Contractual Obligations and the Rome Convention

Aim:
To note the impact of legislation on contractual obligations connected with, or litigated in, a Contracting State.

Objectives.
After careful study of the following notes, and other prescribed readings for this lecture, you will be able to:
1. Discuss the scope of the Rome Convention on the Law Applicable to Contractual Obligations;
2. Discuss the provisions relating to party autonomy in making a contract under the Rome Convention;
3. Explain how the principle of closest connection applies to contracts the choice of law of which is neither expressly chosen nor demonstrated with reasonable certainty.

Choice of Law in Contract Under the E.C. Convention.
The unification of all the rules of private international law within the EC was proposed even before the Brussels Convention of 1968. Although some of the proposals have been shelved (temporarily, anyway) the uniformity of the rules applicable to contractual obligations has been achieved via the ***1980 Rome Convention on the Law Applicable to Contractual Obligations*** which is incorporated into English law with the enactment of the ***Contracts (Applicable Law) Act 1990, s.2(1).***

Scope of the Convention.
Art. 1(1) provides that 'the rules of this Convention shall apply to contractual obligations in *any situation* involving a choice between the laws of different countries.'

However, the matters to which ***the Convention does <u>not</u> apply*** are specified in ***Article 1(2)*** and ***(3)***. They include the capacity and status of natural and legal persons, contractual obligations relating to wills and succession, rights in property arising out of a matrimonial relationship, rights and duties arising out of a family relationship, obligations arising under most aspects of negotiable instruments, ***arbitration agreements and agreement on the choice of courts***, questions governed by company law, agency, trusts, evidence and procedure (subject to Article 14) and insurance (but not re-insurance) of risks situated within the E.C.

Notwithstanding the exceptions, that the Convention applies to '*any situation*' means that it applies not only to contracts having a close or real connection with Contracting States of the E.C. but also to contracts which have no connection with any E.C. Contracting State but which happened to be litigated in a court of a Contracting State. The breadth of the Convention is further conveyed by ***Article 2*** which provides that: any law specified by the Convention is to be applied whether or not it is the law of a Contracting State .

Two points with respect to the interpretation of Art 1(1) now have to be addressed :
(a) What legal system determines whether there is a contractual relationship? and
(b) How is 'countries' interpreted?

(a) What legal system determines whether there is a contractual relationship?
The problem here is that one Contracting State may regard a matter as a contractual obligation whereas another does not because, for example, it lacks consideration. Reasoning by analogy, it may be considered that since ***Article 8(1)*** provides that the *validity* of a contract 'shall be determined by the law which would govern it under this Convention if the contract ... were valid', then the Convention may also determine whether the matter under review is a contractual relationship or not. However, ***Forsyth*** maintains that it would be illogical to extend this principle in order to determine what constitutes a contractual obligation: that is, it would be illogical to employ a provision of the Convention to determine whether the Convention is applicable at all. It is submitted that this comment may have some merit. Perhaps, by way of analogy, it is akin to saying that whereas the Theft Act can provide a definition of theft, it then requires case law to determine whether a theft has been committed in the circumstances of the case under review. In other words, the Theft Act doesn't determine whether a theft has taken place: case law does.

If this reasoning is correct, and if a 'Convention concept' of 'contractual obligation' is to be pursued, then, apart from not being able to rely on the Rome Convention, one cannot rely on the *lex fori* to determine whether a matter is a contractual obligation. Presumably, the ECJ will eventually develop a 'Convention

concept' of what amounts to a 'contractual obligation' and ***Forsyth*** is of the opinion that "the idea of legally binding voluntary agreements will be a crucial part of whatever 'Community concept' the court develops".

(b) How is 'countries' interpreted?

