kingdom) agreed with the Chairman of the Committee of the Whole that an endorsement which

included the words "not transferable" would constitute an effective transfer in so far as the endorsee was concerned, since the endorsee would acquire all rights on the instrument in question except the ability to transfer it further for any purpose other than collection. If the endorsee sought to transfer the bill further for a purpose other than collection, the new endorsee would acquire no rights on the bill.

21. As to the second question raised by the representative of Egypt, he did not believe that the subsequent endorsement of a non-transferable instrument by an endorsee who omitted the words "for collection" or "for deposit" from the endorsement would be valid.

22. Mrs. PIAGGI de VANOSI (Argentina) said that, as she interpreted article 20(3), an endorser would have an obligation to the original endorsee, but not to the subsequent endorsee.

23. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that the problem involved two considerations. The first concerned the situation of an endorser who included a restriction in an instrument. Under the terms of the draft Convention, the endorser was fully liable to any subsequent holder of the instrument. The second consideration was the status of an endorsee who became the holder of such an instrument: his rights would be restricted, since he could not subsequently transfer it except for collection. However, if the endorsee sought to transfer the instrument without stipulating that it could be endorsed only for purposes of collection, instead making it payable to a third party, the transaction was called into question. It had been her understanding that the provisions of the Convention could not fairly be applied to the third party. However, she also believed that, even if the restricted instrument was transferred further without the stipulation that it could be endorsed only for purposes of collection, that condition applied none the less.

24. Mr. VASSEUR (France) agreed with the representative of the Soviet Union. Articles 16 and 20(3) made it very clear that, once the mention "non-negotiable" or "not transferable" was included in an instrument, it continued to apply.

25. Mr. MACCARONE (observer, European Banking Federation) said that, given that such instruments were to be transferred internationally, any difference in interpretation regarding the effect of an endorsement might have serious repercussions for international trade. It might therefore be useful for the draft Convention to state specifically that, even though an endorser did not, contrary to articles 16 and 20(3), include the words "for collection" on the instrument, the instrument would nevertheless be deemed to be for collection only. It was important in the case of a non-negotiable instrument that an endorsee should not gain more rights than were obtainable from the face of the instrument.

26. Mr. DUCHEK (Austria) said he continued to prefer the previous text of the article, which had stated that a transferee was not a holder except for purposes of collection. He also supported the proposal of the representative of France to include the text of article 20(3) in article 16.

27. Mr. SAMI (Iraq) said that the interpretation of article 20(3) put forward by the representative of the Soviet Union was correct and also consistent with the text of article 16. He therefore had no objection to the proposal made by the representative of France.



28. Mr. VIS (Chairman of the Committee of the Whole) suggested that a working group composed of the representatives of Iraq, the Union of Soviet Socialist Republics and the United Kingdom, the observer for the European Banking Federation and himself should be established to seek agreement in that regard. The working group would also consider the drafting changes that the incorporation of article 20(3) into article 16 would require.

29. *It was so decided.*

*The meeting was suspended at 11.25 a.m. and resumed at 12.15 p.m.*

30. Mr. GUEST (United Kingdom) said that the working group proposed that article 16 should contain two paragraphs: one dealing with situations in which the drawer or maker inserted a stipulation prohibiting the transfer of the instrument, and one dealing with situations in which an endorser inserted in the endorsement a stipulation prohibiting further transfer of the instrument. Second, the group proposed that the consequences of the stipulations should be the same in both cases: from the moment at which the stipulation was inserted, the transferability of the instrument should be limited. In the first case, the restriction would take effect from the outset; in the second, it would take effect from the moment of endorsement.

31. Third, it was proposed that, when stipulations were inserted prohibiting the transfer or further transfer of the instrument, the transferee would not be able further to transfer the instrument except for purposes of collection.

32. Fourth, it was proposed that, when a person inserted a stipulation prohibiting transfer of the instrument and an endorsee subsequently endorsed the note but failed to include the words "for collection", such endorsement would be deemed to be an endorsement for collection purposes.

33. Mr. SPANOGLE (United States of America) supported the proposals wholeheartedly, particularly the fourth one.

34. Mr. VIS (Chairman of the Committee of the Whole) said he assumed that all members agreed to the proposals, and noted that the Commission would see the precise wording of the article prior to adopting it.

*Article 27(1) (continued)*

35. Mr. VIS (Chairman of the Committee of the Whole) said that an informal working group composed of the representatives of Japan, the Union of Soviet Socialist Republics, the United Kingdom and the United States of America and himself had concluded, after considering the text of the shelter rule contained in article 27(1), that no change was necessary in the text.

36. Mr. GUEST (United Kingdom), explaining the reasoning by which the working group had reached its decision, cited the example of a situation in which a buyer, A, made a note in favour of a seller, B, the underlying transaction being a contract of sale. There had been no dispute between the parties at the time the note had been issued; consequently, under the draft Convention, B was considered to be a protected holder. Later, however, a dispute as to the quality of the goods sold had developed, so that a claim existed on the underlying transaction, which A might raise against B. B then transferred the note,

which had already reached maturity, to a third party, C, who had no knowledge of the claim.

37. The question that had been raised was whether or not A was entitled to set up his defence against C. Under article 4(7)(b) of the draft Convention, C, having taken the note following maturity, was not a protected holder. However, some members of the Commission had still wondered whether C would take the instrument free of any defences because of the shelter rule in article 27(1). He then drew attention to the wording of article 27(1), which did not say that the transfer of an instrument by a protected holder conferred protected-holder status on the transferee; the transfer merely vested the rights to and upon the instrument in the subsequent holder. It would therefore be possible for A to raise defences against C, since C would acquire the rights to which B was entitled; moreover, B would have a defence opposed to him which would also affect C, since the latter was not a protected holder. Consequently, no change was necessary in article 27.

38. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) welcomed the explanation that had been provided by the representative of the United Kingdom, which had its basis in British law and related to a situation with which countries belonging to the Geneva system were unfamiliar. Article 27(1) was in fact worded in such general terms that it was difficult to understand without such explanation, and demonstrated why, in interpreting the provisions of the draft Convention, it was necessary to refer to examples of similar provisions from national legislation.

*Article 17*

39. Mrs. PIAGGI de VANOSI (Argentina) said that the text of article 17(2) was unsatisfactory and suggested that it should be replaced by the following wording: "In the event of a conditional endorsement, the condition is presumed not to be written." Her amendment was purely a question of drafting and did not affect the substance of the text.

40. Mr. VIS (Chairman of the Committee of the Whole) said that the proposed amendment did in fact alter the substance of the article. As it stood, article 17(2) meant that, if there was a conditional endorsement, the transferee was the holder of an instrument regardless of whether or not the condition stipulated in the endorsement was fulfilled. The question whether the condition was fulfilled was relevant to the liability of the endorser.

41. Mr. SPANOGLE (United States of America) proposed the following subamendment to the Argentine amendment: "In the event of a conditional endorsement, the condition is presumed not to be written as to the party subsequent to the transferee."

42. Mr. ANGELICI (Italy), Mr. ILLESCAS ORTIZ (Spain) and Mr. DELFINO CAZET (Uruguay) supported the United States proposal.

43. Mr. VIS (Chairman of the Committee of the Whole), speaking as the representative of the Netherlands, said that he could not agree to the proposal because it affected the liability of the endorser. When an endorser put a conditional endorsement on an instrument, he was restricting his liability and that restriction should be binding on subsequent parties, as it was if the endorsement contained the words "without recourse".

44. Mrs. PIAGGI de VANOSI (Argentina) said that it was one thing for an endorsee not to have recourse because a restrictive clause had been inserted to restrict liability. It was another thing to subordinate the entire operation to a condition.

45. Mr. VIS (Chairman of the Committee of the Whole) recalled that, according to a study group composed of bankers, a clause to the effect that a person was liable only when a ship arrived was used in certain parts of the world and amounted to a conditional endorsement. He believed it had been held that such an endorsement was allowed and that it was binding on subsequent transferees as was a "without recourse" endorsement. If some members of the Commission disagreed, the matter would have to be discussed. However, that was not the subject of article 17(2), which dealt with the conditions under which a transferee could become a holder.

46. Mrs. PIAGGI de VANOSI (Argentina) supported the text proposed by the representative of the United States. However, if the majority of the members of the Commission disagreed, she would accept their view.

47. Mr. SAMI (Iraq) said that, if the Commission were to adopt the text proposed by the United States representative, it would give subsequent holders of the instrument greater rights than those given to the endorsee. In the circumstances, the Commission might prefer to adopt the solution used in the Geneva Conventions and state that, in the event of a conditional endorsement, the condition was considered null and the endorsement valid.

48. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that article 17 set forth a clear principle: whatever conditions an endorser might include in his endorsement, an instrument was transferable whether or not those conditions were fulfilled. An instrument was transferred by means of endorsement, and the recipient then became a holder. A quite different problem arose as to the effect of a conditional endorsement on subsequent holders, and that aspect was not regulated by article 17, but by articles 25 and 26.

49. In the case of a protected holder, it was obviously of no importance to a subsequent holder whether a condition had been fulfilled or not, and the endorser could not raise any objection on the grounds that he had included a certain condition in his endorsement. If the holder was unprotected, once again article 25 applied, with all its consequences. Thus a condition affected the relations only between the direct parties to an instrument, and in that way, it was easier to resolve disputes between parties in court. The formulation of article 17 was entirely satisfactory and there was no need to amend it. Moreover, the original formulation in the Geneva Convention had been abandoned in favour of it.

50. Mr. GUEST (United Kingdom) supported the interpretation given by the representative of the Soviet Union. It was pointed out in the commentary on the draft Convention (A/CN.9/213) that article 17 expressed the fundamental policy of the Convention that an endorsement might not be made subject to a condition. A condition, to the extent that it affected the liability of the endorser, was to be disregarded. However, the fact that a condition was not fulfilled was not necessarily irrelevant, as it might form the basis of a claim or defence under article 25.

51. Mr. SPANOGLE (United States of America) said that there were some problems in reconciling the rather forceful language of article 17 and the more permissive language of article 40(2) of the draft Convention. The difference between a limitation of liability and a condition was somewhat blurred. Perhaps the Commission should simply ensure that article 17 was limited to the question of transfer, and should revise the article in the manner he had already suggested.

52. Mr. VIS (Chairman of the Committee of the Whole) said that the Commission should make it clear that a conditional endorsement did not prevent the transfer of an instrument; whether a condition was fulfilled or not, there was a holder. The question whether a condition had a bearing on the liability of the endorser was very relevant.

53. Mr. SPANOGLE (United States of America) said that in that case article 17(1) was misleading. It could not be said that an endorsement must be unconditional, but that it could be conditional for the purpose of liability. Article 17 as currently drafted posed problems in relation to article 40. It was not sufficient to argue that article 17 was in a chapter concerned with transfer.

54. Mr. VIS (Chairman of the Committee of the Whole) said that article 17(1) was concerned with transfer. It could not be said that, if a condition was not fulfilled, an instrument could not be transferred to another holder; and endorsement must be unconditional.

55. Mr. DRUEY (observer for Switzerland) said that the view expressed by the representatives of Argentina, the United States and other delegations went in the direction of the Geneva Convention, in the sense that a condition had no effect on the transfer of rights or on liability. That attitude reflected a concern for the clarity of an instrument. Imposing a condition was not the same as excluding liability in general. Thus he supported the proposal made by the representative of the United States.

56. Mr. ILLESCAS ORTIZ (Spain) said that his delegation had difficulty with article 17, since it referred only to the question of the transferability or circulation of an instrument but not to the liability of the endorser. Article 17(2) established clearly that in the case of a conditional endorsement, regardless of whether the condition was fulfilled, an instrument was transferable. However, a régime must be established to govern the liability of the endorser and the way in which that liability affected subsequent endorsers.

57. Mr. VIS (Chairman of the Committee of the Whole) said that the Commission must decide whether it wished to divide the functions of endorsement into two parts. There seemed to be full agreement that an endorsement could not be conditional in respect of making a transferee a holder; however, there were differing views about whether endorsement established liability for the endorser. The Commission could take the view that, in respect of liability, a conditional endorsement was unconditional.

58. Mr. DRUEY (observer for Switzerland) said that a distinction must be drawn between having knowledge as to whether or not a condition had been fulfilled and having knowledge of a condition itself. Articles 25 and 26 were unclear in that respect and must be clarified.

**Summary record of the 344th meeting  
Friday, 27 June 1986, 3 p.m.**

[A/CN.9/SR.344]

*Chairman:* Mr. KARTHA (India)

*Chairman of the Committee of the Whole:*  
Mr. VIS (Netherlands)

*The meeting was called to order at 3.15 p.m.*

**Election of officers (continued)**

1. The CHAIRMAN said that the Commission still had to elect a Rapporteur and three Vice-Chairmen.
2. Mr. GUEST (United Kingdom), speaking on behalf of the Group of Western European and other States, nominated Mr. Duchek (Austria) for the office of Rapporteur.
3. *Mr. Duchek (Austria) was elected Rapporteur by acclamation.*
4. Mr. KANDIE (Kenya), speaking on behalf of the African Group, nominated Mrs. Adebajo (Nigeria) for one of the offices of Vice-Chairmen.
5. *Mrs. Adebajo (Nigeria) was elected Vice-Chairman by acclamation.*
6. Mrs. PIAGGI de VANOSI (Argentina), speaking on behalf of the Latin American Group, nominated Mr. Delfino-Cazet (Uruguay) for one of the offices of Vice-Chairman.
7. *Mr. Delfino-Cazet (Uruguay) was elected Vice-Chairman by acclamation.*
8. Mr. SZASZ (Hungary), speaking on behalf of the Group of Eastern European States, nominated Mr. Wagner (German Democratic Republic) for one of the offices of Vice-Chairman.
9. *Mr. Wagner (German Democratic Republic) was elected Vice-Chairman by acclamation.*
10. *Mr. Vis (Chairman of the Committee of the Whole) took the Chair.*

**International payments (continued)**

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes (continued) (A/CN.9/273, A/CN.9/274 and A/CN.9/285)*

*Article 17*

11. Mr. VIS (Chairman of the Committee of the Whole) said that the earlier discussion of article 17 had been useful because it had made clear that different interpretations were possible. To the extent that an endorsement fulfilled the function of transferring the instrument, it must be unconditional. If the transfer was made conditional, the endorsement would not be considered effective under the Convention in so far as it concerned the transfer function.

12. The difficulty lay in the second function of the endorsement. If it established the reliability of the endorser, article 40(2), which gave an endorser the power to limit or exclude his liability, came into play. Basically, if the endorser stipulated that the endorsement was conditional, he wished to say something about the conditions under which he was liable to subsequent parties in case of dishonour. The question was whether non-fulfilment of the condition meant that the endorser was not liable or, on the other hand, since the endorsement must be unconditional, whether the same rule would apply to the liability function of the endorsement. It appeared that the condition could not simply be disregarded. If an endorser endorsed an instrument to an endorsee, and if a condition was attached to the transaction, the endorser might derive a defence from the fact that the condition was not fulfilled, irrespective of whether the condition had been expressed on the instrument. If the endorser did have a defence against his immediate transferee or endorsee, then reference must be made to article 25, because if a subsequent non-protected holder knew that the condition had not been met, a defence might be set up against that party. Only in that sense did the condition continue to exist with regard to a subsequent holder, according to the apparent understanding of the Working Group.

13. Another possibility was to make the endorsement unconditional not only with regard to transfer, but also with regard to the liability function, so that if there was a conditional endorsement, it would be deemed not to be written both in relation to the transfer and in relation to liability.

14. Mrs. PIAGGI de VANOSI (Argentina) said that she was in favour of the wording of article 17(2) as proposed by the United States, namely, that in the event of a conditional endorsement, the condition was presumed not to be written as to parties subsequent to the endorsee. The proposed wording was a considerable improvement over the current text.

15. Mr. ABASCAL (Mexico) said that his delegation was also inclined to support the wording proposed by the United States because what was needed was a law which would satisfy both common-law and civil-law systems, as well as new banking practices. In order to overcome any difficulties which might arise, the draft provisions should be in keeping with proven legislation. The provision that the endorsement must be unconditional, and that any condition was presumed not to be written as to parties subsequent to the endorsee, contained a rule whose purpose was to preserve the certainty of the rights granted by the document. A change should be made, but it should not go beyond what was strictly necessary to preserve maximum certainty. The basic rule should be that the condition should be presumed not to be written, unless it affected only the liability of the endorser to his immediate transferee. However, even if the condition was written, it should not prevent the transferee from acquiring the status of protected holder, unless it was proven that when he had received the instrument, he had known that the condition had not been met, or that he had intended to act to the detriment of the endorsee who had put the condition.

16. Mr. SPANOGLE (United States of America) said that, if his first proposal was adopted, care should be taken in its drafting to preserve the ability of the endorser to endorse without limitation. Also, it was his understanding that the

principal reason for considering the idea that a condition upon liability might be permitted was that it was used in some banks, particularly in Africa. He asked whether such usage still existed and how prevalent it was.

17. Mr. SAMI (Iraq) said that there must be a clear-cut definition of the liability of the parties. Whether the endorsement was conditional or not, it should not run contrary to what was stated on the instrument. Either the endorser had or did not have liability, and that had nothing to do with article 42 of the draft Convention, which could be interpreted as meaning that the endorser could stipulate the condition of non-acceptance, for example. Under the United States proposal, there would be two kinds of liability: the endorser would be liable both to the endorsee and to the other parties. Such a régime of dual liability should not exist in the instrument. He would therefore prefer to say that the conditional endorsement was valid, and that the conditions might not all be written.

18. Mr. KANDIE (Kenya) said his delegation felt that conditional endorsement should not be permitted. If it were, Kenya would find it difficult to ratify the Convention.

19. Mr. ILLESCAS ORTIZ (Spain) said he felt that the source of conflict lay in the wording of article 17(1). He therefore supported the position of the representative of Argentina.

20. Mr. VIS (Chairman of the Committee of the Whole) said it appeared that article 17 would have to be redrafted in accordance with the United States proposal. He noted that one representative had disagreed with that solution on the ground that, if the condition had been part of the underlying transaction and was not expressed in the endorsement itself, it would have affected a subsequent holder. He read out the United States proposal: "In the event of a conditional endorsement, the condition is presumed not to be written as to parties subsequent to the endorsee".

21. Mr. VASSEUR (France) asked whether it would be possible to return to a matter which had been taken up briefly at the Vienna session, namely, whether the Convention could accept endorsement in pledge. The French banks would like to have that type of endorsement accepted.

22. Mr. VIS (Chairman of the Committee of the Whole) asked what the purpose of such an endorsement was, and in what commercial situations it was used. Such an endorsement should perhaps be included if it was thought that it would be useful in international transactions.

23. Mr. MUÑOZ (observer, Latin American Banking Federation) said that some Latin American countries had specific provisions in their codes of commerce that permitted such endorsements. They were a type of security to a creditor, enabling the holder of the endorsed instrument to collect and exercise all the rights of a holder for the payment of a guaranteed credit. He felt that it was a good idea to consider it.

24. Mr. VIS (Chairman of the Committee of the Whole) read out the relevant provision of the Geneva Convention Providing a Uniform Law for Bills of Exchange and Promissory Notes (art. 19): "When an endorsement contains the statements 'value in security' (*valeur en garantie*), 'value in pledge' (*valeur en gage*) or any other statement implying a pledge, the holder may exercise all the rights arising out of the bill of exchange, but an

endorsement by him has the effects only of an endorsement by an agent. The parties liable cannot set up against the holder defences founded on their personal relations with the endorser unless the holder, in receiving the bill, has knowingly acted to the detriment of the debtor."

25. Mr. VASSEUR (France) said that, for example, a holder of a bill might obtain funds from a bank by yielding the bill as a form of security. Such an endorsement was known as a pignorative endorsement, and occurred mainly between banks.

26. Mr. GUEST (United Kingdom) said that the Working Group had adopted the view that, if there was an instrument which was useful in particular States, an attempt should be made to include an appropriate provision in the Convention. However, there were some difficult questions, such as what defences could be raised under articles 25 and 26 against the bank claiming payment, and what the status of the bank would be as a protected or non-protected holder. It might be possible for the interested delegations to come forward with a written proposal which would take account of the current structure of the Convention and deal with the problems which would necessarily arise.

27. Mr. VIS (Chairman of the Committee of the Whole) asked the representative of France to submit such a proposal.

28. Mr. SPANOGLE (United States of America) said that he would appreciate seeing, in the written proposal, a clarification of exactly what the transaction involved.

29. Mr. CHAFIK (Egypt) said it had formerly been his belief that the concept of pignorative endorsement described by the representative of France should appear in the Convention since it was useful for ensuring short-term credits. He had since learned from Egyptian banking circles, however, that such a procedure was now outdated. Short-term credits were now guaranteed by stocks and shares, and bills of exchange were rarely used. He agreed with the United Kingdom representative that, even if the Commission had wanted to introduce the concept into the Convention, there simply was not time since that would require adjusting all the other articles.

30. Mr. VASSEUR (France) observed that when he had made his proposal at the eighteenth session, he had been told that it was too early. Now he was being told that it was too late.

31. Mr. VIS (Chairman of the Committee of the Whole) said that, at its eighteenth session, the Commission had not yet known under what time constraints it would be working. In any case, the representative of France was still free to make his proposal if he so wished.

#### Article 30

32. Mr. VIS (Chairman of the Committee of the Whole) invited the Commission to turn its attention to the implied waiver in articles 30, 52, 60 and 63. He recalled that earlier drafts of the Convention had always included the possibility of implied waivers, but that some delegations had opposed such a provision because it did not create certainty in international transactions. At the seventeenth session therefore, the Commission had deleted the reference to implied waivers in articles 52, 60 and 63 and left it to the Working Group to discuss the reference in article 30. The Working Group had decided that it was justified to retain the reference in article 30.

33. Mr. CHAFIK (Egypt) said he fully agreed that the Convention should contain as few implied waivers as possible.
34. Mr. ANGELICI (Italy) said that his delegation still had considerable doubts about article 30. The idea that a person could be bound by a signature that was a forgery of his own seemed to conflict with article 32(4) and created considerable uncertainty. A holder could not be sure whether the debtor or the owner of the forged signature was liable, and in such cases a judge would have to apply article 32(4). The act of forgery did not make the person whose signature was forged a debtor, nor did it exonerate the forger. He therefore proposed that the word "impliedly" should be deleted from article 30.
35. Mrs. PIAGGI de VANOSI (Argentina) agreed entirely with the representative of Italy concerning the attribution of liability in accordance with article 30.
36. Mr. VASSEUR (France) said that the use of the word "impliedly" had been inappropriate in articles 52, 60 and 63 and was also inappropriate in article 30. Acceptance of a forged signature must be express and not implied in order to create certainty.
37. Mr. ILLESCAS ORTIZ (Spain) supported the deletion of the word "impliedly" from article 30 in order to make the Convention more internally coherent. If that word was retained, article 30 would conflict with articles 13 and 37.
38. Mr. SPANOGLE (United States of America) observed that the Commission was not discussing whether acceptance of a signature was express or implied but rather the question of authority. In international trade, almost all signatories were corporations and the latter always had individuals to sign for them. The question of whether an individual was authorized to sign was never resolved by examining the instrument itself, but was always determined by an outside authority, and since the question of authority concerned information that was not available on the instrument, the Commission must refer to the usual agency law. For instance, the notion of implied authority existed even when there was no express authority. If the concept of implied authority existed in civil law, a reference to it was required in article 30 and the Commission must clarify that that was what it meant in that article.
39. Mrs. VILUS (Yugoslavia) said that the word "impliedly" from article 30 may create difficulties with regard to burden of proof and interpretation. For these reasons, she proposed that the word "impliedly" be deleted from the draft. Her second choice was to delete both words, i.e. "expressly or impliedly".
40. Mr. MACCARONE (observer, European Banking Federation) said that the concept of implied waiver had been dropped from the other articles because it could create uncertainty in international trade. The reason for deleting that concept from article 30 was not that it could create uncertainty, however, but the fact that such ratification of forgery conflicted with the principle set forth in the first sentence of article 30. He proposed therefore that the second sentence of article 30 should be deleted.
41. The United States representative had referred to the question of authority, but that question did not arise in article 30. Under United States law, authority could indeed be exercised by an agent signing with the name of the principal. Article 30 did not deal with that issue, however, but simply with the issue of forgery.
42. Mr. GUEST (United Kingdom) observed that article 30 concerned both the ratification of forgery and estoppel. First, a person who ratified a forgery must accept liability in accordance with the second sentence of article 30. It would be very difficult to delete the second sentence since that would mean that, even if the victim had ratified a forgery, he would not be bound by it. Second, victims could also ratify a forgery by their conduct, which was what was meant by the term "impliedly". If some delegations were opposed to the use of that term, he would favour deletion of both "expressly" and "impliedly" in order to ensure retention of the second sentence.
43. Mr. ABASCAL (Mexico) endorsed the comments made by the representatives of the United Kingdom and the United States. Article 30 must be read in conjunction with article 4(10), according to which a forged signature included a signature making unauthorized use of mechanical means. Such forgeries obviously raised the question of authority to sign on behalf of a corporation.
44. Mr. MAEDA (Japan) endorsed the statements by the representatives of the United Kingdom and the United States and said that he would prefer to keep article 30 as it was.
45. Mr. MACCARONE (observer, European Banking Federation) said that article 30 applied to liability on the instrument. His objection had related only to such liability. If there were grounds for recognizing ratification of a forgery, there were also grounds for recognizing implied ratification.
46. Mr. PISEK (Czechoslovakia) recalled that, at its seventeenth session, the Commission had deleted all references to implied waiver. At its eighteenth session, however, it had come to see the morality of the United Kingdom argument that the victim of a forgery might benefit from such a forgery unless there was provision to the contrary. There was a difference between article 30 and the other articles from which references to implied waivers had been deleted.
47. Mr. DUCHEK (Austria) said article 30 should probably cover liability for ratification of forged instruments, an important legal concept in some common-law countries. The Yugoslav proposal to delete "expressly or impliedly" was preferable to stating "expressly" but not "impliedly". In any case, the word "impliedly" gave rise to uncertainty and the term "acceptance" might be more apt.
48. Mr. VIS (Chairman of the Committee of the Whole) said he did not object to deletion of "impliedly", as long as the courts reserved the right to invoke estoppel when a person had, by his conduct, impliedly consented to be bound on his signature, though forged. A well-known example was the English case of *Greenwood vs. Martin* in which the court had held a husband liable for a signature his wife had forged, because he had not objected until after her death.
49. Mr. GRIFFITH (Australia) mentioned that the *Greenwood vs. Martin* case had also been the basis for legislation in his country. He preferred to retain the full text of article 30, but, as an alternative, would support deletion of "expressly" or "impliedly", rather than "impliedly" alone.

