LAURI RAILAS

The Rise of the LEX ELECTRONICA and the International Sale of Goods

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THE RISE OF THE *LEX ELECTRONICA* AND THE INTERNATIONAL SALE OF GOODS

Facilitating electronic transactions
involving documentary credit operations

Academic dissertation to be publicly defended by due permission of the Faculty of Law of the University of Helsinki, in the auditorium of Arppeanum, on 16 October 2004 at 10 o'clock.

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PREFACE

The first seeds for this dissertation were planted already some twenty years ago, when I decided to look for a place of study abroad before seeking a permanent position at home. That escapist idea turned out to be much more meaningful than I had ever imagined. My curriculum namely led me to the lectures of many leading experts of international trade and transport law whose enthusiasm and inspiration were impressive.

My working career then took me to places where legal rules are being created. These places included the private sector´s ´soft law factory´, the International Chamber of Commerce (ICC), and the supranational ´hard law factory´, the Council of the European Union in Brussels. Besides, many of my tasks such as participation in the creation of standard form contracts and working as a business lawyer, kept me abreast of international trade law practice too. Out of this background and the bulk of materials collected during the years, I ultimately decided to attempt writing an academic monograph.

It would be impossible to mention all those who have somehow contributed to this study. The exact field of this study was actually introduced to me by Mr. Torbjörn Blomfelt, who chaired UN/ECE Working Party 4 (Trade Facilitation) at the beginning of the 1990s. He recruited me for national EDI working parties and drew my attention to various trade facilitation issues on top of my work in the ICC. The actual topic of this study arose during the first meetings of the ICC´s E-100 Project somewhere in the mid 1990s. Projects usually come and go but this writing project of mine kept hanging on.

After years of contemplation, I finally drew up texts on the topic. Professors Erkki Aurejärvi, Mika Hemmo and Heikki Mattila strongly encouraged me to continue and finalise my study, which first took shape as a paper for the licenciate´s degree in law. Professors Lena Sisula-Tulokas and Jarno Tepora looked after a full time student´s pecuniary and logistical needs and were always available for discussions on the subject. Furthermore, Professors Juha Laine and Matti Rudanko deserve acclaim for serving as scrutinisers of the draft dissertation. Finally, I am very grateful that one of the protagonists of international trade and transport law, Professor Jan Ramberg, has kindly accepted to act as the opponent for this dissertation.

Several persons have granted interviews or provided their valuable time for going into the intricacies of my text. In particular, Mr. Paul Mallon, Director of Legal and Regulatory Affairs of Bolero International Limited, Mr. Asko Räty, Logistics Manager of Storaenso Oyj, and Mr. Tapani Voionmaa, Corporate Counsel of Finnlines Oyj, have all kindly read parts of my manuscript and given useful feedback on it. Mr. José Angelo Estrella Faria from the UNCITRAL Secretariat, Ms. Béatrice Goethals, Senior Product Manager of SWIFT, Mr. Lauri Ojala, Professor of Logistics in the Turku School of Economics, and Mr. Timo Vuori, Secretary General of ICC Finland, have all been available for discussions on the topic or have provided necessary materials relating to it. I wish to express my gratitude to these and other contributions, all of which I cannot possibly list here.

I have received scholarships or other financial support from Merenkulun Säätiö (i.e. the Finnish shipping foundation), Werner Hacklinin Säätiö (i.e. the Werner Hacklin foundation) and the Business Law Forum of the University of Helsinki. Moreover, the University of Helsinki has contributed to the printing costs of the book. The Faculty of Law of the University of Helsinki has accepted my dissertation for its publication series Forum Iuris. Ms. Julie Uusinarkaus from the University Language Centre has revised my English, Ms. Seija Helppi of Mainos Mayday Oy has prepared the layout, and Yliopistopaino has printed the book. I warmly thank all donors and contributors as well as my present employer Messrs. Krogerus & Co. Attorneys-at-Law for granting leeway for the finalisation of this study.

This list of acknowledgements would certainly be incomplete without mentioning Dr. Pirkko K. Koskinen, the Inspector of Karjalainen Osakunta during the years of my elementary legal studies, who kept encouraging me for almost two decades of ´standby´ post-graduate studies.

Needless to say, I am still mostly indebted to my family, to my wife Raija and children Olli, Sanna and Miikka, who endured the hectic writing periods and the financial constraints after daddy and the family´s co-supporter had obstinately decided to become a full-time student once again. I trust my parents would also have liked to see me finalising my post-graduate studies but unfortunately they were never given that chance in the true sense of the word. Time waits for no one, and one has to grab the moment in order to make any dreams and plans come true.

This work presents the law as it stands in the summer of 2004. I have especially tried to follow various rule-creation projects until the latest possible moment, which is 31 July 2004.

At Lauttasaari, Helsinki, 3 September 2004.

Lauri Railas

CONTENTS

LIST OF ABBREVIATIONS

AAA	American Arbitration Association
ABA	American Bar Association
AC	Appeal Cases
ADP	automatic data processing
ADR	alternative dispute resolution
All E.R.	All England Law Report
ANSI ASC X12	American EDI communication standard (ANSI = American National Standards Institute, ASC = Accredited Standards Committee)
ASYCUDA	Automated System for Customs Data
BAL	Bolero Association Limited
BIMCO	Baltic and International Maritime Conference
B/L	bill of lading
BMW	Bayerische Motorwerke
BPO	business process outsourcing
B2C	business-to-consumers
B2B	business-to-business
CA	Cour d´appel
CAD	cash against documents
CARDIS	Cargo Data Interchange System
CCC	Customs Cooperation Council
CEFIC	European Chemical Industry Federation
CFR	cost and freight
CIF	cost, insurance, freight
CIFFO	cost, insurance, freight + free out
CIM	Convention internationale concernant le transport des marchandises par chemin de fer
CIP	carriage and insurance paid to
CPT	carriage paid to
CISG	United Nations Convention on Contracts for the International Sale of Goods
CMI	Comité Maritime International
CMNI	Convention on the Contracts for the Carriage of Goods by Inland Waterways
CMR	Convention relative au contrat de transport international des marchandises par route
COGSA	Carriage of Goods by Sea Act
COTIF	Convention relative aux transports internationaux ferroviaires
CSD	central securities depositories
CUSDEC	customs declaration message
D/A	documents against acceptance
DAF	delivered at frontier
DDP	delivered duty paid
DDU	delivered duty unpaid

DEQ	delivered ex quay
DES	delivered ex ship
DEXPRO	a commercial repository of documentary credit law
DOCDEX	(ICC) Rules for Documentary Credit Dispute Resolution Expertise
D/P	documents against payment
EBRD	European Bank for Reconstruction and Development
EC	European Communities, electronic collection
ECP	electronic commerce project (ICC)
ECE	United Nations Economic Commission for Europe
ECMT	European Conference of Ministers of Transport
EDP	electronic data processing
EECA	European Electronic Component Manufacturers Association
EFT	electronic funds transfer
EFTA	European Free Trade Area
EDI	electronic data interchange
EFIFACT	Electronic Data Interchange for Administration, Commerce and Transport
ESIA	European Semiconductor Industry Association
ESIGN (or E-SIGN)	Electronic Signatures in Global and National Commerce Act
ETC	electronic trade credit
ETL	European Transport Law
ETPS	electronic trade payment systems
ETSP	electronic trade and settlement process
EU	European Union
eUCP	Supplement to UCP500 for electronic presentation
EXW	ex works
DCI	Documentary Credit Insight
DEUPRO	German Trade Facilitation Board
FALPRO	UNCTAD Special Programme on Trade Facilitation
FAS	free alongside ship
FBL	FIATA bill of lading
FCA	free carrier
FIATA	Fédération internationale des associations de transitiares et assimilés
FIO	free in and out
FOB	free on board
GUIDEC	General Usage in Internationally Digital Ensured Commerce
GUIDEC II	A revised version of the same
HE	hallituksen esitys (government proposal)
HTML	Hyper Text Markup Language
IAB	Internet Architecture Board
IANA	Internet Assigned Numbers Authority
IASC	International Accounting Standards Committee
IATA	International Air Transport Association
ICANN	Internet Corporation for Assigned Names and Numbers
ICC	International Chamber of Commerce
I.C.C.	Institute Cargo Clauses
ICLOCA	International Centre of Letter of Credit Arbitration

ICSD	international central securities depositories
ICT	information and communication technology
IDC	name of one consulting company
IEMP	Internet-based electronic marketplace
IESG	The Internet Engineering Steering Group
IETF	Internet Engineering Task Force
I.L.M.	Internation Legal Materials
IMO	International Maritime Organisation
INCOTERMS	International Commercial Terms
INCOTERMS2000	The currently applicable vesion of the INCOTERMS
ISBP	International Standard Banking Practice
ISIN	international securities identification number
ISO	International Organisation for Standardisation
ISOC	Internet Society
ISP98	(ICC) International Standby Practice
ITU	International Telecommunications Union
K.B.	King´s Bench Division
L/C	letter of credit
LWG	legal working group
MINC	Multilingual Internet Names Consortium
Misc.	miscellaneous
MLA	Maritime Law Association
MTO	multimodal transport operator
NCCUSL	National Conference of Commissioners on Uniform State Laws (US)
NCITD	US National Committee for International Trade Procedures
NJW	Neue Juristische Wochenschrift
NNA	national numbering agency
NORDIPRO	Nordic Trade Procedures Board
NSAB (PSYM) 2000	General Conditions of the Nordic Association of Freight Forwarders
NVOCC	non-vessel-operating common carrier
NYC	New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards
N.Y.S.	New York State
ODETTE	Organisation for Data Exchange via Teletransmission in Europe
OECD	Organisation for Economic Cooperation and Development
OJ	Official Journal of the European Communities
OSI	Open Systems Interconnection
OVT	organisaatioiden välinen tiedonsiirto (=EDI)
P&I	protection and indemnity
PKI	public key infrastructure
POD	proof of delivery
POFEC	principles of fair electronic contracting (in ICC GUIDEC II)
RabelsZ	Zeitschrift für ausländisches und internationales Privatrecht, begründet von Ernst Rabel
RDAI	Revue de droit des affaires internationaux
RFC	request for comments

S1 POPS	S1 Trade Finance Purchase Order Processing System
SDR	special drawing right
SFPO	short form purchase order
SGML	Standard Generalised Markup Language
SIMPLE	SIP for instant messaging and presence leverage extensions
SIMPROFRANCE	Simpler Trade Procedures Board (France)
SIP	IETF Session Initiation Protocol
SITPRO	Simpler Trade Procedures Board (UK)
STP	Straight-throug processing
SURF	(Bolero) Settlement Utility for Risk and Finance
SWIFT	Society for Worldwide Interbank Financial Telecommunications
TDCC	a sector-specific EDI standard
TEDIS	trade electronic data interchange systems
TDI	telematic data interchange, trade data interchange
TDI-AP	trade data interchange application protocol
TFT	telematic funds transfer
TKOim	Trade Key Online Image
TPA	trading partner agreement
T.R.	Trade Reporter
TSS	trusted service supplier
TSU	Trade Services Utility
UCC	Uniform Commercial Code (US)
UCITA	Uniform Computer Information Transactions Act (US)
UCP	Uniform Customs and Practice for Documentary Credits
UCP500	The currently applicable version of the UCP
UCS	a sector-specific EDI standard
UETA	Uniform Electronic Transactions Act (US)
UIACP	Uniform International Authentication and Certification Practices (a pre-form of the ICC GUIDEC)
ULIS	Uniform Law for International Sales (1964 Convention)
ULR	Uniform Law Report
UMM	UN/CEFACT Modelling Methodology
UN/CEFACT	Centre for Trade Facilitation and E-commerce of the United Nations Economic Commission for Europe
UNCID	Uniform rules of conduct for interchange of trade data by teletransmission
UNCITRAL	United Nations Commission for International Trade Law
UNCTAD	United Nations Conference on Trade and Development
UNECE	United Nations Economic Commission for Europe
UNIDROIT	International Institute for the Unification of Private Law
UNSM	United Nations Standard Message
UNTDID	United Nations Trade Data Interchange Directory
URC522	(ICC) Uniform Rules for Collections
URCB524	(ICC) Uniform Rules for Contract Bonds
URCG325	(ICC) Uniform Rules for Contract Guarantees
URDG458	(ICC) Uniform Rules for Demand Guarantees
URGETS	Uniform Rules and Guidelines for Electronic Trade and Settlement

URI	uniform resource identifier
URL	uniform resource locator
URR525	Uniform Rules for Bank-to-Bank Reimbursement under Documentary Credits
US	United States
VAN	value-added network
VAT	value-added tax
VICS	a sector-specific EDI standard
VKL	velkakirjalaki (Finnish Promissory Notes Act)
Vp	valtiopäivät (the annual session of the Finnish Parliament)
WCO	World Customs Organisation
WG	working group
WIPO	World Intellectual Property Organisation
W.L.R.	Weekly Law Reports
WP	working party
WTO	World Trade Organisation
W3C	World-Wide Web Consortium
XML	Extensible markup language
XMPP	extensible Messaging and Presence Protocol

I INTRODUCTION

I.1 The objectives of this study

Electronic commerce is, without doubt, one of the most current and probably the most popular topics of legal studies at the moment. The legal framework for electronic commerce is still under the process of development. Yet articles and papers have been written about it for at least a couple of decades. The fast development of e-commerce calls for more certainty. It is the task of international law-making agencies, whether inter-governmental or non-governmental, to establish simple and uniform legal rules and thereby create confidence among consumers and businessmen.

Boosting consumer confidence is one of the principal objectives for e-commerce regulation at the moment. However, I intend to choose a different path by concentrating on business-to-business[1] e-commerce and its development and facilitation in international organisations. There are many organisations active in trade facilitation at international and national levels, and the work done in international organisations will be under consideration here.

The promotion of e-commerce has been an integral part of trade facilitation, at least conceptually, right from the start. The United Nations Economic Commission for Europe (UNECE) founded a Working Party on Facilitation of International Trade (WP.4) in 1961 to "facilitate international trade and transport by promoting rationalisation of trade procedures and the effective use for this purpose of electronic or other automatic data processing and transmission".[2]

The approach chosen also dictates my chosen working method. I intend to look at the legal framework for the international sale of goods not from the perspective of comparative law, but in an attempt to see some light at the end of the tunnel in the creation of a uniform and coherent legal framework of

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1 ´B2B´ e-commerce as distinguished from business-to-consumers (´B2C´). To relieve the reader from the pains of ´decrypting´ a text already full of abbreviations, this text does not use these abbreviations, even though they would already be well-established.

2 Terms of Reference of the Facilitation of International Trade Procedures, http://www.unece.org/trade/facil/wp4_tor.htm, visited on 12.2.2000.

electronic commerce for the international sale of goods and the various dimensions involved therein.

This study describes therefore the development of the legal infrastructure for the international sale of goods by electronic means, particularly in view of the sale of goods involving carriage of the goods by an independent carrier, and in which documentary credits are used as the method of payment and security. This is not an easy task since, although there are many continuing developments in various international organisations and in practice, no uniform framework has yet emerged, but only pieces thereof. Unfortunately, the same goes for messaging and other technical aspects of e-trade.

There is a push towards uniformity in law and in technology. At the same time, the commercial world is developing new methods and concepts for the management of the supply chain from the seller to the buyer. New services are being introduced in logistics, and these are becoming more and more comprehensive. Supply chain management calls for a comprehensive or ´holistic´ view on the production and delivery of goods. A lawyer, on the other hand, traditionally distinguishes between separate contracts and contractual relationships involved in this chain and their characteristics.[3] In an ideal world of harmonised law, legal instruments should be treated like the software used in transactions and should be ´interoperable´ with one another. New services such as the *Bolero System* build largely on the idea of a comprehensive documentary system.Therefore a comprehensive look at it is also indispensable.

What research can do in these circumstances is, first, to understand and describe the developments that have taken or are taking place in the hope of seeing some logic in what is happening. Secondly, research has to be able to manage the developments by putting new legal instruments into context, highlighting their essential features, omitting irrelevant discrepancies, and trying to define a system – yes, more or less one system, emerging from these instruments. This is obviously difficult if one considers the gap between different legal systems and the significant gaps in harmonisation, most notably the lack of harmonisation in property law. To a great extent, however, harmonisation is done by the parties of a transaction by choosing legal systems, rules and instruments applicable to their relationships. This approach has invited me, along with other commentators, to make suggestions *de lege lata* on how to use and interpret existing trade law instruments. Thirdly, and this is the most difficult task, research should suggest changes or new approaches *de lege ferenda* wherever necessary.

Referring to the traditional law of international trade, one can argue that attempts to reach uniformity have been relatively successful in the sense that there are many instruments such as the UN Convention on the Contracts for the International Sale of Goods (CISG), the INCOTERMS, the Uniform Customs and Practice for Documentary Credits, the Institute Cargo Clauses and the Hague-Visby Rules, which can be regarded as predominant instruments, whether

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[3] Juha Pöyhönen has sketched new principles for the law of obligations and property in ´Uusi varallisuusoikeus´ (Helsinki 2000). He departs from analysing traditional legal and contractual relationships and takes the comprehensive notion ´project´ as one of basic legal structure.

alternatives exist or not.[4] Such instruments result from elaboration that has taken sometimes decades to complete. The adoption of the instruments by governments and the business community at large takes often as long a time. However, many instruments and legal institutions have been shaped by practice, from the Rhodian general average to bills of lading and documentary credit and, more recently, to demand guarantees. Generally, however, it has taken a long time for international trade law to find its present shape.

Electronic commerce law is a very new phenomenon. The UNCITRAL Model Law on Electronic Commerce and the resulting implementing legislation, the electronic signatures legislation and the central EC Directives have been enacted only during the last few years.[5] There are several relevant instruments in the pipeline at the moment.[6] Electronic commerce legislation and other regulation are being created during an era in which the CISG has already made its breakthrough and important restatements of contract law have been created.[7] Therefore, seeking uniformity is, or should be, the key objective in making new instruments. Therefore, this study also attempts to bring together various sporadic developments in this dynamic field, analyse them and create some sort of systemacy. The foundation is the existing transnational commercial law, especially its harmonised parts, and new instruments are viewed in light of that.

The essential objective is to examine what roles electronic communications in lieu of traditional trade documentation have in contracting for the sale of goods, their delivery, the use of third party services in separate ancillary functions such as the carriage, transport insurance, and the securing of the rights of the various parties involved.

Much literature exists on international trade issues. There is similarly a bounty of writings on electronic commerce. Each year, a respectable bulk of new materials and literature appears. Similarly, an established legal framework for international sale of goods transactions is in place, and a legal framework for electronic commerce is emerging. Little by little, these two regimes will start to overlap to some extent. This study concerns that overlapping area in particular. Yet, this is not the whole story. The legal framework for electronic commerce is very much based on the notion of functional equivalence established first and foremost by the UNCITRAL Model Law on Electronic Commerce[8].

Based on the notion of functional equivalence, a study on an electronic sale of goods transaction must elaborately describe and analyse practices based on existing trade law to see how electronic equivalents of paper-based practices would and should work, unless one decides to discard many old practices such as

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4 For these instruments, see Chapters I.7., IV.7.2.1., V.3., VII.5.2. and X.4., *post*.

5 See Chapter IV, *post*.

6 Most notably the UNCITRAL preliminary draft convention on electronic contracting (Chapter IV.7.2., *post*), the UNCITRAL preliminary instrument on transport law (Chapter VI.3.2., *post*), the ICC E-Terms 2004 and, indirectly, the revision of the Uniform Customs and Practice for Documentary Credits.

7 The UNIDROIT Principles for International Commercial Contracts and the European Principles of Contract Law, see Chapter X.4.2. and 4.3., *post*.

8 See Chapters IV.4. and VI.3.1., *post*. Functional equivalence had already been applied before that in e.g. INCOTERMS 1990.

the use of bills of lading altogether. Such discarding may however lead to the rejection of new instruments by the business community. On the other hand, analysing practices may lead to the creation of completely new instruments, forming new substantive *lex electronica* (for the use of the concept, see *infra*).

As an example, in late 2001 the International Chamber of Commerce adopted the eUCP to govern the electronic presentation of documents under letters of credit under the Uniform Customs and Practice for Documentary Credits UCP500. The idea of creating or referring to functional equivalents had already been used already in the CMI Rules for Electronic Bills of Lading and in INCOTERMS 1990 a decade earlier.

Adapting existing contract legislation to meet the needs of electronic commerce has taken more than a decade. Both the United States and the European Union introduced new mandatory legislation in this field only at the turn of the millennium. Many aspects of electronic commerce, e.g. those relating to the transportation of goods, are still theory for most companies. This is also because sector-specific legislation has not been adapted to the needs of electronic commerce yet.

As will be seen later, electronic commerce legislation aims to give electronic records the same value as paper documents, but largely leaving existing substantive law intact. At some stages, this approach has been contested. For instance, many experts of documentary credits such as Bernard *Wheble* preferred creating a new trade instrument instead of making the traditional letter of credit electronic.[9]

Although literature on electronic commerce is mushrooming, it is in most cases very general. There are many fewer publications on ´applied´ electronic commerce such as that concerning the sale and transportation of goods. One important inspiration for this study was the Centenary Conference of Comité Maritime International in Antwerp in 1997, which discussed the electronisation of maritime transports. The launch of the *Bolero System* in 1999 was accompanied by an extensive feasibility study[10] which has been thoroughly examined in preparing this study.

From the traditional trade facilitation point of view is a selection of literature. In Scandinavia, these topics were alrerady covered in the 1970s, at first mainly due to efforts to streamline documentation in maritime transport in general. The Swedish professors Kurt *Grönfors* and Jan *Ramberg* have in their various writings covered the multiple dimensions of international trade in the light of electronic commerce, or have analysed the functions of trade documentation in the light of logistic developments. As regards treatises concerning sale of goods transactions from a comprehensive viewpoint covering transportation and documentary credits and laying emphasis on the role of documents, one can mention *Selvig´*s Grenseland[11] in Norway and *Todd´*s work[12]

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9 See Chapter VII.8.2, *post*.

