The Common Frame of Reference as a basis for future harmonisation of the law of sale and lease of goods

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The topic for today's discussion is the content of the political frame of reference – how to prioritise. Professor Beale has in his introductory remarks described the purpose of this morning session, which is to discuss the toolbox function and the optional instrument function of the "Principles, Definitions and Model Rules of European Private Law. Draft Common Frame of Reference", the DCFR, and in this discussion address what topics should be covered and what instruments would be the best model for each of the two purposes.

The original purpose of the DCFR was, according to the Commission, to provide a guide or, in other words, a toolbox for the legislators.[1] This toolbox, which should provide fundamental principles, definitions and model rules, was already in 2004 intended to be used by the EU Institutions "to improve the quality and coherence of the existing *acquis* and future legal instruments in the area of contract law" as well as to simplify the *acquis*.[2] In my view, the DCFR can and should be used for these purposes.

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1 See *Action Plan on A More Coherent European Contract Law*, COM(2003) 68 final (hereinafter referred to as "Action Plan").

2 See *European Contract Law and the revision of the acquis: the way forward*, COM(2004) 651 final (hereinafter referred to as "the Way Forward"). See for a discussion of these purposes *Hugh Beale*, The Future of the Common Frame of Reference, (2007) 3 ECRL, p. 257 et seq.

In this short presentation, I will illustrate and discuss how the DCFR could be used to accomplish an improvement of the existing *acquis* and to help drafting better legal instruments in the future. I will do that by briefly analysing the existing draft Consumer Rights Directive[3] and compare the draft with the rules on sales in general and consumer sales in particular found in the DCFR. I will also address whether the rules in the DCFR on lease of goods would, if enacted or used as a basis for future legislative measures, constitute an improvement of the existing directives in closely related areas. However, before I discuss these two issues, I would like to address whether or not to enact some sort of optional instrument in the area of commercial sales law. On this issue I will be rather brief, as Professor Schwenzer will address the issue in detail in a later presentation.

International commercial sales

The DCFR provides rules for all kinds of legal obligations, including the sale of goods. In book IV on Specific contracts and the rights and obligations arising from them, rules on sales are provided in Part A. This part contains rules on the obligations of the seller, in particular on delivery of the goods and conformity of the goods, the obligations of the buyer, some modifications of the buyer's remedies for lack of conformity, rules on the requirements of examination and notification of lack of conformity, the passing of risk and consumer goods guarantees. This part could not be applied in isolation in any kind of sale.[4] In addition, at least the rules in Book III, Chapters 1–3, some of the rules in Book I and some of the rules in Book VII on unjustified enrichment must be considered in a sales law case together with the specific rules in Book IV.[5]

An optional instrument on sales contracts in isolation thus would require collecting rules from different parts of the DCFR and putting these rules together. As many of the substantive rules in the other books than book IV part A are drafted on the basis of sales law rules in such instruments as the

[3] *Proposal for a Directive of the European Parliament and of the Council on consumer rights*, Brussels 8.10.2008 COM(2008) 614 final, 2008/0196 (COD).

[4] See, e.g., *Ewoud Hondius, Viola Heutger, Christoph Jeloschek, Hanna Sivesand & Aneta Wiewiorowska*, Principles of European Law on Sales (PEL S), 2008, p. 142 et seq.

[5] See, e.g., *Christian von Bar & Eric Clive* (ed.), Principles, Definitions and Model Rules of European private Law. Draft Common Frame of Reference (DCFR). Full Edition, 2009 (hereinafter the DCFR), p. 1335.

CISG[6] and the Consumer Sales Directive,[7] these rules would in general fit very well into an optional instrument on sales contracts. However, most, if not all, member states of the European Union already have rules for commercial sales contracts that work very or at least reasonably well. In addition, all but four of the member countries in the EU, as well as two of the three countries that have applied for EU membership, have ratified the CISG.[8] Thus, a considerable part of the intra EU-trade is governed by the CISG.