50. Mr. ABOUL-ENEIN (observer, Asian-African Legal Consultative Committee) endorsed deletion of "impliedly" from article 30, maintaining that in matters of forgery, it was important to be explicit.

51. Mr. SAMI (Iraq) said that since the word "expressly" had been used elsewhere in the draft Convention, it should be retained in article 30. "Impliedly" could be omitted. The real issue was one of forged signatures, not authorized signatures, a question taken up in article 32.

52. Mr. DRUEY (observer for Switzerland) said the source of confusion in article 30 was not so much "expressly or impliedly" as the ambiguity of the word "accepted". It should be made clear that liability was being accepted towards the holder of the instrument.

*The meeting was suspended at 4.45 p.m. and resumed at 5.10 p.m.*

53. Mr. VIS (Chairman of the Committee of the Whole) urged the Commission to seek a consensus on the basis of the Yugoslav proposal rather than focusing on the word "impliedly" alone.

54. Mr. VASSEUR (France), indicating he would support the Yugoslav proposal, cautioned none the less that if "expressly or implied" was deleted, no mention could be made of a patron's reasons for accepting liability, as they were also implicit.

55. Mrs. PIAGGI de VANOSI (Argentina) said her delegation supported the Yugoslav proposal.

56. Mr. VENKATRAIAH (India) said his delegation preferred to retain article 30 as it stood, but would also support the Yugoslav proposal.

57. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) stressed that the provisions of article 30 should not be associated with articles 52, 58 and 63, which contained the words "expressly waived". To avoid confusion, it would be advisable to have article 30 provide for cases of both expressed and implied confirmation of a forged signature.

58. Mrs. ADEBANJO (Nigeria) indicated that if "impliedly" alone could not be deleted, her country would support the Yugoslav proposal to delete "expressly or impliedly".

59. Mr. ABASCAL (Mexico) said that not only did the Yugoslav proposal fail to clarify the question, but it confused matters. Eliminating the words "expressly or impliedly" left the meaning of consent open to interpretation by every country, according to its own domestic legislation.

60. Mr. SPANOGLE (United States of America), supporting the Mexican and Soviet positions, indicated that in the light of articles 52, 58 and 63, it would never be completely clear whether "impliedly" was actually provided for in article 30 unless it was made explicit.

61. Mr. GANTEN (observer for the Federal Republic of Germany) said he preferred article 30 as it stood but would support the Yugoslav proposal. The concept of "expressly or impliedly" was, however, a useful one, recognized in his own country. In any case, if the Yugoslav compromise were adopted, close attention should be paid to the wording of articles 52, 58 and 63 when article 30 was redrafted.

62. Mr. VIS (Chairman of the Committee of the Whole) suggested the insertion of the phrase "adopted the signature as his own" before the words "or represented". The representatives of Hungary, Italy, Kenya and Yugoslavia, and the observers for Switzerland and the European Banking Federation could serve on a drafting committee that would reword article 30 to reflect that courts could determine liability on an instrument on the basis of a person's conduct.

63. Mr. VASSEUR (France) suggested "give reasons why the signature was his own" as an addition to the final sentence of the article.

*Article 34(2)*

64. Mr. VIS (Chairman of the Committee of the Whole) said that the reason for allowing exclusion of liability only if another party was liable on the bill was that a negotiable instrument was without value unless there was liability on it.

65. Mr. CHAFIK (Egypt) said that the drawer was the principal debtor on the bill until the drawee had accepted it, whereupon the drawer became the guarantor and the drawee became the principal debtor. Thus the drawer could not exclude his liability for payment until the bill had been accepted by the drawee. Accordingly, his delegation could not accept the last sentence of article 34(2).

66. Mrs. PIAGGI de VANOSI (Argentina) said that the principal debtor on a bill of exchange, once it had been accepted, was clearly the acceptor.

67. Mr. MACCARONE (observer, European Banking Federation) said that if the last sentence was amended the entire paragraph would have to be redrafted. Article 34(2) dealt with limitation of liability for acceptance and payment, and it would be illogical only to provide for limitation of liability for acceptance once acceptance had taken place. The rule made more sense as it was currently drafted; irrespective of which party was liable, the important point was that the holder should have someone against whom he could claim payment. In practice the obligation of an acceptor was the same as that of an endorser, even though there was a theoretical difference.

*Article 42(1)*

68. Mr. VIS (Chairman of the Committee of the Whole) said that representatives of States with legal systems which encompassed the concept of *aval* had objected to the provision that there could be a guarantor of a drawee who was not a party to the bill.

69. Mr. SAMI (Iraq) said that it was not clear to him how there could be a guarantor in respect of a drawee who was not the acceptor. Liability which did not exist could not be guaranteed.

70. Mr. VIS (Chairman of the Committee of the Whole) said that the question was not one of a guarantee of liability, but of a guarantee that the bill would be paid.

71. Mr. MACCARONE (observer, European Banking Federation) said that while it might be possible to give a guarantee for a party who was not liable, the question was what kind of liability the guarantor would have.

72. Mr. VIS (Chairman of the Committee of the Whole) said that it would appear to be a primary liability, akin to that of an acceptor.

73. Mr. SAMI (Iraq) said that the drawee's only liability was to pay on the instrument. If the instrument was not accepted, there was no liability.

74. Mr. VIS (Chairman of the Committee of the Whole) said that in commercial transactions it was often necessary to have liability on the part of someone else. For example, it might be that a party who wished to make a promissory note lacked creditworthiness and required a guarantor. There were two approaches to such a problem: the common-law solution was to have a maker or an endorser as an additional party, whereas under civil-law systems the signature of an *avalist* would be required. In essence, both solutions provided for another liability on the instrument. The draft convention basically

followed the civil-law approach, while also making it possible to ensure that payment would be guaranteed.

75. Mr. SAMI (Iraq) said that it was not clear to him what the relationship would be in such an instance between the guarantor and the drawee who was not an acceptor, since the latter could say that he was not liable *vis-à-vis* the guarantor.

76. Mr. VIS (Chairman of the Committee of the Whole) said that if the drawee's guarantor had to pay on the instrument, he would have rights against the drawee, but not on the instrument. As for the liability of the drawee, the matter pertained more to contract.

77. Mr. SAMI (Iraq) said that the drawee was not a party if he did not accept the instrument.

*The meeting rose at 6 p.m.*

### Summary record of the 345th meeting Monday, 30 June 1986, 10 a.m.

[A/CN.9/SR.345]

*Chairman:* Mr. KARTHA (India)

*Chairman of the Committee of the Whole:*  
Mr. VIS (Netherlands)

*The meeting was called to order at 10.10 a.m.*

#### International payments (continued)

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes* (continued) (A/CN.9/273, A/CN.9/274 and A/CN.9/285)

#### Article 34(2)

1. Mr. CHAFIK (Egypt) recalled that the Commission had agreed that bills of exchange must have a principal debtor; that the principal debtor must be the drawer (before acceptance of the bill) or the drawee (after acceptance); and that the principal debtor could not exclude his own liability to payment. If a person paid for goods with a bill of exchange and subsequently excluded his own liability before the bill was accepted by the drawee, he would have received goods without payment, in other words, he would have enriched himself unjustly. As currently worded, article 34(2) would allow the drawer to exclude his own liability for payment once any other party had signed the bill; in fact, he could do so only after the drawee signed the bill to show that he accepted it, thus becoming the principal debtor and converting the drawer into the guarantor. Accordingly he proposed that article 34(2) should be amended by replacing the words "another party is or becomes liable on the bill" by the words "the bill bears the signature of the drawee".

2. Mr. SAMI (Iraq) and Mr. LIU Benku (China) supported the proposal.

3. Mr. VIS (Chairman of the Committee of the Whole) said that the text of the draft Convention represented a compromise between the system of the Geneva Convention, under which the drawer could not exclude his liability for payment, and that of other countries under which a drawer could draw without recourse.

4. Mr. CRAWFORD (observer for Canada) said that he had no difficulty with the text as it stood. While he understood the position taken by the representative of Egypt, he felt that the proposed amendment was too narrow. It would seem that protection against unjust enrichment could be assured by the liability of other parties—for example, the guarantor for the drawer or the guarantor for the drawee.

5. Mr. BARRERA GRAF (Mexico), Mr. PISEK (Czechoslovakia), Mr. GRIFFITH (Australia), Mr. ILLESCAS ORTIZ (Spain), Mr. GANTEN (observer for the Federal Republic of Germany), Mrs. ADEBANJO (Nigeria), Mr. KIM (observer for the Republic of Korea), and Mr. KOCH (Sweden) supported the text as it stood.

6. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) and Mr. DELFINO-CAZET (Uruguay) said that they, too, supported the existing text, which faithfully reflected current practice. Adoption of the Egyptian amendment would place the Convention in conflict with current practice.

7. Mr. SMART (Sierra Leone) said that under article 29, a person was not liable on an instrument unless he signed it; accordingly, he did not see why liability should be limited to the drawee or to the guarantor. In the event of a bill not being honoured, the payee could call on any prior party.

8. Mr. VASSEUR (France) said that he could accept the text of article 34(2) as it stood but would like the limiting clause in the penultimate line to read "only from the time that another party is or becomes liable on the bill".

9. Mr. VIS (Chairman of the Committee of the Whole) said that the majority view seemed to be that article 34(2) should remain as it stood.

*Article 42(1)*

10. Mr. SAMI (Iraq) said that the guarantee referred to could be given only for a drawee who had accepted a bill of exchange; until the drawee accepted the bill, he had no liability. It was impossible to guarantee a non-existent obligation. Accordingly, the wording of article 42(1) should be amended to make that clear.

11. Mr. VIS (Chairman of the Committee of the Whole) recalled that the provision in article 42(1) had been inserted after it had been ascertained by questionnaire circulated among commercial bankers that, although the Geneva system did not make provision for it, in practice there could be an undertaking on an instrument whereby payment was guaranteed even when the drawee had not signed the instrument and therefore had no liability.

12. Since there appeared to be no support for the Iraqi proposal, the text would remain as it stood.

*Article 42(2)*

13. Mr. VASSEUR (France) proposed that article 42(2) should include a specific reference to guarantees created on a separate document, which were very common in his country. It had been noted at the fourteenth session of the Working Group (A/CN.9/273, para. 111) that guarantees were so created in practice, but article 42(2) might be construed as prohibiting guarantees which did not appear on the instrument.

14. Mr. VIS (Chairman of the Committee of the Whole) asked whether it was really necessary to have a special rule governing agreements created outside the instrument.

15. Mr. VASSEUR (France) pointed out that article 30 also covered a situation which was outside the instrument. Omission of any mention in article 42(2) on a separate document of guarantees created would reinforce the argument that the Convention excluded such guarantees.

16. Mr. GANTEN (observer for the Federal Republic of Germany) said that everyone agreed that guarantees by separate act were possible in practice and that the Convention did not prevent parties from concluding obligations outside the instrument. The parallel drawn by the representative of France with article 30 was not relevant, for article 30 dealt with a different situation. Article 42(2) should remain as it stood.

17. Mr. GRIFFITH (Australia) suggested that the concern expressed by the representative of France could be dealt with by including the words "on the instrument" following the words "A guarantee".

18. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) doubted that in practice the French proposal would prove useful. Although its intention was to give the parties greater freedom, it would in effect limit their freedom by predetermining the content of any guarantee given on a separate document. In practice and under the Geneva Convention, such guarantees differed from regular guarantees because they did not become

part of the instrument itself and could be transferred either through cession or as directed on the guarantee itself.

19. The existing text of article 42(2) did not prohibit guarantees outside the instrument, and consequently no amendment was necessary or advisable.

20. Mrs. PIAGGI de VANOSI (Argentina) said that the Geneva system provided for the possibility of a separate guarantee, provided that the bill of exchange indicated on its face the existence of such a guarantee. Such an *aval* served as a guarantee of payment and, indeed, could often promote wider circulation of the instrument.

21. It was difficult to see how a guarantee outside the instrument could be considered implicit in the current text of article 42(2), and she therefore supported the French proposal.

22. Mr. SMART (Sierra Leone) was opposed to the French proposal. In current practice, guarantors normally signed on the bill and were liable to all subsequent parties. If the draft Convention allowed guarantors outside the bill, such guarantors would be liable only to the immediate parties, and that would destroy the whole concept of negotiability of bills.

23. Mr. ABOUL-ENEIN (observer, Asian-African Legal Consultative Committee) said that it was unnecessary to refer in article 42(2) to a guarantee outside the instrument. That kind of guarantee could be given, but not as part of the instrument. It was not excluded by the draft Convention.

24. Mr. BARRERA GRAF (Mexico) and the CHAIRMAN, speaking as the representative of India, supported article 42(2) as it stood, for the reasons given in the Working Group's report (A/CN.9/273, para. 111).

25. Mr. KIM (observer for the Republic of Korea) said that the draft Convention in general did not deal with any agreements made outside the instrument, but that article 42(2) did not in any way exclude a guarantee outside the instrument. He therefore supported the existing text.

26. Mr. KOCH (Sweden) supported the existing text. In that particular article, it would be misleading to mention guarantees outside the instrument.

27. Mr. DELFINO-CAZET (Uruguay), Mr. MAEDA (Japan), Mr. SZASZ (Hungary) and Mrs. ADEBANJO (Nigeria) also supported the text as drafted.

28. Mr. VIS (Chairman of the Committee of the Whole) said that he would take it that the Commission wished to adopt article 42(2) as drafted.

29. *It was so decided.*

*Article 42(6)*

30. Mr. VIS (Chairman of the Committee of the Whole) recalled that article 42(6), a new text, had been drafted to meet the concerns raised in paragraph 110 of the Working Group's report. He would take it, if he heard no objection, that the Commission wished to adopt article 42(6).

31. *It was so decided.*



## Article 46

32. Mr. VIS (Chairman of the Committee of the Whole), drawing attention to the discussion of article 46 in paragraphs 112 and 113 of the Working Group's report, pointed out that article 46(1) and (2) had been redrafted. The new text of article 46(1) provided that the drawer had no power to stipulate that a bill must not be presented for acceptance in those cases where article 45(2) made such presentment mandatory.

33. Mr. ILLESCAS ORTIZ (Spain) said that he had no problem with that exclusion, but was troubled by the phrase "or before the occurrence of a specified event" at the end of the first sentence of article 46(1). If a drawer was allowed to make presentment for acceptance dependent on the occurrence of an event, the draft Convention would by implication be upholding the validity of a conditional bill of exchange, which would contradict the unconditionality stipulated in article 1(2)(b). He therefore proposed the deletion of the phrase in question.

34. Mr. DELFINO-CAZET (Uruguay) said that he supported the text as it stood because it reflected both article 22 of the Geneva Uniform Law and his own country's practice. However, he agreed in theory with the representative of Spain. He himself believed that the intention of the text of article 46(1) was to refer to a specified event that was not an uncertain event; but the wording could be made absolutely clear by adding the words "and certain" after "specified".

35. Mr. VIS (Chairman of the Committee of the Whole) pointed out that, actually, it had not been the Working Group's intention that the event would be certain. The phrase had been included because of evidence received from commercial circles that acceptance of a bill was, in practice, often dependent on an event which might or might not be certain, such as the arrival of goods.

36. Mr. GANTEN (observer for the Federal Republic of Germany) said that he would support the proposal to delete the phrase in question, which introduced an element of conditionality.

37. Mr. LIU Benku (China), noting that article 45(2)(b) stipulated that a bill must be presented for acceptance when the bill was drawn payable at a fixed period after sight, asked whether, when a drawer delayed the date of acceptance as was permitted under article 46(1), the time-limit for payment would also be delayed. That would not be acceptable.

38. Mr. VIS (Chairman of the Committee of the Whole) said that that would not be the case.

39. Mr. BARRERA GRAF (Mexico) said that, while the representative of Spain had a strong argument, he did not believe that the phrase in question introduced an element of conditionality in bills of exchange or that it made payment subject to the occurrence of an uncertain event. It merely referred to the deferral of presentment; once the date of maturity had arrived, the bill must be presented. He therefore supported the existing compromise text.

40. Mr. GUEST (United Kingdom) drew attention to the commentary on article 46 in the secretariat report in document A/CN.9/213, where the reasons for inserting the reference to a specified event had been explained: inquiries among banking and trade institutions had shown that it was normal practice in a

number of countries to delay presentment until, for instance, merchandise had arrived or until after customs clearance. His delegation therefore favoured the existing text.

41. With regard to the question raised by the representative of China, he believed that, if presentment for acceptance was so delayed, and if the bill had been drawn payable at a fixed period after sight, the time for payment would to that extent be postponed. He did not, however, think that should prove unacceptable.

42. Mr. VASSEUR (France) said that French banks liked the existing text and he therefore supported it.

43. Mr. SAMI (Iraq) said that he supported the existing text for practical considerations relating to foreign trade. In fact, he proposed that the same right should be given to the endorser of a bill, as was the case in the Geneva Convention. To do so would be in accord with article 40(2).

44. Mr. SMART (Sierra Leone) said that he favoured the text as it stood. He had sympathy for the position of the Spanish delegation, but only in relation to article 51, dealing with presentment for payment, and not in relation to presentment for acceptance.

45. Mr. CRAWFORD (observer for Canada) noted that the restrictive condition permitted under article 46(1) was in no way addressed under article 47(f); and that, further, under article 50(1)(a), a bill could not be dishonoured by non-acceptance in cases where there had not yet been a due presentment.

46. He did not understand how the holder of a bill the presentment of which had been made conditional upon, for instance, the arrival of merchandise, would know when he could begin to enforce his rights of recourse against the drawer if the merchandise did not arrive. The representative of Mexico had stated that the conditional delay of presentment permitted to the drawer under article 46(1) would in practice be countered by the instrument's fixed date of maturity; but he himself saw no requirement in article 46(1) that, together with the condition, the bill must also stipulate a maturity date.

47. Mr. VIS (Chairman of the Committee of the Whole) said that, when an instrument did not stipulate a maturity date, it was deemed under the draft Convention to be payable on demand.

48. Mr. CRAWFORD (observer for Canada) said that his question was, precisely, how a holder would know when he could begin to demand payment.

49. Mr. VIS (Chairman of the Committee of the Whole) pointed out that the draft Convention did not include the concept of reasonable time, but that article 51(f) imposed a fixed period of one year within which due presentment for payment could be made.

50. He said that he would take it, if he heard no objection, that the Commission wished to adopt article 46 as revised by the Working Group.

51. *It was so decided.*

*The meeting was suspended at 11.35 a.m. and resumed at 12.10 p.m.*

Article 51(h)

52. Mr. VIS (Chairman of the Committee of the Whole) recalled that the different payment practices in various countries had given rise to questions concerning the concept of due presentment in article 51(h). As explained in paragraphs 115 to 117 of document A/CN.9/273, the Working Group had decided to redraft the article with a view to providing that an instrument might be presented at a clearing-house when under the law of the place of the clearing-house or under the rules of the clearing-house such presentment constituted due presentment. If he heard no objection, he would take it that the Commission wished to adopt the revised text of article 51(h).

53. *It was so decided.*

Article 66(2) and (3)

54. Mr. VIS (Chairman of the Committee of the Whole) recalled that, under article 66, a holder of an instrument might, after the instrument had reached maturity, recover from any party liable not only the amount of the instrument but also interest on that amount. If no specific rate of interest had been stipulated previously, the rate was to be determined on the basis of article 66(2), which set it at "[2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country where the instrument is payable. If there is no such rate, the rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main centre of the country in the currency of which the instrument is payable. In the absence of any such rates, the rate of interest shall be [ ] per cent per annum". However, that definition posed problems, since official, or bank, rates were not uniform in all countries.

55. Mr. FELSENFELD (United States of America) said that, as no rate in his country corresponded to the definitions in the first two sentences of article 66(2), the rate specified in the third sentence—" [ ] per cent per annum"—would have to apply. He therefore wished to know what per cent the Commission intended to specify in that sentence.

56. Mr. SAMI (Iraq) proposed that the rate of interest specified should be the official rate, determined by the appropriate centres in each country. To specify a figure of 2 per cent above that rate would result in excessively high payments and was not in the interest of the developing countries, which were already suffering from a heavy debt burden and high interest rates.

57. Mr. ABOUL-ENEIN (observer, Asian-African Legal Consultative Committee) agreed with that view.

58. Mr. GUEST (United Kingdom) said he did not believe that an interest rate of 2 per cent above the official rate was unreasonable, particularly since the commercial rate was higher than the official rate in most countries. He therefore suggested that the brackets should be removed from the 2 per cent figure.

59. The final sentence of article (66)(2), which was of concern to the United States representative, gave rise to some very difficult considerations. Any figure that the Commission specified might be over-generous or unnecessarily punitive,

depending on the economic situation at the time when the rate was applied. It might be useful to adopt the rate awarded by courts in judgements.

60. Mr. CRAWFORD (observer for Canada) agreed that a usable rate should be specified, but wondered whether a judgement rate was any more likely to be uniformly available.

61. In judgements in Canada, particularly during periods marked by fluctuating interest rates, the interest that a holder paid to obtain funds to replace those lost through an instrument in default was considered to constitute an element of the damages suffered by the holder. He therefore suggested that the Commission should consider referring to the rate at which a holder borrowed from his bank.

62. Mr. FELSENFELD (United States of America) questioned the desirability of utilizing the judgement rate, since at least 50 different such rates applied in the United States. He suggested that the prime rate might constitute an acceptable alternative. The prime rate was set by individual banks; in order to set a measurable standard, it might be possible to specify the rate as being the prime rate of the five or seven largest banks in a particular state or in the country as a whole. In any event, the prime rate seldom varied by more than 0.5 per cent from bank to bank. In fact, during periods of prolonged stability, the prime rate was generally uniform throughout the country.

63. Mr. VASSEUR (France) said that, in trying to specify a uniform interest rate, the Commission was faced with an insoluble problem and no proposal, however imaginative, would be acceptable to all delegations. The Banque de France had proposed that the act of signing the Convention should entail an obligation for the signatory State to establish a rate of interest for the implementation of the Convention. Since it was impossible to establish an interest rate for all States, that solution could be useful.

64. Mr. VIS (Chairman of the Committee of the Whole) said that it would be useful to ascertain whether there was an official rate in every country to which reference could be made in the Convention.

65. Mr. FELSENFELD (United States of America) said that in the United States the interest rate payable after default would depend on the state in which the action was brought.

66. Mr. VIS (Chairman of the Committee of the Whole) said that there could perhaps be a reference in article 66 to the rate of interest which would be applicable if payment were demanded on a domestic instrument.

67. Mr. VASSEUR (France) said that, in cases of late payment, the rate of interest applicable in France was an official interest rate determined by government decree.

68. Mr. GANTEN (observer for the Federal Republic of Germany) said that there was no official discount rate in the Federal Republic of Germany. The current rate of interest was very low and would not be realistic for the purposes of the Convention. Nor was there an official judgement rate; the rate was determined in each case in the manner described by the representative of Canada. He could support the Canadian proposal; if that proposal were adopted, it would not matter

whether there was an official judgement rate in a given country, as long as the Convention contained a formulation allowing a judge to calculate the rate. It was important that the rate should not be under the control of the payee. As it stood, the last sentence of article 66(2) was unacceptable.

69. Mr. VIS (Chairman of the Committee of the Whole) said that, if it were found that in cases of payment after maturity there was some kind of official rate in use in every country, that would solve the Commission's problem. It should be borne in mind that, in cases where payment was demanded from one or more endorsers, interest was payable each time. The Commission should find a formula to describe the official judgement rate in each country, and then decide whether the rate should be that of the holder's or the payee's place of business.

70. Mr. CRAWFORD (observer for Canada) said that even very small changes in the wording of article 66 could have a serious impact. In Canada, the official judgement rate was 5 per cent but it was almost never accorded because the holder normally claimed the rate payable on substituted funds, which varied according to the circumstances of the international market. Thus the official rate was not necessarily of great significance, and it would be better to refer to the rate at which claims were judged in domestic matters.

71. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that in the Soviet Union all interest rates were established and applied in accordance with the legislation of the USSR. Strict and detailed laws were laid down by the State Bank and other institutions establishing rates of interest and rates for late payment. Those rates varied, and they could be applied only to operations between Soviet organizations, and not to international payments. Thus there was no single official rate. Moreover, there was no special judgement rate in the USSR.

72. Mr. DRUEY (observer for Switzerland) said that in Switzerland the interest rate for late payments, amounting to 5 per cent, was seldom applied because the plaintiff was always able to prove that his actual damages were higher.

73. Mr. GUEST (United Kingdom) said that the Commission could decide that, if the first two sentences of article 66(2) did not apply, the applicable rate of interest should be a reasonable commercial rate. The rate would then be determined according to the circumstances of each case. That proposal could be combined with the Canadian proposal.

74. Mrs. PIAGGI de VANOSI (Argentina) said that in Argentina there was no official interest rate, and there were even different rates determined by banks in the various provinces or states; a rate of 6 per cent was normally established by the courts in cases of late payment, if it could be proved that the delay had not given rise to increased costs. She could support the United Kingdom proposal.

75. Mr. BARRERA GRAF (Mexico) said that there was an official rate in Mexico but, as in other countries, that rate was considered very low and was not often applied in practice. The Commission could refer to the official rate of interest prevailing in the country of payment and allow the possibility of the claimant proving to the courts that he had suffered greater damage.

76. Mr. VIS (Chairman of the Committee of the Whole) said that, if such a formula were used, it would be necessary to go to court to obtain payment of international bills and notes after maturity, and that situation was not necessarily desirable.