10 Report on the Bolero Feasibility Study 1999 (a second version of the study), at http://www.boleroassociation.net/downloads/legfeas.pdf, visited on 4.8.2003.

11 Fra Kjøprettens og Transsportrettens Grenseland, Oslo 1974,

12 Bills of Lading and Bankers´ Documentary Credits, 3rd edition, London, 1998.

in the UK. The latter, despite its merits, is anchored in English law, which does not include the United Nations Convention on Contracts for the International Sale of Goods.

The author of this study worked for the International Chamber of Commerce[13] in the 1990s. One of the main functions of the ICC is to facilitate electronic and other commerce through uniform rules that parties can incorporate into their contracts. In addition, the ICC has published important commentaries on national laws in the field.[14] Such rules represent ´soft law´ according to a well-known nomer. Around the turn of the millennium, the author approached international rule-making from a public angle within the European Union, which creates rules for the business community to apply largely on a mandatory basis. Therefore both approaches are reflected in this work.

In conclusion, a need is apparent for a multi-dimensional treatise on the electronic commerce issues of the international sale, transportation and finance of goods based essentially on the fruits of international legal harmonisation. I have tried to look at the approximately two-decade history of the regulation process. The first materials to regulate electronic commerce were model contracts and recommendations, generally instruments of ´soft law´,after which legislators finally joined in by the end of the 1990s. Many or most international organisations dealing with commercial matters are somehow connected with the facilitation of electronic commerce. I believe there is already enough established legal materials for an attempt to take a comprehensive look into the possible use and functions of electronic documentation and communications in international trade and transport law. The magnitude of the task must be realised. On the other hand, it is believed that a general overview helps to wander across the many greatly fragmentary developments that are happening in this dynamic area.

This study should thus be seen as an attempt to present the legal infrastructure for the sale of goods involving their carriage and the financing of the trade transaction by electronic means as these stand at the moment this study was finalised. A historical perspective is also attempted. I began my legal writings in the field of history, which still very much influences how I look at the world. The emergence of new rules is a process like the harmonisation of private law or European integration. The basic assumption is that such processes continue if they serve the purposes behind them. Behind harmonisation was the need to promote world peace through trade. The ideologies behind harmonisation have, together with globalisation, created a movement which challenges the legislative authority of national states. During any process mistakes are made. Mentioning these is often as important as reviewing successes. A holistic approach calls for

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13 The International Chamber of Commerce is a non-governmental organisation, which represents business interests before intergovernmental organisations and national governments. A different dimension in its activities is the maintenance of a self-regulatory legal framework through the creation and update of standard rules and practices to be incorporated into contracts as well as some ethical guidelines in the field of marketing, crime prevention and the environment.

14 For instance *Transfer of Ownership in International Trade*, edited by Alexander von Ziegler, Jette H.Ronoe, Charles Debattista and Odile Plégat-Kerrault, ICC Publication No 546, The Hague 1999.

the presentation of a nucleus of the commercial, technical and infrastructural environment in which electronic commerce takes place.

The developments in international organisations have been followed to the furthest possible extent[15] until 31 July 2004. Some materials published or released very close that date are included.[16] Several developments are still under way. The UNCITRAL Working Parties are discussing instruments, one relating to electronic contracting[17] and another to the carriage of goods by sea involving electronic transport documents. It is not known yet what shape these developments will ultimately take, but the arguments for and against the various issues are already interesting research materials. The revision of the UCP has been commenced more recently, and there is little record of the revision for the time being. Yet, the law is never static. This study is generally an account of what the legal framework for electronic commerce in the international sale of goods had become by the summer of 2004.

I.2 Some basic contradictions

The development of the infrastructure for e-commerce involves some contradictions. One of them is between law and logistics. Legal argumentation deals with rights and obligations created e.g. by law and contracts and affecting the various parties of a transaction while a logistical approach relates to the efficiency of supply and distribution. There is a huge advantage gained by promoting electronic documentation which transmits information. Over 200 data elements are required to complete a cross-border trade transaction. Many of these are re-copied and re-keyed as they move from one party of a transaction to the next. The cost of managing trade documentation is estimated by theUnited Nations at 7% of the total value of cross-border trade.[18]

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15 The writer expresses his gratitude to international organisations for the availability of documentation, including preparatory documentation, on the Internet.

16 These are mainly the UNIDROIT Principles of International Commercial Contracts 2004, the ICC E-Terms 2004 and the introduction of the SWIFTNet Trade Services Utility.

17 It is expected, in May 2004, that the relevant UNCITRAL Working Party IV (Electronic Commerce) will finalise the Preliminary draft convention on international contracts concluded or evidenced by data messages by its session in October 2004.

18 Mallon 1997 and 2002. Mallon quotes a WTO/UN source from 1996 and states "an estimated 7.2% of all global trade is lost in paper inefficiencies; the USD 420 billion lost per year corresponds with the total corporate spend on advertising each year (USD 450billion)"(the figure is from McCann-Erickson from 2000). Mallon quotes Financial Times figures, partly estimates, on the size of global trade: USD 57 billion in 1947, USD 3.58 trillion in 1992, USD 5.5 trillion in 2001 and USD 6.75 trillion in 2005.

Mallon 1997 further gives a good illustration of the system under electronic documentation: "Suppliers network into their customers´ products scheduling systems, verifying the time for just-in-time shipments before releasing them. Transport companies link to the same systems, verifying that vehicles are available for loading goods and that receiving bays are free. Information is transferred electronically to customs and deep water carriers as required, ensuring smooth throughput of the shipment. Parties are linked to their banks so that payment is triggered by the receipt of goods or documents."

On top of the above, computerisation makes it generally easier and less expensive to collect and combine information.

The use of electronic documentation would reduce costs dramatically. Moreover, electronic documents add speed. Experiments show that electronic systems can accomplish in a day the same document handling which would require weeks to complete using traditional methods. Automated systems reduce risks posed by human involvement, information being incorrectly reproduced, documents being lost and, where precautions are taken, forgery.

Logistics cannot, however, provide technically reasonable solutions[19] if legislation lags behind and does not recognise technical solutions, or if there is little confidence among business partners on their legal watertightness. A typical example is the bill of lading as a document of title. The bill of lading has been originally created by commercial usage or custom, sometimes legislation, and it works in the paper document environment. Today, a special type of technical and contractual framework is required to establish a facility which could be called ´an electronic bill of lading´.[20]

The contradiction between law and logistics can, however, be turned into an asset. A logistic approach to the functioning of legal rules can be useful. It is closely akin to the economic analysis of law. This school of jurisprudence, which I do not intend to follow categorically, has gained popularity during recent years in my home country of Finland. A central objective of the economic analysis of law is to reduce transaction costs.[21] As applied here, legal instruments should be construed so that, in addition to guaranteeing the legal rights and obligations among the parties involved in a transaction adequately, they facilitate cost-effective logistic management.

Transaction costs can be lowered if the legal framework for conducting transactions is uniform and predictable and, it is submitted, if there is enough flexibility in the system. Uniformity means that legal rules remain the same even if frontiers of jurisdictions are crossed. This can be achieved through legal harmonisation done by international public and private organisations. The question of how much regulation is needed, and how this regulation should be provided are key questions debated among international law-making agencies.

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19 The word ´solution´ is sometimes in parallel use in the legal context as well, see for instance the title of Part Two of the work ´EDI and the Law´ (ed. by Ian Walden), London 1989. In this study, the word has also been used to signify legal rules which have as their purpose the abolishing of legal obstacles to electronic commerce or filling gaps (*lacunae*) in law.

20 Electronic bills of lading exist in commercial projects such as the *Bolero System*, see Chapter VIII, *post*.

21 Transaction costs are often divided, from the point of view of the economic analysis of law, into three main groups, which are

- the legal costs of an individual business transaction;
- the operational costs from the point of view of an individual enterprise; and
- the public costs of market exchange as a whole; the costs arising from legal protection mechanisms and the regulation of the contents of individual rights belong to this category.

A transaction cost analysis aims to reach an optimal level of regulation by comparing the costs of regulation and the risk to be regulated. Regulation is efficient if its costs are smaller than the costs of an unregulated risk, which are calculated by multiplying the costs of a materialised risk by the probality of its occurrence. Otherwise it is not useful to regulate a risk. (Rudanko, pp. 195-198 and the sources cited therein).

The rapid development of technology and the need to remain neutral to technology keep legal rules abstract. Legal instruments such as bills of lading and documentary credits have had centuries of evolution. Technically and legally replicating their functions electronically is possible. Should the legislator or the private sector invest in providing a legal framework that makes it possible to replicate the functions of these instruments based on their usefulness and costs? We may ask if one can truly anticipate the benefits of future instruments. It is always possible that, in addition to lowering the logistic costs of an individual transaction, new instruments such as electronic transaction-oriented security methods emerge. Politicians often highlight the importance of small- and medium-sized enterprises as employers. I believe transaction-oriented finance is particularly useful for new small businesses. In any case, cost-effectiveness determines in the long run the feasibility and success of such services.[22]

The second contradiction relates to the scope of facilitation of electronic commerce. Is it only that e-commerce provides new means to communicate and to conclude contracts, or should one touch upon the substance of a contractual relationship? As we shall see, both approaches are reflected in the contract practice and, to some extent, in the legislative work. The use of electronic methods will undoubtedly have an effect on substantive law. Accelerated communications add new requirements for the parties of a transaction. This will, for instance, undoubtedly add pressure to reduce time-limits afforded to contracting parties to react to each other´s communications or to take a new attitude towards what is to be considered a reasonable time to react in the new circumstances. The availability of contractual information on the Web, in particular standard conditions of contract, may increase the acceptance in business-to-business relationships of the incorporation of standard terms by reference[23].

It has been recognised that electronic commerce creates new conflict of laws problems. It is difficult to determine where the contract is concluded. In many countries still, the formal validity of a contract is determined by the rules of the *lex loci contractus*.[24] Choice-of-law problems are not that apparent when the object of the transaction is delivered by traditional means rather than through the Internet as is the case with software. Yet, the choice-of-law method does not create uniformity since national laws differ, and choice-of-law rules themselves may not lead to simple results since they may require the establishment of the most significant relationship.

In any case, it would be tempting to see the new methods of concluding contracts giving rise to attracting the use of uniform substantive rules in lieu of rules selected on the basis of the traditional conflict of laws system. I am going to

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22 Legal research can nevertheless analyse the legal institutions and needs for reform from a dogmatic point of view. Furthermore, the cost-effectiveness is much higher if, for instance, legislation guarantees the admissibility of electronic media to record information.

23 Unless the availability is not regarded as the equivalent of an attachment; for this see Chapter IV.8.2. and IV.10., *post*.

24 Eiselen, p. 8. According to the Rome Convention on the Law Applicable to Contractual Obligations a contract will be formally valid if it meets the requirements of the place where the contract was concluded or where either party has his usual residence or place of business.

describe the harmonisation of substantive rules as a final stage in the electronisation process of contract law. An overview of some sources of uniform substantive law is covered later. New substantive rules have emerged, however, by applying the functional equivalence method.

A third contradiction is found if we compare the notion of functional equivalence and harmonisation objectives. The scope of electronic commerce remains limited and is very technical in nature. Uniformity could be achieved more easily than with more political issues. On the other hand, electronic methods of contracting and transferring rights and obligations are designed to be functional equivalents of their counterparts on paper. Electronic commerce law thereby supplements other parts of law, which are frequently not harmonised.

A fourth contradiction lies in the nature of the solutions sought. Is it about public legislation or private codes of conduct? This contradiction is reflected in the reactions[25] of the private sector, notably the International Chamber of Commerce, to the work carried out under the auspices of the United Nations Commission on International Trade Law. The American approach has originally favoured the latter alternative, although notable legislation has been enacted recently, whereas the approach of the European Union is to create legislation to regulate the operation of e-commerce. However, EC legislation gives private rules or codes of conduct a role.[26] This is the case particularly as regards marketing to consumers.

Between companies, the legal solutions used may be more innovative and even commercial. The provider of the value-added-network may create, in addition to the technical framework, a multi-party contractual network, which is a self-governing legal system to the extent permitted by the applicable law. This is said particularly in mind of the *Bolero System*[27], which aims to create a system between its participants, whereby various parties involved in a sale of goods transaction are connected to a central registry, which plays a role in controlling the handing over of the goods and, indirectly, the transfer of title through electronic equivalents of bills of lading. The Bolero Service is a commercial venture between the TT Club and SWIFT.[28] The legal regime of the Bolero Service is largely contained in a ´Rulebook´, which is a bye-law or a set of rules of procedure adhered to by the subscribers of the service. Therefore, a part of the legal infrastructure of electronic commerce is provided on a commercial basis and is based on a set of ´proprietary´ rules of procedure protected by copyright[29].

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25 See e.g. the comments by the International Chamber of Commerce to UNCITRAL, doc. A/CN.9/WG.IV/WP. 105.

26 This is the case with Article 16 of the Directive 2000/31/EC of the European Parliament and of Council on certain legal aspects of electronic commerce in the Internal Market, OJ L 178, 17.7.2000, p. 1.

27 On the Bolero project, see Chapter VIII.7., *post*.

28 SWIFT is a cooperative owned by banks the task of which is to supply secure messaging to financial institutions all over the world (see Chapter VIII.2., *post*). The TTClub is a mutual insurance company providing insurance to the transport industry. It insures large liner operators and freight forwarders against their liability. Its members comprise many terminal operators and port authorities. All in all it has about 5000 operational assureds (Mallon, p.24). Today, the owners of Bolero Association Limited include three venture capital companies.

29 In the United States, at least some state level statutes are protected by copyright.

The role of private initiative calls for one more remark. International legal harmonisation proceeds slowly if only the pace of the implementation of international conventions is considered. However, the division line between public and private is gradually melting because many international conventions allow parties to subject themselves under their scope by way of incorporation. Moreover, both international public and private organisations are creating useful contractual instruments ("tools for international trade") for businesses to overcome the boundaries of different jurisdictions. Party autonomy, which is almost universally recognised in international commercial relationships, makes it possible for companies to be their own legislators. It is one of the aims of this study to pinpoint some instruments that are available for such an exercise.

Finally, the development of electronic commerce law has to take a stand on traditional division lines in private law. One of them is between the law of obligations and the law of property. The second is between contract and tort. There is a bounty of diverging doctrine on these issues and the significance of these distinctions varies from jurisdiction to jurisdiction. Each jurisdiction has its own system of rights *in rem* and unification is still in its cradle regarding these issues. Generally speaking, however, one can say a right *in rem* is available against the world at large (*ultra partes*), whereas a right *in personam* (or *inter partes*) applies in the context of a given relationship. A contract is created expressly between one or several parties and sometimes a contractual relationship will be inferred indirectly from the law or from circumstances.[30] Many of the discussions on these issues are of a theoretical nature. What is relevant in my view is, however, that generally in cases of rights *in rem* and tort a universal[31] solution has to be sought to promote electronic commerce, because a contractual application has its limitations. Therefore party autonomy does not suffice, although it has its merits in its flexibility and adaptability.

I.3 Defining the scope of electronic commerce

There appears to be no well-established definition of e-commerce, at least in the legal sense. For instance, the UNCITRAL Model Law on Electronic Commerce adopted in 1996 refrains from giving such a definition. Its approach is, however, rather broad in including the use of the telex or telecopier in some cases.[32] A recent seminar on the subject defined e-commerce as "the use of advanced information technologies for commercial transactions and for all activities

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30 In the fields covered by this study, an indirect contractual relationship is established between the holder in due course of a bill of lading and the carrier having issued it. Similarly, a seller delivering documents to a correspondent or issuing bank is in a ´contractual relationship´ with the bank (see e.g. Gutteridge and Megrah).

31 I.e. applying against the world at large, I do not mean here the unification of law although that is also desirable.

32 See Chapter VI.4.1 *post*.

deriving from those transactions".[33] This definition contains again three different notions, the scopes of which are not obvious. There is, on the other hand, a tendency to differentiate between e-commerce and e-business. The eEurope 2005 Action Plan defines e-business as comprising both e-commerce (which would mean buying and selling online) and the restructuring of business processes to make use of digital technologies.[34]

As one can see, terminology is not finally settled. I do not, however, attempt to make any new suggestions as it does not seem to be useful. Definitions are namely used for commercial, marketing and technical purposes in addition to legal or regulatory ones.

In this study, e-commerce has been partly covered as taking place in the form of EDI (electronic data interchange), which means the transmission of structured messages from one computer to another, [35] as distinct, for instance,

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[33] Summary of the discussions of the Joint OECD/ECMT seminar on the impact of e-commerce on transport, p. 2, at http://www.oecd.org/dataoecd/32/26/2404595.pdf, visited on 18.12.2002.

In the United States, the Uniform Electronic Transactions Act uses the word ´transaction´ in a way that also covers relations with the government.

[34] eEurope 2005: An information society for all; An Action Plan to be presented in view of the Sevilla European Council, 21/22 June 2002; COM(202) 263 final, Brussels 28.5.2002, p. 13.

At times, e-commerce is said to include consumer relations, whereas e-business takes place solely between enterprises. Distinctions are not always consistent: The UN/CEFACT Recommendation 32 entitled ´E-commerce Self-Regulatory Instruments (Codes of Conduct)´ almost invariably refers to e-business despite the title.

[35] EDI has been traditionally described in the United States as "the computer-to-computer, application-to-application or translator-to-translator communication of structured business information in recognised formats" (Perritt Jr. In Baum-Perritt Jr., p. 6). The European Model EDI Agreement borrows the definition of the UN/EDIFACT, UN/EDIFACT Rapporteurs´ Team, April 1991: "Electronic data interchange is the electronic transfer, from computer to computer, of commercial and administrative data using an agreed standard to structure an EDI message". The definition of a ´EDI message´ by the European Model EDI Agreement states that it "consists of a set of segments, structured using an agreed standard to structure an EDI message". The commentary on the definitions states that these essential characteristics specify EDI in comparison with other data exchange methods such as electronic mail. Although EDI was sometimes originally seen as a synonym for electronic commerce, its definitions make it in any case narrower than what is known as electronic commerce today.

See also the comments and analysis regarding the definition of EDI in the UNCITRAL Model Law on Electronic Commerce, Chapter IV.4.1., *post*.

Toh See Kiat would like to establish different terminology by using the term ´Telematic Data Interchange –TDI´ whereas ´TFT´ would stand for ´telematic funds transfer´, which he prefers to keep separate from TDI in his book ´The Law of Telematic Data Interchange´, London 1992. Telematic funds transfer has been developed independently of TDI and solutions have not been developed in parallel, although similarities exist. The most common provider of Electronic/Telematic Funds Transfer (EFT or TFT) services is SWIFT.

The word ´telematic´ comes from the French word *télematique* which was introduced by Simon *Nora* and Alain *Minc* in their book The Computerisation of Society in 1978. It is said to describe the convergence between computers, electronic office equipment and telecommunications into a unitary technology. Toh See Kiat rejects, however, another coined word ´compunications´ by Professor Arthur Oettinger of Harvard. The word ´electronic´ was feared to become obsolete because the equipment would be changing from electronic to entirely photonic (Toh See Kiat pp. 6-7 and 19). EDI has evolved from ´ADP´ (´automatic data processing´) and ´EDP´ (´electronic data processing´); see the reference to this in Toh See Kiat footnote 30 to Chapter I.

from telefax [36]or electronic mail[37]. In practice, however, EDI as now known requires established trading partners in a preset contractual relationship (an interchange or trading partner agreement). However, the use of the internet has facilitated a move towards an open form of electronic contracting, although the Internet is a channel for EDI operations as well (´Web EDI´).

One could perhaps generalise and name the discussion connected with traditional EDI as the first phase of development of electronic commerce, and the legal facilitation of more open electronic contracting (where parties are not preset by an established commercial and contractual framework) as the second phase.[3838] Later, in Chapter X, the development of electronic commerce law has been divided into three stages that refer to the

I.4 From sale to payment

A contract of sale can be defined as "a contract by virtue of which the seller must deliver the goods, hand over any documents relating to them and transfer the property in the goods sold, whereas the buyer is bound to pay the price for the goods and take delivery of them".[39]

Regarding the above definition, electronic commerce affects first the contract itself, i.e. contracting for the sale of goods. It brings in questions of contract formation, evidence and a legal framework applicable thereto. Electronic commerce also affects the delivery of the goods, since delivery in international trade takes place through transportation, which brings in documentary questions. Such issues are also evident as the seller has to hand over documents, which may serve various functions. Such handing over generally amounts to a ´constructive delivery´, which normally releases the seller from further liability after the risk has passed to the buyer.

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[36] Facsimile, or telefax, produces written or paper-equivalent images of written documents. Originally, facsimile machines were designed to perform long-distance copying of paper documents. A facsimile may be initiated or received by a computer, but facsimile technology generally does not produce a non-paper record of the information with further automated processing. The technology simply provides another means of delivering unstructured information. (Electronic Data Interchange Agreements, p. 14). On the treatment and analysis of the facsimile in relation to electronic commerce, see Chapters IV.4.1., in particular footnote 31, and IV.8.4.1., *post.*

[37] E-mail allows the exchange of text files, but the text is essentially unstructured ´free text´. When using E-mail, the ability of the receiving computer to further analyse and process the information is limited. In addition, EDI formats permit users to include some ´free text´ within the messages for special instructions and to modify their programs to act on the codes without human intervention and analysis.