The convention, which has become one of the greatest successes in the international private law sphere, has its drawbacks. Some of these drawbacks of the rules have been remedied in the rules on sales in the DCFR. Other solutions in the DCFR may, in return, have their drawbacks in comparison with the rules in the CISG, at least as they have been interpreted e.g. by the CISG Advisory Council.[9] However, the number of countries in the world that have chosen to be parties to the convention is in itself proof enough that the CISG works for international trade. In addition, it is safe to say that the rules still are well fit also for the present demands, almost thirty years after the diplomatic conference in Vienna in April 1980.

A first step in harmonising the rules in Europe in this area and thus facilitating trade, should in my view be to urge the non-CISG countries to become parties to the CISG. At the same time, Denmark, Finland and Sweden, as well as the non-member country Norway, should be urged to withdraw their Article 94 reservations regarding sales between parties with their places of business in the Nordic countries. Hopefully these countries are already in the process of withdrawing their Article 92 reservations regarding the formation of the contract. These rather uncomplicated steps would make the transaction costs in selling goods within the EU considerably lower and would in my mind be beneficial for commercial parties around Europe.

The benefits of adopting an optional instrument only for commercial sales contracts would in my view be rather small compared to having the CISG applicable for all international sales transactions within the EU. As

6 United Nations Convention on Contracts for the International Sale of Goods, 1980.

7 Directive 1999/44/EC of the European Parliament and of the Council of 25 May 1999 on certain aspects of the sale of consumer goods and associated guarantees.

8 Ireland, Malta, Portugal and the UK are the only four EU member states that are not CISG contracting states. Croatia and FYROM are CISG contracting states and have applied for EU membership. Turkey, also a country that has applied for EU membership, is not a CISG country.

9 The CISG-AC is a private initiative which aims at promoting a uniform interpretation of the CISG. See www.cisgac.com.

75–80% of all trade in goods in the world today is governed by the CISG and the convention is in a true sense global, the benefit of having the CISG applicable would also be that sellers could use the same regime regardless of where they are selling their products.

An optional instrument would also make the present and already complex situation even more complex if that instrument would be applicable in parallel with the CISG.

Consumer sales contracts

The picture is completely different for consumer sales contracts. The existing situation is, as we all know, that the Directive on consumer sales and guarantees from 1999 has been implemented in all member countries of the EU. The directive was rather heavily influenced by the CISG. However, its scope is rather narrow. In essence, it only provides provisions on non-conformity of the goods, on remedies in case of non-conformity and on guarantees. The proposal for a directive on consumer rights aims at revising, *inter alia*, the Directive on consumer sales and guarantees. While the Directive on consumer sales and guarantees is based upon minimum harmonisation, and thus allows member countries to keep or enact mandatory rules providing more protection to the consumer and/or more burdensome obligations for the seller than the rules in the directive, the draft consumer rights directive is based upon full harmonisation. Thus, member countries may not maintain or adopt stricter national rules than those laid down in the proposed directive. There are drawbacks with both approaches. The present situation means that businesses selling to consumers in other countries are faced with fragmented and divergent mandatory rules on consumer sales. That problem would not exist to the same extent if the full harmonisation approach would be adopted. However, that approach would tamper legal development, interfere with basic contract law in the member countries and lead to many border-line issues to be solved. One suggested solution is the Blue Button idea advocated by, *inter alia*, Professor Schulte-Nölke.[10] The theme of this conference does not allow for any exploration of these different alternatives.

[10] See *Hans Schulte-Nölke*, EC Law on the Formation of Contract – from the Common Frame of Reference to the "Blue Button", (2007) 3 ERCL 332 and *Hugh Beale*, From Draft Common Frame of Reference to Optional Instrument, JFT 2009, p. 203 et seq, p. 205–206.