77. Mr. FELSENFELD (United States of America) said that perhaps in reviewing the variety of devices existing in different countries the Commission had found a common denominator and could establish as a standard the rate that would be paid on an equivalent domestic obligation. Such a formulation could be applied in countries where the official rate was normally ignored if it was too low, and also in countries with a fixed official rate. In the United States there would always be a judgement rate in the jurisdiction in which judgement was brought.

*The meeting rose at 1 p.m.*

### Summary record of the 346th meeting Monday, 30 June 1986, 3 p.m.

[A/CN.9/SR.346]

*Chairman:* Mr. KARTHA (India)

*Chairman of the Committee of the Whole:*  
Mr. VIS (Netherlands)

*The meeting was called to order at 3.15 p.m.*

#### International payments (continued)

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes (continued)* (A/CN.9/273, A/CN.9/274 and A/CN.9/285)

#### Article 66(2) (continued)

1. Mr. VIS (Chairman of the Committee of the Whole) invited the Commission to resume consideration of the last sentence of article 66(2), concerning the applicable rate of interest where none of the other rates provided in of article 66(2) was available.

2. Mr. GRIFFITH (Australia) said that a judicial body could determine a reasonable rate of interest, even though there might be some degree of uncertainty while the judicial determination was pending. A provision specifying that the judgement rate in respect of domestic obligations should be applied might not be suitable for all jurisdictions. Any fixed rate would be unsatisfactory as a basis for a continuing convention.

3. Mr. MACCARONE (observer, European Banking Federation) said that there were situations in which instruments payable in one country were drawn in another. A rate of interest expressed in French francs, for example, might not be appropriate for an instrument denominated in United States dollars. The draft Convention should not specify a fixed rate of interest, since courts often disregarded such rates and established other rates of interest. He supported the Canadian proposal that the draft Convention should make reference to the rate of interest which a creditor was required to pay if he was obliged to borrow the money that had not been paid.
4. Mr. VASSEUR (France) said that his delegation could not support the Canadian proposal. French banks were in principle opposed to any interest rate that was not pre-determined and could not agree that the courts should determine such rates. Recourse to the courts would result in unacceptable delays and uncertainty. In France the specific fault of the debtor must be proved before a court could establish a rate of interest higher than the official rate. Judges had no powers of discretion to determine rates of interest.
5. The United States proposal that the article in question should refer to a "reasonable commercial rate" implied an element of appreciation or judgement. Since absolute clarity was required, he could not support that proposal.
6. Mr. FELSENFELD (United States of America) said that a synthesis of views might be achieved if the draft Convention were to specify that the applicable rate of interest was the judgement rate at the place of payment of the instrument. Upon default, the loss would normally be suffered in the place where the instrument was payable. Such a solution would eliminate the problem of ascertaining what constituted a reasonable rate of interest.
7. Mr. GUEST (United Kingdom) said that account should also be taken of other situations, such as those referred to in articles 25, 40 and 67(b), which involved recourse actions.
8. Mr. VIS (Chairman of the Committee of the Whole) suggested that the rate of interest should be that applicable in actions on bills and notes at the place of payment, which might not necessarily be the judgement rate.
9. Mrs. BUURE-HAGGLUND (observer for Finland) said that in Finland there was a judgement rate established by the Central Bank, which was used when the parties to a transaction had agreed that interest should be paid and the rate of interest was left open. There was also, however, a default rate, which was higher than the judgement rate. Article 66(2) seemed to refer to a default rate. The drafting of that paragraph needed to be improved in order to render its intention more explicit.
10. Mr. DUCHEK (Austria) asked whether the United States proposal concerning the interest rate at the place of payment referred to the rate of interest payable by creditors in that country in domestic contractual relations, or to transactions involving bills of exchange. Both of those rates in Austria were very low. On the whole, he had doubts about the proposal and was inclined to support the view of the representative of France that reference to a reasonable rate of interest would lead to uncertainty and was therefore unacceptable.
11. Mr. VIS (Chairman of the Committee of the Whole) said that, under the existing text, in the case of a bill of exchange involving a drawer in the United States of America, a payee in Austria and a holder in Switzerland, if the bill was dishonoured by the drawee and if the holder then sued the payee in a recourse action, the Austrian court was required to apply the United States rate of interest and not the Austrian rate.
12. Mr. FELSENFELD (United States of America) said that the test to be applied in the third sentence of article 66(2) should be no different from the test provided in the first sentence: the rate should be "effective in the main centre of the country where the instrument is payable".
13. Mr. GUEST (United Kingdom) pointed out that, in those countries bound by the Geneva Uniform Rules on International Bills of Exchange and International Promissory Notes, rates of interest would be relatively low. In some countries, in which the normal judgement rate was relatively low, the courts might award damages in excess of those rates for proven losses. He wished to know whether the United States proposal included the latter element.
14. Mr. FELSENFELD (United States of America) said that, where the bank rate of a country was not used to determine damages or interest rates and a different rate was applied as being more suitable, the latter rate would be applicable. It might therefore be advisable to include the word "actually" in the redrafting.
15. Mr. KANDIE (Kenya) said that it might be useful to provide for a method whereby the applicable rate of interest would be the average of the two or three most significant rates.
16. Mr. CRAWFORD (observer for Canada) said that there were only two ways to attain uniformity: either to specify the amount of interest or to use a uniform method of arriving at a rate. He would prefer the second alternative and therefore supported the view that the applicable rate should be determined by the courts or the law of the place of payment. Of course, some delay was inevitable if the goal was to measure the damage suffered by the party.
17. Mr. VIS (Chairman of the Committee of the Whole) asked whether it would be commercially feasible for a Canadian court, for example, to apply New York rates.
18. Mr. CRAWFORD (observer for Canada) replied that it would.
19. Mr. VASSEUR (France) said that any reference to an undetermined rate was undesirable, because what mattered to a bank in an international transaction was the amount of loss which it incurred as a result of being unable to use the uncollected funds in the international market. He therefore proposed that a State should indicate at the time of ratification the rate of interest which would be applicable in the case covered by the last sentence of article 66(2).
20. Mr. FELSENFELD (United States of America) said that the observer for Canada had already described how a single rate might become unrealistic. Efforts must be continued to find a standard which was easily ascertainable in advance but which

remained flexible. It was therefore preferable that the rate should be that of the place of payment at the time when the instrument went into default. In order to meet the French delegation's objection, it might be possible for the parties to stipulate a rate on an instrument when they originally entered into the agreement.

21. Mr. CHAFIK (Egypt) said that he was opposed to the reference in the first two sentences of article 66(2) to a figure of 2 per cent above the official rate. In some cases, that figure might represent an enormous sum of money.

22. Mr. GUEST (United Kingdom) said that, in the United Kingdom, the official rate would be the Bank of England's minimum lending rate to institutions of impeccable creditworthiness. It would not be representative of the cost involved for a trader who borrowed from his own bank, nor would it represent the actual loss resulting from a delay in payment. The figure of 2 per cent above the official rate would compensate the creditor by maintaining him in the same position in which he would have been if payment had been made on time. If rates were extremely high in some countries, perhaps that objective would not be achieved.

23. Mr. MAEDA (Japan) said that he favoured the existing text, because it provided for compensation for delay in case of default after maturity.

24. Mr. SAMI (Iraq) said that, if a creditor suffered losses as a result of a delay in payment, no legal system would prevent him from suing for damages.

25. Mr. NADER (Mexico) said that it would be more appropriate to stipulate interest for non-payment in relation to the unpaid amount only, since one interpretation of article 69(1) would allow for partial payment. Punishment for non-payment should be in proportion to non-compliance.

26. Mr. VIS (Chairman of the Committee of the Whole) said that, if he heard no objection, he would refer article 66(2) and (3), as well as paragraph 12 of document A/CN.9/285, to a drafting group composed of the delegations of Canada, France, Iraq, Kenya, Mexico, the United Kingdom and the United States.

27. *It was so decided.*

#### Article 68(3)

28. Mr. VIS (Chairman of the Committee of the Whole) suggested that, since the problem of *ius tertii* had already been discussed in the context of article 25(3), article 68(3) should stand.

29. *It was so decided.*

#### Article 68(4)(a)

30. Mr. VIS (Chairman of the Committee of the Whole) said that, as explained in paragraph 122 of document A/CN.9/273, the Working Group had decided that a new paragraph (*a bis*) should be included in respect of instruments payable by instalments.

31. Mr. MAEDA (Japan) asked how, when an instrument was payable in instalments by a party other than the drawee,

acceptor or maker, that party could exercise a right of recourse against prior holders in case of partial payments. In order to deal with that difficulty, it might be necessary to add a provision along the lines of article 69(4)(b) to article 68(4) (*a bis*). He would draft such a provision.

#### Article 69(1)

32. Mr. VIS (Chairman of the Committee of the Whole) said that it had been the unanimous view of the Working Group that the holder should not be obliged to take partial payment. It had therefore retained the article in its current form. If he heard no objection, he would take it that the representatives and observers agreed with that view.

33. *It was so decided.*

*The meeting was suspended at 4.30 p.m. and resumed at 5.05 p.m.*

#### Organization of work

34. Mr. VIS (Chairman of the Committee of the Whole) said that the Commission had now completed consideration of the work carried out by the Working Group at its New York and Vienna sessions the previous year. The Commission would consider the texts that it had referred to working groups and drafting groups as they became available.

35. He wished to suggest that, if any delegations had serious reservations regarding articles that had not been considered by the Commission, they should so inform the secretariat, so that the articles could be considered. Delegations were also free to put forward new proposals concerning articles that had already been considered on which there had been differences of opinion. If there were no requests for consideration of articles that had not been discussed, the draft Convention could be considered to be adopted.

36. *It was so decided.*

37. Mr. GANTEN (observer for the Federal Republic of Germany) said that an informal meeting of States parties to the 1930 Geneva Convention providing a Uniform Law for Bills of Exchange and Promissory Notes and the 1930 Geneva Convention for the Settlement of Certain Conflicts of Laws in connection with Bills of Exchange and Promissory Notes and other interested States would be held in the current week to discuss problems that might arise upon adoption of the draft Convention. The following States were parties to these Conventions: Austria, Belgium, Brazil, Denmark, Finland, France, the German Democratic Republic, Greece, Hungary, Italy, Japan, Luxembourg, Monaco, the Netherlands, Norway, Poland, Portugal, the Soviet Union, Sweden and Switzerland, as well as the Federal Republic of Germany.

38. Mr. BERGSTEN (Secretary of the Commission) referring to the question of the relationship between the Geneva Conventions and the draft Convention, said that, if States parties to the Geneva Convention wished to become parties to the draft Convention, they would have to take the necessary action. However, upon reflection they might reach the conclusion that there was in fact no incompatibility between them.

*The meeting rose at 5.35 p.m.*

Summary record of the 347th meeting  
Tuesday, 1 July 1986, 3 p.m.

[A/CN.9/SR.347]

Chairman: Mr. KARTHA (India)

Chairman of the Committee of the Whole:  
Mr. VIS (Netherlands)

The meeting was called to order at 3.10 p.m.

**International payments (continued)**

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes* (continued) (A/CN.9/273, A/CN.9/274 and A/CN.9/285)

*Article 4(10)* (continued)

1. Mr. SPANOGLE (United States of America), speaking also on behalf of the delegation of Canada, proposed that the first sentence in article 4(10) should read: "'Signature' includes a signature by handwriting or a facsimile". That wording would be followed by the definition of "forged signature", which would remain unchanged; article (X) would be deleted.
2. Mr. GANTEN (observer for the Federal Republic of Germany) said that his delegation was not satisfied with the current wording of article 4(10), or with the reservation contained in article (X). He was in favour of the compromise proposal which the representative of the United States of America had just presented.
3. Mr. VIS (Chairman of the Committee of the Whole) inquired whether signature by stamp, which was practised in many countries, would be invalid if the proposal of Canada and the United States was adopted.
4. Mr. SPANOGLE (United States of America) said that, as long as a stamp could be interpreted as representing a facsimile signature, it would be valid.
5. Mr. GUEST (United Kingdom) asked whether the stamp of a bank which was sometimes accompanied by initials, or the Chinese practice of using the *chop* stamp on instruments would be allowable if the Commission adopted the proposal.
6. Mr. GANTEN (observer for the Federal Republic of Germany) said that a stamp would be acceptable if it were a facsimile stamp. Furthermore, although he was not familiar with the Chinese practice, he believed that such stamps could be considered to be facsimile signatures. However, a stamp which bore only the name of a firm would not be sufficient, since it would not provide protection against falsification.
7. Mr. LIU Benku (China) said that, since the practice of using stamps in China was very widespread, China would find it very difficult to accept the proposal.
8. Mr. VIS (Chairman of the Committee of the Whole) asked whether the Chinese stamp replaced a signature and, if so, whether the stamp could be considered to be a facsimile signature.

9. Mr. LIU Benku (China) said that the *chop* stamp could be used to provide facsimile signatures.

10. Mr. VASSEUR (France) said that the definition of "signature" which had just been proposed would be a step backward. He referred to paragraph 10 of document A/CN.9/279, which provided an acceptable definition of signature. The definition proposed by Canada and the United States was too restrictive and was at variance not only with French practice but also with world-wide practice in general.

11. Mr. GRIFFITH (Australia) said that the use of the word "includes" would make the definition inclusive rather than restrictive.

12. Mr. SPANOGLE (United States of America) said that the word "includes" had been carefully chosen as a non-exclusive term. It would be very hard to predict what would be considered an acceptable signature in the twenty-first century. He had intended that express approval should be given to only two varieties of signature, while providing for future changes in legislation and practice.

13. Mr. VIS (Chairman of the Committee of the Whole) asked whether an instrument containing a perforated signature prepared the day after the Convention entered into force, would be acceptable.

14. Mr. SPANOGLE (United States of America) said that such a signature would not be expressly authorized by the definition of "signature" in the proposal. However, given the possibility of changes in legislation and practice, such signatures might become more acceptable in the future.

15. Mr. CRAWFORD (observer for Canada) said that the parties involved in the transaction of international bills of exchange had the right to make inquiries regarding the authenticity of the other endorser's signature. The proposal had been meant not as a step backward but as a compromise which would permit the deletion of article (X).

16. Mrs. ADEBANJO (Nigeria) said that, if the proposal meant that all types of signature would be acceptable, it seemed that the Commission would be retaining article 4(10) without a substantive change in meaning, but would be deleting article (X).

17. Mr. GANTEN (observer for the Federal Republic of Germany) said that, if the proposal allowed for all other kinds of signature, his delegation would not have agreed to it. The word "includes" had been used to make allowances for other forms of handwritten or facsimile signatures, or for something similar to those two means of signature.

18. Mr. SPANOGLE (United States of America) said that the word "includes" had been used to allow for possible changes in legislation or practice. It had been his intention that a facsimile signature should be allowable as a signature regardless of the current legislation in any country which might become a party to the Convention.

19. Mr. SAMI (Iraq) said that his delegation understood that the word "includes" applied to all types of signature, and that

the proposed text was in accordance with the provisions of the Convention which gave all countries the right to apply their national legislation with regard to signatures. If that was the intention of the proposal, his delegation considered article (X) to be superfluous.

20. Mr. CRAWFORD (observer for Canada) said that the actual definition of signature should be limited to a handwritten signature or a facsimile thereof, and that facsimile should be defined.

21. Mr. VIS (Chairman of the Committee of the Whole) suggested that the delegations of Canada, the Federal Republic of Germany, and the United States of America should draft a new text for the consideration of the Commission.

22. *It was so decided.*

#### Article 8(2)

23. Mr. MAEDA (Japan) said that the situation contemplated by article 8(2) was not likely to occur frequently and, in view of the difficulties that the text would create for civil-law countries, he proposed its deletion or revision in order to make its legal effects clearer.

24. Mr. ANGELICI (Italy) supported the Japanese proposal.

25. Mr. GUEST (United Kingdom) said that he was in favour of retaining the current text. The rule was a useful one and should be retained.

26. Mr. VIS (Chairman of the Committee of the Whole) said that, if there was no other support for the Japanese proposal, the existing text should be retained.

27. *It was so decided.*

#### Article 11

28. Mr. ILLESCAS-ORTIZ (Spain) proposed that a paragraph be added to the effect that a holder could complete an instrument only before its maturity. Such an addition would clarify the draft Convention. If an instrument were incomplete upon maturity, it would no longer be a bill of exchange or a promissory note.

29. Mr. VASSEUR (France) said that in France a drawer of a bill of exchange payable on demand often remitted that instrument to a bank for discount. The drawer did not indicate the name of the beneficiary on the instrument and the bank placed its stamp in the place reserved for the beneficiary. He asked whether the Spanish proposal would prevent banks from placing their stamps on the instrument.

30. Mr. VIS (Chairman of the Committee of the Whole) said that under the draft Convention the latest maturity date possible of a demand instrument was one year after the date of issue.

31. Mr. CRAWFORD (observer for Canada) said that the maturity date on a demand instrument was the date on which it was presented for payment.

32. Mr. GRIFFITH (Australia) thought that the proposed addition to article 11 was unnecessary.

33. Mr. DRUEY (observer for Switzerland) said that, if an instrument could be transferred after maturity, it should be possible to complete an instrument after maturity.

34. Mr. VIS (Chairman of the Committee of the Whole) said that, if there were no support for the Spanish proposal, the existing text should be retained.

35. *It was so decided.*

#### Article 28

36. Mr. SPANOGLE (United States of America) said that, in the United States, a holder was presumed to be a holder in due course until such time as a defence was raised; at that time, the burden of proving that he did not have knowledge of the defence would be upon the person claiming the status of holder in due course. If article 28 placed the burden of proving knowledge on a party other than the party wishing to claim lack of knowledge, the article would be conceptually difficult to accept and procedurally almost impossible to apply.

37. Mr. VIS (Chairman of the Committee of the Whole) said that the Working Group had intended the article to mean that, when a party raised a defence or brought a claim, the obligor from whom payment was demanded could rely on his status as a protected holder or on his lack of knowledge of the defence. The claimant would then be required to show that the obligor either knew of the defence or was not a protected holder. Article 28 placed the burden of proof on the person seeking payment.

38. Mr. GUEST (United Kingdom) said that the Bills of Exchange Act of the United Kingdom provided that every holder of an instrument was prima facie deemed to be a holder in due course. That provision created no difficulties and strengthened the negotiability of instruments. He was therefore of the view that article 28 should be retained.

39. Mr. VASSEUR (France) said that French banks attached great importance to article 28. In fact, if that article were deleted, they would urge the French Government not to sign the draft Convention.

40. Mr. SAMI (Iraq) supported the retention of article 28, since it was in conformity with the Iraqi legal system.

41. Mr. ABOUL-ENEIN (observer, Asian-African Legal Consultative Committee) said that article 28 reflected a widely accepted general principle and should therefore be retained in its current form.

42. Mr. SPANOGLE (United States of America) said that he would not insist on his objection.

43. Mr. VIS (Chairman of the Committee of the Whole) suggested that article 28 should be retained.

44. *It was so decided.*

#### Article 34(1)

45. Mr. GANTEN (observer for the Federal Republic of Germany) said that he saw no reason for the inclusion of the word "subsequent" in articles 34(1) or 40(1) and therefore proposed its deletion.

46. Mr. CRAWFORD (observer for Canada) said that the word "subsequent" should be retained in article 40(1), where the endorser engaged to pay all parties subsequent to him but not any party prior to him. It should be deleted from article 34(1): the drawer was the initiator of the instrument and all parties were subsequent in time to him.

47. Mrs. PIAGGI de VANOSI (Argentina) said that she supported the Canadian proposal.

48. Mr. SMART (Sierra Leone) supported the proposal of the observer for the Federal Republic of Germany. The word "subsequent" should, however, be replaced by "prior".

49. Mr. GUEST (United Kingdom) pointed out that paragraph 2 of the commentary on article 34 (1) (A/CN.9/213) was erroneous.

50. Mr. VIS (Chairman of the Committee of the Whole) said that the commentary in question was indeed inaccurate. Deletion of the word "subsequent" might, however, create the danger of including the guarantor of the drawer among the parties who would benefit from the liability of the drawer.

*The meeting was suspended at 4.30 p.m. and resumed at 5 p.m.*

51. Mr. VIS (Chairman of the Committee of the Whole) suggested that, in order to protect a possible guarantor of an endorser, the words "subsequent party" in article 34(1) should be replaced by the words "endorser or the endorser's guarantor". The wording would also be changed in articles 35(1) and 40(1).

52. Mr. VASSEUR (France) said that it would be clearer to say "or to any subsequent party liable".

53. Mr. VIS (Chairman of the Committee of the Whole) said that such a wording would require a change in the meaning of the term "party" as defined in article 4(8).

54. Mr. GUEST (United Kingdom) expressed support for the Chairman's proposal with regard to the change in articles 34 and 35. In article 40(1), however, the concept of subsequent endorser should be retained.

55. Mr. VIS (Chairman of the Committee of the Whole) agreed to that suggestion. If he heard no objection, he would take it that his proposal regarding articles 34(1) and 35(1) was accepted.

56. *It was so decided.*

#### *Article 38(1)*

57. Mr. GANTEN (observer for the Federal Republic of Germany) said that the incomplete instrument referred to in article 38(1) was not the same as that defined in article 11(2), because the latter did not apply in the case of an incomplete instrument which was accepted before it had been signed. Article 38(1) should be amended to refer to article 11(2) and to state that it would apply.

58. Mr. VIS (Chairman of the Committee of the Whole) said that article 38 did appear to be inconsistent with article 11: under article 38, acceptance would take place before the instru-

ment had been completed, whereas under article 11 the instrument could be completed only if it had been signed by the drawer.

59. Mr. GUEST (United Kingdom) said that the problem appeared to be a mere technicality. In a situation where the drawer had not signed the instrument and it was then accepted by another party, it was not deemed to be an instrument under the Convention. Article 38 made acceptance valid in such a situation. An entirely different situation arose in the case where incomplete instruments signed by a drawer could be accepted without completion.

60. Mr. GANTEN (observer for the Federal Republic of Germany) said that he withdrew his objection because it had become clear to him that the incomplete instrument referred to in article 38 was not the same as that defined in article 11.

61. Mr. DRUEY (observer for Switzerland) regretted that the observer for the Federal Republic of Germany had withdrawn his proposal, because it seemed that there was a problem of substance. Frequently the acceptance was sought before the drawer had signed the instrument, and the acceptor had to be protected as well as the drawer. He therefore felt that the application of article 11(2) to such a situation was a valuable suggestion.

62. Mr. MACCARONE (observer, European Banking Federation) said that article 38 was intended to provide for the possibility of acceptance before the instrument was issued. Article 11 therefore had nothing to do with article 38. Perhaps the word "incomplete" was misleading. In article 11, the term "incomplete instrument" was a legal term, whereas in the situation covered by article 38 the instrument was actually incomplete.

63. Mr. VIS (Chairman of the Committee of the Whole) said that article 11 was, however, important in determining the liability of the acceptor if the instrument was completed after he had accepted it in an unauthorized manner.

64. Mr. MACCARONE (observer, European Banking Federation) said that that was the risk involved in signing an instrument before the existence of the instrument itself—a risk of which the acceptor was well aware.

65. Mr. VIS (Chairman of the Committee of the Whole) said that article 11 was therefore relevant in the context of article 38(1).

66. Mr. SPANOGLE (United States of America) thought that it might be advisable to refer the matter to a drafting group.

67. Mr. GUEST (United Kingdom) believed that article 38(1) should be left as it stood.

68. Mr. VIS (Chairman of the Committee of the Whole) said that, if he heard no objection, he would take it that the Committee wished to leave article 38(1) as it stood.

69. *It was so decided.*

#### *Article 4(10) (continued)*

70. Mr. VIS (Chairman of the Committee of the Whole) said that the delegations of Canada, the Federal Republic of



Germany and the United States of America had proposed that the article should be amended to read:

“‘Signature’ includes a handwritten signature, or a facsimile thereof, or any other means of effecting the equivalent authentication, and ‘forged signature’ includes a signature by the wrongful or unauthorized use of such means;”.

71. Mr. VASSEUR (France) said that he wished to make it clear that he considered the words “or any other means” as meaning “or any other non-handwritten means”.

72. Mr. DRUEY (observer for Switzerland) and Ms. BUURE-HAGGLUND (observer for Finland) said that they supported the proposed new wording.

73. Mr. CRAWFORD (observer for Canada), responding to a point raised by the observer for the Latin American Banking Federation concerning the possible validation of SWIFT messages under the draft Convention, said that such messages would be unlikely to qualify as instruments under the draft Convention because of the type of text involved, not because the signature in question might not qualify.

74. Mr. MACCARONE (observer, European Banking Federation), referring to the point raised by the observer for the Latin American Banking Federation, said that the issue in question had already been dealt with in the latest version of the Uniform Customs and Practice for Documentary Credits.

75. Mr. LIU Benku (China) and Mr. GUEST (United Kingdom) supported the proposed new wording.

76. Mr. GANTEN (observer for the Federal Republic of Germany), responding to a point raised by the representative of Australia concerning signatures in the form of a seal or in the form of a stamp or an impression of a seal, said that it was currently impossible to state exactly what would be covered by the draft Convention. The purpose of the proposed wording was to leave open the possibility of new inventions. The courts, the parties themselves or domestic law would have to determine exactly what was to be covered by the draft Convention.

77. Mr. GRIFFITH (Australia) said that, having heard the explanation provided by the observer for the Federal Republic of Germany, he was now in a position to say that he supported the proposed new wording.

78. Mrs. ADEBANJO (Nigeria) said that the proposed text constituted an improvement.

79. Mr. VIS (Chairman of the Committee of the Whole) said that, if he heard no objection, he would take it that the Committee wished to adopt the new wording for article 4(10) proposed by Canada, the Federal Republic of Germany and the United States of America, and to delete article X.