[38] Later, in Chapter X, the development of electronic commerce law has been divided into three stages that refer to the role of the rules in the contracting process. These categorisations have no formal significance and are mainly used for presentational purposes. The title of this work coupled with the often chronological presentation used should be taken as signs of my affection for history.

[39] A/CN.9/WG.IV/WP.91, Possible future work in the field of electronic contracting: an analysis of the United Nations Convention on Contracts for the International Sale of Goods, Working Group on Electronic Commerce,thirty-eighth session, New York, 12-13 March 2001, Legal aspects of electronic commerce, Note by the Secretariat, p.8.

Furthermore, the seller has to transfer property in the goods. Here again, electronic commerce could play a role, since handing over a document of title regularly transfers property in the goods, and there are schemes in which ´documents of title´ exist as declarations in electronic registries. Finally, the buyer must pay for the goods. In documentary credits, payment takes place (through banks as contractual intermediaries) against commercial documents. As these documents may be in electronic form, this brings in questions as to the conformity of the documents with the requirements of the credit and the contract of sale. The delivery of the goods and the documents involves the use of ancillary contracts, which are possibly concluded through an electronic medium. These contracts are, however, independent and regularly subject to a separate legal regime from that of the contract of sale. Yet, these contracts may contain the same data elements or information as the contract of sale, or may refer to it. They may be concluded in one uniform trading platform such as the *Bolero System*. Thus, several contracts are also technically linked to each other.

Electronic commerce affects the entire transaction one way or another. This calls, in my view, for a comprehensive presentation starting from the conclusion of the basic contract of sale and ending at documentary credit operations. The presentation starts from a general introduction and history of e-commerce, which outlines the new international legal instruments for electronic contracting and their role in contract formation. It then moves on to the questions of executing the delivery of the goods by way of transportation and finally to the issues of payment for the goods and the security arrangements relating thereto.

This study can therefore, in general terms, be roughly divided into several parts. The first part (Chapters I to IV) deals with the development of electronic commerce in general. The starting point is a comparison between paper documents and electronic messages and an examination of what functions these have. After that, there will be a general presentation of the basic legal problems particularly characteristic to e-commerce. My method is to present the principal questions at the beginning of the text and to come back to them later in sector-specific parts. This creates regrettable repetition, which I try to tackle with cross-referencing in footnotes.

The text then goes on to describe how these various problems have been approached by the international organisations and in contract practice. The presentation is largely chronological. During the first phase, roughly in the 1980s and early 1990s, international intergovernmental and private organisations wanted to facilitate commerce by creating model rules of reference, such as trading partner agreements. Electronic commerce was done exclusively by companies mainly in the manufacturing or other basic industry, and the consumer aspect was lacking. This phase was sometimes described as an ´infancy´ of EDI law.

At the second phase, which could be said to have started in the latter half of the 1990s at the latest, the Internet had combined electronic networks in a manner which made electronic contracting possible for everyone including consumers. The statutory legislative environment was seen to require rules that would create legal presumptions of the validity of electronic records as documents and rules on electronic signatures which facilitate the formation of contracts. The establishment of the infrastructure could in principle be created by private contractual means, but the European Union had chosen to enhance

electronic commerce with directives which aimed at creating ground rules for the establishment of infrastructure (e.g. rules on third party service providers) and the consumer dimension (e.g. rules on the distance marketing of financial services). Private organisations have remained active during the second phase as well.

The second rough part of this study (Chapters V to VII) deals with the application of electronic commerce to international trade. It could also be labelled as ´applied electronic commerce (sales) law´. It covers the legal regime of electronic commerce as regards the transportation of the goods, with particular focus on transport law and documents, the interplay between sale and transport and the development of an infrastructure that would make it possible to move to an electronic trading system, and especially considers the replacement of the paper-based documentation used in letters of credit. The second part goes on to further analyse the traditional role of letters of credit in the international sale of goods and how to convert this role into an electronic document environment. Although the use of documentary credits has decreased proportionally and many doubts about the practicability of letters of credit have been raised, there has been discussion and initiative for ´an electronic letter of credit´ for over a decade.[40]

Commercial letters of credit could be seen as a sophisticated ´end product´ of the international sale of goods system. They are based on an underlying sale of goods transaction for which they provide financing. The documentation required by the credit normally includes a document evidencing an insurance contract as well as a transport document, very often a bill of lading. The bill of lading as a document of title is instrumental in transferring property and possession to the goods carried. A bill of lading can also be pledged with a bank and act as a security. A commercial letter of credit thereby is connected with a network of contracts, and the documentation presented under a credit reflects this contractual network or chain.

Documentary credits, as they are known today, have been a means of international payment since the middle of the 19th century. They facilitate international trade by providing a secure method of payment against the proper presentation of trade documents. This is achieved by a bank giving its conditional undertaking to pay the seller on behalf of the buyer against presentation of the stipulated documents by the seller to a nominated bank. The current practices associated with documentary credit transactions, which have been codified at regular intervals since the 1930s in the Uniform Customs and Practice for Documentary Credits of the International Chamber of Commerce[41], have evolved over a considerable period of time, and have in many respects remained almost unchanged since the 19th century.[42]

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40 For instance, the *Bolero System* is a project which encompasses electronic letters of credit. Moreover, the E-100 project launched by the International Chamber of Commerce (ICC) in 1994 was aimed to create a new instrument for international trade and payment and not to reproduce the traditional documentary credit as such. The discussion had, however, originally started already in 1989. See Chapters VI and VIII, *post*.

41 The latest version is ICC Publication No. 500 and is referred to as ´UCP500´.

42 SITPRO (Simpler Trade Procedures Board), Electronic commerce, Towards replacing the paper-based letter of credit, a conceptual model, version 1.0, 29/12/94, p. 1.

Letters of credit have developed, from approximately the middle of the 20th century, into trade guarantees. Documentary credits have found new use as trade security in the form of standby letters of credit, which are more or less the same as demand guarantees (guarantees payable on first demand). Today the aggregate amount of standby letters of credit has overtaken that of commercial letters of credit. Standby letters of credit and demand guarantees are documentary instruments since a call for the amount of the guarantee requires documents, at the least a written demand. The doctrines of strict compliance and the autonomy of the credit apply equally to these instruments, although the scope of strict compliance is more limited than it is with commercial letters of credit.[43]

This study will also shortly examine attempts to replace documentary credits. The functions and operation of letters of credit have been analysed in trade organisations, particularly in the International Chamber of Commerce, in order to to create an electronic equivalent for a traditional letter of credit, or to create an ´Electronic Trade Credit´, which could meet the ends of a traditional letter of credit in a slightly different manner. It is, in my view, equally important to pay attention to the misgivings as to the success stories since new instruments are still to come.

Computer-based contracting deals, however, not only with material (´tangible goods´) that lies outside computer systems, but also with material that lies in computer systems, such as software. For software, information systems are also a channel of delivery. In addition, computer technology is widely used to contract for the transfer of assets in banks.

This study, however, will focus on the contracts concluded by electronic means for the international sale of tangible goods, in which case the actual performance of the contract takes place outside computer systems, save the delivery of documents and transfer of title, and which involves therefore transportation of the goods. Attention will be paid to the possibility of using electronic messages and documentation not only in the contract of sale, but also in the related transactions (ancillary contracts) including carriage of the goods, insurance and documentary payment systems and guarantees. It is believed that this process could ultimately lead to an ´electronisation´ of documentary credits as we know them now or to some new innovations with the same functions.

As regards the applications of electronic commerce law, this study also includes a chapter (IX) concerning electronic dispute resolution, particularly in the light of disputes regarding documentary credits, demand guarantees and other trade guarantees to the extent these operate through the presentation of documents. However, many observations made therein apply as regards other trade disputes as well.

The third part is made of Chapter VIII. It describes some main developments in the field of trade facilitation and attempts to give a state-of-play of the documentary requirements of contemporary international trade, with some suggestions added. Moreover, it describes attempts to create comprehensive

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[43] On these principles, see Chapter VIII, *post*.

trading platforms which include as many contracts relating to an international sale of goods transaction as possible. Logistic benefits can be derived from such systems. In a holistic approach, a trade transaction with its many contracts is seen as one entity. A question is cautiously raised about whether the logistic and technical *rapprochement* of contracts could be coupled with legal developments leading to some synchronisation of substantive rules.

The international sale of goods involving transportation of the goods and the use of documentary credits contains several separate contracts or contractual relationships, which are based on different legal regimes and concern different subject-matters.[44] There are, however, factors which interrelate them. They all aim at the same goal: the materialisation of the contract of sale including the supply and delivery of the goods against payment. The goods description and usually details relating to the delivery including particulars of the contract(s) of transport, the contract of insurance as well as particulars relating to the use of documentary credits, especially the documents to be presented under the credit, are normally set in the contract of sale. In traditional document systems, these information elements have to be rekeyed over and over again, which creates costs and possibly discrepancies. The various contracts may have to be transferred to a new buyer or may serve functions of security.

Therefore, this study is based on the idea of seeing international trade and transport as a chain of interrelated contracts and services. The idea is not a novelty. As will appear later in this study, it has been the approach adopted in a number of projects intended to develop international trade procedures.[45] A trade facilitation approach tries to see this chain operating as coherently and uniformly as possible. Parties to a contract of sale should not agree on something which is in conflict with related services, notably the transportation of and the payment for the goods. In electronic trading systems, such problems are even less welcome, since the documentation that has been put into an electronic form may be the key to the execution of rights. Minimising areas of conflict in the underlying legal relationships also serves therefore the facilitation of procedures.

Chapter X covers the fourth and final part of this study and is entitled ´The Third Stage: A Move Towards a Uniform Substantive Law´. It aims at defining the scope of electronic commerce law in facilitating international trade and anticipates a move towards a uniform substantive law accelerated by the emergence of electronic commerce law. Moreover, several observations are made as regards to how legal rules facilitating electronic commerce should be created.

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44 One could generalise that the supply chain consists of the supplier, various intermediaries such as the carrier, and the customer. In the real world, however, this generalisation meets different variations. For instance, the same company can act as a contractual carrier of the goods being at the same time in charge of export and/or import forwarding. The actual delivery of the goods and invoicing can be done by different entities. Outsourcing of activities can lead to multiplication of commercial parties in a trade transaction, which leads to an augmentation of contractual relationships and documentation and communication flows.

45 See e.g. the initiatives within the International Chamber of Commerce, Chapter VII, *post*, and the *Bolero System*, Chapter VIII, *post*. See also Facilitation measures related to international trade procedures, Recommendation No. 18, third revised edition, adopted by the the United Nations Centre for Trade Facilitation and Electronic Business, Doc. ECE/TRADE/271, New York and Geneva, 2001.

There are many interesting problem areas in electronic commerce in the legal and political sense that cannot, and need not, be discussed here, but are mentioned only to indicate some problem areas under constant discusssion in various forums. For instance, intellectual property rights such as domain names as well as copyright and related rights in an information society are important issues, like the regulation of advertising on the net. Standards of encryption, their free circulation, and the organisation of third party service providers generally, not to forget taxation issues, are under constant discussion as well. However, I am not able to treat them here. Likewise, competition issues will mainly be omitted. New technology attracts the attention of competition authorities since investments and efforts in product development easily lead to a dominant position. The same goes for the entire trade policy approach in general.

The scope of this work is still quite wide compared to many traditional academic studies in the field of private law. This study cannot reach the same depth as more traditional studies. This is not only due to lack of space, but also because materials with an international approach are still relatively thin. In any case, I feel that a wide scope is a must if one tries to cover all the essential legal issues of a multifunctional electronic trading system.

I.5 An electronic record as a means of conveying information

Electronic contracts are not fundamentally different from paper-based contracts. This fact has been noted, for instance, by the UNCITRAL Working Party IV (Electronic commerce).[46] The aim of many articles of the UNCITRAL Model Law on Electronic Commerce is to create ´functional equivalents´ in the electronic world for legal concepts used in a paper-based world. The legal facilitation of electronic commerce gives formal and factual credibility to information presented in electronic form. The law of contract formation, as well as substantive contract law, remains fundamentally the same in the electronic world as in the paper-based world.

This applies to traditional notions of contracting, which are based on humanistic models, since human will and decisions and their expression are concerned. However, the use of computers brings in new questions, such as the treatment of automated computer systems, where the humanistic model will not automatically apply. Preprogrammed computers make choices and responses with or without human involvement.

Determining the law applicable on the basis of conflict of laws rules is more complicated in electronic commerce than in other forms of commerce. As consumer protection brings in the application of mandatory norms, the

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46 Note by the Secretariat, doc A/CN.9/WG.IV/WP.95, United Nations Commission on International Trade Law, Working Group IV (Electronic Commerce), thirty-ninth session, New York, 11-15 March 2002.

determination of the applicable law becomes even more complicated. Consumer and other mandatory law is generally national in character, and harmonisation confronts therefore more obstacles. In commercial law, the role of mandatory norms is much less important. This lends an important role to contract practice. However, the freedom of contract might also undermine incentive for creating harmonised law for passing internationally agreed instruments by national parliaments.

I.6 *Lex mercatoria* oriented approach

It would be impossible to analyse each issue presented in this study from the point of view of a variety of national legal systems, although many examples are used. The focus is on instruments created by international organisations. Legal instruments such as the United Nations Convention on Contracts for the International Sale of Goods, the UNCITRAL Model Law on Electronic Commerce, the potential outcome from the UNCITRAL project, which initiated the drafting of a ´draft Instrument on the Carriage of Goods [wholly or partly] [by Sea]´, and the ICC ´eUCP´ for electronic presentations under UCP500 based documentary credits aim at internationally adopted solutions as regards individual aspects of commercial law.

This approach, which is the objective of all international legal harmonisation, has been applied throughout this study. I believe that the emergence of new electronic trading systems will highlight the need for a uniform basis of substantive contract law and actually enhance its use. This basis is formed by instruments of various types, international conventions, model laws, uniform rules created by business organisations such as the International Chamber of Commerce, model contracts and recorded trade practices accessible on the web. Harmonisation is already taking place in the creation of a basic legal framework for electronic commerce that will foster confidence in the use of electronic methods of contracting.

The law of international trade, which is thought to have once constituted a uniform *lex mercatoria* (´Law Merchant´)[47], amalgamated into national legal systems from approximately the 17th or 18th century onwards. Commercial law

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47 Theories and perceptions of the *lex mercatoria* will be discussed in more detail in Chapter X.2.1., *post*. However, a brief introduction already needs to be made here. The background of the discussion on the *lex mercatoria* has to be seen in the light of history. The development of international trade law could be categorically divided into three different phases.

In the late medieval period and during the 16th and 17th centuries, commercial law was pan-European in the sense that it was the law created and applied by businessmen themselves without the interference of the crown and its courts. This commercial law has been called ´lex mercatoria´, ´ius mercatorum´ or ´law merchant´.

However, during the course of the 17th century, law merchant started to convert itself into national commercial law in the European states of the time. The result was either codification (the Napoleonic Code Civil and Code de Commerce) or integration into common law in England by virtue of special courts established during Lord Mansfield. It has been said that the uniformity of law merchant disappeared during this process. >>

started then to develop in different directions. The significance of harmonising the law of international trade has already been recognised for more than one hundred years. Harmonisation efforts have generally been successful if we consider the Uniform Customs and Practice for Documentary Credits (UCP), the Vienna Sales Convention (CISG) or international arbitration istruments. An area in which harmonisation has created patchwork effects is transport law. Progress in harmonisation has partly been achieved through the involvement of governments by creating international conventions and model laws. A relevant part of the achievements have however been achieved by the business community itself by creating self-regulatory rules[48] such as the UCP or the INCOTERMS[49].

The UNIDROIT Principles of International Commercial Contracts and the European Principles of Contract Law have apparently both attracted new friends to the idea of transnational legal principles, at least if one considers the interest that has been shown towards these instruments. At the same time, the evolution

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<< The United States was founded at the end of the eighteenth century. Its international commercial law derived from the English Law Merchant. That Law Merchant is said to have been closer to the Continental Civil Law *à l´époque* (Chandler, III in Transfer of Ownership, p. 417).

During the 20th century, however, hand in hand with the growing international cooperation in other fields, and with a view towards facilitating a drastic increase in the volume of trade as well as to improving the predictability of commercial transactions, the harmonisation of international commercial law was commenced. This work has led to signicant achievements such as the CISG, or the Uniform Customs and Practice for Documentary Credits.

This development has created a school of thought which considers that the world is witnessing the emergence of a new *lex mercatoria*. It would be composed of uniform laws and conventions, international law, general principles of law, standard contracts, uniform rules created by international organisations, trade usages and reported arbitral awards (Lando 1985). The *lex mercatoria* has also been seen as an element of the harmonising of national law, but national law based on harmonisation is not, by definition, pure *lex mercatoria* since the latter is often considered to be an autonomous regime. By contrast, *Goode* considers in his recent article listed below (p.266) that "all rules must ultimately draw for their legitimacy on national legal basis".

For the earliest known treatment entitled *lex mercatoria* which also became known as the ´law merchant´, see Lex Mercatoria and Legal Pluralism, A late thirteenth century treatise and its afterlife, edited translated and introduced for the Ames Foundation by Mary Elizabeth Basile, Jane Fair Bestor, Daniel R. Coquillette and Charles Donahue Jr., Cambridge 1998.

The development and role of the *lex mercatoria* in history and in its contemporary form is described e.g. in Malynes, Lex Mercatoria, 3rd ed., 1686, Paul Rehme, Geschichte des Handelsrechts in Ehrenberg´s Handbuch des Handelsrechts I, Leipzig 1913; Clive M. Schmitthoff (ed.): The Sources of Law of International Trade, New York 1964; Berthold Goldman, Frontières du droit et "lex mercatoria", Archives de philosophie du droit No 9, 1964, pp. 177-192; Ole Lando, Lex Mercatoria in International Commercial Arbitration, 34 International and Commercial Law Quarterly, October 1985 pp. 747-769, and Den ikke-nationale handelvoldgift, in Liber Amicorum in Honour of Alf Ross, Coperhagen 1969 pp. 296-300. For some critical English views, see Mustill, The New Lex Mercatoria: The First Twenty-five Years, 4 Arbitration International (1988) pp. 86-119 and Goode, A New International *Lex Mercatoria*? Juridisk Tidskrift 1999-2000, pp. 253-268.

48 Self-regulatory in the sense of referring to the autonomy of the business community (rather than to the fact that there would be no national law in the interpretation of the rules, i.e. self-executing contracts). See also Chapter X, post.

49 On these instruments, see Chapters VII and V, *post*, respectively.

of soft law amends traditional legal sources. The enlargement of the European Union and new opportunities to harmonise private law through the ´Community method´ among states based on different legal traditions give new arms to harmonisers.

Some writers[50] have used a new concept - *lex electronica* - for the emerging legal framework for electronic commerce. This concept is said to be inspired by the model of the *lex mercatoria*.[51] The present study also builds on this interesting concept which refers to both a separate legal framework for electronic commerce and to the particularly international nature of the *lex electronica*. I would not like to romanticise concepts that are in Latin (which I have not mastered) but to build on their practicality in the presentational sense, and I hope I do not do injustice to purer ´mercatorists´ than myself. The *lex mercatoria* is here understood to be more or less equivalent to transnational commercial law, and the *lex electronica* is its electronic component.

International trade law, based on the fruits of harmonisation or unification and resulting from party autonomy, is seen as a result of a historical development process progressing in parallel to globalisation. Historically, the *lex mercatoria*, understood widely as transnational commercial law with uniform features, certainly exists. Many questions still arise, such as whether it is a system actually autonomous from national law or a full-fledged, coherent and binding legal system.

In any case, the connection with the *lex mercatoria* indicated here leads to some normative consequences in the field of international arbitration. This is because in international arbitration[52] the legal rules applicable to the merits of the case can include, with certain restrictions, ´anational´ law independent of any national legal system. The discussion on the *lex mercatoria* relates normally to this normative or dogmatic side of the coin. As described in the literature cited in

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50 One of the first sources using the concept was V.Gautrais, G.Lefebre et K. Benyeklef, Droit du commerce électronique et normes applicables: L´émergence de la *lex electronica*, Revue de droit des affaires internationaux (RDAI) 1997, p. 547. The authors say that the concept was born around 1996, and that no definition had been established by 1997. From the American literature one can mention Johnsson & Post, Law and Borders – The Rise of the Law in Cyberspace, 1996, which builds equally on the idea of autonomous law of cyberspace equivalent to the *lex mercatoria*. Generally, concepts such as *lex electronica* are said to refer to informal legal rules applying in the context of electronic commerce. Matthew Burstein (in Internet..., p. 28) refers to the substantive law of the Internet. He refers (on p. 29) to *Law Cyberspace* as "the collection of customs and accepted practices developed by courts with guidance from users, governments, and the Internet industry". Gabrielle Kaufmann-Kohler (in Internet..., p. 126) uses the concept in a more restricted meaning referring to usages mainly in the context of contract formation. Other related expressions are *lex mercatoria numerica* used in E.A.Caprioli and R.Sorieul, Le commerce international électronique et normes applicables: vers l´émergence de règles juridiques transnationales, Clunet 1997.330, and *neo lex mercatoria* by C.Kessedjian in Internet..., p. 149 as well as *net lex* by the same author.

51 The authors of the article ´L´émergence de la *lex electronica*´ adopt a wide notion of *lex mercatoria* and follow its developments consistently as regards the *lex electronica*. See Chapter X.2., *post*.

52 The focus on international arbitration is based on its significance to international trade. Domestic arbitration may have similar characteristics, but is not interesting for the purposes of this study.