There are some major differences between the consumer sales directive and the draft consumer rights directive. First of all, it is suggested in the draft directive that the seller (in the draft for some unknown reason called the trader) should have a rather comprehensive duty to provide information to the consumer before the conclusion of any sales contract. Furthermore, the draft directive makes it clear that it is only applicable to the sales part of a mixed purpose contract having as its object both goods and services (Article 21). The draft directive also contains a rule stipulating that the seller shall, if the parties have not agreed otherwise, deliver the goods within thirty days from the conclusion of the contract and that the consumer shall be entitled to a refund of any sums paid if the seller fails to fulfil his delivery obligation (Article 22). No such rule exists in the present consumer sales directive. However, a similar rule was provided in the 1997 Directive on distance contracts.[11] Moreover, the draft directive includes a rule on the passing of risk between the parties.[12]

Another major change is that the very problematic rule in the Directive on consumer sales and guarantees regarding the consumer's choice between repair and replacement, the so called disproportionate test (Article 3), has been modified and replaced with a rule giving the seller the choice between these two remedies (Article 26 in the draft). Instead, the disproportionate test is used for the buyer's choice between either having the goods repaired or replaced or opt for having the price reduced or the contract rescinded (i.e. avoided according to the CISG terminology). Another new provision in the draft directive is the rule on damages, according to which the consumer may claim damages for any loss not remedied.

In legal doctrine it has already been pointed out that, remarkably enough, one could find no reference to, or any real influence from, the DCFR in the present draft directive on consumer rights.[13] There are many reasons why this has to change in the future work on the draft directive on consumer rights and why many of the solutions provided by the DCFR should be the starting point in that revision.

[11] Directive 97/7/EC of the European Parliament and of the Council of 20 May 1997 on the protection of consumers in respect of distance contracts.

[12] This was a subject explicitly excluded from the scope of application of the consumer sales directive, see item 14 of the preamble to the directive.

[13] See e.g. *Martijn Hesselink*, The Consumer Rights Directive and the CFR: two worlds apart?, (2009) 5 ERCL 290.

There are many rules in the draft directive that should, in my opinion, be changed in a way mirroring, or at least be inspired by, the rules in the DCFR. Thus, it would be to turn the world upside down to consider the revision of the consumer rights directive in the future work on a Common Frame of Reference.

A first example is the definition of the consumer. In the draft directive, the consumer is defined as "any natural person who, in contracts covered by this Directive, is acting for purposes which are outside his trade, business, craft or profession". The same definition in the DCFR stipulates that the consumer is "any natural person who is acting primarily for purposes which are not related to his or her trade, business or profession". There is an important difference between these two definitions. The latter explicitly deals with also the so-called mixed purpose transactions, i.e. where the consumer buys goods to be used not only for personal use but also partly in his professional capacity. To what extent such transactions should be regarded as a consumer transaction with the suggested definition in the draft directive is unclear.[14]

Secondly, also a guarantee provided to the consumer is in the draft directive defined in a way which is different from the definition in the DCFR.[15] More important, however, are the differences in legal effects of a "commercial guarantee" (the phrase used in the draft directive) or "consumer goods guarantee" (the phrase used in the DCFR), where the draft directive only states that a guarantee "shall be binding under the conditions laid down in the advertising on the commercial guarantee" and where the DCFR provides rules on the binding effect, the coverage, the conditions for an exclusion of liability and also makes clear that a guarantee reverses the burden of proof.

Another difference is that the draft directive still allows member countries to exclude sale of second-hand goods at public auctions. No such exclusion exists in the DCFR and rightly so.

Yet another difference between the DCFR and the draft directive is how the passing of risk is treated. The idea behind the provision in the draft direc-

[14] The prevailing view among European scholars seems to be that the consumer definition covers also such mixed transactions or acts. However, the Brussels Convention and thus the Brussels I Regulation, which both contain the same definition, has been interpreted in a much more restrictive way. The leading case is Johann Gruber v Bay WA AG, Case C-464/01.