80. *It was so decided.*

*The meeting rose at 6 p.m.*

### Summary record of the 348th meeting Wednesday, 2 July 1986, 10 a.m.

[A/CN.9/SR.348]

*Chairman:* Mr. KARTHA (India)

*Chairman of the Committee of the Whole:*  
Mr. VIS (Netherlands)

*The meeting was called to order at 10.15 a.m.*

#### International payments (continued)

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes* (continued) (A/CN.9/213, A/CN.9/269, A/CN.9/273, A/CN.9/274 and A/CN.9/285 and A/39/17)

#### Article 38(1) (continued)

1. Mr. DRUEY (observer for Switzerland) said that article 38(1) raised two problems: one of substance and one of drafting. With respect to the former, he suggested that article 11(2) should protect the drawee as well as the drawer. An incomplete instrument—one that had not yet been signed by A, the drawer—might be presented to B, the drawee (a bank with which A had an account), in which case the drawee would have no hesitation in accepting the bill. However, subsequently,

another person—an employee of A, having no credit or account with the drawee—might sign the bill thereby becoming the drawer. The instrument might also be incomplete because the sum was not stated. With respect to the drafting problem, he pointed out that the phrase “incomplete instrument” had a different meaning in article 38(1) from the one it had in article 11(1).

2. Both problems could be solved by amending article 11(1) to read: “An incomplete instrument which satisfies the requirements set out in subparagraph (a) of paragraph (2) of article 1 and bears the signature of the drawer or drawee, or subparagraphs (a) and (f) of paragraph (3) of article 1 ...”.

3. Mr. MACCARONE (observer, European Banking Federation) said he could not accept the proposal: only the drawer could create the instrument. His signature was one of the requirements listed in article 1. To suggest that an incomplete instrument could be one that was signed only by the drawee was theoretically incorrect, for under those circumstances there was no instrument.

4. Mr. SMART (Sierra Leone) said that he agreed, although he had sympathy with the argument put forward by the observer for Switzerland. If the drawee accepted a bill that did not bear the drawer’s signature, that was his responsibility.

5. Mr. GANTEN (observer for the Federal Republic of Germany) supported the proposal of Switzerland. The point made by the observer for the European Banking Federation might be correct in the abstract, but was not in line with what happened in practice. It was not uncommon for a drawee to accept an instrument which was not signed by the drawer, and the Convention should take account of that practice. The problem could be dealt with by amending article 38(1) along the lines he had suggested the previous day; however, he preferred the proposal just put forward.

6. Mr. ABASCAL (Mexico) likewise supported the Swiss proposal and for the same reason. He suggested that, instead of mentioning the "drawee", the Convention should refer to the "acceptor", since by signing an instrument the drawee was accepting it.

7. Mr. PISEK (Czechoslovakia) said that an incomplete instrument was simply one in which some of the elements set out in article 1 were missing. There was no need to specify which ones. In his view, "incomplete" could have a different meaning in article 11 and in article 38.

8. Mr. SAMI (Iraq) said that the Swiss proposal would be in complete conflict with the legal system in his country, where a bill of exchange could be created only by a drawer. Article 11 should remain as it was.

9. Mr. ANGELICI (Italy) said that the drawee should be protected and such protection must be furnished under article 11. He supported the substance of the Swiss proposal, although he felt that it might be worded somewhat differently.

10. Mr. EYZAGUIRRE (Chile) supported the Swiss amendment, which was consistent with the practice in Chile.

11. Mr. DUCHEK (Austria) said that he supported the substance of the Swiss proposal.

12. Mr. GUEST (United Kingdom) said that he would be willing to accept the proposal.

13. Mr. VIS (Chairman of the Committee of the Whole), speaking as representative of the Netherlands, said that he would still require that there be the signature of the drawer. That might be an academic question because, clearly, there could not be an international bill of exchange until the bill was signed by the drawer. However, he would like to look very carefully at the Swiss proposal to determine whether it applied only to the case referred to in article 38(1).

14. Speaking as Chairman of the Committee of the Whole, he said that the original purpose of article 38(1) had been to state the rule that a drawee could validly accept a bill before it was signed by the drawer. One member of the Working Group had said that in such a case the bill would be an incomplete instrument. It had never been the intention that article 11 should state the rule, as implied by the observer for Switzerland, that the drawee could create an inchoate international instrument.

15. From the statements he had heard, he concluded that there was support for the Swiss proposal. Accordingly, he noted that the Commission accepted the amendment and asked that a precise text be submitted in writing.

#### Article 48

16. Mr. SPANOGLE (United States of America) said that he would like article 48 to make some provision for delay, as existed in articles 52(1), 58(1) and 63(1). Instead of saying that, if there was delay in the presentment for acceptance, such presentment was dispensed with, it might be more useful to require presentment to be made, even if it were made later than specified in the bill. Alternatively, he would like to know the reason for the difference compared with the other three articles.

17. Mr. VIS (Chairman of the Committee of the Whole) pointed out that, in the case of a bill payable, for example, 30 days after sight, article 47(e) required that such a bill be presented within one year of the date of issue. As currently drafted, article 48 would require that, if for any reason the bill could not be presented for acceptance within that time-limit, it should be regarded as dishonoured by non-acceptance; that would trigger a recourse action. According to the suggestion being made by the representative of the United States, if such a bill could not be presented within one year, the holder would not have an immediate valid recourse.

18. Mr. SPANOGLE (United States of America) said that the drawee—a bank, for example—would normally need some notice if an instrument was to be submitted for payment in another currency or in an exceptionally large amount. It would be desirable for such instruments to be brought in for sight first, and paid later.

19. Mr. VIS (Chairman of the Committee of the Whole) said that, if one year had already elapsed since the date of issue of an instrument, it did not seem that it should be necessary to wait longer. If, for example, it was not possible to present a bill for payment because a war was being waged, it was surely reasonable that after one year the bill should be considered to be dishonoured and payable by the drawer. The same applied in the case of a bill payable on a fixed date; under the draft Convention, the bill could be presented for acceptance up to that date; if it was not presented, it would be payable at maturity.

20. Mr. SPANOGLE (United States of America) said that it was disturbing that, in a situation where a drawee might be able to perform, the fact that the holder did not approach the drawee gave rise to rights against the drawer. He felt that the drawer's contract underlying an instrument was that an attempt would be made to secure payment from the drawee first; it was unsatisfactory that, if the drawee could not be reached, the drawer should have to pay.

21. Mr. VIS (Chairman of the Committee of the Whole) said that that situation prevailed in all legal systems. Presentment for acceptance was optional and, if the bill could not be presented, the drawer became liable.

22. Mr. SAMI (Iraq) said that his delegation supported the view that the wording used in article 52(1) should be incorporated in article 48, paragraph (b). The wording of article 52 was specific and clear to everyone but article 48 left room for numerous interpretations.

23. Mr. VIS (Chairman of the Committee of the Whole) said that it should be noted that, if there was not due presentment for payment, parties that were secondarily liable were discharged. A provision excusing delay was therefore necessary.

24. Mr. SPANOGLE (United States of America) said it was anomalous that in the case of a bill with a time-limit, if the holder was unable for reasons beyond his control to get to a bank until just after the expiry of the time-limit, under the draft Convention he would be able to go back to the immediate endorser, as well as the drawer.

25. Mr. EYZAGUIRRE (Chile) said that his delegation fully supported the current wording of article 48. It was not always mandatory for a bill to be submitted for acceptance; he felt that the one-year time-limit laid down in article 47(e) was reasonable, otherwise acceptance and payment could become confused. He saw no incongruity between article 48 and other articles of the draft Convention. The situations referred to in articles 52 and 58 were quite different, and were unconnected with the obligation to present a bill for acceptance, as they were concerned with delay in presentment for payment and delays in protesting. From the point of view of the Chilean legal system, article 48 was quite reasonable and balanced.

26. Mr. ANGELICI (Italy) said that the use of different wording in article 48 and article 52 could give rise to uncertainties of interpretation and possibly lead to the conclusion that subjective criteria were to be followed in article 48 and objective criteria in article 52.

27. He therefore suggested that article 48, paragraph (b), should read: "When, because of circumstances which are beyond the control of the holder and which he could neither avoid nor overcome, presentment cannot be effected within the time-limits prescribed for presentment for acceptance."

28. Mr. SAMI (Iraq) said that the Italian proposal was very logical and reasonable; objective criteria needed to be followed in article 48.

29. Mr. ILLESCAS-ORTIZ (Spain) and Mr. DELFINO-CAZET (Uruguay) said that they supported the Italian proposal, as it made the draft Convention more secure.

30. Mr. GRIFFITH (Australia) said that he preferred the existing text; it was simple and straightforward and reflected the English and Australian legislation on bills of exchange. It was not necessarily desirable for the text to mention whether or not circumstances had been beyond the control of a holder or could have been avoided or overcome.

31. Mr. VENKATRAMIAH (India) and Mr. GOH (Singapore) said that they supported the existing text of article 48, paragraph (b).

32. Mr. GUEST (United Kingdom) said that he supported the existing text of article 48. The words "with reasonable diligence" were used in articles 58 and 63, and it would be difficult at such a late stage to start inserting provisions which were more elaborate.

33. Mr. DUCHEK (Austria) said that it was not clear from the commentary (A/CN.9/213) why in comparable situations an objective test was used in article 52, and a subjective test in article 48. The same test should be used in both cases, and an objective test was always better than a subjective one. He therefore supported the Italian proposal.

34. Mr. VIS (Chairman of the Committee of the Whole) said that the Working Group had always considered that present-

ment for acceptance was different from presentment for payment, and that different criteria should apply.

35. Mr. SMART (Sierra Leone) said that his delegation supported the existing text; it was simple and straightforward, and conformed with Sierra Leone's legal system.

36. Mr. VIS (Chairman of the Committee of the Whole) said that it was undesirable for the Commission to split into two camps corresponding to civil-law and common-law countries. A provision should not be rejected because it did not accord with individual national law.

37. Mr. DRUEY (observer for Switzerland) said that, in the example mentioned by the representative of the United Kingdom, articles 58 and 63 both contained the wording found in article 52(1). There was always an objective criterion in a case where something should have been done and had not been done. "Reasonable diligence" applied where a cause of delay ceased to operate, as in article 52(1). Presentment for acceptance was a case where something had to be done. He therefore supported the Italian proposal.

38. Mr. VIS (Chairman of the Committee of the Whole) noted that the Geneva Convention used the term "without delay"; the term "reasonable diligence" came very close to that concept.

*The meeting was suspended at 11.35 a.m. and resumed  
at 12.20 p.m.*

39. Mr. GUEST (United Kingdom) said that the articles in question had been discussed extensively by the Working Group and he hoped to preserve the existing text. He understood the reasons for the United States proposal, and it was difficult to justify the omission in article 48 of a paragraph similar to that in article 52(1). The rule in articles 48 and 50(1) could, indeed, be harsh in some circumstances, but it was justifiable because it prevented the prolongation of the one-year period beyond the date on the bill. The United States proposal might have some virtue with regard to the time-limit in article 47(f). Even there, it was questionable whether it was necessary to cover a very exceptional situation in which the drawer stipulated that a bill must be accepted within a short time-limit.

40. He had difficulty with the proposal of the representative of Italy, which would require changes not only in article 48(b) but also in article 50(1) and possibly article 63(2)(a). He supported the requirement of reasonable diligence in the existing text of article 48(b) because it covered two situations: one involving a *force majeure* impediment and one in which, for instance, the drawee, or the endorser to whom notice of dishonour must be given, could not be traced. It would be difficult to bring the latter situation within a case of *force majeure*. He hoped it would be possible to adopt article 48 as it stood.

41. Mr. SPANOGLE (United States of America) proposed an amendment incorporating his own points as well as the proposal of the representative of Italy. The following new article 48(i) would be added:

"Delay in making a necessary presentment for acceptance within a time-limit specified in the instrument is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor

overcome. When the cause of the delay ceases to operate, presentment must be made with reasonable diligence.”

42. The current article 48 would then become article 48(2) and subparagraph (b) would be amended to read:

“(b) When a necessary presentment for acceptance cannot be effected within the time-limits prescribed in article 47 owing to circumstances which are beyond the control of the holder and which he could neither avoid nor overcome.”

43. Thus, his proposed article 48(1) would apply only to necessary presentments and only when a time-limit, assumed to be shorter than the statutory time-limit, was specified in the instrument itself. Article 48(2)(b) would apply when no time-limit had been stated in the bill itself and consequently the statutory one-year period applied—a very long period indeed, to his way of thinking—and when presentment could not be effected because of *force majeure* defined in the terms suggested by the representative of Italy. If neither article 48(1) or (2)(b) applied, then article 49 would come into play.

44. It was important to separate the two different situations: one where the bill itself specified a short time-limit and one where the full one-year limit was available. In the former case, a binary formulation was not desirable and therefore his text introduced gradations that did not overstate the effects of a late presentment. In the latter case, the Italian proposal made perfectly good sense.

45. Mr. ANGELICI (Italy) said that he supported the United States amendment.

46. Mr. VASSEUR (France) said that although it was late to be introducing such complications, he was ready to support the United States proposal provided the text was carefully drafted. His delegation would like to be able to study the proposal in French translation.

47. Mr. CHAFIK (Egypt) said that the United States proposal seemed acceptable but needed detailed study. He would like to see the proposal in writing.

48. Mr. EYZAGUIRRE (Chile) insisted that the wording of article 48 adequately reflected the intent of the article, which was to exempt the holder of an instrument from presentment for acceptance. The article had nothing to do with delay in presentment for payment or in presentment for protest. Consequently, he did not believe that the text should be amended.

49. Mr. VIS (Chairman of the Committee of the Whole), speaking as the representative of the Netherlands, endorsed the remarks made by the representative of Chile. If a drawer included on an instrument the stipulation that it must be presented for acceptance within 30 days and the holder of the instrument failed to present it, the drawer was then free of any liability in the matter. However, the article should clearly indicate that, if circumstances prevented the holder from presenting the instrument for acceptance, the drawer remained liable, as the important issue was the drawer's liability.

50. Speaking as the Chairman of the Committee of the Whole, he suggested that further discussion of the article in question should be deferred until the text of the proposals made by the

representative of the United States was available in written form.

51. *It was so decided.*

#### Article 71

52. Mr. SPANOGLE (United States of America) said that article 71 might pose a problem for small banks which, while not located in a money centre, nevertheless engaged in international transactions and received instruments from foreign jurisdictions. The problem would arise when an instrument drawn payable in a foreign currency was submitted for payment in that currency and the bank to which it had been submitted did not have access to that currency in the amount requested. The problem could be solved either by requiring that the holder should notify the bank in advance that payment was desired in a currency other than that of the place of payment, or by including in the draft Convention a provision which would give a bank three days in which to acquire the currency requested without dishonouring the bill.

53. Mr. GUEST (United Kingdom) said that the problem was not a serious one. In any event, it was the responsibility of the seller or the maker of the note to see that the necessary arrangements for payment were made.

54. Mr. SPANOGLE (United States of America) said he was thinking of the “contrived dishonour” of an instrument. It was conceivable that a holder or payee might wish to dishonour an instrument through the use of a surprise tactic such as requesting payment in the currency originally specified on the instrument, when it was obvious that the currency was unobtainable. Such an action would create a serious problem for the obligor.

55. Mrs. PIAGGI de VANOSI (Argentina) agreed that the situation described by the representative of the United States might occur. However, the solution lay in requesting the holder to give advance notice to the bank that the payment was required in foreign currency, as was done under Argentine domestic legislation. Under those circumstances, it would be impossible for an instrument to be dishonoured.

56. Mr. VASSEUR (France) said that a situation such as the one described by the representative of the United States was unheard of. Even if such a situation should occur, it was not the purpose of the draft Convention to deal with the matter in such detail; such matters were better dealt with outside the context of the Convention. The issues covered in article 71 were extremely complicated, and it would not be advisable to add to their complexity.

57. Mr. VIS (Chairman of the Committee of the Whole) drew attention to article 41 of the Geneva Uniform Law for Bills of Exchange and Promissory Notes, concerning stipulations for effective payment in foreign currency. A similar provision was to be found in the Uniform Commercial Code of the United States of America. He therefore did not believe it was necessary to include more detailed provisions in the draft Convention, and inquired whether the representative of the United States wished to press his point.

58. Mr. SPANOGLE (United States of America) said that, as his point had received little support from other members of the Commission, he would not insist on it.

**Summary record of the 349th meeting  
Wednesday, 2 July 1986, 3 p.m.**

[A/CN.9/SR.349]

*Chairman:* Mr. KARTHA (India)

*Chairman of the Committee of the Whole:*  
Mr. VIS (Netherlands)

*The meeting was called to order at 3.15 p.m.*

**International payments (continued)**

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes (continued)* (A/39/17; A/CN.9/261, A/CN.9/273, A/CN.9/274 and A/CN.9/285; A/CN.9/WG.IV/WP.30)

*Article 71 (continued)*

1. Mr. SPANOGLE (United States of America) observed in connection with his proposal concerning article 71(2) that in the United States it was not possible to have a foreign currency account on-shore. Such accounts must be offshore and obtaining foreign currency from an offshore source could take two to three days. He was therefore concerned that the Convention might be used to put forward a contrived disowner. He agreed with the representative of Argentina that, if a payee wanted currency rather than credit, he would have to give advance notice so that the bank could obtain such currency without that giving rise to a disowner.
2. Mr. VIS (Chairman of the Committee of the Whole) observed that, according to article 45(2)(c), the drawee must be informed if a bill was to be drawn payable elsewhere than at his place of residence or business, so that he could obtain the necessary funds. A similar procedure could be followed with regard to bills to be paid in a foreign currency. The best approach might be to add a new paragraph to that effect in article 45. He first wished to know, however, whether other members saw a practical need for advising the drawee if a bill was to be drawn in a foreign currency.
3. Mr. GRIFFITH (Australia) said that he saw no need for giving drawees advance notice if bills were to be drawn in foreign currency.
4. Mr. CRAWFORD (observer for Canada) said that requesting that a bill be paid in a foreign currency would not create any problem in Canadian banking circles. In the United States, however, there were many banks which did not have the resources to effect such transactions without notice.
5. Mr. ABOUL ENEIN (observer, Asian-African Legal Consultative Committee) said that he could support the United States proposal, as amended by the representative of Argentina, since it responded to a practical need.
6. Mr. SAMI (Iraq) said that he had no problem with the United States proposal.
7. Mr. MACCARONE (observer, European Banking Federation) observed that, because of exchange control regulations, it was quite common in some countries for drawees to be unable to

pay in foreign currency without the authority of the competent domestic body. Prior notice as proposed by the United States would therefore be necessary.

8. Mr. VIS (Chairman of the Committee of the Whole) observed that, if the Commission agreed that such advance notice was required, it must now determine how long the period of notice must be and should also consider what would happen if such notice was not given. Finally, it should consider what would happen if in such cases a bill was dishonoured and created a right of recourse against a secondary party in accordance with article 71.

*Article 72*

9. MR. GANTEN (observer for the Federal Republic of Germany) said that he wished to propose the addition of the words "and provisions relating to the protection of its currency" after the words "exchange control regulations" in article 72(1). In many countries, making out bills in a foreign currency could create problems with regard not only to exchange control regulations but also to domestic laws on protection of the national currency, such as that in force in his country.

10. Mr. CHAFIK (Egypt) said that Egypt also had a domestic currency law and he therefore supported the proposal by the observer for the Federal Republic of Germany.

11. Mr. VIS (Chairman of the Committee of the Whole) said that, if he heard no objection, he would take it that the Commission decided to adopt the proposal by the observer for the Federal Republic of Germany.

12. *It was so decided.*

13. Mr. EFFROS (observer, International Monetary Fund) proposed the insertion in article 72(1), after the words "bound to apply", of the words "or may be taken into consideration," so as to extend the principle set forth in article 72(1) to permissive and not just mandatory situations and make it clear that members of the International Monetary Fund could implement the relevant provisions of the Fund Agreement or other similar international agreements concerning the implementation of other countries' exchange control regulations. There were some international agreements which did not require States parties to comply with other countries' exchange control regulations, and the Convention should make it clear that it was not eliminating the freedom of the courts to decide whether or not a country should apply another country's exchange control regulations.

14. Mr. VIS (Chairman of the Committee of the Whole) asked whether there were in fact any international agreements which gave States parties the option whether or not to apply other countries' exchange control regulations.

15. Mr. EFFROS (observer, International Monetary Fund) said that under article 10 of the 1930 Geneva Convention on conflicts of law, the law of non-signatory States would not apply.

16. Mr. PELICHET (observer, Hague Conference on Private International Law) said that the proposal by the observer for the International Monetary Fund referred to the mandatory rules of third States, which were acquiring increasing importance in conflicts of law. Article 7 of the Rome Convention allowed

judges to take the mandatory rules of third States into consideration, and the proposal by the International Monetary Fund was in fact following the evolution of international private law. Article 72 should take into consideration international conventions which allowed judges to take mandatory rules of third States into account in order to cover all possible currency exchange situations. He therefore supported the proposal.

17. Mr. VASSEUR (France) said that he too, for the same reasons, supported the proposal by the observer for the International Monetary Fund.

18. Mr. VIS (Chairman of the Committee of the Whole) said that, if the country of the place of payment was a party to a convention which included that optional element, that would create uncertainty. The Commission must therefore take a policy decision as to whether, unless a State was actually bound to apply other States' exchange control regulations, it must or must not take them into consideration.

19. Mr. DUCHEK (Austria) said that the option to take such regulations into account derived not from domestic law but from international agreements. He agreed with the Chairman that the practical implications of the proposal under consideration were not clear. In any case, what was meant by international agreements? The Rome Convention did not apply to bills of exchange and he did not see how the 1930 Geneva Convention on conflicts of law could cover that situation. Besides, most of the provisions of the draft Convention conflicted with the 1930 Geneva Convention, and aligning the two conventions as proposed in the present instance was not going to alter that situation significantly. It was the 1930 Geneva Convention that required changing not the draft Convention. He did not agree that there was an international trend towards taking account of the mandatory rules of third States. The Hague Conference had in fact decided in 1985 that such an approach was not appropriate.

20. Mrs. BUURE-HAGGLUND (observer for Finland) said that she shared Austria's hesitation to accept such an amendment in view of the dispute over article 7 of the Rome Convention allowing the application of mandatory rules of a third State and its rejection at the Hague Conference on Private International Law. It was generally accepted that the mandatory rules of the forum could be applied in addition to the law applicable otherwise, which was in keeping with the current draft. If the amendment was accepted, the phrase "applicable in its territory" would have to be changed.

21. Mr. ANGELICI (Italy) said that a distinction must be drawn between the concepts "to apply" and "to take into consideration" in private international law, and reference must be made to both. For the sake of certainty, it would be preferable to say that the State "must" take into consideration the exchange control regulations which it was bound to apply by virtue of international agreements to which it was a party.

22. Mr. MARTYNOV (Union of Soviet Socialist Republics) said that the proposal of Austria and Finland would lead to uncertainty. Moreover, mandatory rules had not yet achieved international recognition and had been rejected by most States at the Hague Conference.

23. Mr. VIS (Chairman of the Committee of the Whole) said that, in view of the general lack of support for the proposal of the International Monetary Fund, he would take it that it was

not accepted. In that case, perhaps the representative of Italy would withdraw his proposed amendment.

24. Mr. ANGELICI (Italy) said that he would do so.

25. Mr. VIS (Chairman of the Committee of the Whole) asked whether the International Monetary Fund would have problems with the current wording.

26. Mr. EFFROS (observer, International Monetary Fund) said that his chief concern had been to make the provision more inclusive.

#### *Article 73(2)*

27. Mr. MAEDA (Japan) said that he was concerned about the appropriateness of the current wording. It was necessary to add, at the end of the article, a provision similar to that contained in article 68(3), which would read as follows: "except where the drawee pays a holder who is not a protected holder and knows at the time of payment that a third person has asserted a valid claim to the instrument or that the holder acquired the instrument by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery".

28. Mr. VIS (Chairman of the Committee of the Whole) asked whether it was not obvious that article 68(3) applied.

29. Mr. MAEDA (Japan) said that the addition was necessary because, according to article 73(2), payment by the drawee discharged all parties of their liability. However, payment by a drawee who had knowledge of theft did not discharge all parties.

30. Mr. SPANOGLE (United States of America) said it appeared that the representative of Japan had made a good point, in that article 68(3) did not cover the same ground in respect of the discharge of the drawee, because it was limited to the "party", as defined in article 4(8). Unless the drawee had accepted the instrument before payment, he would not have signed it and therefore would not be a party to it. Article 73(2) therefore needed to be modified for the sake of consistency.

31. Mr. VIS (Chairman of the Committee of the Whole) said that the original draft of article 68 had contained a reference to the drawee. Since the drawee had no liability, however, the decision had been made not to include him in that article. Consequently, the drawee must be covered in article 73(2).

32. Mr. SAMI (Iraq) said that it would be preferable to include a reference to the drawee in article 68(3).

33. Mr. VIS (Chairman of the Committee of the Whole) said that it was not possible to do so because the drawee could not be discharged, having no liability.

34. Mr. VASSEUR (France) said that he supported Iraq's suggestion because it would clarify the situation.

35. Mr. VIS (Chairman of the Committee of the Whole) asked how the article would then be drafted.

36. Mr. CHAFIK (Egypt) said that he did not agree with Japan because there was a great difference between the situation in article 73(2) and that in article 68(3). In the latter, it was a question of the party's being discharged if he paid, and not being discharged if he did not, while in article 73(2), the drawee paid and the other parties were discharged.

37. Mr. VIS (Chairman of the Committee of the Whole) said that, if the drawee paid in the circumstances of article 68(3), i.e., improperly, the consequence was that he was not allowed to debit the account of the drawer, and the drawer was not discharged. In his view, it was a question of proper payment. The Working Group had always maintained, however, that article 68(3) was not concerned with payment by the drawee.

38. Mr. CHAFIK (Egypt) said that, in article 73, the drawee was not discharged; rather, the other parties were discharged, even if payment was made improperly.

39. Mr. VASSEUR (France) said that the wording of article 68(3) could be changed to read: "a party does not pay validly if he pays a holder who is not a protected holder and knows at the time of payment, etc."

40. Mr. VIS (Chairman of the Committee of the Whole) said that that would require a definition of the term "validly".

41. Mr. CHAFIK (Egypt) said that the current text should stand, because the question was whether the drawee had paid in good faith. The whole point of article 73 was that the other parties were not liable.

42. Mr. ILLESCAS-ORTIZ (Spain) said that the proposal by the representative of Japan perhaps went too far. Improper payment by the drawee and improper collection of the instrument should have no effect on the liability of intermediate holders.

43. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that, in drafting article 73, the Working Group had based itself on the principle that the drawer and drawee were guarantors and were discharged of liability only if there was no protest. If the payee was paid, it did not matter whether the payment had been proper or improper. Perhaps there had been an inadvertent omission in the wording of the paragraph, which had led to confusion.

44. Mr. VIS (Chairman of the Committee of the Whole) said that he tended to agree with the representative of Japan. Article 73(2) seemed to be an application of the principle laid down in article 73(1). If the drawee paid in suspicious circumstances, the drawer was not discharged.

45. Mr. CHAFIK (Egypt) said that he did not agree that article 73(2) was merely an application of article 73(1). Article 73(2) meant that, whether the drawee paid properly or not, the other parties were discharged. The drawer remained liable under article 68(3). There was thus no relationship between articles 73(1) and 73(2).

46. Mr. VIS (Chairman of the Committee of the Whole) said that, in his view, the mere fact of payment by the drawee did not automatically discharge the other parties. If the drawee paid to a non-holder, for example, the other parties were not discharged.

47. Mr. DRUEY (observer for Switzerland), Mr. ANGELICI (Italy), Mr. SEVON (observer for Finland), Mr. GRIFFITH (Australia), Mr. SMART (Sierra Leone), Mr. SPANOGLA (United States of America), Mrs. PIAGGI de VANOSI (Argentina), Mr. KOCH (Sweden) and Mr. CHAFIK (Egypt) supported the amendment proposed by the representative of Japan.

48. *Article 73(2), as amended by the representative of Japan, was adopted.*

*The meeting was suspended at 4.45 p.m. and resumed at 5.20 p.m.*

#### *Article 80(1)(c)*

49. Mr. GANTEN (observer for the Federal Republic of Germany) said that the rule contained in article 80(1)(c) would be straightforward if a date was inserted on the bill. A problem arose, however, where the acceptor, when accepting the bill, did not insert the date, since such acceptance, even without a date, would constitute acceptance under the provisions of article 37. There was therefore need to amend the provision by determining the date from which prescription was to be calculated. It would be preferable to take the date on which the instrument was drawn, and he therefore wished to suggest the addition of the following text to article 80(1)(c): "or, in case no such date is shown, from the date of the instrument;"

50. Mr. SAMI (Iraq) said that bills were payable upon presentation to the drawee, and were presented for payment and not for acceptance.

51. Mr. VIS (Chairman of the Committee of the Whole) said that, while he too was of the view that the holder of a demand bill was entitled only to payment and not to acceptance, the Working Group had decided that a demand bill could be presented for acceptance within one year of the date of its issue. If article 80(1)(c) was removed, then the possibility of a bill payable on demand being accepted must also be removed.

52. If he heard no objection, he would take it that the Commission wished to accept the proposal of the observer for the Federal Republic of Germany.

53. *It was so decided.*

#### *Articles 4(7)(a) and 25(1)(c)*

54. Mr. CRAWFORD (observer for Canada) said that on behalf of the *ad hoc* working party composed of the representatives of Canada, Egypt, Japan, Mexico, Nigeria and the United Kingdom, he wished to propose that, in article 4(7)(a), the words "other than in paragraph 25(1)(c)(ii)" should be inserted after the reference to article 25, and that article 25(1)(c) should be amended to read:

"(c) Any defence resulting from:

- (i) the underlying transaction between himself and the holder;
- (ii) any other transaction between himself and the holder that would be available as a defence against contractual liability."

The latter proposal sought to clarify the extent to which relations between parties might be used to set up defences to liability under the instrument.

55. Mr. HERRMANN (International Trade Law Branch) said that the proposal sought to implement a substantive decision of the Commission to provide for a rule under which a holder might become a protected holder although he had knowledge of a defence arising from the underlying transaction between himself and the immediate party. In order to achieve that goal in

article 4(7)(a), it had been necessary to split the provisions contained in article 25(1)(c), which did not distinguish between the underlying transaction and other transactions.

56. Mr. SPANOGLE (United States of America) said that it was his understanding that a number of representatives had difficulty with the inclusion in article 4(7)(a) of any reference to article 25. The word "parties" was used in articles 4 and 25 for different purposes. It had been his understanding that the Commission would arrive at a definition of protected holder which spelt out the defences for which knowledge was important, not by cross-reference but by direct statement.

57. Mr. HERRMANN (International Trade Law Branch) said that the *ad hoc* working party had come to the conclusion that it would be impossible to avoid the reference to article 25 in article 4(7)(a).

58. Mr. VASSEUR (France) pointed out that, in the French version of the proposed wording of article 25(1)(c)(ii), the word *transaction* should be replaced by *opération*.

59. Mr. ILLESCAS-ORTIZ (Spain), referring to the Spanish version of the proposed wording of article 4(7)(a), said that the phrase should be eliminated because, in Spanish, "non-acceptance or non-payment" contained the concept of "dishonour".

60. Mr. BERGSTEN (Secretary of the Commission) said that the general drafting group would examine the translations of the texts of proposals contained in conference room papers.

61. *Articles 4(7) and 25(1)(c), as amended, were adopted.*

*Articles 4(11) and 71(1)(bis) (A/CN.9/XIX/CRP.3)*

62. Mr. CRAWFORD (observer for Canada) said that an *ad hoc* working party composed of the representatives of Czechoslovakia and Nigeria and the observers for Canada and the International Monetary Fund had proposed that the following text should be added to the end of article 4(11):

"provided that this Convention shall apply without prejudice to the rules of the intergovernmental institution or to the stipulations of the agreement".

It had also proposed that article 71(1)(bis) should be replaced by the following text:

"(1) (*bis*) When the amount of an instrument is expressed in a monetary unit of account within the meaning of article 4(11) and the monetary unit of account is transferable between the person making payment and the person receiving it, then, unless the instrument specifies a currency of payment, payment shall be made by transfer of the monetary unit of account. If the monetary unit of account is not transferable between those persons, payment shall be made in the currency specified in the instrument or, if no such currency is specified, in the currency of the place of payment."

63. *Articles 4(11) and 71(1)(bis), as amended, were adopted.*

*Article 7(5) (A/CN.9/XIX/CPR.4)*

64. Mr. SPANOGLE (United States of America) said that an *ad hoc* working party composed of the representatives of Bangladesh, Egypt, the German Democratic Republic, Mexico, the United Kingdom and the United States of America and the observer for Canada had proposed that article 7(5) should read as follows:

"(5) A rate at which interest is to be paid may be expressed either as a definite rate or as a variable rate. For a variable rate to qualify for this purpose, it must vary in relation to one or more reference rates of interest in accordance with provisions stipulated in the instrument and each such reference rate must be published or otherwise available to the public and not subject, directly or indirectly, to unilateral determination by the payee or by any person named in the instrument at the time the bill is drawn or the note is made."

65. Mr. VIS (Chairman of the Committee of the Whole) wished to know at what time the reference rate must be published.

66. Mr. SPANOGLE (United States of America) said that, assuming that the rate varied over time, the reference rate should be published during the term of the instrument. The publication of the rate either at the time of issuance or at the time of payment would not be sufficient since the reference rate was variable.

67. Mr. NADER (Mexico) said that, in his view, the reference rate should be published when the interest rate was determined.

*The meeting rose at 6 p.m.*

### Summary record of the 350th meeting Thursday, 3 July 1986, 10 a.m.

[A/CN.9/SR.350]

Chairman: Mr. KARTHA (India)

Chairman of the Committee of the Whole:  
Mr. VIS (Netherlands)

*The meeting was called to order at 10.15 a.m.*

#### International payments (continued)

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes* (continued) (A/CN.9/273, A/CN.9/274, and A/CN.9/285)

*Article 7(5) (continued) (A/CN.9/XIX/CRP.4)*

1. Mr. VIS (Chairman of the Committee of the Whole) invited the Commission to resume its consideration of the proposal contained in document A/CN.9/XIX/CRP.4, which had been introduced at the 349th meeting.

2. Mr. ABASCAL (Mexico) said he wished to clarify that reference rates should be published or otherwise available to the public throughout the life of the instrument, and not necessarily on the date of payment.

3. Mr. FELSENFELD (United States of America) said that it was unclear whether the phrase "at the time the bill is drawn or



the note is made" referred to the time of unilateral determination or the time when the reference rate was published or otherwise made available to the public.

4. Mr. VIS (Chairman of the Committee of the Whole) thought that the phrase referred to the publication of reference rates.
5. Mr. CRAWFORD (observer for Canada) said he thought that the text was appropriately worded. Ambiguity might arise only if the term "reference rate" was understood to mean the prime rate of a particular bank that was published only once, rather than each time the rate changed. However, if some members of the Commission were interpreting the term in that manner, there might be a need to clarify the text.
6. Mr. SPANOGLE (United States of America) said that the working party which had drafted the text had agreed that, if the reference rate was to be a variable one, it would be published frequently, i.e., before, during and after the life of the instrument. If some members of the Commission did not find that clear, perhaps the wording should be appropriately modified.
7. The phrase "or by any person named" had been selected in preference to the "party" concept: the payee would not have signed the instrument at the time of issue, and thus might not be considered to constitute a party to it. However, on considering the fact that the reference rate might imply a relationship to a particular bank or to a person who had absolutely no relation to the transaction, he had come to believe that the phrase "or by any party to the instrument" might actually be preferable, since it covered all possibilities except the payee.
8. Mr. HERRMANN (International Trade Law Branch) said that the last phrase of article 7(5) would be reviewed by a drafting group. For that reason, he wanted to know whether, in order for a rate to qualify as a variable rate, it was necessary to assess the conditions obtaining at the time when the instrument was made.
9. Mr. SPANOGLE (United States of America) said he believed that the phrase "at the time the bill is drawn or the note is made" referred to the determination by the person named in the instrument or, to use the term which he preferred, the "party to the instrument".
10. Mr. VASSEUR (France) favoured the use of the phrase "person named" at the end of the paragraph. The representative of the International Trade Law Branch had set out the difficulties which might arise in that regard. He did not see why unilateral determination should take place at the time an interest rate was recalculated, and consequently suggested that the phrase "at the time the bill is drawn or the note is made" should be deleted.
11. Mr. VIS (Chairman of the Committee of the Whole) pointed out that the phrase referred to the reference rate, which could not be under the control of a person named in the instrument.
12. Mr. NADER (Mexico) said that the final clause of the proposed text was intended to prevent persons named in an instrument from being able to determine the reference rate. Such determination could be made only under the conditions stipulated in the text.
13. Mr. SPANOGLE (United States of America) said that the current wording of the proposed text made it possible for a

person who was never intended to be the holder of an instrument, but who might in fact become one, to designate the reference rate. It was important to preclude such a situation.

14. Mr. VIS (Chairman of the Committee of the Whole) conceded that the United States representative had a valid point. It might perhaps be useful to identify the parties concerned—drawers, drawees, payees, guarantors etc.—as long as the substance of the proposed text was retained. A drafting group should be able to settle any questions relating to the actual wording of the text. He suggested that the Commission should adopt article 7(5), subject to any drafting changes which a drafting group might make.

15. *It was so decided.*

*Article 7(5 bis) (A/CN.9/XIX/CRP.5 and 6)*

16. Mr. ABASCAL (Mexico) said that he and the representative of the United Kingdom had attempted to formulate a compromise text which would reconcile their positions with regard to floating interest rates. It had become clear to each, however, that their positions were irreconcilable, and they had consequently decided to submit separate proposals for a new paragraph (5 bis) to be added at the end of article 7. The text which his delegation wished to propose, contained in document A/CN.9/XIX/CRP.5, was the following:

"In order for a floating interest to be agreed to, the instrument shall at the same time indicate the rules agreed on to prevent fluctuations, whether upwards or downwards, from having consequences which, according to reasonable criteria in international trade, are contrary to equity, to the detriment of any of the parties and of the holder of the instrument."

17. His decision to propose that text was based on consultations held with other members of the Commission who felt that floating interest rates must be contained but feared that banks might not accept such a provision in the draft Convention because the rate might be unfavourable to them. The usefulness of the Convention might thus be jeopardized. He himself believed, however, that, the banks' fears notwithstanding, the text would improve the draft Convention.

18. Article 7(5), which the Commission had just adopted, was designed to deal with current economic realities. Nevertheless, it constituted a departure from three important principles of the law of negotiable instruments. The first principle was that such instruments must be complete entities that did not deal with any extraneous issues. Second, such instruments should be expressed in terms of a fixed amount. Finally, such instruments should not be subject to any externally-imposed conditions. The proposed paragraph (5 bis) thus tried to prevent article 7(5) from having any inequitable consequences.

19. Implementation of the proposed text would require imagination on the part of the parties concerned, who should display fairness and good judgement.

20. Miss DONOHUE (United Kingdom), introducing document A/CN.9/XIX/CRP.6, said that, following discussions with the representative of Mexico, her delegation had decided to propose that the following text should be included as the new paragraph (5 bis):

"Where the rate at which interest is to be paid is expressed as a variable rate, it may be stipulated that such rate shall not be less than or exceed a specified rate of interest."

21. Her delegation's proposal differed from that put forward by the representative of Mexico in that it left the determination of the rate of interest largely to the parties involved. There was a precedent for such a procedure in the case of promissory notes. She believed that her delegation's proposal would result in somewhat less uncertainty among banks than would the Mexican proposal.
22. Mr. VASSEUR (France) said that the Mexican proposal seemed to impose more restrictions, while the United Kingdom proposal, which he himself favoured, gave more freedom. He wished to point out that credits allocated on the basis of floating interest rates did not come directly from banks, but were acquired by banks from international capital markets. Thus the banks themselves only passed on to the recipient of the credits allocated, the rates to which they themselves were subject.
23. Mr. SPANOGLE (United States of America) said he was glad to note that the differences between the two positions had narrowed greatly, particularly since he believed that the limitation of rates should be a provision of the draft Convention.
24. While he had a slight problem with the proposal put forward by the representative of the United Kingdom, which recognized only certain types of limitations, he did not favour the setting of mandatory limits as called for in the Mexican proposal, for two reasons. Such a practice prohibited the use of the simpler and more common variable-rate clause, as in the case of the Libor 30-day rate. The use of the term "reasonable criteria" was also problematic, since its definition was subject to different interpretations.
25. Mr. PISEK (Czechoslovakia) said that, while he would be satisfied with article 7 without the addition of paragraph (5 *bis*), he nevertheless preferred the United Kingdom proposal to the Mexican proposal because it afforded greater flexibility in the determination of interest rates to the parties involved in the transaction in question, who were best equipped to understand the ramifications of any decision taken. Moreover, the Mexican proposal might result in uncertainty regarding specific rates, and might make it difficult for them to be recognized by a court, thus creating as many difficulties for debtors as for creditors.
26. The CHAIRMAN, speaking as the representative of India, agreed that the Mexican proposal might create difficulties, given that the terms "reasonable criteria in international trade" and "equity" could be subject to different interpretations, depending on the jurisdiction involved.
27. Mr. DELFINO-CAZET (Uruguay) said that there were two aspects to each proposal. In the first place, the Mexican proposal would make it mandatory, where parties agreed to have a floating interest rate, to establish limits above and below which the rates could not go, whereas the United Kingdom proposal would leave the establishment of such limits to the discretion of the parties. In that respect, he supported the Mexican proposal.
28. In the second place, there was the question of how to determine the limits. According to the United Kingdom proposal, the rate could not be higher or lower than a rate to be determined, whereas the Mexican proposal used other criteria. In that respect, the United Kingdom proposal was the better of the two, although the wording of the proposal could be improved by adding a reference to reasonable criteria.
29. Mr. MAEDA (Japan) supported the United Kingdom proposal.
30. Mr. GRIFFITH (Australia) said that while the content of the United Kingdom proposal was implicit in article 7(5) as it stood, he saw no harm in making it explicit.
31. Mr. DUCHEK (Austria) said that, while he fully understood the concerns of the representative of Mexico, the Mexican proposal had two drawbacks. First, it made the establishment of limits mandatory. He could envisage cases in which the parties might not want to establish any limits; in such cases, they would have to resort to some means of payment other than those provided for in the Convention.
32. Second, it contained an element of uncertainty embodied in the requirement that the agreement reached between the parties in order to prevent too wide a fluctuation must not have consequences which, according to reasonable criteria were contrary to equity. Since that phraseology could lend itself to various interpretations, it would discourage the use of international instruments. He was in favour of the United Kingdom proposal, although he did not think that it was essential.
33. Mr. EYZAGUIRRE (Chile) said that article 7 should remain as it stood with the addition of the stipulation that the interest rate could be either fixed or variable. The Mexican proposal, which would make it mandatory for parties to adopt certain rules based on complicated criteria, would limit the free circulation of instruments. It might be necessary to modify article 1(2)(b), because of the stipulation in that paragraph that an international bill of exchange must contain an unconditional order directing the drawee to pay "a definite sum of money".
34. Mr. VIS (Chairman of the Committee of the Whole) recalled that the question of whether article 7(5) conflicted with article 1(2)(b) had been discussed at great lengths and he did not wish to reopen the discussion.
35. Mr. CHAFIK (Egypt) said that he understood the concern which had led the representative of Mexico to submit his proposal. The weakness of the proposal was that it would make it mandatory to establish rules to limit the extent to which the interest rate could fluctuate. Perhaps the two proposals could be combined by amending the Mexican proposal to make it refer to the rules "which may be" agreed on; it would then be clear that it was not mandatory for the parties to agree on such rules.
36. Mrs. ADEBANJO (Nigeria) said that she supported the United Kingdom proposal because it was simpler to interpret and would allow the parties to negotiate an interest rate in the event that a rate was expressed as a variable rate, without making such negotiations mandatory.
37. Mr. ABOUL-ENEIN (observer, Asian-African Legal Consultative Committee) said that, for the reasons stated by previous speakers, he could not support the Mexican proposal. Instead he favoured the United Kingdom proposal.
38. Mr. SEVON (observer for Finland) said that the point made in the United Kingdom proposal was implied in the Convention as it stood. That proposal might be interpreted to mean that the only way of stipulating limitations on a variable rate was the one specified in the proposal. Accordingly, he would prefer to dispense with paragraph (5 *bis*).
39. Mr. KOCH (Sweden) said that the mandatory limitation proposed by the Mexican representative would create great

uncertainty because the text would lend itself to different interpretations in different legal systems. If, for any reason, the parties wished to opt for a variable interest rate and the Convention did not permit such a rate, then they would use another means of payment. The provision would thus detract from the free circulation of international instruments. He was not certain that the intent of the United Kingdom proposal could be implied from the draft Convention as it stood. Accordingly, he supported the proposal.

40. Mr. SAMI (Iraq) said that, for the reasons stated by previous speakers, he supported the United Kingdom proposal.

41. Mr. VIS (Chairman of the Committee of the Whole) said there appeared to be support for the United Kingdom proposal, although some representatives believed that it should be modified. Accordingly, he noted that the Commission decided that a provision along the lines proposed by the United Kingdom delegation should be added as article 7 (5 *bis*). The Commission would try again to reach consensus before adopting the final text of that paragraph.

*The meeting was suspended at 11.35 a.m. and resumed at 12.05 p.m.*

42. Miss DONOHUE (United Kingdom) revised her delegation's proposal. The words "or that the variations may be otherwise limited by express provisions on the instrument" should be added at the end of the paragraph.

43. Mr. FELSENFELD (United States of America) said that the words "by express provisions" should be deleted.

44. Mr. SEVON (observer for Finland) said that the words "on the instrument" should be inserted in the paragraph proposed by the United Kingdom delegation after the words "may be stipulated".

45. Mr. VIS (Chairman of the Committee of the Whole) said that the new paragraph 5 *bis* would read:

"Where the rate at which interest is to be paid is expressed as a variable rate, it may be stipulated on the instrument that such rate shall not be less than or exceed a specified rate of interest, or that the variations are otherwise limited."

*Article 20 bis (A/CN.9/XIX/CRP.7)*

46. Mr. VASSEUR (France) read out a proposed new article 20 *bis*:

"When an endorsement contains the statements 'value in security' (*valeur en garantie*), 'value in pledge' (*valeur en gage*), or any other statement implying a pledge, the endorsee

- (a) Is a holder by virtue of article 4(6) and (7) and article 28;
- (b) May exercise all the rights arising out of the instrument;
- (c) May only endorse the instrument for purposes of collection;
- (d) Is subject to claims and defences which may be set up against the endorser only in the cases specified in articles 25 and 26.

Such an endorsee, having endorsed for collection is not liable upon the instrument to any subsequent holder."

47. The proposed new article filled a gap in the draft Convention concerning endorsement in pledge. It had been drafted on the basis of the terminology used elsewhere in the draft Convention and in article 19 of the Geneva Convention.

48. There was a fundamental difference between a holder of an instrument by virtue of a transfer endorsement or endorsement in pledge, and a holder of an instrument by virtue of an endorsement for collection. An endorsee for pledge was a protected holder against whom the régime of defences for semi-protected holders referred to in article 25 (2 *bis*) could be set up.

49. Mr. VIS (Chairman of the Committee of the Whole) said that in the legal doctrine of the Netherlands, an endorsee for pledge could exercise rights on an instrument only in the name of his endorser. There was no liability of the endorser to subsequent transferees. Obligors on an instrument could set up against the endorsee only those defences that could be raised against the endorser.

50. Mr. GANTEN (observer for the Federal Republic of Germany) said that he supported the French proposal; it was necessary to include endorsement in pledge in the draft Convention, along the lines of article 19 of the Geneva Convention. Under German law, which was based on the Geneva Convention, an endorsee exercised rights on an instrument in his own name.

51. Mr. DRUEY (observer for Switzerland) said that he supported the French proposal, but that paragraph (d) should be amended to make it clear that an endorsee for pledge would be protected in exactly the same way as any other endorsee under articles 25 and 26 of the draft Convention.

52. Mr. SAMI (Iraq) and Mr. DUCHEK (Austria) said that they supported the French proposal.

53. Mr. FELSENFELD (United States of America) said that it was not clear how the proposed new article would apply in common-law countries, or why the endorsee was to be given the rights in question.

54. Mr. VIS (Chairman of the Committee of the Whole) said that, under article 9 of the United States Uniform Commercial Code, an instrument could be given in pledge. There was nothing similar in the negotiable instruments law, however.

55. Mr. VASSEUR (France) said that he had already given the example of a bank which might want to endorse an instrument temporarily to another bank as a guarantee for an advance on the understanding that, when the advance was reimbursed, the instrument would be returned; thus the first bank would have the benefit of the interest payable for the remaining term of the instrument.

56. Mr. FELSENFELD (United States of America) said that, in the light of those explanations, he was favourably inclined towards the French proposal.

57. Mr. DELFINO-CAZET (Uruguay) said that he supported the proposal, although the wording could perhaps be refined.

58. Mr. VIS (Chairman of the Committee of the Whole) asked whether the reference in paragraph (b) to all rights arising out of the instrument would include the right of the endorsee to demand payment and be paid. If that were so, it should be made

clear that he could receive payment only on behalf of the endorser and not on his own behalf.

59. Mr. VASSEUR (France) said that the endorsee was entitled to receive payment on his own behalf, unlike the endorsee in the case of endorsement for collection, referred to in article 20 of the draft Convention.

60. Mr. CRAWFORD (observer for Canada) said that the article proposed by France would seem to be creating a new class of holder. In addition to article 28, he wondered whether, for instance, article 17 ought not also to be mentioned, since any statement implying a pledge on the instrument itself could be considered a condition within the meaning of article 17. It might also be necessary to state that the endorsement must occur before maturity.

61. Mr. VASSEUR (France) said that he would have no objection to deleting the reference to article 28, since in any case that article would apply automatically.

62. Replying to requests for clarification from Mr. VIS (Chairman of the Committee of the Whole) and Mr. DUCHEK (Austria), he said that the legal effects of an endorsement under his proposed article 20 *bis* differed from those of an endorsement under article 20(1). In his proposed article, the endorsee acted in his own name and would therefore be subject not to all claims and defences under article 20(1)(c) but only to those defences which might be set up against the endorser under articles 25 and 26. He further explained, in reply to Mr. PISEK (Czechoslovakia), that, when the original endorser for pledge later repaid the value in pledge which had been advanced to him, he became once again the holder of the instrument, which would then specify on its face that the advance had been repaid and that the endorsement had ceased to have effect.

63. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that the Working Group had decided against including a provision such as that being proposed by the representative of France because banks had generally indicated that there was no need for it, the usual practice being to put instruments in pledge by means of an agreement outside the instrument between holder and endorsee.

64. The experience in her own country was that such transactions were very complicated and could lead to many problems: as, for instance, when instruments were transferred in pledge as

a way of circumventing trade contracts that prohibited sales, thus leading to contract disputes, or when banks did not recognize an endorsee for pledge as a true holder and denied his right to the normally transferable guarantees on the instrument. She therefore opposed the inclusion of the proposed article.

65. Mr. BRANDT (German Democratic Republic) said that he agreed with the Soviet representative. It should be left to national law to regulate that kind of endorsement, in order to facilitate the use of the draft Convention by all.

66. Mr. CHAFIK (Egypt) said that he shared the view of the Soviet representative, and opposed the French proposal also because it was his understanding that such endorsements had become obsolete and were no longer used by banks. The introduction of such a provision would, moreover, require a very attentive study of its implications for other provisions of the draft Convention, and it was too late to embark on such a study.

67. Mr. VASSEUR (France) said that it was not true that endorsement in pledge was anachronistic: French banks used it internationally and had asked for the inclusion of a provision governing it.

68. Mr. BARRERA GRAF (Mexico) said that he could not support the French proposal because there was no time to examine all its links with other parts of the draft Convention. It should have been submitted earlier, to the Working Group.

69. Mr. VIS (Chairman of the Committee of the Whole) said that he had to acknowledge a certain responsibility in the matter: the representative of France had indeed submitted his proposal to the Working Group at a time when he himself had been Chairman. Not knowing that the forthcoming session would be the last round of discussions, he had advised the representative of France that the French proposal did not fall within the Working Group's narrow mandate and that only the full Commission could consider it. There was unfortunately now not even time to set up a small *ad hoc* working group to consider the implications of the proposal. He could only conclude therefore that, in view of the many substantive objections that had been raised, the Commission did not wish to adopt the proposal contained in document A/CN.9/XIX/CRP.7.