Chapters IX.5.3.and X.2, *post*, an arbitrator detaching himself from national law gets involved in an innovative norm-creation process. This innovation can already be done by the parties. The incorporation of anational sources of law can be effected contractually in most cases even if the dispute is settled before a state court.[53]

Less formal out-of-court dispute settlement methods such as conciliation or ADR can without doubt resort to similar methods in determining the legal rules applicable, where the case is to be decided according to law. As will be seen later, legislators have placed an emphasis on out-of-court dispute settlement methods in the context of electronic commerce but this is usually done with consumer contracts particularly in mind. In any case, this study follows the example of the texts listed in footnote 50, *supra*, by linking electronic commerce law to the discussions concerning the autonomous nature of business law. Using the same methology as the literature on the *lex mercatoria*, one can examine international conventions or model laws, standard form contracts, arbitral awards, usages and legal principles applicable to electronic commerce.

The *lex electronica* could thus be seen as an empirical category comprising different elements already existing or still in the pipeline, including international model laws, conventions, directives, legislation at the national level, model contracts and codes of conduct. As such it is a useful supplement of the *lex mercatoria* in one of its widest senses, which might have practical implications in the field of arbitration. The concepts and their scope are discussed in more detail in Chapters X.1. and X.2., *post*.

This study will examine a number of instruments which may facilitate electronic commerce. Some of these instruments are mandatory, such as the EC Directive[54] on electronic signatures and equivalent legislation at the national level, some are recommendations for legislators (model laws) or traders, as well as model contracts. Some sources are ´hard´ law, some ´soft´ law. This distinction is nowadays well known to many fields of law from public international law to European law and is increasingly used in private law as well. Many recognised sources of international trade law are soft law instruments as they have not been promulgated by a legislator.

It is difficult to determine with objective criteria what makes an instrument soft law. One can look at the specificity and usefulness of the instrument for commercial transactions. One can look at the representative status of the organisation that issued the instrument, how many members it has, and whether both providers and users of of the product are represented in the membership. Another criterion is the expertise of the people that have elaborated the instrument. The 1990s saw the elaboration of important restatements of commercial law, the UNIDROIT Principles and the European Principles, which

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53 A suggestion on changing the Rome Convention on the Law Applicable to Contractual Obligations to allow references to anational law has been made, and has been subject to consultation in a White Paper, see Chapter X.3.2, *post*.

54 Directive 1999/93/EC of the European Parliament and of the Council of 13 December 1999 on a Community framework for electronic signatures, OJ L 13, 19.1.2000 p. 12.

were not drafted by democratic bodies, where parties other than experts mainly from academic circles would have had a say. Yet, these instruments have attracted much interest. Soft law will be examined more closely in Chapter X.2.2., *post*.

Commercial law is generally based on the notion of party autonomy. Parties may choose the law or the rules which govern their contract. If they decide to submit the disputes arising from their contractual relationship to arbitration, the legal regime to be applied may greatly be disconnected or detached from the influence of national law and the rules and procedures applicable to the dispute settlement as such.

As the volume of electronic commerce grows, the participants attach importance to the different instruments and trading tools such as the model contracts that will eventually largely determine the scope and contents of the *lex mercatoria*. I have based this study partly on the existing *lex mercatoria* as regularly seen in legal literature and in commercial practice. I have, myself, decided to follow a broad definition which is more or less the same as transnational commercial law or ´the law proper to international economic relations´.[55]

The approach chosen here is greatly logistical and connected to trade facilitation. The aim of trade facilitation enhanced by international and national public and private organisations is to reduce the impediments created by unnecessary or inefficient trading patterns, particularly relating to the delivery and transportation of the goods and to the growth of international trade and prosperity. The instruments which are examined and presented here are therefore connected to that objective. Thus, a great deal of selection is made as to the scope. Aspects of consumer-related issues do not, as a rule, receive attention.

On the other hand, dispute settlement, particularly in the form of arbitration, involves questions similar to those for electronic contracting, the role of party autonomy and the appreciation of form requirements as to documentation, procedures and communications. One could even see dispute settlement as part of the logistical process relating to the life-cycle of a commercial contract. Indeed, logistical notions such as speed and costs have been in the forefront of international symposia for some time already.

The assessment of evidence in electronic form is one of the key questions in electronic commerce. Electronic commerce law therefore crosses the frontier of traditional private law and procedural law in many ways. In fact, electronic commerce law is a ´transillumination´ of traditional trading and other working methods and has interfaces with several fields of law.

As said, this study is based on international instruments, whether public or private. Some of them are still under preparation, due to which they have to be viewed with caution. Yet, the problems encountered and the initial solutions contemplated give some guidelines for the direction and speed of development. A good illustration is the reluctance in many forums to create a uniform substantive law for electronic commerce.

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55 Cf. Goldman 1986, p. 113.

Due to the purported international nature of this study and the enormous complexity of doing it otherwise, the references to national law made here are mainly exemplary. This study does not therefore have the ambition to constitute a tract of comparative law analysis on the issues covered. A comparative method is used in some places for teleological purposes to pave the way for harmonisation. The emphasis is, as said, on international legal instruments. There is perhaps one exception to this. English law has, however, been examined in more depth since it is regularly applied to cases of shipping and marine insurance and forms the background law of the *Bolero System*, which is, at the moment, the principal practical experiment of an electronic sale of goods system based on a central registry. Provisions of national law are therefore of importance to the establishment of the *lex electronica,* and can even constitute parts of it.[56]

This study attempts to examine on a horizontal level the developments in the legal facilitation of commerce where electronic records are used to convey information. In addition to the fact that the issues dealt with in this study are the normal components of an international trade transaction, it is also this notion of ´electronic´ which combines the detailed issues dealt with here. Writing such a study brings garlic to the author´s mind, if an awkward comparison is admitted. An entire menu, even a beer, can be made using garlic. Similarly, more or less everything in trade can become ´electronic´. Too much of either however can quench the appetite. What I mean to say is that although the use of electronic records may spread one day throughout trade procedures, including throughout dispute settlement facilities, even then the fact that the information is in electronic form remains only a spice and not the menu itself. The basic foundations of commercial and procedural law remain in place although certain details may change.

I.7 The key role of the Vienna Convention

It is probable that the *lex electronica* will largely be based on the existing instruments as regards substantive law is concerned, although their adaptation may be needed in some cases. For reasons of presentational convenience, one of them is shortly introduced here.

It could easily be said that the United Nations Convention on Contracts for the International Sale of Goods, which was signed in Vienna in 1980 and is often referred to as the ´Vienna Convention´, forms a cornerstone of the contemporary

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[56] Many relevant provisions of English law are, in turn, based on international or supranational instruments. English conflict of laws rules are based on the EC Convention on the Law Applicable to Contractual Obligations signed in Rome in 1980.

Mixing national law with the doctrine of the *lex mercatoria* (as a general category of the *lex electronica)* is obviously against even a lowest common denominator conception of it. Still, transnational commercial law is certainly influenced by national law. Good examples are the English law behind marine insurance and the US law on software. See further Chapter X.2., *post*.

For the *lex electronica* as a part of the *lex mercatoria*, see Chapter X, *post*.

legal framework for the international sale of goods. As *Bonell* puts it "(i)t is no exaggeration to say that the United Nations Convention on Contracts for the International Sale of Goods represents a landmark in the process of international unification of law".[57] By 16 March 2004, a total of 63 states had ratified the Convention, with the notable exception of the United Kingdom. [58] The Convention governs the formation of the contract of sale (Part II) and the rights and obligations of the seller and the buyer arising from such a contract (Part III), and it applies to contracts of sale of goods between parties whose places of business are in different states, when the states are contracting states, or when the rules of private international law lead to the application of the law of a contracting state.[59]

Under Finnish law, for instance, this means that contracts of sale between a party whose place of business is in Finland and a party having its place of business in another contracting state would be covered by the Finnish enacting statute[60] of the Sales Convention. It is irrelevant whether the delivery of the goods would take place in Finland or elsewhere. Moreover, should the Finnish rules of private international law be applied, a sales agreement between a Finnish seller and a buyer in a non-contracting state (like the United Kingdom) would be covered by the Convention, in the absence of a choice of law clause in favour of some other law, since the Finnish rules of private international law make the seller´s law applicable to the sales contract.[61] It should be added that the domestic Finnish Sales Act[62] applies to sales between parties having their places of business in Finland and Sweden, Norway, Denmark and Iceland in case Finnish law is to

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57 Bonell 1996, p. 1.

The adoption of the CISG was a result of over fifty years of work.This work started as early as 1929, when the International Institute for the Unification of Private Law commenced work on a uniform law for international sales. The idea came from the German comparativist Ernst *Rabel*.

58 The 1980 Vienna Convention was preceded by two Uniform Laws on International Sales signed at the Hague in 1964:

the Uniform Law on the International Sale of Goods (ULIS) and the Uniform Law on the Formation of Contracts for the International Sale of Goods (ULF). These Uniform Laws did not gain wide adherence as only nine states ratified them.

59 CISG Article 1 paragraph 1. However, Article 95 allows states a possibility to declare that they are not bound by subparagraph (1)(b) of Article 1 of the Convention. Such a declaration remained recorded on 4 May 2002 for China.

For the CISG, see e.g. John Honnold, Uniform Law for International Sales under the 1980 United Nations Convention, 3rd edition, The Hague 1999; and Bianca-Bonell, Commentary on the International Sales Law, The 1980 Vienna Sales Convention, Milan 1987. The scope of the Convention as regards the subject-matter of the sale will be examined in Chapter X, *post*.

60 Laki kansainvälistä tavaran kauppaa koskevista sopimuksista tehdyn yleissopimuksen eräiden määräysten hyväksymisestä, 20.3.1987/795 v. 1988.

61 Laki kansainvälisluonteiseen irtainten esineiden kauppaan sovellettavasta laista 387/64, based on the 1955 Hague Convention on the Law Applicable to International Sales of Goods. This Convention has now been amended by the 1986 Hague Convention on the Law Applicable to Contracts for the International Sale of Goods.

62 Kauppalaki 355/1987.

be applied. The Finnish law, like the corresponding sales laws in the Scandinavian countries, have not, however, incorporated Part II of the Convention concerning contract formation.

The CISG becomes applicable through geographical connecting factors or, unless a reservation is made, through the application of the rules of private international law, which almost invarably include the possibility for the parties to opt for the law applicable to their contract. Thereby the scope of the Convention can be extended by the parties´ choice. To the extent party autonomy is permitted by the relevant private international rules, parties can opt for the law applicable to non-international sales, or they can, it is submitted, make the CISG applicable by referring to the law of a contracting state, although their places of business are in a non-contracting state. The Convention did not envisage a possibility for direct incorporation of the Convention without necessarily incorporating it as part of national law, which is a technique used recently in international law making.[63] However, party autonomy is often regarded as allowing this.[64] Chapter X will discuss questions of the incorporation of international trade law instruments into contracts and their application as the ´law applicable´ in some more detail. Suffice to say here that the CISG is a relevant component of any legal rules designated by the parties and arbitrators.

The drafters of the CISG apparently saw that the Convention´s uniformity might be jeopardised by differing national interpretations. Article 7 provides therefore that in interpreting the Convention, regard is to be had for its international character and to the need to promote uniformity in its application and the observance of good faith in international trade.[65] The same article refers further to the general principles on which it is based before the rules of the *lex causae* are resorted to.

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63 This is a possibility provided by e.g. the UNCITRAL draft convention on electronic contracting, see Chapter IV.7.2., *post*.

64 This is a technique used in e.g. the ICC Model International Sale Contract (Manufactured Goods Intended for Resale), ICC Publication No. 556.

65 This provision brings to mind a parallel - the obligations of the EU Member States to keep in mind the objectives of the Treaty of Rome.

II BUSINESS AND LEGAL CHARACTERISTICS OF ELECTRONIC COMMERCE

In this chapter, an overview of electronic commerce is given from a technical and market perspective while taking at the same time time a look at the main legal and infrastructural problems encountered in the transition to electronic contracting. This is meant to serve as an introduction to the substance. The aim is to describe the main developments and problems of electronic commerce with a view to coming back to them throughout the study with a more solution-oriented approach.

The first three subchapters deal with major commercial or technical trends of or prerequisites for the development of electronic commerce. First, some data about the rise of the volume of electronic commerce are given. Second, the rise of electronic commerce is shown to be based on technical developments in the computer and software industry and the emergence of the Internet. More particularly, however, communication standards and their harmonisation play a pivotal role, and the lack of convergence constitutes an obstacle equal to that of legal harmonisation. New business models are rising, and the need for third party service providers to verify messages leads to commercialisation of trust. Third, it is put forth that in the service of the international sale of goods electronic commerce inevitably forms part of logistics and should be seen in conjunction with other trade facilitation measures.

The remaining sub-chapters deal with legal issues of electronic commerce. As the presentation should serve the objectives of the international sale of goods involving transportation of the goods and the use of documentary payment systems, the focus is on general issues relating to contract law. As already mentioned, this study more or less turns a blind eye on issues relating to trade policy, taxation, intellectual property rights, competition and marketing, which are more a subject for texts having a political or consumer law dimension in mind.

II.1 The recent expansion of electronic commerce

It is very difficult to define the volume of electronic commerce today. A report released by UNCTAD[1] forecast that registered Internet users could total 655 million by the end of 2002, which makes a year-on-year increase of 30 per cent when compared with 2001. The value of goods and services bought and sold over the Internet was to reach 2.3 billion US dollars, which makes a 50 per cent rise from 2001.[2] At the same time, the report suggested that the volume of net trading would reach as high as 3.9 billion US dollars by the end of 2003. According to the UNCTAD E-Commerce and Development Report 2002, the present growth rates will lead to a situation in which around 18 per cent of all purchasing by companies and individuals could be done in cyberspace in 2006. The actual realisation of the figures is uncertain. Forecasts of the value of global e-commerce in 2003 ranged between USD 1.408 billion and USD 3.878 billion. The share of business-to-business transactions out of the total of world e-commerce was commonly calculated at around 95 per cent.[3]

In the United States, the leading users of e-commerce are manufacturing and merchant wholesalers. The share of e-commerce in total business-to-business trade in 2001 was 14.9 %.[4] According to one study, by 2004 business-to-business e-commerce would represent nearly 10% of all trade between enterprises, although that figure was less than 1 % in 2001.[5] According to the same source, by 2006, the penetration of e-commerce in logistics and storage would be 30%.

II.2 In search of technical interoperability and convergence

The information-carrying power and flexibility of electronic messages have improved.[6] In early electronic commerce, messages consisted mainly of unlabelled

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1 E-Commerce and Development Report 2002 (UNCTAD), November 2002. In fact, this report quotes figures from the International Telecommunications Union (ITU).

2 As a comparison, American consumers have been estimated to have paid $ 1.2 billion for various Internet content excluding gambling and pornography. This sum is barely one quarter of what Websites raised by selling advertising space (estimate by the firm eMarketer; The Economist, December 21st 2002 – January 3rd 2003, p. 91.

3 E-commerce and Development Report 2003 (UNCTAD, November 2003), p. 17.

4 Ibid., p. 20.

5 E-commerce and Development Report 2003 (UNCTAD, November 2003), p. 21,quoting Forrester Research.

6 The Internet is made up of three layers. At the bottom is a physical layer, across which communication travels. This means the computer or wires that link computers to the Internet. In the middle is a ´code´ or ´logical´ layer – the code that makes the hardware run. At the top is a ´content´ layer – the actual stuff that gets transmitted across the wires. (Organizations involved in technical coordination of the Internet, ICC Doc. 373-31/5, quoting the work of Lessig).

data fields in a prescribed form. There was a need for the software producers and system integrators to keep the agreed form, which led to inflexibility.

A new approach to message form has emerged from the World Wide Web. Experience with Hyper Text Markup Language (HTML), the format for Web documents derived from the Standard Generalised Markup Language (SGML), led to making SGML extensible. In this way, the Extensible Markup Language (XML) was born. This language has now overtaken the earlier formalistic messages used in EDI, although EDI remains in use in some systems. The power and flexibility of newer message forms and their ability to integrate data into a documentary context sets the stage functionally for electronic contracting.[7]

A discouraging development, however, is that there is now a ´patchwork´ of XML standards as parties and organisations involved in international trade create their own, often proprietary standards for XML-messaging.[8] A message standard is an (internationally) agreed template that parties involved in a transaction can use and abide by in order to exchange structured information. A party using its own proprietary standard has to persuade others to use the same standard or computer ´language´ in order to be interoperable with them. Two interoperable systems for instance understand store accounting terms in a similar fashion.

The next step beyond interoperability is one in which various interoperable standards are convergent. Convergence makes it possible for the information system to read messages that are produced by a different information system by converting them into a readable form. In order to reach convergence, all players within a given industry agree on using the same physical representation or ´language´ throughout the transaction life cycle. Interoperability and convergence make it possible for importers and exporters, financial institutions, other trade service providers and market infrastructures, back-office applications and interactive computer databases to be interconnected with each other.

This interconnection leads to the establishment of ´Web services´, where various services offered in electronic form are commercially linked to one another.[9] The service is based on a ´platform´ which is a computer programme used by the server and which links various resources available to the service.[10]

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7 GUIDEC II, Electronic Contracting, p. 3.

8 Paul Miserez, Converging message standards for e-trade, DCI Vol 8 No 1, p. 6.

9 The concept of Web services refers to automated interaction over the Internet between computers that are managing different business processes, in such a way that they generate a ´grid´ of computers in which each machine is able to feed other machines the input they require and/or obtain from them the information it needs. This interaction occurs via software that is designed to use other software, the communication between the two being based on Internet standards and protocols (E-commerce and Development Report 2003, pp. 31-32).

10 Processing power or storage capacity is not concentrated in one place but pooled together in the network and used when needed. Different operating systems work together. Similarly, Web services apply the standards embodied in XML to enable a computer to identify the resources. There is, however, a need to safeguard interoperability between the different platforms, which is a field with heavy competition.

The platform may include sophisticated technical solutions such as multi-vendor catalogs, negotiation systems and online payment transaction solutions.[11] Web services are in a process of development and do not yet always meet the requirement of comprehensiveness despite contrary claims.[12]

Moreover, standards interoperability and convergence greatly increase the potential for ´straight-through processing´ (or ´STP´), which means the ability to process data without human intervention. The use of STP then makes it possible to reduce operational cost by eliminating the need to re-key information and speeds up processing. Its use also reduces errors and risks as well as the possibility of fraud.[13]

Standards are still in need of being more convergent. If convergence is attained for XML-based message standards, the business world may eventually accept the new electronic business methods. It would be ideal if the solution reached could cover the entire trade transaction flow from a sale contract to documentary credits.[14] In a closed proprietary system, possibly based on the use of a central registry, one solution may already be used throughout the transaction, including the contract of sale, the contract(s) of transport and eventually documentary credits. Some projects that aim for convergence are mentioned in Chapter VIII.2.1.4., *post*.

II.3 Commercial trends

Literature on the business management aspects of electronic commerce is mushrooming in a manner similar to electronic commerce law. For the purposes of this study, it should be sufficient to show the contact points between legal trade facilitation relating to the international sale of (tangible) goods and some commercial trends of e-business. I will limit myself to the delivery phase of the transaction which is now seen as a network.

II.3.1 The management of the supply chain and the role of electronic marketplaces

There are reasons to believe that e-commerce will have an impact on international trade transactions. In physical flows of goods, product information can be made available in virtual ways. E-commerce thereby gives companies access to more markets and customers. Information flows eliminate paper-based approaches to work. Financial flows improve payment mechanisms.[15]

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11 Grieger, p. 161.

12 The travel agency sector has advanced notably by linking hotels, airlines and other service providers.

13 Miserez, p. 6.

14 As stated by Paul Miserez, Converging message standards for e-trade, DCI Vol 8 No 1, pp. 6-7.

15 Berger in Gower 1, pp. 430-431.

The availability of information in real time during the delivery and transportation processes will inevitably have an impact on production and distribution, i.e. on how the obligations in sales transactions are met. E-commerce has the capacity through information, such as tracking and tracing, to revolutionise the way that goods and services are delivered (´e-fulfilment´).[16] One of the striking effects is that the performance gap can no longer be hidden. If there is a gap between the level at which a company´s supply chain could work and how it is working in practice, it will show. Real time information adds pressure for more effective communications between the parties under the contract of sale. I believe this will inevitably lead to increased demands for conformity in delivery obligations. The stages of delivery and corresponding notices of non-conformity, where it occurs, can not necessarily be approached by traditional methods and delivery itself may have to be looked at as a process.

Information systems, if utilised properly, can create a competitive advantage for companies by helping them in to manage their business in many ways. ´Supply chain management´ is the integration of key business processes from end user to the original suppliers that provide products, services, and information, which add value for customers and other stakeholders.[17] The management of the supply chain can provide savings e.g. by identifying optimal inventory levels and thereby reducing warehouse space, leading to higher quality products, increased productivity and added flexibility. One of the benefits of supply chain management is information integration and standardisation. Like economics and law, supply chain management theory also discusses transaction costs, although definitions may vary.[18]

As the supply chain moves towards external integration with business partners, it becomes necessary to establish a total supply chain network with an integrated database capable of supporting relevant supply chain activities. Traditionally, this network was created by EDI as one-to-one connections between companies. Open networks such as the Internet are now making it possible to form ´electronic marketplaces´ for various relationships including business-to-government, business-to-business, and business-to-consumer, amongst others.[19] Business-to-business Internet-based electronic marketplaces have been established in various industries, supporting the exchange of goods and services. The firm operating the marketplace is often referred to as the ´intermediary´, and may be a participant in the market as a buyer, a seller, an independent third party, or a multi-firm consortium.[20]

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16 Ibid., p. 434.

17 Grieger, p. 1, quoting Lambert, D.M., Cooper, M.C. & Pagh, J.D., Supply Chain Management: Implementation Issues and Research Opportunities" (International Journal of Logistics Management, vol 9 (1998) no. 2, pp. 1-199, p. 1.