[15] See Article 2(18) in the draft directive and IV.A.-6:101 in the DCFR. The term consumer goods guarantee, the term used in DCFR, seems to be a much better term than commercial guarantee, being the term used in the draft directive. See also the DCFR, p. 1391.

tive, Article 23, seems to be almost the same as the idea behind Article VI.A.-5:103, i.e. to stipulate that the risk passes when the consumer actually gets the goods into his physical control and to make an exception for the case where the consumer, due to the his or her breach of the obligation to take physical control, has failed to take the goods into his or her physical control. However, there are several differences between the rules that provide good examples on why it would be beneficial for the quality of the rules of the draft directive to use the rules in the DCFR. First of all, the draft directive uses the words "has acquired the material possession of the goods" without defining material possession. The DCFR instead uses "takes over the goods", a phrase any sales lawyer would recognize from e.g. the CISG (see Article 69). Secondly, the draft directive does not define the legal consequences of the fact that the risk of or damage to the goods pass to the consumer. In Article IV.A.-5:101, as well as in Article 66 CISG, the legal effect is explicitly stated as being that if the risk has passed to the consumer, loss of or damage to the goods does not discharge the consumer from the obligation to pay the price, unless the loss or damage is due to an act or omission of the seller.

Both the draft directive and the DCFR address the issue on when a consumer has to notify a seller about a non-conformity. According to Article 28(4) of the draft directive, the consumer shall, in order to benefit from his rights in cases of non-conformity of the goods, "inform the trader of the lack of conformity within two months from the date on which he detected the lack of conformity". In contrast, the DCFR in Article III.-3:107 explicitly makes clear that the consumer does not have to give notice within a reasonable time to be able to rely on the lack of conformity. One major reason for this rule in the DCFR was that the requirement of detection, i.e. actual knowledge on the part of the consumer, in all important cases would be the same as not applying any notice requirement at all. However, the rationale behind such a complete – or almost complete – lack of notice requirement is, to say the least, dubious. Before the directive on consumer sales and guarantees was implemented in the member countries, most continental European legal systems included a notice requirement also where the buyer was a consumer. A change of position in on this issue in the draft directive, and thus re-introducing a duty of providing notice within a reasonable time after the consumer ought to have detected the defect, would in my view constitute a positive step.

In both the draft directive and the DCFR we find rules according to which the seller is liable at most – if the parties have not agreed otherwise –

during two years from the actual handing over of the goods. However, also in this respect the draft directive is unclear. In Article 28(1) of the draft directive it is stated that the seller is liable "where the lack of conformity becomes apparent within two years as from the time the risk passed to the consumer". This provision has to be read in conjunction with paragraph 4, according to which the consumer shall inform the seller "within two months from the date on which he detected the lack of conformity". A first question which could be raised is if the word "detected" in the last paragraph is the same as "apparent" in the first paragraph and if so, why two different terms are used? If the terms are regarded to have the same meaning, a second question is of course why the consumer should be given a period of two years and two months within which he or she could hold the seller liable for non-conformity and not be given the two-year period one would find in the DCFR Article IV.-4:302(2) and Article 39(2) CISG. In this respect, the rule in the DCFR is to be preferred.

One of the most important areas where the draft directive is not clear enough and needs definitions and rules, concerns the provisions on the remedies for non-conformity. Pursuant to Article 26 of the draft directive, the consumer may resort to the remedies of having the lack of conformity remedied by repair or replacement, have the price reduced and have the contract rescinded in certain cases where the seller has, *inter alia*, refused or failed to remedy the lack of conformity.

Nowhere in the draft directive is guidance provided on to what extent a consumer may have the price reduced. In this case, one could envisage several different interpretations. One interpretation would be to have the price reduced with an amount equal to the difference in value between conforming and non-conforming goods, i.e. the typical damages remedy in Anglo-American law.[16] Another alternative would be to reduce the price in such a way that the reduction is proportionate to the decrease in value of what was actually received compared to the value of what would have been received by virtue of a conforming performance.[17] There may be a considerable difference between these two alternatives. If one would adopt the rules in the DCFR on

[16] See e.g. Sect. 53(3) of the Sale of Goods Act (1979), where, in the case of breach of warranty of quality, such loss is prima facie the difference between the value of the goods at the time of delivery to the buyer and the value they would have had if they had fulfilled the warranty.