Art 19(1) provides that Scotland & England are different territorial units; but ***Art 19(2)*** provides that states consisting of different territorial units are 'not bound to apply this convention to conflicts solely between the laws of such units.' Thus, the U.K. had the choice of whether to apply the Conventions in the case of conflicts between the laws of different parts of the United Kingdom. That choice is now contained in ***s.2(3)*** of the ***Contracts (Applicable law) Act 1990*** which provides that: *'notwithstanding Article 19(2) ... the Conventions shall apply in the case of conflicts between the laws of different parts of the United Kingdom'* i.e. the *Rome Convention is applicable to conflict between Scots law and English law.* However, it must be borne in mind that in the event of a dispute over the interpretation of an issue, the House of Lords will take judicial notice of Scots law and/or English law and will ***not*** require the assistance of the ECJ: the jurisdiction of the ECJ in matters relating to interpretation as provided for by the *Brussels Protocol on Interpretation 1971* will ***not*** apply to Scots -English cases.

Matters to which the Convention Does NOT Apply

The matters to which the Convention does not apply are specified in ***Article 1(2)*** and **(3)**. They include the capacity and status of natural and legal persons, contractual obligations relating to wills and succession, rights in property arising out of a matrimonial relationship, rights and duties arising out of a family relationship, obligations arising under most aspects of negotiable instruments, ***arbitration agreements and agreement on the choice of courts***, questions governed by company law, agency, trusts, evidence and procedure (subject to Article 14) and insurance (but not re-insurance) of risks situated within the E.C.

Determination of the Choice of Law: The Principle of Party Autonomy; Article 3

Article 3(1) provides that:

'A contract shall be governed by the law chosen by the parties. The choice must be expressed or demonstrated with reasonable certainty by the terms of the contract or the circumstances of the case. By their choice the parties can select the law applicable to the whole of part only of the contract.'

Thus, just as the parties to a contract can choose the proper law at common law (***R v International Trustee For The Protection Of Bondholders*** (1937)), so the Rome Convention also respects the principle of party autonomy: ***Article 3(1).*** However, a problem may arise in trying to establish that the choice of law has been demonstrated with 'reasonable certainty'. In such case, recourse to ***Article 18*** of the Convention may be of use since, in relation to other provisions of the Convention, it provides that: *'regard shall be had to their international character and to the desirability of achieving uniformity in their interpretation and application'* .

As to whether a choice of law clause is valid [cf. the common law requirements for being *bona fide and legal*], ***Article 3(4)*** provides that: *'The existence and validity of the consent of the parties as to the choice of the applicable law shall be determined in accordance with the provisions of Article 8, 9 and 11.'* [1]

Furthermore, *and in contrast with the position at common law*, ***Article 3(2)*** provides that the parties 'may at any time' [including a time subsequent to the conclusion of the contract, perhaps even, to the time when litigation is pending] 'agree to subject the contract to a law other than that which previously governed it.' This applies irrespective of whether that law was expressly chosen or demonstrated with reasonable certainty or determined via 'other provisions of this Convention.' However, 'any variation by the parties of the law to be applied made after the conclusion of the contract shall not prejudice its formal validity under Article 9 or adversely affect the right of third parties.' [2]

[1] Article 8 refers to existence and material validity; 9 refers to formal validity; and 11 refers to incapacity, (see infra). ***Article 8*** is the ***Rome Convention*** equivalent of the 'putative proper law' at common law, although a party may rely on the law of his habitual residence to establish lack of consent

[2] *All extracts are from **Art.3(2)** of the Rome Convention*

The Applicable Law of the Contract in the Absence of a Chosen Law:

The Principle of Closest Connection; Article 4

In the absence of an expressed or an implied choice of law, ***Art.4(1)*** provides that ' ... *the contract shall be governed by the law of the country with which it is most closely connected*.' Whereas this provision appears similar to 'the closest and most real connection' test at common law (***Bonython v Commonwealth of Australia*** (1951)), Art.4(1) refers to 'the law of the *country* with which [the contract] is most closely connected' and not the '*legal system*' with which the common law provision is associated.