18 See Grieger, pp. 111-122.

19 In these marketplaces, electronic connections are established through the Internet by using network technologies like communication protocols such as TCP/IP, HTTP, wireless, programming languages (Java or scripting), cryptography algorithms or mark-up standards such as HTML, SGML or XML (see *supra*).

20 Grieger, summary/v. Grieger cites a figure given by Deloitte Consulting: in July 2000, a total of 1,447 electronic marketplaces were identified. An estimate was given that in 2003 there would have been 20,000 electronic marketplaces.

An e-marketplace can thus be defined as an online service to the benefit of buyers and sellers, offered by a neutral and independent market service provider against a fee.[21] Several buyers and sellers meet to buy or sell goods or services, which is regularly illustrated by a ´butterfly model´. Horizontal marketplaces serve a wide range of industries, whereas vertical e-marketplaces are geared to the needs of a particular industry.

There is a growing tendency to use the more general term ´Internet trading platform´, which is a wider concept than ´electronic marketplace´, as the latter is mostly understood as being confined to buying and selling. Some platforms namely have functionalities relating to settlement and fulfillment such as logistics and payment. A full-fledged service in this respect would entail contracting (buying or selling), the management of transportation, trade finance, insurance and government relations. What are termed ´integration platforms´ integrate the IT infrastructure of several parties to enable electronic document exchange. In this way, the technical and commercial meanings of the word ´platform´ go hand in hand.[22]

The story of e-marketplaces has not been a simple success story. The performance of most e-marketplaces has been generally unimpressive.[23] The number of marketplaces fell after the bursting of the IT bubble soon after the turn of the millennium. However, there are public attempts to encourage the use of electronic marketplaces.[24] Moreover, marketplaces designed predominantly for consumers have gained ground, which illustrates the potentials of the concept.[25]

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21 B2B Internet trading platforms: Opportunities and barriers for SMEs, A first assessment by Maria Perogianni, Enterprise Papers No 13 – 2003, p. 7.

22 The use of the term ´Internet trading platform´ is recommended by the Report of the expert group on B2B Internet trading platforms, Final report to the Commission, 2003, on p. 4. The report lists various forms of Internet trading platforms:

- company websites, sometimes serving as entrances to an exclusive extranet which is available only to customers and registered site users,
- product supply and procurement exchanges,
- specialised or vertical industry portals, providing a ´sub-web´ of information, product listing, discussion groups and other features (used e.g. in equipment leasing),
- Web-EDI, serving payments, information exchange and purchase order requests, and
- e-marketplaces.

The terminology of Internet trading platforms includes

- pinboards, which provide an opportunity to announce a concrete desire to buy or to sell something and to prepare for a transaction;
- exchanges or matching systems which, in contrast to pinboards, facilitate the negotiation process, and the platform provides some mechanism for the matching process;
- auctions are normal price-finding procedures supported by the Internet trading platform with the seller initiating the procedure of finding the highest price, or the buyer initiating to find the lowest price (reverse auction);
- catalogues that combine the selling catalogues of different sellers; and
- collaboration platforms that enable the exchange of information to optimise ordering and delivery.

23 Berger in Gower 2, p. 447.

24 For the European Commission´s efforts, see Chapter IV.2., *post*.

25 See At the drop of a hammer, Online Auctions have been a runaway success, The Economist May 15th 2004, A survey on e-commerce, pp. 9-10; as well as A market too far, Why some business-to-business exchanges have been slow to take off, ibid., p. 10.

A distinction can be drawn between open and closed marketplaces representing corresponding business models. Closed marketplaces (established using EDI or through the Internet) are formed between companies (B2B). These are often industry-specific, and the number of companies involved is limited. Communications take place through a closed company-owned (frequently called ´proprietary´) networks[26]. The partners are known and connected to each other in many ways, the system is characterised by a high degree of information sharing and collaboration, and the networking also functions as a security method.[27] There may be commercial implications: the buyer is restricted to a defined set of sellers, and a seller is committed to sell only to a specified buyer or small group of buyers. This actually constitutes a closed business model.[28]

In such a model, the relative numbers of and availability of alternatives are among the factors determining bargaining power. Bargaining power has often proven to be greater in the buying role, assuming that many potential suppliers exist or can be induced to exist. Chains have been built in industries in which there is a need for specialised goods, such as in the automotive, aerospace and similar industries. Captive supply chains manufacture goods that are made to the buyer´s specifications.[29]

In terms of electronic commerce, traditional electronic data interchange (EDI) is based on the chain model because of the difficulty and complexity of setting up interconnected databases and the means of reliably transferring information between them. The chain also provides a useful framework to organise the legal setup for the interchange. EDI is established bilaterally between trading partners through an agreement[30] that is intended to suffice for all transactions that the parties will carry out. EDI has thus greatly promoted the development of trade chains in the recent years at the expense of free choice in the marketplace.

Open Internet-based marketplaces are established, not only between companies, but between companies and consumers, or between companies and authorities. The market is open with an unlimited number of participants, and the trading partners may also be unknown. The network is open and unprotected due to which security and authenticity is needed. There is usually a low degree of information sharing and collaboration.[31] Although chains have become common in recent years, the open market model retains a great advantage over the closed chain model and a slight advantage over the semi-closed portal model. The advantage is of course created by increased price competition in an open market. Moreover, an open market can be regarded as more innovative and responsive to changing circumstances.[32]

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26 In the Internet-based environment firewalls are usually used.

27 Grieger, p. 150 table 26.

28 GUIDEC II of the ICC, published in November 2001, p. 2.

29 Ibid.

30 On interchange agreements, see Chapter III, *post*.

31 Grieger, p. 150 table 26.

32 GUIDEC II, p. 2.

Effective supply chain management occurs in an environment where communication links are well-established. It is therefore submitted that closed models, at least in technical terms, would be more suitable. The challenge for open electronic commerce techniques is to facilitate efficient production and distribution.

One of the critical points for electronic marketplaces is interconnection in commercial terms. Customers depend on end-to-end transactions, which involve value-added services or supply chain functionality that often lies outside the markeplace´s own competence. These services include activities such as logistics, risk management, maintenance and repair, and order fulfillment. Successful marketplaces, or rather trading platforms, enable a series of connections to support end-to-end solutions.[33]

Web services have the potential to combine various supply chain systems and facilitate their integration, and to establish links to services such as logistics and finance. They are also helpful in outsourcing[34] various activities.

In *Grieger´*s view, "as supply chain management is characterized by its end-user oriented and extended nature, further investigations might extend the quest for integration across the entire IEMP network to include logistics service providers, financial service providers, application providers and other third parties". He adds that marketplaces could "mediate the ´communication and information flow facility structure´ of ultimate supply chains".[35] These remarks show a connection to the present study. Communication and information flow facility, in order to be truly useful, should deal with legally significant communications and documentation in electronic form.

II.3.2 Electronic commerce and logistics

The word ´logistics´ was originally used in a military sense to mean the optimisation of support functions for combat activities, although its civil use has become more widespread. In its civilian use, logistics is understood to mean the management and optimisation of material, information and capital flows. Logistics is concerned with the cost-efficiency of the supply and delivery chain starting from the supplier and ending at the end user´s premises. Participants in the chain should cooperate to reach optimal solutions for each party involved.

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33 Grieger, p. 162 citing A.T.Kearney.

For instance, *Celarix* and *SmartShip.com* offer services that help shippers and their customers to arrange small and large-scale transportation. *ClearCross* and *myCustoms.com*, on the other hand, maintain online databases and related services that help shippers to manage tax, duty and customs laws in different countries.

34 The term Business Process Outsourcing (BPO) is defined e.g. as "contracting with an external organization to take primary responsibility for providing a business process or function" (E-commerce and Development Report 2003, p. 137 and the sources referred to therein).

35 Grieger, pp. 269-270. He refers to the *ChemConnect* network that covers a variety of different strategic alliances and, thereto a lot of connections made through e-hub connection; see http://www.chemconnect.com, visited on 1.4.2004.

A new concept, ´e-logistics´, has emerged to denote the use of information technology in the service of the supply and delivery chain.[36] An ´e-supply chain´ harnesses the Internet-based technology and its applications to drive improvements in planning, design, collaboration, execution, management, and the efficiency of the supply chain.[37]

The relationship between electronic commerce and logistics is based on the fact that ordering materials through the Internet (´e-procurement´) will become more and more common. This applies not only to business-to-business but also to business-to-consumer relationships.[38] Methods of transportation and delivery will have to be adapted to the new needs, especially to the need for a fast or on time delivery.

Logistics services are often outsourced to specialist companies which offer ´third-party logistics´. This service is carried out by an external company on behalf of a shipper and covers the management of multiple logistics services.[39] These activities are offered in an integrated way, not on a stand-alone basis. The co-operation between the shipper and the external company operation is regularly a continuous relationship.[40] The market has created a branded concept of ´fourth party logistics´, which develops outsourced logistics services even further by taking a fully holistic approach to its customers´s logistical process. What is characteristic of ´4PL´ is the extremely strong use of IT capabilities, an assembly of organisations with a full spectrum of required capabilities, the culture of innovation and the management of information flows.[41]

In addition to distribution, e-commerce may affect sales management by cutting the sales organisation and moving to a more direct relationship between the manufacturer and customer.[42] Electronic commerce and communications can affect the supply chain in various ways. For instance, sales and supply chain management includes risk management, which in turn consists of many components from tackling physical risks to contractual risks and insurance matters.[43]

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36 See e.g. ´Information and technology in the supply chain, virtually there? The reality of eMarkets´, PricewaterhouseCoopers 1991, and ´The changing shape of European logistics, PELS Yearbook 2001, The e-logistics marketplace as the challenge for logistics service providers´, PricewaterhouseCoopers 2001.

37 E-Business Logistics Technology Roadmap ELO 2002-2005, Version 2.0, p. 24.

38 E-commerce and Logistical Consequences, http://www.oecd.org/dataoecd/56/22/2662099.pdf, visited on 18.12.2002, p. 1;

39 These services include some of the following: operation of a vehicle fleet, warehouses, packing, labeling and sub-assembly, managing of international movements, warehouse monitoring, routing and scheduling.

40 E-Business Logistics Technology Roadmap ELO 2002-2005, Version 2.0, p. 24.

41 Bedeman and Gattorna in Gower, pp. 482-484.

In another context (see Chapter IX.4.2., *post*), the ´fourth party´ is a metaphor for applications that enhance the process and thus do more than simply deliver the expertise of the human third party across the network. The metaphor views the network as a ´communication network plus more´.

42 Räty, p. 3.

43 Räty, p. 8.

An important development is the increase of information in the supply chain. E-commerce is particularly well-suited to providing information such as product tracking and tracing. Shipment tracking and monitoring of delivery increase the information about the situation, status, and condition[44] of cargo in the delivery chain.[45] These are also important matters for the delivery of the goods under the contract of sale and for the execution of the contract of transport.

The availability of information in real time gives impetus to look at the carrier´s obligations to deliver to the correct consignee and puts the role of trade documentation in recording the consignee and cargo particulars in a new light. Information is available all the time, not only when the ship sails to sea. Carriers can be in situations in which they do not know to whom to deliver the cargo because of conflicting claims, some of them potentially based outside the contract of carriage.

Legislation gives weight to the good faith of the parties as to the physical condition of cargo or conflicting claims in respect to it. The legal provisions were created during an era when information about the condition of the goods and the parties´ rights in respect to them were not general information. Modern technology facilitates and market conditions often compel the disclosure and distribution of relevant information in the chain.

Another dimension, which is even more crucial to this study, is the streamlining of documentary processes by using electronic records instead of paper documents. This process requires that the functions of various documents used in connection with a trade transaction are analysed, whether the contemporary documentary process is actually relevant, or whether parts of it can be considered redundant. As already noted, managing trade documentation is an important cost factor to businesses.

New services have also emerged for the management of trade documentation.What the *Bolero System*, which is the most well-known example of the new approach, is doing is interconnecting various operators in a transaction by providing an electronic platform for the document flows between them. As the documents are electronic messages exchanged in the system that replicate the functions of paper documents, the use of the system is close to the idea of outsourcing trade documentation functions. Obviously, the information content and use of the messages is run by the companies themselves.

A project launched by the Finnish Ministry of Transport and Communications[46] in the late 90s found that an international sale of goods transaction required 34 different documents. Surprisingly, however, the number of documents used in trade inside the European Union amounted to 31, whilst purely domestic Finnish trade required 26 documents. There are documents in use which are either country-specific or sector-specific.

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44 If the cargo has been loaded into containers, or is packed in a way that covers defects, its condition is not conspicuous during the transportation. There are, however, situations where new information on cargo condition is obtainable during the transportation.

45 For the role of Wi-Fi technology in logistics, see Chapter III, note 1, *post*.

46 Logistics Chain EDI Project, p. 5.

The report made on the basis of the project demonstrates that all pertinent information between the trading partners, the seller and the buyer, has already been created and documented during the offer and order confirmation stages. Documents created at a later stage, notably the invoice and the transport document, merely repeat the same information regarding the contract of sale.[47]

As the Finnish ministry report suggested, data exchange between trading parties can be carried out faster and more securely by employing electronic messaging. Cost savings are made by eliminating unnecessary documentation and avoiding duplication by way of repetitive keying or copying of information into documents or information systems. Parties may decide to use electronic trading platforms which increase the benefits of electronic communication.[48]

The use of the Internet has different effects in terms of logistics. It has enabled small- and medium- sized enterprises (SMEs) to share in the commercial flows it generates. At the same time, however, the Internet and e-commerce are reshaping and transforming the way in which the production and distribution of marketable goods is organised.[49] Industry will respond to the increasingly stricter demands of customers by offering a range of new products and services, which leads to an increasing use of tailor-made products. The use of information and communication technology will help to increase collaboration between the players in the production and distribution chain. The production chain is directly linked to demand and inventory has virtually disappeared from the production stage.[50]

As for transportation, highly fragmented consignments need to be delivered globally within a very tight timeframe and at low cost. E-commerce can contribute to achieving an efficient distribution system by using online bidding for transportation and shipment tracking.[51] Although information technology

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47 A transport document contains, however, information specific to the contract of carriage. A model examined in the middle of the 1990s, the Electronic Trade Credit (ETC) within the International Chamber of Commerce, would have used the sale contract´s data elements such as the goods description, price, insurance particulars etc. to obtain simple confirmations from the contracting participants (carriers, insurers etc.) in a transaction.

48 A list included in the *Bolero Feasibility Study 1999* is given in the preamble of Chapter VIII.7., *post*.

49 Summary of the discussions of the Joint OECD/ECMT seminar on the impact of e-commerce on transport, p. 2, at http://www.oecd.org/dataoecd/32/26/2404595.pdf, visited on 18.12.2002.

50 Ibid., p. 3; the automobile industry serves as an example of ´tailor-made´ goods, where cars are produced to meet the exact requirements of a customer.

One of the most famous abbreviations in logistics is ´JIT´or ´JOT´ i.e. "just-in/on-time" signifying first and foremost the avoidance of unnecessary storage or inventory of goods. Should an anecdote be admitted here, even burglars in Belgium are considered to apply this strategy to their activities: they do not take with them anything which they might not be able to place on the market, however, they register anyway the existence of objects with certain characteristics that may be of interest to their clientele. Once there is a customer, for instance, for a blue BMW station wagon, the burglar makes a second visit to his source.

51 See also Sähköisen tiedonsiirron kehittäminen vaarallisten aineiden kuljetuksissa (The development of electronic data interchange in the transportation of dangerous goods), a study ordered by the Ministry of Transport and Communications of Finland conducted by Viatek Oy, 12.6.2001, at http://www.mintc.fi/www/sivut/dokumentit/julkaisu/julkaisusarjat/2001/34a.html, visited on 25.11.2003.

yields business opportunities for SMEs, some advanced technological facilities, like those used in shipment tracking, may require investments beyond the possibilities of SMEs.[52] Therefore, the impact of e-commerce in terms of competition may be detrimental to them. This could be a matter for public policy.[53] On the other hand, technological development increases the functionality and reduces the cost of technical devices, e.g. computerising haulage.[54]

II.3.3 Commercialisation of trust

In addition to technical qualities, the system needs to guarantee message security and to assure the authenticity of messages. As portrayed in GUIDEC II, the need for trust has to be commercialised. The industry to provide trust services helps to transfer part of the risk from the parties in a transaction to third party service providers. The service providers may authenticate messages, provide payment and credit services and assist in reviewing security, information flows and other technical aspects of the system concerned. Managing information flows may be coupled with the management of documentation flows. The management of the trade documentation of a company could be largely outsourced to an electronic service provider.

Networked computers make and perform contracts with increasing frequency using the various business models described above. Parties can now automate the contract formation process and manage it much as they manage their other critical information processes. The automation may lead prevailing commercial structures towards classic market economy models.

Automated processes can improve the inclusion of the real relationship between the parties as they evolve. In EDI, the contract formation process has been "front-loaded" in the sense that it is a manual process done once and for all when a link in the chain is established. The contractual framework is thus already created in specificity in the beginning. GUIDEC II suggests, however, that an ideal way of establishing a legal relationship is to agree on the ´ground rules´ by way of an initial enabling contract, and to allow further contracts to draw in specific details. Unfortunately, GUIDEC II does not specify which ground rules are meant.

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52 Members of the transport industry have, already for years, offered interactive services on the Internet ranging from booking, shipment tracking, schedules, vessels particulars and plans, even ship auctions. (Gauthier, ETL 1997, p. 695).

53 Summary of the discussions of the joint OECD/ECMT seminar on the impact of e-commerce on transport., p.4.

54 See Informaatiotekniikka kuorma- ja pakettiautokuljetuksissa (Information technology in truck and van carriages), a study ordered by the Ministry of Transport and Communications of Finland and conducted by Viatek Oy, 30.6.2001, at http://www.mintc.fi/www/sivut/dokumentit/julkaisu/julkaisusarjat/2001/35a.html, visited on 25.11.2003.

A documentary credit transaction done in an electronic form may be seen as implementing these ideas. The commercialisation of trust has produced systems such as the *Bolero System*, in which a third-party service provider combines several relevant parties (banks, carriers, insurance companies) in a trade transaction through a rulebook, which lays down the ground rules for several transactions. A bill of lading which traditionally carries the function of ´a token of trust´ is reproduced electronically in this system.

II.4 Functions of paper to be replaced

In order to understand the legal problems relating to the replacement of paper documents by electronic messages, one has to take a look at the various functions of paper in an international commercial transaction.

II.4.1 Functions of paper generally

Toh See Kiat[55] has listed five primary functions of paper in international trade.

Paper is a carrier of information and instructions; a carrier of authentication symbols and devices; a carrier of evidence; a carrrier of legally significant symbols; and, last but not least, paper serves formal legal functions. The customary way to denote the authenticity of a paper document is a signature. As we shall see, an equivalent for a hand-written signature can be produced by electronic means. The function of paper as a carrier for legally significant symbols means that documents can evidence rights, e.g. ownership or possession.

The formal legal functions of paper documents are usually laid down in national law.[56] A document may need to be in writing before it is valid or enforceable. It may need to exhibit statutorily specified contents or phraseology or it may need to adopt a specified format. Relations with national authorities have been particularly paper-bound. Yet these can easily be replaced by electronic reporting. A good example is the breakthrough of electronic customs clearance in many countries.

As we shall see later, there are definitions of ´electronic records´ in various instruments relating to electronic commerce. It may be useful to note that what is characteristic to any ´document´ or ´record´, irrespective of the method of its presentation, is that it is constituted of a set of data or information recorded as such.[57]

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55 Toh See Kiat, p. 1.

56 Ibid., p. 4. Some international conventions may of course contain requirements as to the form of information, see f.ex. the Hamburg Rules in Chapter VI, *post*.

57 Grönförs 1991, p. 67.

II.4.2 Documents as carriers of rights – the concept of abstraction

Particular attention has to be paid to documents which evidence rights and obligations in a manner that is is tied to a tangible document and cases in which the possession and delivery or surrender (*traditio*) of the document constitute legal effects. Paper as a physical material facilitates its physical possession and the transfer of rights recorded on it. There is only one paper called ´original´ (or a preset number of ´originals´) representing the rights and the equivalent information recorded on it. The conceptual function behind an original is the uniqueness or singularity of a set of data. One has to verify that a set of data content is used only once for a given purpose. As it is not possible to deliver data physically, a transfer of rights embodied in the agreed data content must follow other patterns such as the assignment (*denuntio*) of rights.[58]

Documents represent rights in various senses. Negotiable instruments such as promissory notes, cheques or bills of exchange relate to the payment of money. The debtor can pay the person by producing the instrument and can be sure that he does not have to pay a second time. The creditor, as long as he or she possesses the instrument, does not have be afraid that the payment wil be made to somebody else.[59] Such documents concern the payment of a sum of money, which is a generic obligation.

Documents of title such as bills of lading are, under many domestic laws, also negotiable instruments[60], but more accurately they represent rights to goods, which is usually a specific, but sometimes a generic obligation.[61] Although bills of lading are regulated by international conventions, which deal with their functions in contracts of transport, national law also has a role to play in governing the nature and some aspects of the commercial operation of the instrument and its role in transferring rights to the goods in a proprietary sense.[62] When the right is specific, it establishes a right to the goods themselves, which is generally valid against the world at large being a right *in rem* or a security right.[63] In transport law, transport documents which are not documents of title but a right to control the goods during transport are tied to the possession of a duplicate.

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58 Grönfors 1991, p. 69, referring also to Reinskou, Bill of Lading and ADP, Description of Computerized System of Carriage of Goods by Sea, Journal of Media Law and Practice 1981, as well as to Henriksen, The Legal Aspects of Paperless International Trade and Transport, 1982.

59 Schnauder, p. 1642.

60 English lawyers usually refer only to ´document of title´ since one cannot, under English law, transfer a better title as one can do with negotiable instruments proper, such as bills of exchange, see Chapter VI, *post*.