70. *It was so decided.*

*The meeting rose at 1 p.m.*

### Summary record of the 351st meeting Thursday, 3 July 1986, 3 p.m.

[A/CN.9/SR.351]

Chairman: Mr. KARTHA (India)

Chairman of the Committee of the Whole:  
Mr. VIS (Netherlands)

*The meeting was called to order at 3.10 p.m.*

#### International payments (continued)

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes* (continued) (A/CN.9/274; A/CN.9/XIX/CRP.9, 10, 11, 12 and 13)

Articles 69(4) and 68(4) (*a ter*) (A/CN.9/XIX/CRP.9).

1. Mr. MAEDA (Japan) introduced the amendments proposed by his delegation in document A/CN.9/XIX/CRP.9. The beginning of paragraph 69(4) should read as follows:

“(4) If the holder takes partial payment from a party to the instrument other than the acceptor, the maker or the guarantor of a drawee:

“(a) ...”.

2. He also proposed that a new subparagraph (*a ter*) should be added to article 68(4), which would read:

“(a *ter*) If the holder of an instrument payable by instalments at successive dates receives payment of any instalment from a party to the instrument other than the acceptor, the maker or the guarantor of the drawee, the holder must give such party a certified copy of the instrument and of any authenticated protest.”

3. Mr. VIS (Chairman of the Committee of the Whole) said that he understood that the guarantor of the acceptor and the guarantor of the maker would also be included in article 68(4) (*a ter*).

4. Mr. MAEDA (Japan) said that only the guarantor of the drawee did not have the right of recourse against the drawee or any other party. He referred the Commission to article 44 of the draft Convention.

5. Mr. VIS (Chairman of the Committee of the Whole) asked whether that meant that the Convention did not give any right to the guarantor of the drawee who paid the instrument on maturity.

6. Mr. MAEDA (Japan) said that that was so, at least on the instrument.

7. Mr. VIS (Chairman of the Committee of the Whole) asked whether, in a case where the holder took partial payment from the guarantor of the drawee, the guarantor of the drawee was discharged to the extent of the partial payment. If that was so, such a provision should be included in article 69(3).

8. Mr. MAEDA (Japan) said that article 69(3) should be amended to read as follows:

“(3) If the holder takes partial payment from the drawee, the guarantor of the drawee, the acceptor or the maker:

“(a) The guarantor of the drawee, the acceptor or the maker is discharged of his liability on the instrument to the extent of the amount paid; ...”.

9. Mr. VIS (Chairman of the Committee of the Whole) supported that proposal.

10. Mr. DRUEY (observer for Switzerland) said that the addition of a reference to the guarantor of the drawee to article 69(3) destroyed the system according to which the primary responsibility for payment lay with the drawee, the acceptor and the maker, those being the persons against whom a protest should be made in the case of non-payment. The guarantor of the drawee should therefore be mentioned in article 69(4) but not in article 69(3).

11. Mr. VIS (Chairman of the Committee of the Whole) said that, according to article 43(2), the liability of the guarantor of the drawee was a primary responsibility.

12. Mr. DRUEY (observer for Switzerland) said that he understood that protest would be made against non-payment by the drawee and not against non-payment by his guarantor.

13. Mr. SAMI (Iraq) asked why the guarantor of the acceptor or the guarantor of the maker should not also be mentioned in article 69(3), along with the guarantor of the drawee.

14. Mr. VIS (Chairman of the Committee of the Whole) said that, in accordance with article 69(3), if the holder took partial

payment from the acceptor, the acceptor was discharged of his liability on the instrument to the extent of the amount paid. If the guarantor of the acceptor paid, the acceptor would remain liable to the guarantor of the instrument for the amount paid.

15. Mr. CRAWFORD (observer for Canada) said that, under article 69(3), if the holder took partial payment from any person named on the instrument, the liability of that person would be partially discharged and the instrument would be dishonoured to the extent of the amount unpaid. That applied without discrimination to any person who made a payment on the instrument, the rights of guarantors and parties guaranteed being preserved by article 44.

16. Mrs. PIAGGI de VANOSI (Argentina) said that, assuming that the guarantor of the acceptor paid, the acceptor would be liable to his guarantor because the acceptor was the person who bore primary liability and must reimburse his guarantor. However, in article 43(2), the nature of the liability of the guarantor was quite different.

17. Mr. VIS (Chairman of the Committee of the Whole) said that, if the guarantor of the acceptor paid, the bill would not be considered as dishonoured and the guarantor of the acceptor would then have a right on the bill against the acceptor.

18. Mr. BARRERA GRAF (Mexico), supported by Mrs. PIAGGI de VANOSI (Argentina) and Mr. DELFINO-CAZET (Uruguay), said that article 69(3) and (4) should contain references to the guarantor of the drawee.

19. Mr. DUCHEK (Austria) said that he agreed that a reference should be made to the guarantor of the drawee in article 69(3). Perhaps reference should also be made to the guarantor of the acceptor.

20. Mr. MAEDA (Japan), responding to a suggestion made by Mr. VIS (Chairman of the Committee of the Whole), said that he agreed that the beginning of article 69(3) should read: “If the holder takes partial payment from the drawee or the acceptor or the maker or their guarantor”.

21. Mr. CRAWFORD (observer for Canada) endorsed the suggestion put forward by the Chairman of the Committee of the Whole. Although he did not consider article 69(4) entirely acceptable, he was willing to agree to the inclusion of a reference to the guarantor in that article.

22. Mr. DRUEY (observer for Switzerland) said that care must be taken to ensure that everybody who was entitled to a certified copy of the instrument and of any authenticated protest was covered by article 69(4).

23. Mr. VIS (Chairman of the Committee of the Whole) suggested that the Committee should complete consideration of A/CN.9/XIX/CRP.9 at a later date.

*Article 66 (continued) (A/CN.9/XIX/CRP.11)*

24. Mr. FELSENFELD (United States of America), introducing the first amendment proposed by the *ad hoc* working party in document A/CN.9/XIX/CRP.11, said that the last sentence of article 66(2) would apply to a number of countries, including his own. The purpose of redrafting that sentence was to make a more specific reference to the level of the rate of interest. The working party therefore proposed that the last sentence should read:

"In the absence of any such rates, or where there is more than one such rate, the rate of interest shall be the rate that would be required to be paid if legal proceedings were taken in the jurisdiction where the instrument is payable."

25. Mr. GRIFFITH (Australia), supported by Mr. FELSENFELD (United States of America) and Mrs. PIAGGI de VANOSI (Argentina), suggested that the words "required to be paid if legal proceedings were" should be replaced by the words "recoverable in legal proceedings".

26. Mr. DRUEY (observer for Switzerland), supported by Mr. GLATZ (Hungary), Mr. FELSENFELD (United States of America), Mr. CRAWFORD (observer for Canada) and Mr. GANTEN (observer for the Federal Republic of Germany), proposed that the first two sentences of article 66(2) should be deleted and that paragraph (2) should read: "The rate of interest shall be the rate that would be recoverable in legal proceedings taken in the jurisdiction where the instrument is payable".

27. Mr. VIS (Chairman of the Committee of the Whole) said that, if he heard no objection, he would take it that the Committee wished to adopt the proposed wording for article 66(2).

28. *It was so decided.*

29. Mr. FELSENFELD (United States of America), introducing the second amendment proposed by the working party, said that the issue that arose in article 66(3) was very similar to the one just dealt with in paragraph (2). The working party therefore proposed that the last clause of paragraph (3) should read: "... or, if there is no such rate, then at such rate as is reasonable in the circumstances".

30. Mr. CRAWFORD (observer for Canada) suggested that the rate referred to in paragraph (2), as just adopted, should also apply in paragraph (3).

31. Mr. FELSENFELD (United States of America), supported by Mr. GANTEN (observer for the Federal Republic of Germany), said that, if the aim was to achieve the same goal as in paragraph (2), the current wording of paragraph (3) should simply be amended in accordance with the proposal put forward by the working party.

32. Mr. VIS (Chairman of the Committee of the Whole) said that he took it that the change in the last clause of article 66(3) was accepted.

33. *It was so decided.*

34. Mr. FELSENFELD (United States of America), introducing the third amendment proposed by the working party, said that the proposed new paragraph (2 *bis*) would read as follows: "Nothing in paragraph (2) prevents a court from awarding damages or compensation for additional loss caused to the holder by reason of delay in payment." Although the first two sentences of paragraph (2) had been deleted, the principle underlying the new paragraph (2 *bis*) would remain valid.

35. Mr. BRANDT (German Democratic Republic) said that he had some misgivings about the new paragraph because, as he understood it, a legal judgement would be a pre-condition for awarding damages or compensation.

36. Mr. VIS (Chairman of the Committee of the Whole) said that such would be the case, unless the parties agreed on a

justifiable amount. Obviously the damages or compensation could not be imposed by one party on another.

37. Mr. GANTEN (observer for the Federal Republic of Germany) said that he understood the comment made by the representative of the German Democratic Republic; however, the new paragraph implied that, although a court might award damages or compensation, the parties were free as a matter of course to agree on such damages. He therefore supported the new paragraph.

38. Mr. CHAFIK (Egypt) said that he understood the new paragraph in the same way and would support it also.

39. Mr. VIS (Chairman of the Committee of the Whole) said that, if he heard no further comments, he would take it that the new paragraph (2 *bis*) would be added.

40. *It was so decided.*

*The meeting was suspended at 4.55 p.m. and resumed at 5.25 p.m.*

Article 48 (continued) (A/CN.9/XIX/CRP.14)

41. Mr. SPANOGLE (United States of America) said that the United States delegation proposed the following addition to article 48:

"(1) Delay in making a necessary presentment for acceptance within the time-limit stated within the bill is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of the delay ceases to operate, presentment must be made with reasonable diligence."

42. The text would apply only to instruments in which a time-limit was specified within which a bill must be presented for acceptance, i.e., where the one-year rule did not apply. It would not apply to situations where no time-limit was specified.

43. Mr. DUCHEK (Austria) asked what effect the provision would have if the circumstances which prevented presentment or acceptance did not cease.

44. Mr. VIS (Chairman of the Committee of the Whole) said that the drawer would remain liable. If he heard no further comments, he would take it that the new paragraph 48(1) was accepted.

45. *It was so decided.*

46. Mr. SPANOGLE (United States of America) said that paragraph 2 of his delegation's proposal would transform paragraph (a) of article 48 into paragraph (2) of that article.

47. Paragraph 3 of the proposal would take the objective criteria of civil-law systems in respect of necessary presentment and apply them to the one-year time-limit in a new paragraph (3) of article 48, which would read as follows:

"(3) When a necessary presentment for acceptance cannot be effected within the time-limit prescribed in article 47(e) due to circumstances which are beyond the control of the holder and which he could neither avoid nor overcome, the necessary presentment for acceptance is dispensed with."

48. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that the proposed new paragraph should refer not only to article 47(e) but also to article 47(d).
49. Mr. VIS (Chairman of the Committee of the Whole) said that presentment for acceptance was optional in respect of a bill drawn payable on a fixed date. The situation provided for in article 47(e) was the only one in which presentment was mandatory.
50. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that, while she had no objection to the proposed paragraph (3), the specific reference to article 47(e) must be replaced by a more general reference to article 47.
51. Mr. VIS (Chairman of the Committee of the Whole) said that reference might be made to both subparagraphs (d) and (e).
52. Mr. CHAFIK (Egypt) asked whether it would be necessary to wait for a further period of three months after the one-year time-limit if a holder of a bill of exchange could not effect the necessary presentment for acceptance within the time-limit prescribed in article 47(e) owing to circumstances beyond his control.
53. Mr. VIS (Chairman of the Committee of the Whole) said that a further three-month waiting period was not necessary, since expiry depended on the date of acceptance. The policy of the Commission had always been to include within the draft Convention rules which were already widely established. He wished to suggest that, subject to minor drafting modifications to the proposed paragraph (3), which he would discuss with the representative of the Soviet Union, the Commission should adopt paragraphs 2 and 3 of the United States proposal.
54. *It was so decided.*
- Article 30 (continued) (A/CN.9/XIX/CRP.13)*
55. Mr. CHELOTI (Kenya) introduced the amendment proposed by the *ad hoc* working party, composed of the representatives of the European Banking Federation, Kenya, Switzerland and Yugoslavia, in document A/CN.9/XIX/CRP.13. The second sentence of article 30 would read as follows:
- “Nevertheless, where such person has accepted to be bound by the forged signature or represented that the signature was his own, he is liable as if he had signed the instrument himself, according to the terms of such acceptance or representation.”
56. The term “accepted” adequately covered the intention of the text and the working party therefore felt that the words “expressly or impliedly” were not needed.
57. Mr. VIS (Chairman of the Committee of the Whole) requested clarification of the meaning of the words “according to the terms of such acceptance or representation” in the proposed new text.
58. Mr. CHELOTI (Kenya) said that the idea was that a principal could decide to limit the circulation of an instrument and accept to be bound by it only to a limited extent.
59. Mr. VIS (Chairman of the Committee of the Whole) said that, where the signature of the payee on an instrument was forged and the forger, posing as payee, transferred the instrument to a party A, and A transferred to B, and B to C, and where C took recourse against the payee, the payee could now agree to pay and implicitly adopt the signature or could state that, although the signature was not his, he would accept to be bound. He could not see, however, how it would be possible for the payee to say that the instrument would not circulate.
60. Mr. HERRMANN (International Trade Law Branch) said that the main situation envisaged by the working party was one in which a principal might expressly or impliedly accept to be bound *vis-à-vis* a particular party or holder. The working party had felt that in such case only those persons who learned of the acceptance to be bound were estopped from invoking the forgery.
61. Mr. SPANOGLA (United States of America) said that the purpose of providing for acceptance to be bound was not only to protect the holder while he was holding the instrument but also to protect the holder in the sense that he might transfer the instrument. The words “according to the terms of such acceptance or representation” should therefore be deleted.
62. Mr. GRIFFITH (Australia), said that the phrase in question would lead to great uncertainty and should therefore be deleted.
63. Mr. VIS (Chairman of the Committee of the Whole) said that, if he heard no objection, he would take it that the Commission agreed to accept the proposed modification of the second sentence of article 30, after deleting the words “according to the terms of such acceptance or representation”.
64. *It was so decided.*
- Article 41(3)*
65. Mr. VIS (Chairman of the Committee of the Whole) invited proposals for filling the blank which had been left in article 41(3).
66. Mr. GANTEN (observer for the Federal Republic of Germany) said that the text should refer to one of the methods of determining the interest rate provided in article 66. He would prefer the method provided in article 66(2). Article 41(3) could therefore read “... plus interest calculated in accordance with the provisions of article 66(2) upon return of the instrument”.
67. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that there was no reason why the method specified in article 66(2) should be used instead of the one specified in article 66(3).
68. Mr. SPANOGLA (United States of America) said that the method specified in article 66(2) was more viable.
69. Mr. VIS (Chairman of the Committee of the Whole) suggested that the proposal should refer to article 66 without mentioning specific paragraphs.
70. *It was so decided.*

Summary record (partial)<sup>a</sup> of the 352nd meeting  
Monday, 7 July 1986, 3 p.m.

[A/CN.9/SR.352]

Chairman: Mr. KARTHA (India)

*The meeting was called to order at 3.15 p.m.*

**International payments (continued)**

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes* (continued)

1. The CHAIRMAN invited the members of UNCITRAL to consider the nature of the recommendation which the Commission should make to the General Assembly with respect to the adoption of the draft Convention on International Bills of Exchange and International Promissory Notes.

2. Mr. BERGSTEN (Secretary of the Commission) said that the draft Convention might be adopted by a diplomatic conference or by an international organ such as the General Assembly of the United Nations. In selecting the procedure, account should be taken of the cost involved and the extent to which changes might be made in the text during the process of adoption.

3. One would expect a full diplomatic conference, lasting from five to six weeks, to conduct a thorough review of the draft Convention. While most participants would be delegates to UNCITRAL, a significant number would be new delegates, unfamiliar with the text of the draft Convention, its structure and the basic compromises which had been reached. On the basis of previous similar conferences, the cost of such a conference could be estimated at about \$3 million.

4. Another option was to recommend the convening of a short diplomatic conference for the purpose of attaching final clauses to the draft Convention and opening it for signature. The Office of Legal Affairs had advised the secretariat that, since such a procedure essentially meant that UNCITRAL would meet as a diplomatic conference, it would be extremely complicated and was not to be recommended.

5. Another possibility was for the General Assembly to convene a short diplomatic conference to review specific points only. In such a case, the determination of which points should be reviewed would normally be made by the Sixth Committee on the recommendation of Member States after the draft Convention had been submitted to the General Assembly.

6. The final, and most likely, possibility was for the draft Convention to be adopted by the General Assembly on the recommendation of the Sixth Committee. If that option were followed, it would be advisable to recommend that the Sixth Committee should not change the substance of the draft Convention and should limit itself to inserting the preamble and final clauses. Such action by the Sixth Committee would be part of its normal activities and would therefore entail no additional cost.

7. If the Commission recommended to the General Assembly at its forty-first session that a diplomatic conference should be

held, such a conference was not likely to be convened before 1988. If it recommended that the draft Convention should be adopted by the General Assembly on the recommendation of the Sixth Committee, it was unlikely that the Sixth Committee would act on that recommendation during the current year. The Sixth Committee would probably wish to circulate the text of the report of UNCITRAL, which would not be available before September 1986, to Member States for comment.

8. Whichever body adopted the draft Convention would be required to reach agreement on its final clauses. It seemed highly unlikely, however, that there would be declarations or reservations on the part of signatories and the final clauses were likely to be standard. The Commission might nevertheless wish to recommend the number of signatories that should be required for the entry into force of the Convention. In the view of the secretariat, it would be advisable to recommend a small number. The Commission might also wish to recommend the period that should elapse after receipt of the required number of signatures in order for the Convention to enter into force.

9. Mr. GANTEN (observer for the Federal Republic of Germany) said that a number of points in the draft Convention still remained to be clarified. The financial crisis of the United Nations made it unlikely that a full diplomatic conference would be convened to review all the articles of the draft Convention. Neither a short diplomatic conference nor the submission of the draft Convention to the General Assembly for adoption offered any possibilities for substantive discussion of the text. A group of experts could perhaps be established to review the draft Convention before it was sent to the Sixth Committee and to circulate the draft to Governments for their consideration and comments. If the Sixth Committee was not likely to consider the draft Convention before 1987, then it might be possible for UNCITRAL to make changes in the text after consultation with the group of experts.

10. Mr. BERGSTEN (Secretary of the Commission) said that such a procedure was possible and would have the advantages of permitting a final review of the text and of enabling rectifications to be made where problems were found. It would be important, however, to define the mandate of the group of experts since it was likely that it would be required to consider substantive points. The consideration of substantive points by the group of experts would also have a delaying effect on the procedure for adoption of the draft Convention. He also wondered how much time would be needed for the consideration of the report of the group of experts during the next session of UNCITRAL.

11. Mr. VIS (Netherlands) said that, for the reasons stated by the Secretary of the Commission, his delegation was not in favour of recommending that a diplomatic conference should be convened. From a substantive point of view, the General Assembly was the proper body to adopt the Convention. He supported the proposal made by the observer for the Federal Republic of Germany that a group of experts should be established, since that would be the cheapest and simplest way of putting the final touches to the draft Convention. It seemed unlikely that the Sixth Committee would consider the draft Convention in 1986 and it might therefore be possible to do the necessary further work on the draft. If the Commission could assure the General Assembly that Governments had had the

<sup>a</sup>No summary record was prepared for the meeting after 4.15 p.m.



opportunity to express their views on the draft Convention, it might be possible to convince the Sixth Committee that the text of the draft Convention should remain unchanged.

12. Mr. IBRAHIM (Egypt) said that the usual procedure for adopting a convention was to hold a diplomatic conference. However, in view of the current financial crisis of the United Nations, his delegation was in favour of appointing a group of experts to conduct a thorough review of the draft Convention. That would enable the Commission at its next session to decide whether to hold a diplomatic conference or to adopt the procedure proposed by the observer for the Federal Republic of Germany.

13. Mr. SAMI (Iraq) said that the draft Convention had not been discussed thoroughly and that the entire text should be re-examined with a view to reaching a standard legal uniform rule. To that end, a diplomatic conference should be convened in order to discuss the draft Convention article by article. If the diplomatic conference were convened in two years' time, the financial situation of the organization might have improved. The proposal made by the observer for the Federal Republic of Germany was not practical because the designation of a group of experts would present a number of problems.

14. Mr. GOH (Singapore) said that the Commission should not convene a diplomatic conference because of the financial implications. His delegation was in favour of the proposal that the Sixth Committee should submit the draft Convention to the

plenary session of the General Assembly for ratification. He opposed the establishment of a group of experts to examine the draft Convention because such a group might undo what had been achieved at the current session. If delegations felt that further discussion was necessary, perhaps the Commission could continue its discussion of the draft Convention at a future session.

15. Mr. WOOLMAN (United Kingdom) said that his delegation supported the establishment of a group of consultants or experts to conduct a brief and limited review of the draft Convention. Assuming that that could be done soon, allowing time for Governments to submit their comments, he asked whether the Commission had to take a decision at the current session regarding the procedure for the adoption of the draft Convention.

16. Mr. BERGSTEN (Secretary of the Commission) said that, if the Commission was in favour of designating a small group of experts, which would conduct a final review of the draft Convention and produce a final text in 1987, it should inform the Sixth Committee that it wished the Committee to consider the draft Convention in 1987. That would allow the Sixth Committee to indicate whether it was feasible to finalize the draft Convention in such a manner, or whether it would be more advisable to convene a diplomatic conference.

*The discussion covered in the summary record ended at 4.15 p.m.*

### Summary record of the 353rd meeting Tuesday, 8 July 1986, 10 a.m.

[A/CN.9/SR.353]

*Chairman:* Mr. KARTHA (India)

*The meeting was called to order at 10.15 a.m.*

#### International payments (continued)

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes (continued) (A/CN.9/274)*

1. Mr. GANTEN (observer for the Federal Republic of Germany) recalled that at the previous meeting he had expressed the view that further work was needed on the text of the draft Convention. Assuming that a diplomatic conference to adopt the draft Convention would not be held, he recommended that the Working Group should be reconvened for a two-week session before the end of the year, at which all States Members of the United Nations would be given an opportunity, within a brief time-limit, to comment on the final revised text. The Working Group would have a strict mandate to scrutinize the draft Convention only with a view to eliminating inconsistencies and polishing the drafting of the text, and to take into account proposals made by Governments when finalizing the draft. The Commission should give final consideration to the draft Convention at its twentieth session in 1987, which might have to be extended by a week for that purpose, and the final draft should be forwarded to the Sixth Committee for adoption and opening for signature at the forty-second session of the General Assembly.

2. Mr. VENKATRAMIAH (India) noted that many Member States would object to sending representatives to participate as observers in a session of the Working Group of the Commission. He therefore suggested: that the Working Group should not meet; that the text of the draft Convention should be submitted to Member States for comment by a specified date; that the secretariat should then compile and analyse the comments in time for the 1987 session of the Commission, which would then adopt the final draft and submit that text to the Sixth Committee in 1987, with a request not to embark on a substantive review but to deal with the text expeditiously.

3. Mr. GRIFFITH (Australia) said that, although his delegation would prefer the Commission to take a final decision on the draft Convention at the current session, it reluctantly supported the proposal of the observer for the Federal Republic of Germany since the balance of opinion was that it was premature to adopt a final text. The Working Group should meet to ensure that the wording was technically satisfactory in the various languages, and to consider the responses of Governments within that same narrow parameter. Member States would not feel excluded, since they could raise points at the twentieth session, when the Commission would probably be able to finalize the draft Convention in the first week and deal with all other agenda items over a three-week session.

4. Mr. BARRERA GRAF (Mexico) said that to refer the draft Convention once again to either the Working Group or the Commission would simply lead to a repetition of the conflicts and views already aired. The functions of the Working Group

had ended with the current session. Since a diplomatic conference was out of the question for financial reasons, the Sixth Committee should be asked to appoint a group of experts who would finalize the text with the help of a document prepared by the secretariat containing the text as currently revised and outlining the points discussed. The final draft would then be submitted for adoption to the forty-second session of the General Assembly, which would set the minimum number of ratifications needed for the Convention's entry into force.

5. Mr. GOH (Singapore) said that, since many developing countries would have difficulty sending representatives to meetings of the Working Group and since the comments by Governments would undoubtedly reopen certain questions and raise new issues, he felt the Commission itself should reconsider the draft Convention at its next session, after which the text would be transmitted to the Sixth Committee.

6. Mr. DUCHEK (Austria) observed that, after 15 years of work on the draft Convention by the Commission or its Working Group, the feeling had now emerged that the text needed further improvement. However, discussions could continue for years before all were convinced that the ideal text had been produced. He believed that the Commission should decide that in substance the draft Convention had now been finalized: at most, drafting improvements could be made and the text scrutinized for inconsistencies. That should be done by the Commission with the help of the Working Group, before the end of 1986. He was opposed to sending the draft text to Governments for comments, since Governments would then raise substantive matters that had long been resolved.

7. Mr. TREVES (Italy) said that the final clauses of the future Convention would have to contain provisions regarding: the Convention's entry into force and the requirements for ratification and accession; denunciation of the Convention; the question whether reservations would be allowed and on which provisions; and the relation of the Convention to other conventions. The last two points were the most delicate.

8. The drafting of the final clauses would have been the most sensitive task of the plenipotentiary conference. Some other forum was now needed which combined the necessary political authority and technical wisdom to adopt those clauses. He believed that that forum was the Commission, rather than the Working Group, the Sixth Committee or the General Assembly. The secretariat should draft a set of final clauses for consideration by the Commission at its 1987 session, and the final text should be referred to the Sixth Committee.

9. Mr. DRUEY (observer for Switzerland) said that, in abandoning the traditional format for the adoption of international conventions, the Commission would be breaking new ground. Diplomatic conferences were normally vested with the final political and substantive responsibility for the international instruments they were about to adopt, and he questioned whether the Sixth Committee of the General Assembly could assume substantive responsibility for the draft Convention under consideration. Perhaps the Commission might seek a way of assuming that responsibility itself. In any event, the Commission must be given sufficient time to conduct the final paragraph-by-paragraph reading of the Convention normally undertaken by a diplomatic conference.