To overcome the absence of an applicable law being chosen in accordance with Art.3, Art.4 provides for ***rebuttable presumptions*** to be applied to choose the applicable law. This generates an immediate response from ***Cheshire and North*** (Private International Law, 12/e, 1992 at p490) who state (in relation to the whole of Article 4) that the *re-introduction* of presumptions 'turns the clock back as far as English law is concerned'.

In essence, ***Art.4*** consists of ***three principal parts.***

1 Art.4(1) provides for a contract to be governed by the law of the country with which it is most closely connected.

2 paragraphs (2) - (4) contain presumptions of which, arguably, the most important is contained in paragraph (2). This is a presumption which refers to the contract being most closely connected with the law of the country where, *inter alia*: the party who is to effect the performance which is characteristic of the contract has, at the time of the conclusion of the contract, his habitual residence, or, in the case of a body incorporate or unincorporate, its central administration. Other presumptions relate to where immovable property is situated (paragraph 3); and where, in the case of a contract for the carriage of goods, the country in which, at the time the contract is concluded, the carrier has his principal place of business if that is also the country in which the place of loading or the place of discharge or the principal place of business of the consignor is situated (para.4).

3 The *third* and final part of Art.4 is contained in paragraph 5, which provides that the rebuttable presumptions shall be disregarded if it appears from the circumstances as a whole that the contract is more closely connected with another country. However, notwithstanding this attempt to combine a high degree of certainty with flexibility, suffice it to say that it remains uncertain whether a court can rebut a presumption unless it has first applied the closest connection test; the precise purpose of the presumptions given that they might be dispensed with; and the impact of paragraph 5 in relation to paragraphs 2 - 4.

In more detail: the determination of the applicable law in ***Art.4(2)***revolves around two integral elements, viz; there is (i) the territorial connection of (ii) the party who is to effect the performance which is characteristic of the contract. These are integrated via a *presumption of closest connection* which provides that: 'it shall be *presumed* that the contract is most closely connected with *the country* [it doesn't say *law* of the country in ***Art.4(2)***] where the party who is to effect the performance which is characteristic of the contract has, at the time of conclusion of the contract, his habitual residence, or, in the case of a body corporate or unincorporate, its central administration.'

Art.4(2) then goes on to provide that if the contract is made in the course of a *'party's trade or profession'*, then the country of closest connection *'shall be the country in which the principal place of business is situated or, where under the terms of the contract the performance is to be effected through a place of business other than the principal place of business, the country in which that other place of business is situated'*.

Other points arising from Art. 4 include:

1. Another presumption provides that the country of the situs of immovable property is the country with which any contract having that immovable property as its subject matter has the closest connection: ***Article 4(3).***
2. ***The non-applicability of the presumption in contracts for the carriage of goods***. In such contracts, the country of closest connection will be the country in which ... 'the carrier has his principal place of business (provided that country is also either] the place of loading or the place of discharge [of the goods] or [where] the consignor [has his] principal place of business'. ***Art.4(4).***

3 ***Art.4(5)*** provides that the presumption in Art.4(2), (3) and (4) 'shall be disregarded if it appears from the circumstances as a whole that the contract is more closely connected with another country'. (i.e. ***presumptions in (2), (3) & (4) are all rebuttable***).

The doctrine of characteristic performance.

Collier refers to this as '*... a new concept, borrowed from Swiss law (surprisingly perhaps, since Switzerland is not a member of the [E.U.].*' It is perhaps, an innovative, if criticised, aspect of the Rome Convention. The ***Giuliano-Lagarde*** Report (the official Report on the Rome Convention) indicates that in (say) the case of a contract for the supply of goods or services, it is the provision of the goods or services, not the payment of money for them, which is the characteristic performance. The presumption of a contract having its 'characteristic performance' most closely connected with a particular country will not apply, however, if the characteristic performance cannot be determined. Nor will it apply (as has been noted, supra) if it appears from the circumstances as a whole that the contract is more closely connected with another country: ***Art. 4(5)***.