61 Cf. Grönfors 1991, p. 78.

62 Latin jurisdictions such as France seem to classify bills of lading as credit instruments, see Chapter VI, *post*.

63 Such a right exists as to the representative document itself and as to the goods represented by them, see Chapter V, *post*. A transfer of a negotiable instrument could be considered either as an assignment of debt evidenced by it or as a right *in rem* to the document itself, See Kaisto 2001, pp. 496 ff. The solution to this problem could have implications relating to private international law, since the law of the place where the document is (*lex carta sitae*) may come into play.

Securities such as shares, bonds and warrants are traditionally documents which are tradable and represent ownership in a company or a claim of money. These may traditionally be transferred in ways similar to negotiable instruments. The similarities between securities and commercial negotiable instruments used in the sale and transportation of goods may be established to analyse how immaterialised securities systems work and how experiences with these could be transferred to the use of commercial documents.

I use mainly my own (Finnish) legal system to illustrate how negotiable instruments and securities operate. Generally, the same ideas seem to be valid in other jurisdictions referred to in this study. Negotiable instruments are documents which are issued to bearer, to a named person or order or to order.[64] Bills of lading are also negotiable in the same ways.[65] The law safeguards the exchange functions of these documents by protecting a party who has acquired the document in good faith[66] against debtor´s arguments relating to the credit relationship. Good faith does not protect the recipient if the document is forged or if there is a fundamental flaw in consent such as coercion or the incapacity of the issuer. Neither is a holder in good faith entitled to a claim on a document which is invalidated.[67] Once the transferor has transferred the possession of the document together with an indorsement, where necessary, the transfer is also valid against the creditors of the transferor.[68] The debtor is not liable to pay, unless the negotiable instrument is presented and surrendered to him.

Securities are generally understood to be instruments which tie the exercise of certain rights to the possesion of a document. The Finnish Companies Act, chapter 3 § 9, makes the transfer of shares subject to the provisions of the law of negotiable instruments. This equation between shares and negotiable instruments defines the former as merchantable. The merchantability and the public nature of the markets are the essential features of securities under 1 § 1 of the Finnish Securities Markets Act.[69] Bonds are securities within the meaning of the act, and so are certain other documents. Finnish law like other Nordic laws has created dematerialised securities markets, see *infra*.

Finnish law defines the nature of the document as a negotiable instrument or as a security dependent on functional characteristics, which means generally that the title of the document does not count. It is also possible that any document representing the goods could be made negotiable or transferable, although the law does not directly deal with these documents.[70] Once the

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64 VKL (Promissory Notes Act) § 11.

65 The general law on negotiable instruments contained in VKL is, however, applicable only to monetary obligations (Aurejärvi, p. 13). The provisions of the Maritime Code apply to bills of lading.

66 VKL § 14 states that unless the recipient of the document knew or ought to have known that the transferor was not able to dispose of it this cannot affect the right of the recipient in respect of it.

67 VKL § 17.

68 VKL § 22.

69 Karjalainen-Parkkonen, p. 15.

70 See however L asiakirjain kuolettamisesta (act on amortisation of documents) 14.8.1901, where a number of documents such as bills of lading and warrants are listed.

document is transferred, the creditors of the transferor cannot validly claim the goods represented by the document. National law can also be more restrictive as to what documents can represent rights in respect to goods. Under English common law, especially, a well-established practice is required to make a particular paper qualify for a document of title.[71]

Legal literature sometimes uses the concept of abstraction.[72] Abstract rights are separable from their original *causa*, which in a very pure sense of abstract rights does not necessarily exist, and can often be transferred independent of the situation in the original legal relationship. Negotiable instruments relating to the payment of money are rather abstract in that no underlying transactions may be invoked, and the good faith required from the party surrendering it relates to the rightfulness of the possesion of the document. Bills of lading represent an abstract undertaking by the carrier to deliver the goods in their recorded shape to a consignee surrendering an original bill of lading in good faith. Good faith may protect a party in commercial transactions without it being tied to the possession of negotiable instruments. Under Finnish law, good faith protects a purchaser of goods which do not belong to the seller in respect of which the seller is the borrower or deposit-holder.[73] Furthermore, according to the brand new edition of the UNIDROIT Principles of International Commercial Contracts, an assignee of a right acting in good faith is protected.[74]

Good faith has a more general meaning in the laws of many jurisdictions and international trade (see II.7., *infra*). In legal transactions, whether or not it is accompanied by negotiable instruments, good faith has a specific meaning and standards and measures are established under national law.[75] Under international maritime conventions[76], the good faith of the consignee surrendering a bill of lading creates ´estoppel´ for the carrier to refer to circumstances in the underlying contract of transport and the carrier´s obligation becomes abstract vis-à-vis such consignee. International conventions do not, however, define what is the good faith standard that they require.[77]

Abstract undertakings are frequently seen as a contradiction to accessory undertakings, and they are often described as ´independent´. For instance,

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71 See Chapter VI, *post*.

72 There is no uniformity as to how this concept is used in the Finnish doctrine, see Kaisto 2001, p. 490.

73 Kauppakaari (Handelsbalken) from 1734 § 11(4) and 12(4).

74 See Chapter V.9., *post*.

75 For the substantive aspects of good faith under Finnish kauppakaari §§ 11(4) and 12(4) as well as VKL 14 § and in other Scandinavian countries, see Kaisto 1997, pp. 268 ff. See also Aage Thor Falkanger, God tro, En studie om kravet till god tro som vilkår for å erverve eller opprettholde privatrettslige rettigheter, Oslo 1999. The measure can be objective such as that of *bonus pater familias* or it can be more related to circumstances.

76 See Chapter VI, *post*.

77 UNCITRAL draft instrument on the carriage of goods by sea (draft as contained in doc A/CN.9/WG.III/WP.32, 26 August 2003) Article 38 attempts to define the carrier´s good faith when taking information to transport documents when goods are delivered to the carrier. However, good faith remains undefined in the tripartite relationship shipper-carrier-indorsee.

guarantee obligations can be absolute and need not be based on a default in the underlying transaction. This is the case with demand guarantees. The guarantor undertakes to guarantee the default in the transaction simply ´on first demand´. Although some documents will have to be furnished, the independence is not mitigated by the need to furnish documents. The only exception to the guarantor´s undertaking to pay is generally fraud. If the beneficiary´s fraud under the relationship can be established, the guarantor is not liable to pay.

Generally speaking, one of the major challenges of e-commerce legislation is to define how to deal with abstraction in an electronic environment. It requires a policy decision that delineates to what extent abstract undertakings should be allowed to exist. Will the enhanced dissemination of information in IT society change the picture so as to require more carefulness for good faith to effectively exist? Technically, it is possible to obtain and record information on the condition and ownership of the goods in real time. This decision is to be made by legislators and courts.

II.4.3 Dematerialisation of rights

The move towards electronic commerce represents a large-scale dematerialisation of rights from paper-based systems in favour of intangible electronic records. However, dematerilisation is not a new phenomenon and is related to the idea of abstraction.

Probably one of the earliest examples of dematerialisation was the dematerialisation of monetary gold by the issue of bank-notes and the establishment of bank accounts. Rights to land are often recorded in registries and these registries have more or less replaced documents of title in their domain.[78]

Paradoxically, in the development of dematerialisation, the use of paper to record rights once constituted a major breakthrough. In international trade, the emergence of documents of title and negotiable instruments by way of mercantile custom was an extremely useful development in facilitating transfer of property and the use of security rights and deferred payment.

Now, at the present stage of dematerialisation there is an attempt to get rid of paper by replacing its functions with records in electronic registries. Recent examples of dematerialisation are securities dematerialisation systems that have been established to reduce the paperwork, expense and risks associated with physical documents and bearer bonds. Despite variations between jurisdictions, the main participants in a dematerialised securities system are the depository (or custodian), the issuer, trading intermediaries and the investor. Investors trade in dematerialised securities through their trading intermediaries in a recognised securities market such as a stock exchange. The depository maintains an electronic system of accounts in a central registry. This central registry contains a

[78] Bolero Feasibility Study 1999, p. 24.

record of the holdings of securities by depositary participants on behalf of investors, as well as the rights and restrictions arising therefrom.[79] The depositary functions are separate from the functions of clearing and settlement systems[80] although they may be carried out by the same organisation.

Some of these securities systems are also immobilisation systems, meaning that they retain the physical security in a vault and give the holder dematerialised rights to the security by virtue of the holder being the account-holder.[81] In the Nordic countries, the use of paper equity has been abolished as regards listed equity and bonds with the introduction of electronic recording systems.[82] The effects of the possession of a physical document have been replaced by a book entry in a stock registry. Entries in centrally organised, or at least centrally coordinated, computer systems enjoy public credibility and are conclusive. The aim of the systems is not to imitate securities in terms of presentation, but to replace their functions[83] electronically. It is possible to register pledges of a stock account. The legal relations between the various parties concerned follow from national law.

The international sale of goods and transports may be in line to follow the example given by securities systems. In this study, some commercial undertakings to replace traditional trade documents such as bills of lading by electronic title registries or other solutions are examined in detail. The transition to electronic documentation in international trade as a final stage of dematerialisation is not easy. The replacement of bonds and securities takes place under an individual national legal system, where the various rights relating to the equivalents of securities and their relationship with one another can be determined with a reasonable certainty.

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79 Note by the UNCITRAL Secretariat: Transfer of rights in tangible goods and other rights, Doc A/CN.9/WG.IV/WP.90, para. 48.

80 ´Clearing´ means the processing of a trade as well as establishing what the investors owe each other as a result of the transaction. ´Settlement´ means the transfer of value between the investors so as to complete the transaction.

Examples of clearing settlement systems are Cedel in Luxemburg, Euroclear in Brussels, CREST and the Central Gilts Office in London, SICOVAM in France, Monte Titoli in Italy, and the Depository Trust Corporation in the United States.

There are similar systems in the Nordic countries, Canada, Germany, the Netherlands, South Korea and Singapore. The transmission of instructions and information during the clearing and settlement process is conducted through various secure communication networks such as SWIFT or Cedcom. These instructions may be checked against validation rules such as the International Securities Identification Number (ISIN) to ensure their accuracy. The organisation that allocates ISIN numbers in a particular country is the National Numbering Agency (NNA), which is normally a stock exchange. The flow of securities across borders is simplified through the development of global custody networks, international central securities depositories (ICSDs) and links between national central securities depositories (CSDs). The system makes it possible for settlement systems, CSDs and custodians to offer comparable settlement services to a wide range of national markets (Doc A/CN.9/WG.IV/WP.90, paras. 54 and 59).

See also Chapter VIII.11.2., *post*.

81 Bolero Feasibility Study 1999, p. 24.

82 In Finland, the system is based on two statutes, Laki arvo-osuusjärjestelmästä (17.5.1991/826) and Laki arvo-osuustileistä (17.5.1991/827).

83 The ´functional equivalence´ approach. The functions of securities could be informational, evidentiary and symbolic (Henrikssen, p. 52).

When international trade instruments are replaced, however, one has to take into account a multitude of legal functions for trade documentation and the treatment of the instruments under a multitude of legislations and legal regimes. For instance, sea transport documents are subject to three convention-based legal regimes, and a fourth regime, the UNCITRAL draft Instrument for Carriage of Goods [wholly or partly] [by Sea][84] which is hoped to address electronic transport documents, is in the pipeline. Moreover, in an international sale of goods transaction involving carriage of the goods and possibly documentary credit operations represents a multitude of legal relationships, each governed by its own *lex causae*, and in which the relationships are sometimes in conflict with one another.[85] The multitude of relationships leads to an augmented number of third parties involved in a transaction. It is practically impossible to agree contractually on rights *in rem* which effect a large number of parties.

When physical shares and bonds were eliminated in Finland in the 199´s, the transition period was set to take place within a few years. Nonetheless, the part of equity not susceptible to the reform still remains in physical form. The part susceptible is however subject to a unitary system where physical shares no longer exist.

In international trade, dematerialisation has to take place gradually. Therefore physical and electronic documentation must coexist for a long time. Obviously the same right cannot be represented in two different forms.[86]

II.5 Evidence in electronic form

The use of computerised material as evidence is widely discussed in most legal materials on EDI and electronic commerce. One must distinguish between two distinct aspects here, the admissibility of computer records as evidence in general on the one hand, and their probative value on the other.[87]

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84 The draft Instrument will be examined more elaborately in Chapter VI.3.2., *post*. The scope of the convention is still open due to which the words´wholly or partly´and ´by Sea´ are in parentheses.

85 I will later suggest more ´interaction´ between the legal instruments governing these relationships by mentioning a couple of examples of conflicts between the contract of sale and the contract of transport. A potential conflict may be even be taken into account when independent guarantee instruments or documents of title are used.

86 This obvious principle is called the ´guarantee of singularity´. Se Chapter VI.3.1., *post*.

87 The law of evidence in the United States uses the concept of ´authentication´ widely. "The requirement for authentication... is satisfied by evidence sufficient to support a finding that the matter in question is what its proponent claims" (Perritt Jr. in Baum-Perritt Jr. pp. 344-346 quoting Federal Rules of Evidence 901(a) and 901(b)). The law of evidence in common law countries has traditionally required extrinsic evidence to establish the authenticity of a text. Usually the controversy is over authorship. In the context of electronic commerce, the term ´authentication´ is most often used in the more limited sense of proof of authorship. See however the various definitions for the word, *infra* and Chapter IV, *post*.

As far as the admissibility of computer records is concerned, no important obstacles should be encountered, as the rule is generally gives the freedom to provide evidence by any means, in particular in commercial disputes.[88] More important, legislation equates computer records with paper documents more and more. In Chapter IV, *post*, the UNCITRAL Model Law on Electronic Commerce, the EC Directive 31/2000 on electronic commerce and the relevant US laws will be presented. Such general electronic commerce legislative materials usually make electronic records funtionally equivalent to paper documents. The assessment of the probative value is a more complicated matter. In common law countries, at least two basic principles of evidence deserve mentioning, namely the *hearsay rule*, the *best evidence rule* and to some extent, the *opinion rule*.[89]

The law of evidence is more formal in the common law jurisdictions than it is where civil law system prevails. In civil law countries are no formal rules of evidence similar to the hearsay rule or best evidence rule. In many civil law jurisdictions such as in the Nordic countries, Germany and Japan, all relevant

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88 Presentation by Anne Troye, Commission of the European Communities, entitled ´Tedis Programme, second phase, legal issues´, at the seminar ´EDI/OVT-juridiikan kehitys´, organized by the Finnish Data Communication Association in Helsinki on 27 November 1991.

89 The *hearsay rule* derives from the adversarial nature of legal proceedings in the common law tradition whereby a party proves his case by calling witnesses with personal knowledge of events. The witnesses´ accounts can be challenged by cross examination. A witness without first hand knowledge of the events, or a document, cannot be challenged in cross-examination. This kind of evidence is categorised as hearsay and is normally excluded.

English common law knows many exceptions to the hearsay rule, which are pertinent to litigation in e-commerce matters. Some of these are general, some sector specific.The Bankers´ Books Evidence Act 1879 permits the proof of certain ´banker´s books´ by means of copies, if these are from the ´ordinary books´ and the relevant entry into them has been made "in the usual and ordinary course of business". In the United States there is a similar ´business records exception´.

The *best evidence rule* is a requirement that where a party wishes to put forward as evidence the contents of a document he should produce it to the court in the form of an original document rather than a copy. This rule is seen as the ´original document rule´, and is also in American practice. Electronic messages may not have a paper original at all. Therefore a rigid understanding of what is to be seen as ´an original document´ is very unproductive. Therefore e-commerce legislation in common law countries needs to address originality in particular.

In civil law countries, the ´best evidence´ rule is not recognised, nor is it recognised in all common law jurisdictions (Cova Arria, p. 714).

The opinion rule draws a distinction between facts and inferences. Truth can be obtained from persons with direct knowledge of the relevant facts. It is only for the court to make inferences from these facts, unless the the subject-matter is one requiring special knowledge or skill, or unless a fact and its inference are too interwoven to facilitate their separation.

For the application of these rules, see Bradgate, Rob, Evidential Issues of EDI, in ´EDI and the Law´, ed. By I. Walden, London, 1989, pp. 9-42; Toh See Kiat pp. 239-250; and Baum-Perrit Jr pp. 344-359. See also Trading with EDI, The Legal Issues, edited by Hans B. Thomssen and Bernard S. Wheble, London 1989.

The *parol evidence rule* sets forth that oral evidence is generally not admissible to interpret an agreement in a written record and should also be mentioned here. The purpose of the parol evidence rule is to "give legal effect to whatever intention the parties may have had to make their [written contract] a final and perhaps also a complete expression of their agreement."

information is admissible, with the court being left to decide what weight to attach to any particular piece of evidence.[90] In some countries, the law itself defines the level of the probative value of the means of evidence. This is the case with Luxemburg civil and commercial codes. The Luxemburg law itself provides that if the provisions of the law have been fulfilled *inter alia* in respect of the storage of data, the probative value of computer records is the same as for written documents.[91]

This study emphasizes the role of arbitration as a dispute settlement method. In arbitration, the law of evidence appears in an adapted form, since arbitrators have generally more freedom to detach themselves from the stringent requirements of national law, including rules of evidence.[92]

As already noted above, the evidentiary value of computer records is gradually evolving thanks to legislation based on the UNCITRAL Model Law on Electronic Commerce or Directive 2000/31/EC on electronic commerce. A recent note[93] by the UNCITRAL Secretariat shows that despite the fact that there are not many court decisions on the legal value of electronic records, the "few recorded cases show an evolution towards legal recognition of electronic records and data messages, but also some uncertainty as to their admissibility both as a means for the formation of contracts and as evidence of the content of contracts".[94]

II.6 Liability issues in electronic communication

The risks relating to the communication process are generally speaking error, absence of authority and system failure.[95] These may be due to technical or non-technical causes. Communication takes place through sending messages and by transferring documents and notices between the parties. The relevant parties who may, in theory, bear the consequences of the above mentioned risks are the sender, the receiver and the processor, who is the communications facility provider.

One has to distinguish between risk and liability. Risk indicates who is to bear the consequences of an error or a system failure (the ´systemic risk´) in the first place. The risk in a commercial relationship is governed by the commercial

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90 For Finland, see the Committee Report regarding the revision of the Finnish Contracts Act (Kom 1990:20), pp. 61-63. The report emphasises the role of information security for the reliability of information in electronic form as evidence.

91 Troye, Helsinki 27.11.1991, Bradgate in Walden, p.28.

92 See Chapters II.8. and IX.5.4., *post*.

93 Doc. A/CN.9/WG.IV/WP.104, Add.3. paras. 3 to 7.

94 In the US for instance, the courts seem to have taken a liberal approach to the admissibility of electronic records, including e-mail. The US courts have dismissed arguments that e-mail messages were inadmissible evidence because they were unauthenticated and parol evidence (see *supra*).

95 Toh See Kiat, p. 285.

or contract law applicable. It determines, for instance, what impact an incorrect offer or acceptance may have on the rights and obligations of the parties in a contractual relationship. We may also approach risk and liability in the much narrower context of sheer electronic messaging. These two approaches are reflected in the interchange agreement practice. A systemic risk of a gigantic institutional nature actualises when an operator or other intermediary goes bankrupt. Where such an intermediary has assets in electronic form which are not separated from the assets of its clients, all the elements of a tremendous mess will be present.

Liability is concomitant with the responsibilities of the parties involved. We may start with the communications facility provider. He has to take care of the conveyance of the message in the correct format and protocol while safeguarding against the corruption of the message. Moreover, he must secure that the message is conveyed to the recipient while preserving the confidentiality of the message.[96] A failure to meet these responsibilities may lead to liability to the originator or the recipient of the message. This liability is usually excluded to the extent possible by the general conditions of the telecommunication service.[97]

Where liability cannot be vested on the intermediary, parties using the service have to divide the risk not attributable to the operator between themselves. This is regularly done contractually. Contract practice is varied on this question. For instance, the European Model EDI Agreement makes the party engaging an intermediary liable for his errors and omissions. In Finland, such liability might also result from general contractual principles.[98] It is submitted that this may well be the case with many other jurisdictions as well.

The relationship between the facility provider and one or both parties to an electronic transmission is generally governed by a contract. If the provider is making its facilities available to both the originator and the receiver as one service, then they may both be parties to the contract with the provider. The *Bolero System* defines its role and liability during the operation of the system in its service contracts[99], which are distinct from the Bolero Rulebook. All parties using the system (´Users´) abide by the service contracts and the rulebook.

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96 Mostehar in Walden, pp. 49-55.

97 Liability may be excluded in respect of consequential loss, or it may be limited up to a certain amount. The rules relating to the onus of proof may have an impact on the actualisation of liability. It is difficult for the customer to prove a fault by the operator. Reference can be made to the reverse liability regime for transport operators, which generally have the onus to prove that a loss or damage was not due to their act or omission (see Sisula-Tulokas in ´OVT ja Oikeus´, pp. 37-46).

It is more difficult to exclude liability with regard to breach of confidentiality. If the provider is a public telecommunications operator, there are both statutory and licence obligations in relation to interference with messages and confidentiality. (Mostehar in Walden, p.51)

98 Sisula-Tulokas in ´OVT ja Oikeus´, p. 41. See also Sisula-Tulokas, Datatransmissioner och riskfördelningen för befordringsfel, and in Festskrift till Kurt Grönfors, 1991, p. 403.

99 In the case of the Bolero Association, it is the BAL Service Contract, and in the case of Bolero International, the Operational Service Contract. The Bolero Rulebook refers to these instruments in Rule 2.1(3) in its relations between the defined users of the system. Moreover, liability arising from obligations owed by one user to another is excluded in Rule 2.1(2). For the liability regime of the Bolero System, see Chapter VIII.7.1.6., *post*.