[17] See e.g. Art. 50 CISG on price reduction and Article III.-3:601 on the right to reduce price (price reduction).

this issue, one would opt for the latter alternative and could use the provision in Article III.-3:601.[18]

Another remedy that the consumer could resort to is to have the contract rescinded. No guidance is provided about the legal effects of such a rescission of the contract. Therefore, it is unclear whether rescission of the contract would have the same legal effects as avoidance in the CISG and termination in the DCFR. Such effects are provided in Article III.-3:509 of the DCFR and the restitutionary effects are provided in Articles III.-3:510–514.[19]

The uncertainty of the effects of the draft directive is even greater regarding the remedy of damages. According to Article 27, the consumer may claim damages for any loss not remedied. Nothing could be found regarding the meaning of the terms damages and loss, the calculation of the damages or if any exceptions could and should be applied. Thus, the rule in the draft directive creates uncertainty regarding the general extent of the loss which should be compensated, i.e. whether the reliance or expectation interest should be compensated, the types of losses to be compensated, whether or not a foreseeability test should be applied, whether the damages should be reduced if the loss in part is attributable to the consumer or whether the consumer should take reasonable steps to have the loss reduced.[20] Without such guidance, considerable uncertainty is created. As way of example, the rule is at present formulated in such a way that one reasonable interpretation seems to be that the loss should be compensated even if the loss was not foreseeable for the seller, a rule which clearly would go too far.

The last, and for business a very problematic area, is the scope of the draft directive in the parts dealing with sales contracts. The same problem exists in the present directive on consumer sales and guarantees. The present directive and the draft directive primarily deal with non-conformity and remedies for lack of conformity. However, any buyer of goods knows that a buyer has two primary interests in the sales transaction, and that is to receive conforming goods and to receive them on time. At present, and as suggested in the draft directive, matters dealing with the seller's obligation to deliver the goods on time and the remedies if the seller does not deliver the goods on time are left to the national legislators to decide. The only exception is the rule in Article 22 of the draft directive, stipulating that delivery should be made within a

[18] See DCFR, p. 910 et seq.

[19] Basic provisions on the same issue could be found also in Articles 81–84 CISG.

[20] These aspects of the right to damages and the calculation of such damages could be found in Arts III.-3:701–III.-3:707.

maximum of thirty days from the day of the conclusion of the contract. If the seller fails to perform that obligation, the consumer is entitled to a refund of any sums paid. Does this mean that the consumer is released from his obligations under the contract, i.e. in fact an *ipso facto* avoidance? In theory and, as a matter of fact, also in practice the rules on the remedies for delay vary considerably between different member countries. This means that the seller will be confronted with considerably different rules when in delay with delivery. Thus, the seller cannot, without having investigated the rules in the relevant member country, be certain if and when the buyer has a right to enforce performance, when the buyer has a right to rescind/avoid/terminate the contract and in what cases the buyer is entitled to compensation in the form of damages and for what. The same is true for the buyer's obligations and the seller's remedies if the buyer does not perform these obligations.

Drafting rules on these issues based upon the DCFR would facilitate greater certainty for both consumers and sellers. Moreover, drafting rules based upon the DCFR would be considerably better for e.g. the suggested rules regulating the seller's delay in performing his delivery obligation. A rule stipulating that the maximum time for performing the delivery obligation is thirty days is of course a very blunt instrument that would not be appropriate for a considerable amount of cases. An application of Article III.-2:102 on time for performance, providing that the delivery obligation must be performed within a reasonable time after it arises, would provide the necessary flexibility. Also the rules in Articles III.-3:301 on the right to enforce performance, in III.-3:401 on the right to withhold performance, in III.-3:502, 503, 507, 509, 510, 511, 512, 513 and 514 on termination for fundamental non-performance, on termination after notice fixing additional time, on notice of termination, on effects of termination and on restitution after termination, as well as the rules in Articles III.-3:701 et seq. on damages should be used.