Forsyth notes that the major grounds of criticism of the doctrine of characteristic performance are "*that it is not straightforward to determine what the 'characteristic performance' of a particular contract may be; and that ... the trend in the common law was away from the technique of presuming what the* lex causae *is*." Furthermore, 'characteristic performance' has no necessary connection with the place of performance, a contracting factor recognised by English law. That characteristic performance is linked with the habitual residence of the party who is to effect it is a point criticised by ***Collins*** who questions whether reference to such a personal connecting factor is appropriate in the context of commercial contracts.

Restrictions on Party Autonomy:

(1): Consumer Contracts and Contracts of Employment; Articles 5 and 6.

Articles 5 and 6 of the ***Rome Convention*** contain special provisions in relation to consumer contracts and individual contracts of employment. These have the effect of either limiting the ambit of the general choice of law provisions or excluding the presumptions. As ***Kaye*** notes: *'A general exceptional choice of law provision [for consumers and for employers] is not a feature of preexisting English conflict of laws rules'*.[3]

Article 5: Consumer Contracts.

Art.5(1) provides that a consumer contract is one *'the object of which is the* supply of goods ***or*** services to a person *('the consumer') for a* purpose *which can be regarded as being* outside his trade or profession*, or a contract for the provision of credit for that object.*'

Where a consumer contract exists, ***Art.5*** provides that a choice of law by the parties 'shall not have the result of depriving the consumer of the protection afforded to him by the mandatory rules of the law of the country in which he has his habitual residence'. The difference between this provision and that of 'overriding statutes' at common law is that ***Art.5*** protects the consumer with the laws of his (the consumer's) <u>*habitual residence;*</u> whereas, at common law, protection is via statutes of the ***lex fori*** or the ***lex causae*** (the chosen law) - neither of which is necessarily the law of the consumer's habitual residence. However, this protection is afforded to the consumer <u>only</u> if one of the situations provided for in ***Art.5(2)*** is satisfied, viz;

(a) *in the country where the consumer has his habitual residence the conclusion of the contract was preceded by a specific invitation addressed to him or by advertising, and he had taken in that country all the steps necessary on his part for the conclusion of the contract;* **or**

(b) *the other party or his agent received the consumer's order in that country;* **or**

(c) *the contract is for the sale of goods and the consumer travelled from that country to another country and gave his order there, provided that the consumer's journey was arranged by the seller for the purpose of inducing the consumer to buy.*

Thus, if any one of the situations in (a) - (c) apply and an express choice of law has been made, then that choice of law will apply *subject* to the protection afforded to the consumer by the mandatory rules of the law of the country in which he has his habitual residence: ***Art.5(3).***

[3] [(1991) 3 Law for Business 194 at 195]

Article 6: Individual Contracts of Employment

Art.6(1) provides that notwithstanding a choice of law (as provided for under Art.3) an employee shall not be deprived of the protection of the *mandatory rules* of the otherwise applicable legal system. ***Art.6(2)*** provides that this 'otherwise applicable legal system' is (a) 'the law of the country in which the employee habitually carries out his work in performance of the contract,' or, (b) if he does not habitually work in any one country, 'by the law of the country in which the place of business through which he was engaged is situated.' Whereas, at common law, the ***EP(C)A 1978*** [See now the ***Employment Rights Act 1996***] gave protection to an employee who ordinarily works in Great Britain, irrespective of choice of law, ***Art.7(2)*** of the ***Rome Convention*** provides that the protective legislation of other countries may be enforced in the U.K.'s courts, when applying the Convention, even though that law has not been chosen by the parties. (See infra).

Further restrictions on the parties' autonomy.[4] (2): Article 3(3) and Article 7

Art.3(3) provides that where '*... the parties have chosen a foreign law, whether or not accompanied by the choice of a foreign [court] [and] where all the other elements relevant to the situation are connected with one country only the choice of law shall not ... prejudice the application of ... the law of that country which cannot be derogated from by contract, hereinafter called "mandatory rules"*'. So, for example, if the parties to a contract were French, the contract was to be performed in France and, indeed, all other aspects of the contract were connected with France, ***Art.3(3)*** provides that even if the parties choose (say) English law to govern their contract and they submit to the jurisdiction of the English courts, the English courts will, nevertheless, apply the mandatory rules of French law.