10. Mr. SMART (Sierra Leone) said that, if the Commission decided to dispense with a diplomatic conference and transmit

the draft Convention directly to the Sixth Committee, the text should be submitted first to Governments for their comments, which merited serious consideration.

11. He agreed with the representative of Singapore that many Governments would be reluctant to send representatives to participate in a new session of the Working Group on International Negotiable Instruments.

12. Mr. VIS (Netherlands) urged the Commission to view the situation in its proper perspective. Since it was unlikely that the draft Convention would be adopted at a traditional diplomatic conference, the Commission must compensate for that lack by its own procedures.

13. Despite some inconsistencies and lacunae, the draft Convention was in relatively good shape. However, the fact that the Working Group had succeeded in producing a text in more or less final form did not mean that the draft Convention should be adopted as a whole. As had been rightly pointed out by other speakers, the final adoption of a convention was usually done on an article-by-article basis. He therefore believed that devoting one more year to consideration of the draft text was both justified and necessary.

14. It had become apparent that some provisions of the draft Convention might conflict with provisions of the Geneva Uniform Law. It would therefore be necessary for the Contracting Parties to the Geneva Convention to determine how they might resolve that situation. Their decision would have to be reflected in a final clause of the draft Convention.

15. He did not believe that the Sixth Committee of the General Assembly was a proper body for adopting a convention, even with the help of the secretariat. However, he did believe that observations from Governments regarding the most recent draft of the Convention should be sought, in an effort to compensate for the fact that a diplomatic conference would not be held. He therefore proposed that the Working Group should be convened once again, in advance of the twentieth session of the Commission, to consider the comments from Governments and deal with the aforementioned inconsistencies and lacunae. Under the circumstances, it would be appropriate to invite all States to attend the meetings of the Working Group.

16. Finally, all members of the Commission should be informed that the draft Convention was to be adopted at the twentieth session, to prevent the recurrence of any confusion on that issue. At its twentieth session, the Commission might discuss the findings of the Working Group, agree on the final clauses of the draft Convention, adopt the text of the Convention and transmit it to the Sixth Committee.

17. Mr. SEVON (observer for Finland) said that his delegation would have preferred to see the Commission adopt the draft Convention during the current session, as originally intended. However, that would have necessitated an unduly hasty consideration of each article, which would not have been in keeping with the standards that the Commission had set for its work. It was therefore with regret that he supported the proposal to postpone consideration of the final draft of the Convention until the Commission's twentieth session. However, delegations should refrain from reopening the debate on substantive questions which might not have been resolved to their liking.

18. The work of readying the draft Convention for an article-by-article examination at the twentieth session would require

that the Working Group meet well in advance of that session. It should be made clear, however, that the Working Group's task would be limited to eliminating inconsistencies in the text and making the necessary drafting changes. The draft Convention should be transmitted to Governments once the Working Group had finalized the text. It would be inappropriate for the Commission to transmit the text directly to the Sixth Committee with a recommendation for adoption, given that UNCITRAL was composed of a limited number of members. Once the views of Governments had been obtained, the text could then be transmitted to the General Assembly at its forty-second session.

19. The secretariat should prepare a model set of final clauses for consideration at the Commission's twentieth session. In addition, the States parties to the Geneva Convention should meet to formulate their position regarding the relationship between the two instruments. Finally, in its report to the General Assembly, the Commission should make it quite clear that the draft Convention would be adopted in 1987.

20. Mr. CUKER (Czechoslovakia) said that, as the decision not to hold a diplomatic conference to adopt the draft Convention constituted a departure from normal procedures, the draft text should be sent to Governments in its current form for their comments. Those views should be obtained prior to the twentieth session of the Commission so that they could be analysed by UNCITRAL at that time. He agreed with the representative of India that there was no need for the Working Group to consider the draft text prior to the twentieth session.

21. Mr. QADER (observer for Bangladesh) maintained that the practice of holding diplomatic conferences for the adoption of conventions was not merely a matter of tradition but one of substance as well. Thus far, no better system had been found. He suggested that, once the inconsistencies and drafting problems in the text had been worked out, the draft Convention should be sent to the Sixth Committee of the General Assembly, which could decide how it ought to be adopted. Only then should the text be sent to States for their comments.

22. Mr. EYZAGUIRRE (Chile) said it was clear that some further revision of the text of the draft Convention was still necessary. Final clauses were also required. He believed that the text should be sent in its current form to Governments for comments, after which the Working Group might make its final revisions, taking those comments into account. Then, at its twentieth session, the Commission might review the draft Convention article by article and decide on the final clauses.

23. Mrs. PIAGGI de VANOSI (Argentina) believed that the Working Group should be reconvened to finalize the text of the draft Convention. In addition, the secretariat should obtain the views of countries belonging to the Geneva system concerning possible conflicts between the draft Convention and the Geneva Uniform Law. She was in full agreement with the views expressed by the representative of the Netherlands.

24. Mrs. ADEBANJO (Nigeria) was in favour of transmitting the text directly to Governments for their comments. Those comments could then be considered by the Working Group and, subsequently, by the Commission at its twentieth session. The draft Convention would then be transmitted to the Sixth Committee for consideration, on the understanding that that Committee would not make any substantive changes in the text.

25. Mr. KOCH (Sweden) said it was clear that further work was needed on the existing text. That work should be done by the Working Group, which should be given the mandate of scrutinizing the text from the technical viewpoint and identifying any inconsistencies. Since everyone seemed to agree that there should be no diplomatic conference, he suggested that, instead of submitting the text to Governments for their comments—a procedure which might easily lead to a reopening of discussions on matters of substance—Governments should be given an opportunity to express their views at the next session of the Commission.

26. Mr. MARTYNOV (Union of Soviet Socialist Republics) supported the suggestion made by the representative of India. There would be no point in convening the Working Group for a further two-week session and then discussing the results of its work at the Commission's next session. That would almost totally offset the savings effected by the decision to dispense with a diplomatic conference—the normal procedure for adopting conventions.

27. Instead, the text of the draft Convention agreed to at the present session should be circulated to Governments for their comments—including comments on consistency within the text and on technical aspects. The secretariat could then transmit the comments to the Commission at its next session, together with the draft final clauses it might have prepared. Inviting States which were not members of the Commission to attend the next session of UNCITRAL to discuss the final text of the draft Convention would be an acceptable alternative to holding a diplomatic conference.

28. Mr. LIU Benku (China) thought that the draft Convention should now be sent to Governments for their comments and that the Working Group should analyse those comments and submit its analysis to the Commission at its next session.

29. Mr. CLIVENCIA (Spain) said that he could agree to the suggestion that the draft Convention should be adopted by the Sixth Committee. First, however, the remaining shortcomings in the text should be eliminated at a further session of the Working Group. The resulting text should then be submitted to Governments for their comments. After receiving and analysing the comments, the secretariat could issue a further report, which the Commission could consider at its twentieth session. Ideally the Working Group would by that time have drafted the final clauses.

30. Mr. GLATZ (Hungary) said that the technical task of identifying inconsistencies and lacunae might be performed better by the secretariat than by the Working Group. Since there was no question of holding a diplomatic conference, Governments must be given an opportunity to make their views known before the draft Convention was submitted to the Sixth Committee. That could be done by inviting all interested Governments to attend the next session of the Commission. At that session, the Commission should feel under no pressure to complete work on the draft Convention in the space of one week.

31. Mr. BRANDT (German Democratic Republic) agreed that the existing draft should be sent to Governments for their comments and that the secretariat should submit an analysis of the comments to the Commission at its next session, at which time the text could be finalized and adopted article by article. The amount of time that would be needed to adopt the draft

Convention would depend on the type of comments that were submitted.

32. Mr. MAKEKA (Lesotho) fully supported the proposal made earlier by the representative of India.

33. Mr. SAMI (Iraq) concurred with the majority view that the draft Convention should be circulated to all Governments for their comments. The Working Group could then meet to consider, analyse and reach a compromise on the comments. It could then submit a revised text to the Commission at its next session, to which all States could be invited. The text would, naturally, have to be considered article by article.

34. Mr. PFUND (United States of America) said that the difficulties arising from the desire to dispense with the normal procedure of convening a diplomatic conference were being compounded by the fact that the Commission's current session had been curtailed. He very much doubted that the Commission would be able, at its next session, to review the entire draft Convention in the light of the comments submitted by Governments unless the Working Group met to review those comments first. The Commission must decide forthwith whether work on the draft Convention could be completed in time for the text to be submitted to the Sixth Committee at the forty-second session of the General Assembly.

35. Mr. ABOUL-ENEIN (observer, Asian-African Legal Consultative Committee) said that he was in favour of giving all States Members of the United Nations an opportunity to comment on the draft Convention and requesting the Working Group to consider those comments prior to any final decision by the Commission. The decision as to whether the text should be approved by the Sixth Committee or by a diplomatic conference could be deferred until such time as a final decision had been taken on the actual text.

36. Mr. BERGSTEN (Secretary of the Commission) said that a consensus seemed to be forming that a diplomatic conference should be dispensed with, and that the procedure followed must involve the general membership of the Organization as far as possible. It had been suggested that all States should be invited to participate in the Commission's twentieth session. It was the established procedure that all States were invited as observers, but the Commission could recommend that the Sixth Committee, in its resolution on UNCITRAL, make that invitation specific. As to the suggestion that the text of the draft Convention should be circulated to Governments for comments, there were time constraints involved. The secretariat had scheduled a session of the Working Group on International Contract Practices from 1 to 12 December 1986 at Vienna; those dates could be used for a session of the Working Group on International Negotiable Instruments, or alternatively a session could be held from 8 to 19 December 1986, or from 19 to 23 January 1987. There would be insufficient time to circulate the text to Governments for comments, and submit them in documentary form to the Working Group on any of those dates. Furthermore, if a session of the Working Group was held in December or January, the text of the draft Convention would not be resubmitted to Governments prior to the Commission's twentieth session, but would simply appear in the report of the Working Group. The secretariat could make an analysis of comments from Governments and also review the text for technical inconsistencies and omissions and submit its comments to the Working Group; comments from Governments would then be submitted to the Commission at its twentieth session.

37. A four-week period from 20 July to 14 August 1987 had been reserved at Vienna for the Commission's twentieth session; the dates had been selected with a view to finalizing the Legal Guide on Drawing Up International Contracts for the Construction of Industrial Works. It should be borne in mind that the General Assembly might not approve the full four-week session. The secretariat believed that it would be better not to convene a session of the Working Group, but to invite comments from Governments; that procedure would allow more time and might elicit comments from a wider group of States.

38. Mr. DRUEY (observer for Switzerland) asked whether it would be possible to adopt the draft Convention article by article at the twentieth session of the Commission.

39. Mr. BERGSTEN (Secretary of the Commission) said that, if the Commission could complete that task within two weeks, or 10 working days, there would be eight days left to consider the Legal Guide and other matters; the last two days were not usually available for substantive discussion.

40. Mr. VIS (Netherlands) said that, if there was no meeting of the Working Group, the Commission would need much more time at its twentieth session to consider the draft Convention, since it was very difficult to adopt changes at a large meeting without having had the possibility of considering them in detail. It would be useful if comments from Governments could be placed before the Commission in documentary form at its twentieth session, with an analysis provided by the secretariat, and made available to the Working Group in raw form. Since Governments had already commented on the draft Convention two years previously, there should be sufficient time for them to submit additional comments.

41. Mr. MAKEKA (Lesotho) asked whether there would be financial implications if the Working Group met in December.

42. Mr. BERGSTEN (Secretary of the Commission) said that there would be no difficulty in scheduling a meeting in December since the General Assembly had agreed that there could be three meetings of working groups in 1986, and only two had been held so far.

43. With regard to the point raised by the representative of the Soviet Union, there would be financial implications in adopting an alternative procedure to a diplomatic conference, but they would be considerably lower than those involved in holding a conference.

44. Mr. MARTYNOV (Union of Soviet Socialist Republics) asked whether it would be possible for the draft Convention to be circulated immediately to Governments, without waiting for a General Assembly decision.

45. Mr. BERGSTEN (Secretary of the Commission) said that the text of the draft Convention could be circulated in the name of the Secretary-General on the basis of a request made by the Commission; that procedure had frequently been followed in the past. The text should be ready for circulation by early August. The normal procedure was for a note verbale to be sent to Permanent Missions in New York with copies to Permanent Missions accredited to Vienna.

46. Mr. BERAUDO (France) said that he hoped that the dates fixed for the session of the Working Group on Interna-

tional Contract Practices would not be changed, as meetings of other bodies dealing with topics in the field of international transport had been scheduled in the context of those dates. It was not worth holding a further meeting of the Working Group on International Negotiable Instruments; it had taken so long to draw up the draft Convention that a few extra weeks would not suffice to review the whole text. Since the Commission had decided not to hold a five-week diplomatic conference, it must avoid devoting a two-week session of the Working Group and two weeks at its own twentieth session to the same task. The Commission should confine its consideration of the draft Convention to two weeks at its twentieth session, so as to allow time for the other items on its agenda.

47. Mr. CUKER (Czechoslovakia) said that it was premature to send out the text of the draft Convention for comments, as the Sixth Committee might decide that a diplomatic conference should be convened.

48. Mr. BERGSTEN (Secretary of the Commission) said that, if the Commission wished to consider the draft Convention at its twentieth session in the light of comments from Governments, it would be advisable to circulate the text of the draft Convention as soon as possible, whether the comments were to be reviewed by the Working Group or the Commission. If the Sixth Committee decided that a diplomatic conference should be held, the draft Convention would still have to be sent to Governments for comments.

49. Mr. GRIFFITH (Australia) said that, if the Commission decided not to have a meeting of the Working Group, it would have to have a clear idea about the purpose of deferring the question of the draft Convention to its twentieth session. A consideration of the draft Convention article by article was desirable but, because of the time constraints, articles or groups of articles already approved by the Commission should be left aside. The Commission would have to consider textual amendments, in some cases proposed by Governments, but it should not consider new matters or reopen questions which had already been settled unless there was time available. The Commission had failed to complete its work at the current session and it must

finalize work on the draft Convention at the twentieth session. On that basis, his delegation would be prepared to dispense with the meeting of the Working Group.

50. Mr. BERGSTEN (Secretary of the Commission) said that the secretariat was aware that, if the Commission decided not to hold a meeting of the Working Group, it would have a heavy responsibility in preparing documentation for the twentieth session. It would send out the text of the draft Convention as early as possible, leaving adequate time to receive comments, especially from Governments not represented at the current session. Its report to the twentieth session would include an analysis of the comments received, as well as its own comments about technical and drafting questions. It could also prepare a chart showing which provisions had been adopted by specific decision of the Commission, especially at its current session, although that would not necessarily preclude the possibility of raising the matters again.

51. Mr. GANTEN (observer for the Federal Republic of Germany) said that it should be made clear that it would be possible to adopt the draft Convention at the twentieth session only if the preparations were so thorough that discussions such as those which had taken place during the current week could be avoided. The secretariat must study the draft Convention very carefully to identify possible inconsistencies and drafting defects and also any omissions. The task that was to have been done by the Working Group would therefore have to be carried out, to a large extent, by the secretariat, with advice from experts if necessary.

52. The CHAIRMAN said that there seemed to be general agreement that there would be no meeting of the Working Group; that the secretariat would circulate the final text of the draft Convention to Governments as soon as possible; and that before the twentieth session of the Commission the secretariat would prepare the necessary documentation on the draft Convention, as well as draft final clauses, seeking the advice of experts if necessary.

*The meeting rose at 1 p.m.*

### Summary record (partial)<sup>a</sup> of the 355th meeting Wednesday, 9 July 1986, 10 a.m.

[A/CN.9/SR.355<sup>b</sup>]

*Chairman:* Mr. KARTHA (India)

*The discussion covered in the summary record began at 10.25 a.m.*

#### International payments (continued)

(a) *Draft Convention on International Bills of Exchange and International Promissory Notes* (continued) (A/CN.9/274)

1. Mr. BERGSTEN (Secretary of the Commission) recalled that a letter from the Norwegian Ministry of Justice, containing

a proposed addition to paragraph (3) of article 23 *bis*, had been circulated the previous week. In the absence of any further indication, he would assume that the Commission had decided not to consider it.

2. The CHAIRMAN said that that understanding was correct.

#### Article 1 (A/CN.9/XIX/CRP.7)

3. Mr. VIS (Netherlands) said that the purpose of the amendments appeared to be to limit the application of the Convention to instruments that were locked into bank channels. The Working Group had discussed that idea and had rejected it as being too restrictive. He therefore opposed the amendment.

4. Mr. MAEDA (Japan) endorsed that statement.

<sup>a</sup>No summary record was prepared for the meeting before 10.25 a.m.

<sup>b</sup>No summary record was issued for the 354th meeting.

5. The CHAIRMAN said that it was thus understood that the Commission rejected the proposal.

Articles 44, 68, 69 and 73 (A/CN.9/XIX/CRP.15)

6. Mr. MAEDA (Japan) introduced the amendments proposed by the delegations of Japan and the Netherlands in document A/CN.9/XIX/CRP.15. The amendment to article 44 was designed to reflect the view, expressed at a previous meeting, that payment by a guarantor, whether full or partial, discharged of liability the party for whom he had become guarantor. Accordingly, the following should be added as article 44(1):

"Payment of an instrument by the guarantor in accordance with article 68 discharges the party for whom he became guarantor of his liability on the instrument to the extent of the amount paid."

The existing text of article 44 would become article 44(2).

It was further proposed that, in article 68(4), the following subparagraph (*a ter*) be added:

"If an instrument payable by instalments at successive dates is dishonoured by [non-acceptance or] non-payment as to any of its instalments and a party, upon the dishonour, pays the instalment, the holder who receives the payment must give the party a certified copy of the instrument and any necessary authenticated protest in order to enable such party to exercise a right on the instrument."

8. That would cover cases where A made a promissory note payable by instalments at successive dates to B and the note was subsequently endorsed by B to C, and by C to D. If D then presented it for payment of one instalment to A and A dishonoured the note by non-payment of that instalment, D could then exercise his right of recourse against C. C would then pay D and would have a right of recourse against B and a right on the instrument against the maker, A. Because C could not receive the note, he would need some other document in order to exercise that right. Those documents were the certified copy of the instrument and the authenticated protest, if he was exercising his right of recourse against B; he would need only a certified copy of the instrument if he exercised his right of recourse against A, the primary obligor. The words "non-acceptance or" were in square brackets because it had yet to be determined whether it would be conceivable for a drawee to accept some, but not all, of the instalments.

9. With respect to article 69, paragraph (3)(a) should read as follows:

"If the holder takes partial payment from the drawee, the guarantor of the drawee, or the acceptor or the maker:

"(a) The guarantor of the drawee, or the acceptor or the maker is discharged of his liability on the instrument to the extent of the amount paid; and ..."

10. Article 69(4)(b) would read as follows:

"If the holder takes partial payment from a party to the instrument other than the acceptor or the maker or the guarantor of the drawee:

"(a) ...

"(b) The holder must give such party a certified copy of the instrument and any necessary authenticated protest in order to enable such party to exercise a right on the instrument."

The words "any necessary authenticated protest" had been added because, if the party making payment was the guarantor, the acceptor or the maker, or if the protest was dispensed with according to article 58(2), or if a party making payment exercised a right on the instrument against a primary obligor, the party making payment did not have to be given the protest in order to exercise a right on the instrument.

11. In article 73(1), the words "a right of recourse" should be replaced by the words "a right on the instrument". The right of recourse as outlined in paragraphs 55 to 64 covered only rights on an instrument against a secondary obligor. The term "right on the instrument", which was also used in the proposed amendment to article 69(4)(b), was much broader and would cover all rights on the instrument.

12. Mr. BRANDT (German Democratic Republic), Mr. SAMI (Iraq) and Mr. ABASCAL (Mexico) supported the amendment to article 44.

13. Mr. SAMI (Iraq) also agreed to the proposed amendment to article 68. However, he suggested that the words "non-acceptance or" should be deleted, as they were superfluous. In case of non-acceptance, the amount due would still be due.

14. Mr. VIS (Netherlands) said that it would not be wrong to retain the words, even though some members might consider them superfluous.

15. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that there was not enough time for a detailed analysis of the proposal concerning article 68(4) (*a ter*) but that at first sight it could be supported. The words "non-acceptance or" should be included, since recourse could occur even after non-acceptance; the paragraph would then cover all types of recourse which might arise in cases of payment by instalments.

16. In article 68(4) (*a bis*), of the draft Convention, the words "or a party" should be deleted. Inclusion of those words suggested that the payment was not a normal payment but a payment by recourse. If that was the case, the party needed not only a receipt but also a copy of the protest.

17. Mr. VIS (Netherlands) said that, whether it was an acceptor or the maker of a note who made payment by instalments, there were equally valid reasons to give him the right to require that mention of the payment be made on the instrument. He therefore preferred the existing text of article 68(4) (*a bis*).

18. Mrs. KAZAKOVA (Union of Soviet Socialist Republics) said that she agreed that the text did not refer only to the drawee, but also to the acceptor and the maker; however, it must be made clear what parties were being referred to, and parties with secondary liability should not be included.

19. Mr. VIS (Netherlands) said that, when a person was paid by instalments, it was required that he hand over the instrument

to the person making payment. That rule protected the latter party: if an instrument was transferred to a protected holder, a person who had already made payment might have to pay again. There were cases where an obligor could not be given the instrument, as in the case of payment by instalments; the instrument should then remain in the possession of the payee, so that he was maintained as a holder and was able to request the payment of further instalments. However, the need to protect the party who had paid remained. If in a recourse situation on an instalment bill or note, a party who was secondarily liable had paid, it was for his protection that a mention was made on the bill, so that there could not be a protected holder of that particular instalment. He felt that the existing text must stand so as to protect the obligor, whether he was primarily or secondarily liable.

20. Mrs. PIAGGI de VANOSI (Argentina) said the words "or a party" were clearly designed to protect anyone—either a principal or secondary obligor—who had made a partial payment on an instrument payable by instalments. Otherwise, if reference was made only to the maker or the acceptor, there was no protection for a secondary obligor and, if there was no receipt or record of title, payment could be demanded from a person who had already paid. Article 50 was closely connected with article 68.

21. Mr. MAEDA (Japan) said that he was in favour of the existing text. Article 68(4) (*a bis*) and 69(5) were designed to ensure that a party making payment was not in danger of being forced to make double payment, while articles 68(4) (*a ter*) and 69(4)(b) were designed to enable a party to exercise a right on the instrument. Thus the two sets of provisions had different purposes and should both be retained.

22. Mr. VIS (Netherlands) said that, in the proposal for a new paragraph (4) (*a ter*) in article 68, the words "upon the dishonour" should be changed to "upon dishonour" and the words "who receives the payment" should be changed to "who receives such payment" in order to bring the paragraph into line with other articles.

23. The CHAIRMAN said that, if he heard no objection, he would take it that all the proposals in document A/CN.9/XIX/CRP.15 were adopted.

24. *It was so decided.*

*Modifications proposed by the drafting group (A/CN.9/XIX/CRP.12 and Add.1)*

*Article 1(2)(e) and (3)(e)*

25. Mr. HERRMANN (International Trade Law Branch), introducing the modifications proposed by the drafting group, said that the drafting group had endeavoured to prepare appropriate wording for the substantive amendments adopted by the Commission and to establish corresponding versions in the six official languages of the United Nations. As regards article 1(2)(e) and (3)(e), it was proposed that the opening words should be replaced by:

"(e) Specifies at least two of the following places and indicates that any two so specified are situated in different States:".

26. *It was so decided.*

*Article 2*

27. Mr. HERRMANN (International Trade Law Branch) said that the drafting group had wished to make the article apply irrespective of conflict-of-law rules, but had been unable to find an acceptable wording. It had therefore opted for a slightly more imperative wording and proposed that the beginning of the sentence should be amended to read: "A Contracting State shall apply this Convention without regard to whether ...".

28. Mr. VIS (Netherlands) said that the modification of article 2 narrowed the scope of the Convention. Although only Contracting States would be bound by the Convention, it had always been felt that if non-Contracting States, because of their own conflict-of-law rules, applied the provisions of the Convention, article 2 would apply to those States.

29. Mr. DUCHEK (Austria) said that the modified text of article 2 was acceptable. It would not prevent a non-Contracting State from applying the draft Convention if its internal law made that possible. The Convention was addressed only to Contracting States, but non-Contracting States were not restricted by any wording regarding the scope of application.

30. Mr. LEBEDEV (Union of Soviet Socialist Republics) said that the new wording of article 2 was not in conformity with the usual practice in conventions on international private law and other conventions adopted by UNCITRAL so far, nor for that matter with actual practice. The Contracting State was not necessarily directly involved in the actual application of the Convention—as, for instance, in cases involving arbitration outside State courts. His delegation believed that it was better to retain the original wording with the following slight change: "This Convention shall apply without regard to whether ...".

31. Mr. VENKATRAMIAH (India), Mr. VIS (Netherlands), Mr. SEVON (observer for Finland) and Mr. WOOLMAN (United Kingdom) supported the proposal of the Soviet Union representative.

32. The CHAIRMAN said that, if he heard no objection, he would take it that the Commission wished to adopt the new wording of article 2 proposed by the Soviet Union representative.

33. *It was so decided.*

*Article 4(7)(a)*

34. Mr. HERRMANN (International Trade Law Branch) said that it was proposed that the words "other than in paragraph(1)(c)(ii) thereof" be inserted after the words "referred to in article 25". That modification followed the wording already approved by the Commission, with the addition of the word "thereof".

35. *It was so decided.*

*Article 4(10) and (x)*

36. Mr. HERMANN (International Trade Law Branch) said that it was proposed that the text of article 4(10) be replaced by:

“(10) ‘Signature’ means a handwritten signature, or a facsimile thereof, or any other means of effecting the equivalent authentication, and ‘forged signature’ includes ....”.

Article X would then be deleted.

37. *It was so decided.*

Article 4(11)

38. Mr. HERRMANN (International Trade Law Branch), said that it was proposed that the end of the text be amended to read:

“... two or more States, provided that this Convention shall apply without prejudice to the rules of the intergovernmental institution or to the stipulation of the agreement.”