The originator has many similar responsibilities to those of the provider, but in addition he has to make sure that the message is correctly addressed to the recipient and that it is properly authorised. The originator also has obligations in respect of the contents of the message, namely that it accords with the terms of the transaction and has gone through any necessary copyright clearances. Moreover, he has to keep a data log. The typical responsibilities of the recipient, on his part, are to check that the message is really intended for him, and to acknowledge and verify the message.

The responsibilities of the originator and the recipient stem generally from the contractual framework applicable to the relationship between them. This framework normally provides for a limitation of liability as well as an exclusion in *force majeure* situations.

This study does not lay an emphasis on systemic risk or liability issues outside the relationship between contractual parties in the relevant contracts, although their existence may be noted in some places.

II.7 Formation of contracts

The formation of contracts is a wide topic and I will have to limit myself to only studying the questions of particular interest to electronic commerce, such as the question of whether one can distinguish and shape rules of the formation of an electronic contract as such. There are, in fact, rules especially created for regulating the formation of contracts by electronic means. So far, these relate generally to EDI, which even was once, at an earlier stage of technical development, seen as a synonym for electronic contracting.[100] As already noted, there have been many definitions of EDI. An essential feature is, however, that structured business data is transferred between computers by means of

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100 Nurmi (*op.cit.* p.13) refers to an equation between electronic contracting and EDI in American literature, most notably to Perritt Jr. in Baum-Perritt Jr., p. 6-7. Perritt Jr. defines electronic contracting as follows: "(e)lectronic contracting involves the exchange of messages between buyers and sellers, structured according to a prearranged format so that the contents are machine processible and automatically give rise to contractual obligations". He also states that "EDI is a popular shorthand acronym for electronic contracting".

On the other hand, Perritt Jr. also considers that electronic contracting to be a subset of electronic messaging. Electronic contracting is distinguished from other forms of electronic messaging in that the content of the message and the conduct of the sender and receiver are legally operative facts.

The UNCITRAL Working Group (IV) on Electronic Commerce, which is in the process of preparing a draft Convention on Electronic Contracting, has not seen the necessity to define electronic contracting. However, a Note of the Secretariat (A/CN.9/WG.IV/WP.95, para. 10) states that it appears from the deliberations of the group that the notion has been used to refer to the formation of contracts by means of electronic communications, or ´data messages´, within the meaning of Article 2 subparagraph (a) of the UNCITRAL Model Law on Electronic Commerce. Thus, ´electronic contracting´ is regarded as "a method for forming agreements, and not a subset based upon any specialized subject-matter". See Chapters V and VI *post*.

telecommunications. Electronic mail and telefax are not EDI, because they are unstructured, based on few standards and not transmitted from application level to application level.[101]

EDI has been based on a predetermined contractual framework, which has amended the existing legal framework as regards electronic contracting. As will be noted later in Chapter IV, UNCITRAL is currently working on a draft convention on electronic contracting, which would govern contract formation through the use of electronic messages in particular. It would also apply in an open environment.[102] This subchapter gives only a general outline of the issues involved in contract formation, and the topic will be discussed more elaborately in Chapter IV, *post*, in conjunction with recent legislative efforts.

Three possibilities of contract formation can be distiguished as regards the involvement of technology.[103] The first one deals with a procedure in which both parties participate actively during the actual contracting, where both the offer and acceptance are readable to human eyes during the process. An example of this procedure is one made through fax or electronic mail. In the second type of procedure, one party is active while the other party gives the expression of will or ´contracting expressions´ through electronic equipment. The third type of procedure is where a contract is concluded between computers automatically without the intervention of either party. All these possibilities still require human intervention, an expression of will, at some stage, be it at the stage of prior programming. Many parts of electronic contracting can thus be approached on the basis of traditional contract law principles.

Modern contract law is generally built on the principle of consensualism, which means that form requirements as to the conclusion of contracts are non-existent or minimal. Both civil law and common law countries follow a consensualist approach.[104] Article 1.2 of the UNIDROIT Principles of International Commercial Contracts states that "(n)othing in these Principles requires a contract to be concluded in or evidenced by writing. It may be proved by any means, including witnesses". This provision takes into account that various legal systems may impose form requirements, some of which may be imposed on condition that they affect the validity of the transaction, some simply for reasons of evidencing the act. Generally, the form, place and time of contracting, all

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101 Toh See Kiat p. 7.

102 For the concepts of open and closed electronic commerce, see Chapters III and IV, *post*.

103 Note by the Secretariat, UNCITRAL Working Group IV (Electronic Commerce), thirty-ninth session, New York, 11-15 March 2002, doc A/CN.9/WG.IV/WP.95, paras. 70-79.
Nimmer (Electronic Contracts: Part I, Computers and Law; April/May 1996 p. 37) distinguishes between four scenarios of contracting:
- human to human,
- human to computer (or reverse),
- computer to computer (with prior agreement), and
- computer to computer (without prior agreement).

104 Brasseur in ´Le processus du formation du contrat´, p. 609.

affected by the use of an electronic medium, are relevant issues in contract law since they may bear various legal consequences.[105] Furthermore, Article 2.1 of the said principles states that "(a) contract may be concluded either by acceptance of an offer or by conduct of the parties that is sufficient to show agreement".

Article 11 of the the CISG provides that a contract of sale need not be concluded in or evidenced by writing and is not subject to any other requirement as to form. Furthermore, it may be proved by any means, including witnesses. Correspondingly, Article 29 provides that a contract may be modified or terminated by the mere agreement of the parties.[106] Form requirements may, however, be created by national law, for instance, regarding certain consumer contracts. Moreover, some contracting states of the CISG have reserved the right to impose written form requirements in accordance with Article 96 of the Convention.[107]

From the point of view of regulating electronic commerce, it is more opportune to regard such contract formation issues which are more mechanical than ´cognitive´ or public policy oriented. This means also that contract formation by electronic means covers only a thin layer of the relevant issues involved.[108]

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105 Milland in Walden, pp. 43-48. For instance, form may affect the validity of the contract, the place of contracting may affect the law applicable to the contract, jurisdiction, or the applicable trade usages, and the time of contracting may have substantive consequences e.g. with respect to limitation periods and, moreover, because statutes do not act retroactively and do not catch transactions that were entered into before their entry into force. See Owzia, pp. 601 et seq.

106 Paragraph 2 of Article 29 provides, however, that a contract in writing which contains a provision requiring any modification or termination by agreement to be in writing may not be otherwise modified or terminated by agreement. However, a party may be precluded by his conduct from asserting such a provision to the extent that the other party has relied on that conduct.

By contrast, Article 3.2 of the UNIDROIT Principles states that a contract is concluded, modified or terminated by the mere agreement of the parties. The difference lies in that the CISG provision takes into account the possibility that some domestic laws require consideration (for this, see Chapter V.9., *post*), whereas the principles treat this as a very distant possibility.

107 See Chapter X, *post*. Although requirements as to written form are virtually nonexistent in the Convention, its Article 13 contains nevertheless a provision stating that for the purposes of the Convention, ´writing´ includes telegram and telex.

108 The consensualistic approach requires that two or more expressions of will meet in a sufficient manner. The constitution of will and decision-making are ´cognitive´ aspects of contract law, as are notions like good faith. An important movement of ´Psychology and Law´ has existed since 1960 and is gaining ground in other continents (Stéphanie Michaux in ´le Processus de formation du contrat´, pp. 789 et seq.). One of the dimensions of a cognitive dimension of contract law is ´game theory´, see Michaux in *op.cit.*, pp. 834 et seq. On the legal functions of psychological elements such as intentions, mutual assent and consent in e.g. English and French law, see Owzia, part I ´Basic Notions relating to the Formation of Contract(s)´, pp. 187-392. In his treatment, part II, p. 393 et seq., deals with ´Mechanism of Formation of a Contract´. I would think that this second part constitutes the domain in which electronic commerce could have an impact.

A contract is based on an offer and an acceptance[109], which have to be, one can generalise, essentially similar in order to establish an agreement between contracting partners. The consensualist approach is based on the ´will theory´ that lends itself in most cases to an analysis of an agreement in terms of offer and acceptance as the respective expressions of the wills of the parties.[110] Under Finnish law as well as under the laws of the Scandinavian countries, an offer is binding for the party making it as soon as the offeree has become aware of its contents. Under German law, an offer becomes binding when it reaches the offeree. An offer ceases to be binding in both legal systems above, if it is rejected or the time-limit for answering set out therein has lapsed. Equally, an answer to an offer has to reach the offeror, in the case of parties at a distance and communicating through letters, telex, fax or other means (this evidently applies to electronic transmissions as well) in the time-limit set out or that would be normal under the circumstances. Both in Scandinavia and Germany, a delayed acceptance is considered to constitute a new offer, as an answer the conditions of which deviate from the offer.[111]

Under English law, the minimum prerequisites for a legally enforceable agreement are an intention to enter into legal relations, the making of an offer, acceptance of that offer communicated to the offeror and some kind of ´consideration´.[112] At common law, an offeror is not bound by his offer even if a deadline had been set for acceptance. The reason is that common law does not recognise that a person is bound by a promise without being met by a right, interest, profit or benefit accruing to him from the other party.

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109 At least the rules set forth in the CISG have been drafted mainly with a view to dealing with cases where a contract is formed through offer and acceptance. It may be possible to reach an agreement through a complexity of communications between parties, without discerning a clear offer or acceptance. A majority of commentators seem to consider that the Convention also deals with agreements reached without resorting to the traditional offer-acceptance scheme. Note by the Secretariat, UNCITRAL Working Group IV (Electronic Commerce), thirty-ninth session, New York, 11-15 March 2002, doc A/CN.9/WG.IV/WP.95 para. 65.

Article 2(1) (Manner of formation) of the UNIDROIT Principles of International Commercial Contracts provides that "A contract may be concluded either by the acceptance of an offer or by conduct of the parties that is sufficient to show agreement."

110 Owzia, p. 307. In the Nordic doctrine, suffice to say, a contract is a bilateral act in law in the sense that it is a combination or ´merger´ of two or more inter-related acts in law. An act in law is regarded in the Nordic countries as an expression of will made by a party or person with a view of constituting, changing, ceding or repudiating rights with a legal effect (Risto Nurmi, Elektroninen sopimus, Helsinki 1997, p. 13-22). An expression of will can be explicit or implied or may be inferred from the conduct of a person, e.g. silence can, under certain circumstances, be construed to imply consent.

Therefore, one must sometimes consider not exactly the expression of will but its mere existence, or simply a party´s consciousness of certain facts.

There are several methods of interpreting a contract. The subjective method tries to determine what the parties´ actual intention was, irrespective of the language used. The objective method looks for a normal interpretation in the light of the normal use of language. There are linguistic and legal principles for the interpretation of contracts. See the Committee Report regarding the revision of the Finnish Contracts Act (Kom 1990:20), pp. 15-32.

111 Lando, Udenrigshandelens kontrakter, udenrigshandelsret 1, 4. udgave, Kobenhavn 1991, pp. 23-24.

112 Milland in Walden, p. 43. See Chapter V.9., *post*.

The current Uniform Commercial Code of the United States, and in particular its relevant Article 2, does not generally address the question of when a sales contract is formed. The basic principles come from common law concepts of offer, acceptance and rejection.[113] In the US Uniform Commercial Code there is a provision on ´firm offers´ which cannot be withdrawn.[114] The purpose of this provision is to give support to the offeror´s serious intent to make his offer binding. There are, however, form requirements for firm offers, as they have to be in writing and have to be signed.

The French law approach lies between the Scandinavian and German approach and the Anglo-American ones. An offer made without setting a time-limit for its acceptance, can be repudiated until it is accepted. If, however, the offeror has declared that the offer is irrevocable, he is bound to his offer. The same applies if he has set a time-limit for its acceptance.

As regards contracts *inter absentes*, there are different theories as to when the contract is deemed to be concluded by virtue of an acceptance of an offer. These theories will be listed in the ´logistical´ order from the earliest possible moment to the last. The theories have an impact not only when the contract is deemed to be concluded but also as regards cancelations or alterations of expressions of will.

According to the *declaration theory* (or ´rule´, where followed by law), acceptance is effective in principle as of the date when the offeree has taken the decision to accept the offer but, since a purely internal psychological element is an uncontrollable fact, the will of the offeror has to be expressed. It is at the moment when the second (offeree´s) will is emitted that the accord of wills materialises. A mere fact of writing the letter of acceptance is sufficient for the conclusion of contract without the need of dispatching it. This theory obviously meets evidentiary difficulties.[115]

Following the *expedition or dispatch theory*, acceptance will not be operative until actually dispatched. The contract will be concluded at the moment when the letter of acceptance has been posted (*postal rule*). This theory is a variation of the declaration theory, basically to resolve the problem of proof. Both the declaration and dispatch theories are in fact concerned with the action of the acceptor without a role being assigned to the offeror in respect of the efficacity of acceptance.[116]

When what is called *reception theory* is followed, acceptance produces effect at the moment when it reaches the offeror, e.g. when the letter of acceptance has been delivered to the place of the offeror. Actual physical reception is not, however, required. The German language uses the term *´Zugangstheorie´* which signifies that the deciding moment is dependent upon the communication being available to the recipient in the sense that it has been placed at his disposal in a

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113 Nimmer, part II, p. 38.

114 UCC Section 2-205, Lando, pp. 31-32.

115 Owzia, pp.551-552.

116 Ibid., pp, 552-553.

place in which he would expect to receive communications in the normal course of business and in a manner that is comprehensible to him.[117] Before then there is no contract and after then the knowledge of the offeror is immaterial. This theory is useful in terms of proof, but still the knowledge of the offeror of the contents of the communication is not needed.[118]

Finally, according to *information theory*, the acceptance of an offer constitutes a contract only when the offeror has actual knowledge of the acceptance. The basis of this theory is the perfect concordance of wills. This theory is to the advantage of the offeror in the same way as the declaration theory was beneficial to the acceptor. Generally, a parallel is drawn between this theory and that of reception. Under both theories the efficacity of the communication of acceptance is determined in relation to to the position of the offeror.[119]

There are many combinations of these theories. It is possible to combine reception and information theories. This is known as the *theory of presumed knowledge*. According to this view, acceptance of the offer is in principle operative when it comes to the notice of the offeror, but reception thereof raises a presumption of knowledge as to its content. This presumption may be rebutted by the offeror, but the burden of proof lies on him.[120]

Continental legal systems have generally speaking adopted the *reception rule*, according to which the binding effects take place when the communication has been received by the addressee.[121] Anglo-American law applies the *postal rule*, according to which the binding effect takes place when a communication is mailed or sent. The reception rule is more practical in the context of electronic communications, and Anglo-American legal culture has somewhat accepted the reception rule in the context of EDI.[122] The above rules have, however, been established with traditional mail in mind. They reflect technology that causes a time lapse between the time the communication is sent and when it is received. An offer can be accepted instantaneously. Electronic commerce, particularly the

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117 Eiselen, p. 3.

118 Owzia, p. 553. If the answer is simply yes, there is no problem. If, however, a positive answer is coupled with additional terms, the offeror may, under many legal systems be bound by them without knowing them. See e.g. Chapter IV.8.3. on the battle of forms, *post*.

119 Ibid., pp. 553-554.

120 Ibid., p. 554. It is possible to combine the dispatch and reception theories in way that an acceptance is binding when dispatched provided it reaches the offeror. It is even possible to combine dispatch and information theories by holding the offeror bound from the moment the acceptance is dispatched, whereas the offeree is bound only when the offeror has obtained knowledge of the acceptance.

121 However, there are differences as to what the notion of ´received´ means. It may mean the time, the form or even the content of the communication of acceptance. The German doctrine and case law have interpreted Article 130(1) of the BGB to the effect that a communication has not only to reach the addressee´s sphere of control but it also has to be in a form so as to ensure the possibility for the addressee to become aware of it. The latter element has been further subdivided into requirements such as the language of the communication or delivery within normal working hours. (UNCITRAL Doc. A/CN.9/WG.IV/WP.104/Add.2, para 6.

122 This has taken place in the case of the ABA Model Trading Partner Agreement.

use of the Internet, may often involve the instantaneous acceptance of offers. However, as stated later, it is not clear whether the rules relating to instantaneous communications are applicable.

The reception rule has been chosen to be applied in the CISG as regards contract formation. Part II of the Convention is thus based upon the principle that communications are effective upon receipt. Article 15 of the Convention provides that an offer becomes effective when it reaches the offeree. Moreover, an offer, even if it is irrevocable, may be withdrawn if the withdrawal reaches the offeree before or at the same time as the offer. The Convention further clarifies in Article 24 that "an offer, declaration of acceptance or any other indication or intention ´reaches´ the addressee when it is made orally to him or delivered by any other means to him personally, to his place of business or to his mailing address or, if he does not have a place of business or mailing address, to his habitual residence".[123]

This reception rule of the Convention relates, however, predominantly to contract formation although exceptions also in that area can be found.[124] The substantive part (Part III) of the Convention is based on the ´dispatch rule´, according to which a message is effective when dispatched.[125] This principle is generally set out in Article 27 which states that "unless otherwise expressly provided in this part of the Convention, if any notice, request or other communication is given or made by a party in accordance with this Part (*i.e*. III) and by means appropriate in the circumstances, a delay or error in the transmission of the communication or its failure to arrive does not deprive that party of the right to rely on the communication". There are however provisions such as Article 49(4) relating to the seller´s remedies requiring that a communication has to be received by a party in order to be effective.

The division between dispatch and reception should be made by considering who should bear the risk for errors in communication. Eiselen considers that when a party is initiating communication, he should bear the risk for the success of the communication. This even applies to responsive communication, unless there is reason to reallocate the risk. For instance, where a message is sent to invoke rights after breach of contract, the risk of the communication should be transferred to the party in breach rather than to the innocent party.[126] Therefore,

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123 Commentators of the United Nations Sales Convention have observed that the notion ´reach´ in Article 24 of the Convention was made dependent upon external, easily provable facts and was meant to relieve the originator of the risk of defective communications of a declaration of will within the recipient´s organisational sphere. This would mean that Article 24 of the CISG does not require an opportunity for the recipient to gain awareness of the declaration. Attempts to take into account national public holidays and customary working hours would have created uncertainty. UNCITRAL Doc. A/CN.9/WG.IV/WP.104/Add.2, para 9.

124 See arts 19(2) and 20(1).

125 Analysis of the CISG Convention by the UNCITRAL Secretariat, doc. A/CN.9/WG.IV/WP.91, para. 54, Eiselen, pp. 9-10.

126 Eiselen, p. 5. Eiselen concludes that "(w)ho should bear the risk of failed communications should therefore be decided after the relative position of each of the parties in regard to the communication has been considered".

dispatch theory has been adopted in such situations. The allocation of risk should be made in accordance with what is reasonable in the situation. CISG Article 71 concerns the suspension of performance in a case where it becomes apparent that the other party does not perform in certain circumstances. The party suspending performance does not, however, bear the risk and dispatch theory is applied despite the drastic nature of the measure.

Whether the law applicable relating to contract formation, or contractual communications in general, is based on the reception rule or the dispatch rule, the implementation of these rules is not insurmountable for electronic commerce, since the UNCITRAL Model Law on Electronic Commerce provides, in Articles 15(1) and 15(2), funtionally equivalent rules as regards when a message has been dispatched and when it has been received.[127]

Contract formation involves issues which are less mechanical and require psychological (´cognitive´), social or public policy aspects to be taken into account. The traditional, mostly psychological aspects of contract formation are effects of error, fraud and coercion. Further the requirement of good faith imposed by the parties has a psychological content. However, good faith is understood in different ways. It can therefore be divided into two senses. One of them is honesty in fact, and the other is reasonableness and equity.[128] "While a common law lawyer would not combine the doctrine of good faith with that of unconscionability, it is not unheard of for a civil lawyer to argue that a party who seeks performance of an unconscionable contract does not act in good faith."[129] Unconscionability is a matter to be taken into account for social reasons and amounts often to the public policy of a state, due to which the provisions on good faith are usually mandatory law.

Good faith obligations can affect, in addition to the formation of the contract, precontractual negotiations or the performance of the contract, depending on the legal regime. The most famous legislative disposition dealing with good faith performance is found in Section 242 of BGB, the German Civil Code.[130] The CISG does not impose an explicit obligation on the parties to act in good faith, which remains only to be taken into account in the interpretation of the Convention, pursuant to Article 7(1). Article 1.7 of the UNIDROIT Principles, however, imposes a clear obligation in this respect and affects all stages of the contractual relationship.

Unconscionability relates often to the use of standard conditions. Good faith provisions may be resorted to to adjust an unconscionable term or to disregard it. In the doctrine and legal regulation of standard form contracts, there are aspects

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127 Later in Chapter IV, the contract formation rules of the CISG will be studied in more detail in the light of the UNCITRAL Draft Convention on electronic contracting, the UNCITRAL Model Law on Electronic Commerce and the CISG Advisory Council´s First Opinion regarding electronic communications and the CISG.

128 The Dutch Civil Code (NWB) has differentiated between these two requirements. Statutes such as the English Unfair Contract Terms Act 1976 and the German ABGB 1976 also tackle unconscionable contracts expressly.

129 Farnsworth, p. 9.

130 It states: "The debtor is obliged to perform in such a manner, as faith and credit ("Treu und Glauben") with regard to what custom requires."

of a technical nature relating to how contract terms are brought to the attention of the contracting partner. There are also aspects as to the content of the provisions. The former type of aspects can be tackled by mechanical contract formation rules and principles, although the latter are more subjective and cannot be regulated in detail.