Since ***Art.3(3)*** provides that *'all ... elements relevant to the situation [must be] connected with one country only,*' it is inapplicable to situations where the mandatory rules are connected to a number of other countries. In such circumstances, ***Art.7(1)*** provides that *'effect may be given to the mandatory rules of* the law of another country *with which the situation has a close connection, if and in so far as, under the law of the latter country, those rules must be applied whatever the law applicable to the contract.*' This clearly discretionary provision is exercised by having regard to the *'nature and purpose'* of the mandatory rules *'and to the consequences of their application or non-application.'* The uncertainty to which this provision gives rise was sufficient reason for the United Kingdom to enter a reservation to *Art.7(1)* and, subsequently, provide in ***s.2(2)*** of the ***C(AL)A 1990*** that ***Art.7(1)*** 'shall not have the force of law in the United Kingdom.'

In contrast, Article 7(2) has been given effect in English law. It provides that: *'Nothing in this Convention shall restrict the application of the rules of the law* the law of the ***forum*** *in a situation where they are mandatory irrespective of the law otherwise applicable to the contract.'*

In essence, this means that *'Article* 7(2) *allows English courts to continue to apply the overriding provisions of English statutes' (*per **McClean,** Morris: The Conflict of Laws, *4/e). **McClean** continues by noting that a good example 'is furnished by the* **Employment Protection (Consolidation) Act 1978** *which provides that "for the purposes of this Act it is immaterial whether the law which (apart from this Act) govern's any person's employment is the law of the [UK], or of a part of the [UK], or not.*'"[5]

Particular aspects of the Contract:

Material (or Essential) Validity

Collier notes that: *'The existence and validity of the contract or a term thereof is to be governed by the putative proper law* **Art.8(1),** *but a party may rely on the law of his habitual residence to establish lack of consent:* **[Art.8(2)]**' This latter provision may be relied upon where, for example, a legal system (e.g. Danish law) provides that silence can amount to consent. Thus, ***Art.8(2)*** ensures that a party who does not reply to an offer made to him, an offer which includes a choice of a governing law in which silence *does* amount to consent, is not bound by that term.

4 **N.B:** ***Mayss,*** in Conflict of Laws. London: Cavendish, 1994, asserts that: *'The concept of mandatory rules is one of the key issues in the Rome Convention where it is used under at least six different provisions, namely Articles 3(3), 5(2), 6(1), 9(6), 7(1) and 7(2). Whilst the first four provisions apply in very limited circumstances, the last two are of a much wider scope. Article 7(1) is related to the mandatory rules of a foreign country, and Article 7(2) is related to the mandatory rules of the forum. Only the latter provision is given effect in English law, ...'*

5 See now ***ss.196*** & ***204 Employment Rights Act 1996***.

Formal Validity.

Where the parties are in the same country when the contract is concluded, then the contract is formally valid if it is regarded as such either by the applicable law or the law of the country where it is concluded: ***Art.9(1)***; whereas if it is concluded when the parties are in different countries, then either the applicable law or the law of either of those countries may apply: ***Art.9(2). Where a contract is concluded by an agent, the country in which the agent acts is the relevant country for the purposes of paragraphs 1 and 2: Art.9(3).*** *Art.9(4)* provides for the possibility of using the putative proper law, and *9(5)* and *(6)* provide for exceptions in relation to consumer contracts and immovables. In essence, Art.9(5) provides that the formal validity of a consumer contract is governed by the law of the country in which the consumer has his habitual residence; and Art.9(6) provides, inter alia, that where the subject matter of a contract is a right in immovable property *'it shall be subject to the mandatory requirements of form of the law of the country where the property is situated if by that law those requirements are imposed irrespective of the country where the contract is concluded and irrespective of the law governing the contract*.'