Lease of goods by consumers

Another closely related area is lease of goods for personal use. Today, such transactions often meet the needs of the consumer in the same way as a sale of goods transaction. For the consumer, there is in many cases no considerable difference between buying goods and leasing the same goods for a shorter or longer period of time. In the marketplace, numerous contract variants exist, systematically belonging somewhere between contracts of sale and con-

tracts of lease, such as contracts with a financing purpose where the lessee has an option to become the owner, hire-purchase contracts, conditional sales, sales with a retention of title, and financial leasing contracts. In all the cases where the consumer is placed in more or less the same position as a buyer, the consumer has a reasonable expectation to have the same rights as in an ordinary sale.

However, also in the classical lease of consumer goods, a consumer should be entitled to expect certain protection or at least rules providing the same result as the rules on sales. I know that I am not the only one who has been at a loss, arriving at an airport in another European country, renting a car for the week-end and in concluding the agreement ticking a lot of boxes and providing signatures on a lot of dotted lines without having any real idea of the rights and obligations following from entering into the agreement. No directive exists at present regarding this type of contract. In my opinion, the rules provided in part B of book IV on lease of goods, together with some of the rules in book III on obligations and corresponding rights, would constitute a very good foundation on which to build a set of rules for the lease of goods. In such a work, one should also address all the cases between sales and lease of goods and consider these problems in a consistent way. That would also have the benefit of bringing the consumer credit directive, at present being implemented in the member countries, into the process of making the consumer protection rules more coherent.

General thoughts on how to continue

The two areas above have been used as illustrations of when and how the DCFR could and should be used as a model for improving the existing *acquis* and for future legislation. My personal view is that such piecemeal use of the DCFR should constitute the first step and maybe the only step in the near future. The usefulness of the DCFR could thus be tested with some mandatory and some non-mandatory rules in a setting where the institutions of the EU have already been active and where there is a clear need of better and more coherent rules. I am convinced that such a test would clearly show that the rules provided in the DCFR, as well as all the comparative information behind it, constitute a very important building block in the process of better law-making within the EU.

As all lawyers who are dealing with the existing Community legislation in the field of consumer law know, the present situation is not at all satisfactory.

The rules are sometimes unclear and the directives cover only certain areas of sometimes considerable importance and sometimes of hardly any importance. Furthermore, the present rules do not address all real problems and in fact in some instances create problems to both consumers and professionals that did not exist before the specific rule was created and enacted.

In an ideal world, we should, building upon the research and the results of the DCFR, develop an instrument that in a coherent way deals with consumer transactions from pre-contractual information and other pre-contractual duties, to rights and obligations regarding the transactions as such, to rules controlling the terms used in individual and standard form contracts and to remedies for breach of contract. Such an instrument should, if based upon structure basically received from the DCFR, take into consideration most of the present consumer directives or at least the issues addressed in these directives. In the development of such an instrument, it should be emphasised that most parts, if not all, of the DCFR must be considered, at least as a check-list on what issues one might have to consider in developing the final product. Such a work should in my view start immediately instead of trying to make the four directives considered in the draft directive on consumer rights a more coherent product. Of course such a work would encounter certain problems, such as developing an instrument containing mandatory and non-mandatory rules and even optional rules together with important definitions needed for the sector.

In the area of business-to-business contracts, the most important thing with the DCFR is that it exists, and that it contains such an enormous amount of information, results of comparative research and important discussions on questions and problems we encounter in the field of private law. More research and more discussion about the quality of the different rules of the DCFR is probably needed before the legislative bodies of the EU should take the next step and try to develop one or several optional instruments covering business contracts. In the meantime, it could not be emphasised enough that a way has to be found very soon to ensure that the DCFR as presented is kept up-to-date. The work on updating the information and on one or several optional instruments in the field of commercial contracts should of course start right away, but that work should be allowed to take time and should closely involve those parties with an interest in these questions. In this area of law, my opinion is that we should start with general contract law and related areas of law and not try to encompass specific contracts in the first round.