39. *It was so decided.*

Article 7

40. Mr. HERRMANN (International Trade Law Branch) said that it was proposed that the three new paragraphs adopted by the Commission be worded as follows:

“(5) A rate at which interest is to be paid may be expressed either as a definite rate or as a variable rate. For a variable rate to qualify for this purpose, it must vary in relation to one or more reference rates of interest in accordance with provisions stipulated in the instrument and each such reference rate must be published or otherwise available to the public and not subject, directly or indirectly, to unilateral determination by any person who, at the time the bill is drawn or the note is made, is named in the instrument as payee, drawee, or actual or prospective party or other holder.

“(5 bis) Where the rate at which interest is to be paid is expressed as a variable rate, it may be stipulated expressly on the instrument that such rate shall not be less than or exceed a specified rate of interest, or that the variations are otherwise limited.

“(6) If a variable rate does not qualify under paragraph (5) of this article or for any reason it is not possible to determine the numerical value of the variable rate for any period, interest shall be payable for the relevant period at the rate calculated in accordance with article 66(2).”

41. Mr. GANTEN (observer for the Federal Republic of Germany) asked why the words “or prospective” had been added in the last line of the new paragraph (5).

42. Mr. HERRMANN (International Trade Law Branch) said that the wording originally approved by the Commission had been “... a person named in the instrument”. The Commission had instructed the drafting group to find a wording that would ensure that the provision could not be interpreted as covering a party named in an instrument in the context of a variation clause. The drafting group had tried to list all the parties which should be covered and to exclude any bank or party mentioned in connection with the variation clause.

43. Mr. VIS (Netherlands) thought that the policy underlying the last few lines of paragraph (5) was to protect parties who at

the time of payment either were obliged to pay on an instrument or had the right to receive payment.

44. Mr. PFUND (United States of America) said that the maker was in fact included because he would fall into the category of an actual party. The drafting group’s goal had been to specify a series of persons who, as the instrument passed from hand to hand, should not be able to tamper with the rate.

45. The CHAIRMAN said that he would take it, if he heard no objection, that the Commission wished to adopt the modification proposed by the drafting group.

46. *It was so decided.*

*The meeting was suspended at 11.45 a.m. and resumed at 12.05 p.m.*

Articles 16 and 20(3)

47. Mr. HERRMANN (International Trade Law Branch) said that, following a decision by the Commission to clarify the legal effect of a clause or endorsement restricting further transfer, it was proposed that the existing text of article 16 should become paragraph (1), with the addition of the words “, and any endorsement, even if it does not contain words authorizing the endorsee to collect the instrument, is deemed to be an endorsement for collection.”.

48. Paragraph (2) would consist of the former article 20(3), amended by the addition of the following words at the end of the sentence: “, and any subsequent endorsement, even if it does not contain words authorizing the endorsee to collect the instrument is deemed to be an endorsement for collection.”.

49. Mr. SMART (Sierra Leone), noting that he had not been present when the articles in question had been discussed, said that he found the additions unnecessary but could accept them.

50. *The proposed modifications were adopted.*

Article 17(2)

51. Mr. HERRMANN (International Trade Law Branch) said that it was proposed to add a second sentence to article 17(2): “The condition is deemed not to have been written as to parties and transferees subsequent to the endorsee”. It had not been clear to the drafting group whether the Commission had intended the amendment to replace the original paragraph (2), but it had been felt that for the sake of clarity it was better to retain the original paragraph (2), which dealt with the question of transferability, and to add a new sentence concerning liability.

52. Mr. VIS (Netherlands), supported by Mr. MAEDA (Japan), said that he had misgivings regarding the proposed addition. The condition would be on the instrument, after all, and subsequent endorsees would therefore have some knowledge of it.

53. The point that should be made in article 17(2) was that the condition did not affect the negotiability of the instrument, and that the endorsee was therefore a holder whether or not the condition had been fulfilled. The commentary on article 17 in document A/CN.9/213 had rightly noted that the fact that a condition was not fulfilled was not, however, irrelevant, particu-



larly with reference to defences that could be raised. It was probably therefore not correct to say that the condition was "deemed not to have been written".

54. *The proposed modification was adopted.*

55. The CHAIRMAN said that the position of the representatives of the Netherlands and Japan would be reflected in the report.

*Articles 23 and 23 bis*

56. Mr. HERRMANN (International Trade Law Branch) said that it was proposed that article 23(1)(c) should read: "(c) A party or the drawee who paid the instrument to the forger directly or through one or more endorsees for collection."

57. Article 23(2) should read:

"(2) However, an endorsee for collection shall not be liable under paragraph (1) if at the time:

"(a) At which he pays the principal or advises the principal of the receipt of the proceeds of the instrument, or

"(b) He receives the proceeds of the instrument, whichever comes later, he is without knowledge of the forgery, provided that such absence of knowledge is not due to his negligence."

58. The parallel provisions in article 23 bis should be amended accordingly. Thus, article 23 bis (1)(c) would read: "(c) A party or the drawee who paid the instrument to the agent directly or through one or more endorsees for collection."

59. Furthermore, article 23 bis (2) would read:

"(2) However, an endorsee for collection shall not be liable under paragraph (1) if at the time:

"(a) At which he pays the principal or advises the principal of the receipt of the proceeds of the instrument, or

"(b) He receives the proceeds of the instrument, whichever comes later, he is without knowledge that the endorsement does not bind the principal, provided that such absence of knowledge is not due to his negligence."

60. Mr. VIS (Netherlands), supported by Mr. SAMI (Iraq) and Mr. SMART (Sierra Leone), suggested that, in both articles 23(2) and 23 bis (2) the words "At which" in subparagraph (a) should be moved to the end of the *chapeau* of article (2), after the words "at the time".

61. The CHAIRMAN said that he would take it, if he heard no objection, that the Commission wished to adopt the modifications to articles 23 and 23 bis proposed by the drafting group, as further modified by the representative of the Netherlands.

62. *It was so decided.*

*Article 25(1)(b)*

63. Mr. HERRMANN (International Trade Law Branch) said that it was proposed that article 25(1)(b) should read:

"(b) Except as provided in paragraph (2 bis) of this article, any defence based on an underlying transaction between

himself and the drawer or between himself and the holder succeeding himself or arising from the circumstances as a result of which he became a party;"

64. The meaning of that provision required some elucidation. It did not cover any transaction with a maker, and it covered a transaction with the drawer only where payment had been requested from the acceptor. The drafting group had also felt that, in the original text, the reference to an underlying transaction between the party and "a previous holder" was misleading. The article actually meant to refer to a transaction between the party from whom payment was requested and the party immediately subsequent to himself, not the previous holder. Thus, it would not matter whether, in a recourse, payment was requested from him by a remote holder or by his endorsee.

65. Mr. VIS (Netherlands) said that article 25 in general was extremely difficult to understand and had to be scrutinized very carefully. He found the wording of article 25(1)(b) inelegant, and proposed changing the word "an" before the word "underlying" to "the", and replacing the words "holder succeeding himself" by the words "party subsequent to himself".

66. Mr. FELSENFELD (United States of America) suggested that the remainder of the meeting should be devoted to a discussion of the procedure for the adoption of the draft Convention.

67. Mr. BERGSTEN (Secretary of the Commission) recalled that there were three options. First, in accordance with normal procedure, a three-week diplomatic conference could be recommended to the Sixth Committee of the General Assembly. Second, the Working Group could meet in early January, at Vienna, and the Commission would then devote two or three weeks to the draft Convention at its twentieth session. Third, no Working Group meeting would be scheduled, but the Commission would devote a full three weeks in 1987 to reviewing the draft Convention.

68. Those three options had varying financial implications and it was probable that, in the light of the current financial crisis, the General Assembly would not agree to a diplomatic conference, at an estimated cost of \$2 million to \$2.2 million. Furthermore, requesting a conference might delay the Commission's work, since it would not be known until December 1986 whether the request had been granted or denied.

69. It would cost \$670,000 to consider the draft Convention at both a meeting of the Working Group at Vienna from 5 to 16 January 1987 and during two weeks of the Commission's twentieth session. It would cost \$800,000 if the Working Group met, and the Commission then devoted three weeks in 1987 to the draft Convention. Comments from Governments would have to be received by about 15 November 1986 to prepare for a January 1987 meeting of the Working Group and, owing to time constraints, they would have to be considered without an analytical compilation. Documentation would be easier, and therefore less costly, for the third option, which would probably reduce expenses to \$550,000. It would mean, however, that the entire burden of reviewing the draft Convention would rest upon the Commission at its twentieth session.

Summary record (partial)<sup>a</sup> of the 356th meeting  
Wednesday, 9 July 1986, 3 p.m.

[A/CN.9/SR.356]

Chairman: Mr. KARTHA (India)

*The meeting was called to order at 3.05 p.m.*

**International payments (continued)**

(a) Draft Convention on International Bills of Exchange and International Promissory Notes (continued) (A/CN.9/274)

1. Mr. BERGSTEN (Secretary of the Commission) recalled the three options available for dealing with the draft Convention. The first was to follow the normal procedure and request the Sixth Committee to convene a three-week diplomatic conference. The second was for the Commission to resume consideration of the draft Convention during its twentieth session for 10 to 15 days, after a Working Group session early in January 1987 to discuss any remaining problems. The third was for the Commission to take up the draft Convention at its twentieth session without a prior meeting of the Working Group. Under the second or third option, if the draft Convention was discussed for two weeks at the twentieth session, up to eight days would remain for the discussion of other items; if the draft Convention took up three weeks of discussion, only three days would remain for the consideration of other items.
2. The CHAIRMAN invited members to indicate their positions on each of the three options.
3. Mr. DRUEY (observer for Switzerland) asked whether the Commission actually had the power to decide that there would be a diplomatic conference and whether, if the draft resolution which the Commission would submit to the Sixth Committee did not mention the possibility of such a conference, the Sixth Committee might nevertheless decide to convene one.
4. Mr. BERGSTEN (Secretary of the Commission) said that the Commission could only make a recommendation. The final decision rested with the Fifth and Sixth Committees.
5. Mr. BERAUDO (France) felt that a diplomatic conference was the most appropriate way of obtaining a good legal text. It would also allow States to examine the articles and review the structure of the draft Convention. It would enable drafting committees to work in various languages and would be conducted under the rules of procedure for such conferences. As to the argument that a diplomatic conference would cost too much, he felt that the Sixth Committee should bear the responsibility of deciding whether quality should be sacrificed for financial reasons.
6. Mr. MARTYNOV (Union of Soviet Socialist Republics) said that his delegation supported the convening of a diplomatic conference for the same reasons as had been given by the delegation of France. Although the final decision would be taken by the Fifth and Sixth Committees, he felt that the question of substance should take precedence over that of finances.
7. Mr. BRANDT (German Democratic Republic) said that he also supported the convening of a diplomatic conference.

8. Mr. LEAES (Brazil) said that, although he felt that a diplomatic conference would be preferable, he would support the second option because it would allow the Working Group to meet and consider States' comments and opinions.

9. Mr. VIS (Netherlands) believed strongly that a diplomatic conference was neither justified in the circumstances nor necessarily the best procedure for adopting the draft Convention. Diplomatic conferences were more appropriate to the adoption of public law than to that of private law. Moreover, he noted that the UNCITRAL Arbitration Rules had been adopted without a diplomatic conference. He therefore supported either the second or the third option.

10. Mr. DUCHEK (Austria) said that he supported the second option, because he felt that further work was needed on the text before it could be sent to the General Assembly. If there had been a real possibility that the Sixth Committee would convene a diplomatic conference despite the financial implications, he would have supported the first option. A session of the Working Group in January would be useful; without it, there would not be enough time to finalize the text at the Commission's twentieth session. Three days would certainly be insufficient time to discuss the other matters which the Commission would have before it at that time.

11. Mr. SAMI (Iraq) also supported the second option. It would be premature to request a diplomatic conference; the draft Convention was incomplete and contained many shortcomings and contradictions. All States should submit their comments and observations for the Working Group session prior to the twentieth session of the Commission. If it was found that many States disagreed about the readiness of the draft Convention, the Commission could then recommend the convening of a diplomatic conference.

12. Mr. QADER (observer for Bangladesh), supported by Mr. GOH (Singapore), said that he preferred the option of a diplomatic conference. If, however, the General Assembly decided that it would adopt the draft Convention, then he would be in favour of the Commission itself finalizing it.

13. Mr. SMART (Sierra Leone) said that it was clear that the lack of support for the idea of convening a diplomatic conference was largely due to the high cost involved. The same argument could be used against the proposal to convene a session of the Working Group to review the draft Convention. Consequently, the only viable option was for the Commission itself to finalize the draft Convention.

14. Mr. VENKATRAMIAH (India), supported by Mrs. ADEBANJO (Nigeria), expressed support for the third option.

15. Mrs. VILUS (Yugoslavia) said that, while she would support the third option if the idea of a diplomatic conference was not feasible, she doubted whether the Commission would be able at its twentieth session to consider both the draft Legal Guide on Drawing Up International Contracts for the Construction of Industrial Works and the draft Convention on International Bills of Exchange and International Promissory Notes.

16. Mr. IBRAHIM (Egypt) said that he was in favour of the convening of a diplomatic conference. Only the General Assem-

<sup>a</sup>No summary record was prepared for the meeting after 5.30 p.m.

bly could determine whether the financial situation of the Organization precluded that possibility and the Commission could not decide on a recommendation until that question had been determined.

17. The CHAIRMAN noted that a majority of the members of the Commission supported the second option.

18. Mr. BERGSTEN (Secretary of the Commission) suggested that the Commission should request the Secretary-General to send the draft Convention to all States and interested international organizations for comments. The draft Convention and the comments received would be submitted to the Working Group in January 1987. The Commission would then consider the draft Convention at its twentieth session in the light of both the comments received and the report of the Working Group. In its report on the work of its nineteenth session, the Commission should therefore indicate that the draft Convention would be ready for submission to the General Assembly in 1987.

19. *It was so decided.*

20. Mr. BERAUDO (France), supported by Mr. LEAES (Brazil), said that, since the Working Group would be taking the place of a full diplomatic conference, its mandate should not be restricted. Substantive modifications to the text might be proposed in the Working Group and during the twentieth session of the Commission.

21. Mr. DELFINO-CAZET (Uruguay) said that the mandate of the Working Group should be broad enough to permit it to correct any inconsistencies and lacunae in the draft Convention.

22. Mr. QADER (observer for Bangladesh) questioned the procedure used to ascertain the majority view in the Commission.

23. Mr. SEVON (observer for Finland) said it was his understanding that, if the Commission's request for a four-week session in 1987 was not approved by the General Assembly, the Commission would not include consideration of the draft Legal Guide on Drawing Up International Contracts for the Construction of Industrial Works on the agenda of its twentieth session.

24. Mr. LEBEDEV (Union of Soviet Socialist Republics) expressed disappointment and concern at the method used by the Commission to arrive at its decision. It would have been better to report to the General Assembly that opinions within the Commission were divided and that more information was required before a decision could be reached.

25. He wondered whether the financial difficulties of the Organization would really preclude a diplomatic conference and whether the Sixth Committee was ready to adopt a convention on such a specialized subject through the simplified procedure that was being endorsed.

26. Mr. VIS (Netherlands) supported the view of the Soviet Union representative that, if the procedure decided upon was retained, the realities of the discussion just held should be reflected in the Commission's report.

27. Mr. SAMI (Iraq) agreed that the report of the Commission should reflect the diverse views which had been expressed during the discussion. His delegation was in favour of increasing

the membership of the Working Group, since it was important to ensure that both civil-law and common-law countries were adequately represented.

28. Mr. EYZAGUIRRE (Chile) said that the Working Group should be composed of all the members of the Commission and should have a relatively broad mandate. He agreed with the observer for Finland that the Commission could not devote its twentieth session exclusively to the draft Convention; it would have before it many other important items.

29. The CHAIRMAN said that, if he heard no objection, he would take it that the composition of the Working Group would be expanded to include all members of the Commission.

30. *It was so decided.*

31. Mr. DRUEY (observer for Switzerland) said that, since the Commission had agreed to expand the Working Group, the modifications proposed by the drafting group with regard to article 2 and a number of other articles should be the first matter to be taken up by the Working Group.

32. Mr. BERGSTEN (Secretary of the Commission) said that the Commission at its next session might wish to return to the question of the composition of working groups. The expanded composition of the Working Group would not have any financial implications.

*Modifications proposed by the drafting group (A/CN.9/XIX/CRP.12 and Add.1 and Add.2)*

*Article 25(1)(b)*

33. Mr. HERRMANN (International Trade Law Branch) said the representative of the Netherlands had proposed that article 25(1)(b) should be amended to read:

“(b) Except as provided in paragraph (2 bis) of this article, any defence based on the underlying transaction between himself and the drawer or between himself and the party subsequent to himself or arising from the circumstances as a result of which he became a party;”

34. Mr. MAEDA (Japan) supported the proposal.

35. *The proposed modification was adopted.*

*Article 25(1)(c)*

36. Mr. HERRMANN (International Trade Law Branch) said the drafting group had proposed that article 25(1)(c) should be amended to read:

“(c) Any defence resulting from:

- (i) The underlying transaction between himself and the holder;
- (ii) Any other transaction between himself and the holder that would be available as a defence against contractual liability.”

37. *The proposed modifications were adopted.*

*Article 25(2)*

38. Mr. HERRMANN (International Trade Law Branch) said the drafting group had proposed that article 25(2) should be amended to read:

“(2) Except as provided in paragraph (2 *bis*), the rights to an instrument of a holder who is not a protected holder are subject to any claim to the instrument on the part of any person.”

The word “valid”, which had appeared before the word “claim”, had been deleted, and that the same change had been made in articles 25(3)(a), 26(2) and 68(3).

39. Mr. VIS (Netherlands), supported by Mr. MAEDA (Japan), said that the drafting group’s mandate had been to clarify the meaning of the word “valid”, but not to delete it. The classical rule of *ius tertii* was that the obligor could not set up the claim of a third party to the instrument as a defence to his own liability, and the Commission should adhere to that rule.

40. Mr. HERRMANN (International Trade Law Branch) said that the drafting group, after considering several proposed drafting modifications, had concluded that it would be advisable to delete the word “valid”.

41. Mr. MAEDA (Japan) said that he was in favour of retaining the word “valid” in the text of article 25(2).

42. Mrs. PIAGGI de VANOSI (Argentina) said that her delegation considered that the retention of the word “valid” in article 25(2) would give the impression that a judicial decision had been taken with regard to the validity of the claim. However, the deletion of that word would also give rise to objections, and she suggested that the wording of the relevant part of article 25(2) should be modified to read “a claim based on law”.

43. Mr. HERRMANN (International Trade Law Branch) suggested that the word “valid” should be retained in all places in which it had been deleted, and the Working Group should be requested to propose a better wording which it would present to the Commission at its next session.

44. *It was so decided.*

#### Article 25(2 *bis*)

45. Mr. HERRMANN (International Trade Law Branch) said the drafting group had proposed that article 25(2 *bis*) should be amended to read:

“(2 *bis*) A holder who is not a protected holder and who took the instrument before maturity is subject to a defence under paragraph (1)(b) or to a claim under paragraph (2) of this article only if he took the instrument with knowledge of such defence or claim or if he obtained the instrument by fraud or theft or participated at any time in a fraud or theft concerning it.”

Those modifications had been made by the drafting group in an attempt to implement the Commission’s decision, which had been based on the proposal by the representative of Japan to retain the original text but to add to it the words “except that a holder who takes the instrument after the expiration of the time-limit for presentment for payment is subject to any claim or defence upon the instrument to which his transferrer is subject”. The drafting group had felt that the same idea could be simplified by making article 25(2) applicable only to a non-protected holder who took an instrument before maturity.

However, he personally believed that the new wording resulted in a difference in the substance of article 25(2 *bis*).

46. Mr. MAEDA (Japan) agreed that the drafting group had changed the substance of article 25(2 *bis*); he therefore proposed that the wording of his original proposal should be retained.

47. Mr. HERRMANN (International Trade Law Branch) suggested that the Commission should adopt the original wording of article 25(2 *bis*) and add the following sentence, along the lines of the proposal by the representative of Japan:

“However, a holder who takes the instrument after the expiration of the time-limit for presentment of payment is subject to any claim to or defence upon the instrument to which his transferrer is subject.”

48. *It was so decided.*

#### Article 30

49. Mr. HERRMANN (International Trade Law Branch) said the drafting group had proposed that the second sentence of article 30 should be amended to read:

“Nevertheless, where such person has assented that he was bound by the forged signature or represented that the signature was his own, he is liable as if he had signed the instrument himself.”

50. Mr. VIS (Netherlands) questioned the use of the word “assented”, and suggested that the phrase “assented that he was bound” should be amended to read “assented to be bound”.

51. Mr. BURNS (Australia) said that his delegation shared the misgivings of the representative of the Netherlands, and asked why the word “assented” had been chosen to replace the word “accepted”.

52. Mr. HERRMANN (International Trade Law Branch) suggested that the original wording “accepted to be bound” should be retained.

53. *It was so decided.*

#### Articles 34(1), 35(1) and 40(1)

54. Mr. HERRMANN (International Trade Law Branch) said the drafting group had proposed that the words “any subsequent party” in article 34(1) and the words “any party” in article 35(1) should be replaced by the words “any endorser or any endorser’s guarantor”. The words “any subsequent party” contained in article 40(1) should be replaced by the words “any subsequent endorser or such endorser’s guarantor”.

55. *The proposed modifications were adopted.*

#### Article 38(1)

56. Mr. HERRMANN (International Trade Law Branch) said the drafting group had proposed that a second sentence should be added to article 38(1), reading:

“In such case, article 11 shall apply accordingly to completion by the drawer or another person.”

The observer for Switzerland had suggested that there might be an inconsistency between article 11 and article 38(1), and, as authorized by the Commission, had submitted a proposal directly to the drafting group in which reference was made to article 11(2) only. However, the drafting group had considered that such a reference would not be sufficient, since it would only cover the instance of a completion without authority and then set forth the legal consequences of such completion, but it would not expressly allow the completion of such an instrument which had been accepted before it was signed by the drawer; the completion would relate primarily to the signature of the drawer himself and another formal requisite deriving from article 1(2).

57. Mr. VIS (Netherlands), supported by Mr. DELFINO-CAZET (Uruguay), Mr. BURNS (Australia) and Mr. KOCH (Sweden), suggested that the Commission suspend discussion of the modifications proposed by the drafting group and that the secretariat should submit them to the open-ended Working Group once it had received observations from Governments.

58. Mr. BERGSTEN (Secretary of the Commission) said that the drafting group had submitted the modifications as requested by the Commission. He believed that it would be more logical for the Commission to accept the modifications of the drafting group and incorporate them into the text of the draft Convention as contained in document A/CN.9/274.

59. Mr. VIS (Netherlands) said that the Secretary's suggestion would have been acceptable if the drafting group had not gone beyond its mandate.

60. Mr. DUCHEK (Australia) said that if the Secretary's suggestion was not accepted, then most of the work done during the past week would have been in vain. He therefore believed that the modifications proposed by the drafting group should be accepted as part of the Commission's report and submitted to the open-ended Working Group.

61. Mr. BERGSTEN (Secretary of the Commission) said that the document to be submitted by the secretariat to the Working Group would indicate the parts of the draft Convention that had been modified by the drafting group but had not been discussed by the Commission in plenary.

62. *It was decided that the remaining modifications proposed by the Working Group would be incorporated into the text of the draft Convention to be circulated to Governments and international organizations for their comments, and to indicate that those proposals had not been reviewed by the Commission.*

63. The CHAIRMAN thanked the members of the drafting group for the valuable work they had done.

*The discussion covered in the summary record ended at 5.30 p.m.*

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## VI. New international economic order

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## VII. Other topics

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## IV. CHECK-LIST OF UNCITRAL DOCUMENTS

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<b>A. List of documents before the Commission at its nineteenth session</b>		
<b>1. General series</b>		
A/CN.9/272	Provisional agenda	Not reproduced
A/CN.9/273	Report of the Working Group on International Negotiable Instruments on the work of its fourteenth session (Vienna, 9–20 December 1985)	Part two, I, A, 1
A/CN.9/274	Draft Convention on International Bills of Exchange and Promissory Notes: text of draft articles as revised by the Commission at its seventeenth session or by the Working Group on International Negotiable Instruments at its thirteenth or fourteenth session: note by the secretariat	Part two, I, A, 2
A/CN.9/275	Report of the Working Group on International Contract Practices on the work of its ninth session (New York, 6–17 January 1986)	Part two, III, A
A/CN.9/276	Report of the Working Group on the New International Economic Order on the work of its eighth session (Vienna, 17–27 March 1986)	Part two, II, A
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A/CN.9/278	Electronic funds transfers: report of the Secretary-General	Part two, I, B
A/CN.9/279	Legal implications of automatic data processing: report of the Secretary-General	Part two, V
A/CN.9/280	Co-ordination of work: activities of international organizations on certain aspects of arbitration: report of the Secretary-General	Part two, IV
A/CN.9/281	Current activities of international organizations related to the harmonization and unification of international trade law: report of the Secretary-General	Part two, VI
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A/CN.9/285	Draft Convention on International Bills of Exchange and International Promissory Notes: response to requests of the Working Group on International Negotiable Instruments: note by the secretariat	Part two, I, A, 4
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A/CN.9/XIX/CRP.16	Draft Convention on International Bills of Exchange and International Promissory Notes	Appeared as annex I to A/41/17, and reproduced in the present volume, part three, I

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<i>Document symbol</i>	<i>Title or description</i>	<i>Location in present volume</i>
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A/CN.9/WG.V/WP.17/ Add.9	Draft Legal Guide on Drawing Up International Contracts for Construction of Industrial Works: chapter XXV: Termination of contract: report of the Secretary-General	Part two, II, B

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<b>D. List of documents before the Working Group on International Contract Practices at its ninth session</b>		
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## V. CROSS-REFERENCES: UNCITRAL DOCUMENTS REFERRED TO IN THE PRESENT VOLUME AND REPRODUCED IN THIS VOLUME OR AN EARLIER VOLUME OF THE YEARBOOK

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## 3. *Official Records of the General Assembly*

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## 5. *Summary records*

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