Scope of the Applicable Law: Article 10.

Art.10(1) provides that *'The law applicable to a contract by virtue of* **Articles 3-6** *and* **12** *of this Convention shall govern in particular:*

a. interpretation;
b. performance;
c. within the limits of the powers conferred on the court by its procedural law, the consequences of breach, including the assessment of damages in so far as it is governed by rules of law;
d. the various ways of extinguishing obligations, and prescription and limitations of actions;
e. the consequences of nullity of the contract.

Art 10(2) *In relation to the manner of performance and the steps to be taken in the event of defective performance regard shall be had to the law of the country in which performance takes place.'*

Incapacity.

Art.11 provides that: *'In a contract concluded between persons who are in the same country, a natural person who would have capacity under the law of that country may invoke his incapacity resulting from another law only if the other party to the contract was aware of this incapacity at the time of the conclusion of the contract or was not aware thereof as a result of negligence'*.

Other Provisions of the Rome Convention include:

Art. 12 which provides for voluntary assignment, i.e.:

1. *The mutual obligations of assignor and assignee under a voluntary assignment of a right against another person ('the debtor') shall be governed by the law which under this Convention applies to the contract between the assignor and assignee.*
2. *The law governing the right to which the assignment relates shall determine its assignability, the relationship between the assignee and the debtor, the conditions under which the assignment can be invoked against the debtor and any question whether the debtor's obligations have been discharged.*

Art. 14(2) provides that a contract or act intended to have legal effect may be proved by any mode of proof recognized by the law of the forum (say English law) ***or*** by the applicable law ***or*** by the law of the country where the contract was concluded *(lex loci contractus)*, ***providing*** that such mode of proof can be administered by the forum. So, for example, in ***Leroux v. Brown*** (1852), where the plaintiff failed to enforce a contract valid by French law but unenforceable in English law because it was not evidenced in writing, the fact that the French courts permit an oral contract to be proved by oral evidence now means that an English court which, of course, also permits oral evidence, would be bound to admit such testimony in an enforcement action. Furthermore, if the plaintiff succeeded in gaining a favourable judgment in France, he would find it relatively easy to enforce it in England.

Art. 15: renvoi does not apply. Thus, the position is the same under the Rome Convention as it is at common law.

Art. 16: 'The application of a rule of the law of any country specified by this Convention may be refused only if such application is manifestly incompatible with the public policy ('ordre public') of the forum. ***Collier*** is of the opinion that "The use of the word 'manifestly' signifies that the exception must be restrictively applied and that the court must then 'find special grounds for upholding an objection' based on public policy."

Art. 17 the Convention does not apply retrospectively;

Art. 18 provides for uniform interpretation; and

Art. 19 relates to States with more than one legal system.

Art.30(1) provides that the Convention shall remain in force for 10 years [from 1/4/91] and

Art. 30(2) provides that 'If there has been no denunciation it shall be renewed tacitly every five years.'

Summary

The Rome Convention applies to contractual obligations only. The liability of one party to compensate another for a tortious act is not provided for. That ***Art.1*** applies to '... contractual obligations in any situation' means that the Rome Convention is in no way restricted to the connection which a contract, or the parties to a contract, might have with a State which is party to the Convention. With respect to the matters to which the Rome Convention applies, the common law no longer applies: i.e., the Rome Convention *replaces* and does ***not*** supplement the common law in these matters.

References

Clarkson & Hill. *Jaffey on the Conflict of Laws*. London: Butterworths, 1997, Ch.5

Collier, *Conflict of Laws*. Cambridge: C.U.P., 2/e 1994, Ch.12

North & Fawcett, *Cheshire and North's Private International Law*. London: Butterworths,

13/e 1999, Ch.18

O'Brien. *Smith's Conflict of Laws*, 2/e. London: Cavendish, 1999, pp314-369.