II.8 Applicable law and dispute resolution

These topics are presented in this study as principal subjects of discussion in the field of electronic commerce. They were not widely discussed during the earlier stages of the development of electronic commerce, but have come into focus together with the rapid development of the use of the Internet, by consumers especially. When electronic commerce is not based on a preset contract between regular business partners, the issues of applicable law and dispute resolution contain an element of uncertainty.

Conflict of laws in the context of the Internet is very problematic, because the use of the Internet is characterised by the fact that national borders do not apply, while conflict of laws rules aim to localise legal acts and events under a particular national legal system. Therefore, notions relying on the geographical location do not always provide a practical solution to disputes which arise from the use of the Internet. As stated by *Boele-Woelki* in an international conference on the subject at issue "the Internet and the Savignian method, which was used as the basic point of departure when the conflict of laws rules of the EC Convention on the Law Applicable to Contractual Obligations of 1980 were drafted, are not on an equal footing".[131]

Where the choice-of-law rule relies on places as connecting factors, problems will arise where neither the contracting parties nor the goods, services or other subject-matter of a contract, may have a significant relationship with a place and no other place has been moved to for the purposes of entering into or performing a contract.[132]

It could nevertheless be stated, by and large, that as long as the Internet is no more than a means of communication under the sale of tangible goods, nothing or little will change. If the performance of the relevant obligation takes place offline, the existing rules of private international law referring to the place of performance of the contract remain relevant.[133] Where the performance takes place online, the place of performance cannot be used as a connecting factor, but one has to resort e.g. to the location of each of the parties involved. As business relations will become more and more complex, party autonomy remains the safest method of gaining predictability in the contractual relationship.[134]

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131 Katharine Boele-Woelki, Applicable Law in Electronic Commerce, a presentation at the 19th Annual Meeting of the Institute for World Business Law - "Forging Trust in Electronic Commerce: Law and Dispute Resolution", Paris 1998.

132 Kronke in Internet..., p. 74.

133 Huet, p. 7.

134 Kronke in Internet..., p. 75, Naimark, p. 22.

Private international law rules in most countries[135] give parties the freedom to choose the law applicable to their contractual relationship (party autonomy). The principle of party autonomy is embedded in the 1980 Rome Convention on the Law Applicable to Contractual Obligations and the 1955 Hague Convention on the Law Applicable to International Sales of Goods (and its revision in 1986). In an established commercial relationship, the parties may use an interchange agreement defining the obligations of the parties in respect of the data interchange. The standard interchange agreement models contain a choice-of-law clause. If an interchange agreement does not cover the substantive aspects of the transaction[136] there are two contracts between the parties, one covering the rights and obligations relating to communication and one relating to the substantive aspects of the commercial relationship. The choice-of-law clause should select a law which is sufficiently elaborate and liberal in questions of electronic commerce.

The freedom of the parties to choose the applicable law may be limited by consumer or other mandatory legislation (*jus cogens*). The term ´mandatory´ has at least two meanings. Lawyers in Continental Europe may use it to denote rules which cannot be excluded or modified by contract but which may nevertheless be replaced by a choice of foreign law if the rules are not of such overriding character so as to form part of the *ordre public* of the forum. In this broad sense the term is used in Article 3(3) of the EC Convention on the Law Applicable to Contractual Obligations. [137] In traditional English legal language, however, the term ´mandatory´ was used to denote rules of such a compelling character that they will be considered to apply even to a contract which is otherwise governed by foreign law, and a choice-of-law clause cannot be used to evade them.[138] Article 7 of the same Convention uses the term mandatory in this sense. Article 7 applies in the international context, and involves provisions to which the state attaches such importance that it requires them to be applied whenever there is a connection between the legal situation and its territory, whatever law is otherwise applicable to the contract.[139]

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135 General restrictions in this respect have prevailed in the legislation of Latin American countries.

136 American Trading Partner Agreements do this.

137 Article 3(1) of the EC Convention 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 or a part only of the contract".

Moreover, article 3(3) provides that "the fact that the parties have chosen a foreign law, whether or not accompanied by the choice of a foreign tribunal, shall not, where all the other elements relevant to the situation at the time of the choice are connected with one country only, prejudice the application of rules of the law of that country which cannot be derogated from by contract, ... (the) ´mandatory rules´".

138 Goode, Commercial Law, p. 920.

139 These laws are often called ´overriding´ or *´lois d´application nécessaire´*. Typical examples of such laws are foreign exchange regulations, import-export licences or competition laws. See the Green Paper on the conversion of the Rome Convention of 1980 on the law applicable to contractual obligations into a Community instrument and its modernisation, Brussels 14.1.2003, COM (2002) 654 final, pp. 32-34. See also the Inter-American Convention on the Law Applicable to International Contracts, Art. 11.

Special attention should be paid to choice-of-law clauses in standard form contracts which parties incorporate by reference since a court may treat the incorporation as invalid. The parties´ express choice should be a result of a safeguarded and properly documented process.

If there is no choice of law done by the parties, it is even much more difficult to determine the law applicable to the contract by choosing the determining connecting factors. The same problems exist in determining the scope of the CISG to see when a contract of sale is to be regarded as international within the meaning of the Convention.[140]

Conflict of laws in the context of electronic commerce is often approached in legal literature from a consumer law point of view. This is because a mandatory law element usually exists in consumer law. In the international sale of goods from business to business, however, there are fewer mandatory requirements. On the other hand, a multitude of conflict of laws issues exists.

In this study, conflict of laws situations may relate to the contract of sale, to the contract of transport, to the contractual relationships involved in documentary credit or contract guarantee operations as well as to the dispute settlement. It would not be very easy to try to give a comprehensive general account of all conflict of laws in relation to the international sale of goods in the context of electronic commerce. However, as the various contracts may eventually be linked to one another by being concluded through or evidenced by storing information in a general electronic trading platform such as that provided by the *Bolero System*, it is worth noting that a variety of national laws will coexist in the system. This is not only because various contracts or contractual relationships are governed by different laws, but also because different aspects of an individual contractual relationship may be governed by different laws.

This severability, the contractual splitting up on an issue-by-issue basis is generally referred to by the French term *dépeçage*. In international trade, dépeçage is in some cases unavoidable. For instance, a multimodal transport contract incorporates a number of transport mode specific laws, which apply mandatorily to the period the goods remain under an individual mode of transport. However, the traditional private international law of many countries does not necessarily admit depeçage, although the 1980 EC Convention on the Law Applicable to Contractual Obligations now expressly admits it. National courts of the convention states are bound to follow this rule. The more complicated the legal structures of international trade become, the more laws are in principle involved. This problem can be tackled by choice-of-law clauses, but is one of the reasons why uniformity of regulation should be sought by legal harmonisation or by contractual means. The parties can largely opt for their own legal rules among the increasing number of *lex mercatoria* instruments.

Due to the absence of uniform laws for electronic transactions in the field of trade and transport establishing electronic bill of lading systems, the desired results will have to be achieved through contractual arrangements such as the

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140 For this question, see Chapter X, *post*.

Bolero Rulebook. Such arrangements may be based on a single national law. However, as they touch upon fields that are subject to mandatory national legislation, at least parts of the transactions may have to be governed by the law applicable to the system as well as by relevant national laws.

It is, however, worthwhile to note the efforts that have been made in the European Union to tackle this issue. It has been recognised that the EC Convention on the Law Applicable to Contractual Obligations signed in Rome in 1980 is in need of revision. The European Commission has recently published a Green Paper inviting interested parties to express their opinion on this Convention very often referred to as ´Rome I´.[141]

It is presumed that the majority of private law issues relating to electronic commerce are contractual rather than non-contractual. It could be presumed that some issues relating to liability in tort might arise, for example, in connection with third party service providers and in transport law in cases where no contractual relationship exists. It is worthwhile to mention attempts to reach Rome II, which is not Constantinople, nor even on the threshold of the EU´s future enlargement, but a potential legislative instrument relating to law applicable to non-contractual liability.[142]

The law of tort is traditionally one of the applications of the *lex loci delicti commissi* or the law of the country with the most significant relationship to the event.[143] Liability in tort is also a matter of jurisdiction, because a harmful effect may arise in country A while the negligence took place and the damage was thereby caused in country B.[144] This study will largely have to omit questions relating to non-contractual liability.

Disputes arising from electronic commerce can be settled, in principle, by similar means as other disputes, although the use of evidence in electronic form may require its recognition by the relevant jurisdiction and is technically more demanding. Disputes between commercial partners may be settled, in addition to more amicable means, including conciliation and Alternative Dispute Resolution (ADR), by litigation or by arbitration. In consumer contracts, however, arbitration is usually more or less out of the question, except in the United States. In parallel with the principle of party autonomy in private contract law, parties may agree on an exclusive jurisdiction[145] or arbitration clause. As regards consumer

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141 Green Paper on the conversion of the Rome Convention of 1980 on the law applicable to contractual obligations into a Community instrument and its modernisation, COM (2002) 654 final, 14.1.2003.

142 See the Proposal for a Regulation of the European Parliament and the Council on the Law Applicable to Non-contractual Obligations ("Rome II"), Brussels 22.7.2003, COM (2003) 427 final. When the Amsterdam Treaty came into force in 1999, cooperation in civil matters was transferred under the Community method meaning, in a nutshell, the Commission´s initiative monopoly, (in this case) codecision procedure, and a binding nature of the successful outcome.

143 Kronke in Internet..., pp. 67-68.

144 Council Regulation (EC) No 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgements in civil and commercial matters, OJ L 12, 16.1.2001, p. 1.

145 See Chapter VI of the Convention on Jurisdiction and the Enforcement of Judgements in Civil and Commercial Matters signed in Brussels 1968 (revised 1999).

contracts concluded through electronic means, there is a tendency in the EU to see that ´consumer confidence´ on electronic commerce should be particularly boosted by efficient out-of-court settlement procedures.[146]

Questions relating to the dispute settlement in electronic commerce and the use of electronic dispute settlement mechanisms will be examined in greater detail in Chapter IX, *post*. That chapter is written particularly with a view to resolving disputes relating to letters of credit and predominantly "documentary" in nature, but most of what is said applies to all commercial disputes. As will be seen, the treatment will be greatly biased towards commercial arbitration. The main reason is the need to focus this study on international and formalistic issues and the capability of arbitration to shape non-state rules of law.

Litigation is based generally on national procedural rules. Out-of-court dispute settlement systems other than arbitration are less formalistic, at least in the mandatory sense of viewing them. Although arbitration is formalistic, the rules applicable to it often allow dispensing with an oral hearing, which makes it possible to "delocalise" the dispute settlement. Arbitrators can, in certain situations, apply other legal rules than state law to determine a contractual dispute. Therefore it is interesting also as a means of shaping new legal rules for electronic commerce.

II.9 Form requirements and conflict of laws

As a generalisation, legal acts are expected to comply with the form requirements imposed by law (or legal rules) governing them.[147] Form requirements may be nonexistent, i.e. the law is permissive, or they may be stringent. In international trade transaction, several jurisdictions are regularly involved, and conflicting form requirements may therefore be imposed. This matter will be dealt with later in connection with bills of lading and documents of title.[148] However, some general observations about the scope and various approaches to the problem are needed here.

Firstly, national law may give different form requirements different impacts.[149] The most stringent ones make the observance of the form requirement a prerequisite for the entire validity of the transaction. The potential voidness may be absolute or merely procedural, e.g. the contract is inadmissible in evidence. The less stringent form requirements with legal effect may e.g. deprive the parties of some ancillary rights such as enforcing a security right.

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146 Article 17 of the Directive 2000/31/EC on electronic commerce (OJ No L 178, 17.7.2000, p. 1) requires the Member States to ensure that their legislation does not prevent the out-of-court settlement of disputes by available electronic means.

147 This law is sometimes called the ´adjective law´, which is defined as "so much of the law as relates to practice or procedure" (Bentham; Osborn´s Concise Law Dictionary, Seventh Edition by Roger Bird, London 1983). On the role of form in legal acts, see Sauli Mäkelä, Formaalisuus oikeudellisessa prosessissa (Formality in legal process), Helsinki 2002.

148 See Chapters VII and VIII, *post*.

149 For form requirements and their impact under Finnish law, see Nurmi, pp. 108-117.

Some form requirements are simply guidelines, the observance of which has no legal consequences.[150] It is the form requirements under different national laws that have a bearing on the rights and obligations of the parties that are of interest here.

The issue of the observance of form requirements has a jurisdictional dimension. First, national jurisdictions tend to have different policies as regards foreign form requirements when they run into a by case involving the problem. These policies were analysed by the *Bolero Feasibility Study 1999*.[151] Should a liberal attitude be taken to the problem in the courts of any state, the fact that a foreign jurisdiction having a link to the contract or transaction might be able to interfere at least at the stage in which the contract or court judgement ignores the formality has to be enforced.

Some jurisdictions[152] are likely to validate the contract if the formalities comply with either the law governing the contract (*lex contractus*) or the law of place of contracting (*lex loci contractus*). The validation takes place by the courts treating the question in accordance with its conflict of laws rules and its own substantive law. If the non-compliance with the foreign formality rendered the contract void, the parties could rely, in legal proceedings instituted in such states, on the law chosen by them. Alternatively, they could rely on the fact that the contract was concluded in a state which treats the form used by the parties as valid (*locus regit actum*). Furthermore, the courts in these jurisdictions might generally ignore a foreign formality if that formality merely renders the contract inadmissible in evidence.[153]

Another group[154] categorised by the *Bolero Feasibility Study 1999* resembles the first, but courts there do not generally ignore foreign evidentiary rules regarding writing requirements. A third group, identified by the study is characterised by the fact that some kind of restrictive rule is applied. Often this means that the contract must comply with the law of the place of execution or the law of the place of performance.[155]

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150 A classification of form requirements is found in e.g. the Committee Report regarding the revision of the Finnish Contracts Act (Kom 1990:20, p. 70).

151 Bolero Feasibility Study 1999 at http://www.boleroassociation.org/downloads/legfeas.pdf (visited on 4.8.2003), pp. 37-38. Map 2 of the Feasibility Study (p. 34; Allen&Overy Global Law Maps by Philip R. Wood) shows how the world is divided concerning the question of governing law of contract formalities.

152 This group consists of states the laws of which are based on English law, i.e. states of the British Commonwealth, e.g. England, Canada, Australia, New Zealand, India, Pakistan, Malaysia, Bangla Desh, Nigeria, Kenya, and Israel.

153 This is because evidence issues are treated as procedural issues, which are governed by the *lex fori*.

154 This group consists of the sphere of influence of continental Romanic-German law, i.e. Continental Europe, the Nordic States, Scotland (sic!), Japan, Quebec, Egypt and many other African states influenced by French law.

155 Many Latin American jurisdictions, such as Brazil, Argentina and Peru belong to the third group. The study also points out the significance of the Bustamante Convention of 1928 and the Montevideo Convention of 1940 as complicating factors.

In the United States, as well as in many East European, Central Asian and Arabic jurisdictions like those of the Indochina, the law is developed in this question. Russia, China, Sothern Africa, Turkey and Mexico, amongs others, are unallocated.

One category might be states, the courts of which apply some form requirements based on the *lex fori* to the contract irrespective of the law governing the contract. Form requirements constitute examples of overriding national provisions that apply independent of the choice-of-law of the parties.[156]

Parties are mostly free to amend the form requirements by agreeing that valid and enforceable obligations may be created by exchanging electronic messages. Sometimes there exists, however, a form requirement exists that an agreement validating electronic communications must be in writing or signed or both.[157]

In Europe, the EC Convention on the Law Applicable on Contractual Obligations provides, in Article 9, that the law governing the contract pursuant to the Convention, or the law of the state where the contract is made, shall determine the formalities to be followed in concluding the contract. This applies only where the contracting parties are in the same state. If the parties are not in the same state, the same article adds that the state where an agent has his place of business, has to be taken into account in determining e.g. the place of contracting. Reference is made again to the reception rule, which applies by virtue of various legal instruments regulating commerce, and which signifies that the contract is concluded when and where an acceptance reaches the party making the offer.[158]

It should be added that the Convention addresses the form of unilateral undertakings by a party relating to an act or contract by stating that the question will be determined according to the law, which governs the legal relationship (or would govern in case it were constituted) or the law of the country where the unilateral undertaking was made.[159]

The Convention contains exclusions that are relevant to international trade. Article 1 excludes obligations that are based on the negotiability of instruments such as bills of exchange and promissory notes, as well as insurance contracts, where the risk is situated within the territories of the members of the European Communities. It is arguable that since bills of lading as documents of title are treated by many jurisdictions as negotiable instruments they are excluded from the scope of the Convention.[160]

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156 This means that they are mandatory in the sense British lawyers have understood them, see Goode´s remarks *supra*.

See A More Coherent European Contract Law, OJ C 63, 15.3.2003, p. 8.

157 Electronic Commerce Agreement, part A Chapter 1 Section 3.1 (Explanatory Remark), Recommendation No. 31, first edition, adopted by UN/CEFACT, Doc. ECE/TRADE/257.

158 See also the UNCITRAL draft convention on electronic contracting, Chapter IV.7.2., *post*.

159 Article 9(4) of the Convention.

160 Under English law, the situation may be different, as the bill of lading is only "quasi-negotiable", see Chapter VI, *post;* see however Debattista in Transfer of Ownership, pp. 142-143.

As will be noted, the relevance of this provision in the context of electronic commerce is reduced by the fact that the adherents to the EC Convention, the Member States of the European Union have agreed, by way of adopting Directive 31/2000 on electronic commerce, to facilitate contracting by electronic means, save some exceptions.[161]

II.10 Information security and data protection

Information security and data protection are prerequisites of effective and reliable interchange. Data protection requirements are imposed by law. In certain cases these requirements could be imposed by contract. The EC Directive disallows transfers of data where legislation does not provide adequate safeguards for privacy, but information may be transferred under contract clauses fulfilling the same purpose.

Information security clauses are the standard ingredient of any interchange agreement. The duty of maintaining confidentiality is not normally required by law, but by the very nature of the business transaction. Security can be construed narrowly to mean keeping the contents of the messaging out of the reach of the outside world. In the wider sense, however, it means safeguarding the correct origin and integrity of the message. There is a question of the security of the computer system of each of the users, in addition to which there is the security of the network. Security here means making sure that there is no change in the message during transport, that confidentiality is assured, that an authentic message is received and that reliable means of storage for effective proof is ensured.

Security is attained most notably by encryption and the use of electronic signatures. There exist various techniques of cryptography such as public key cryptography. These techniques have been the subject of trade policy disputes since US authorities have wanted to prohibit the export of encryption products. Cryptography has often been considered a matter of state security. In Europe, a local industry for these products has emerged. For instance, France has maintained a national policy on encryption devices. An important step forward was the recognition that encryption for confidentiality purposes should be separated as far as possible from the use of cryptography for authentication.[162] In the US and in Europe, there have been extensive discussions about the openness of encryption techniques to public authorities.[163]

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161 For the Directive, which should have been implemented by now by the Member States, see Chapter IV.7.1., *post*.

162 One of the first instances where this matter was addressed were the OECD Guidelines for Cryptography Policy of 1996, available at http://www.oecd.org/dsti/sti//it/secur/prod/e-crypto.htm, visited on 16.2.2003.

163 In the United States, government intervention is secured through the use of the ´Clipper-Chip´.

An essential role in safeguarding security is played by third party service providers, which are often network operators. Third party service providers have a role to play, for instance, in the authentication of electronic messages by holding the public keys of commercial partners. The authentication procedure is based on the presumption that the public key, which consists of a series of numbers, in fact belongs to the signatory. The authentication of messages through third party service providers could be connected with a central registry (such as in the Bolero System), which performs other functions such as recording information relating to title to goods, or it could alternatively be conducted by independent notaries. In the mid-90´s, the idea of using what were termed ´cyber-notaries´ to authenticate messages and possibly to carry out other commercial tasks such as verifying commercial information was portrayed in some commercial models[164] of electronic commerce. The use of public notaries is a constituent element of the U.S. law. Even the electronic commerce legislation enacted lately in the US has provisions on notarial services.[165]

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164 Report to the Joint Committee on Electronic Trade Payment Systems (ETPS) by a ´Strategic Drafting Working Party´, ICC Doc No 321-35-3/9, 20/1/1995. See Chapter VII.8.2, *post*.

165 The US Uniform Electronic Transaction Act section 11, see Gabriel, p. 4.

III THE EARLY DEVELOPMENTS OF E-COMMERCE AND EDI

It would not be an easy task to define when exactly electronic commerce saw daylight since electronic methods in the form of telegrams have been used in commerce for more than a century. Indeed, some electronic means of communication, widely referred to as ´teletransmission´, have been widely used in commercial communications on top of paper documentation.

One can distinguish various stages in the use of information technology starting from the recording of information in computers, together with the processing and management of information. These functions can be described as back-office functions inside an entity such as a trading company. It was only after the adoption of computers to process and store commercial information that electronic means of commercial interchange between two or more companies became an imaginable alternative.[1] The use of information technology then advanced to the use of information exchange between organisations, which eventually made electronic commerce possible. All technological developments have to be integrated into commercial thinking before they become useful. One could write a separate study on the psychological barriers to this integration.

The term ´electronic data interchange´ began to appear in use in the early 1970s.[2] It has become known to mean, as already noted, the electronic transfer

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1 The first computers used commercially in the 1960s or 70s were mainframe computers; PC´s came into use in the late 1980´s and laptop computers in the 1990s. One recent development is Wi-Fi (wireless fidelity), a technology that uses radio frequencies to provide high-speed Internet connections for devices such as laptops and ´personal digital assistants´ (PDAs) whose defining feature is mobility. In industries such as manufacturing, logistics and retailing, and thanks to electronic ´tags´ that can be attached to products or components and transmit information about their location and functioning, the Wi-Fi can be used to manage various aspects of production and distribution.

2 Foreword of the Model Electronic Data Interchange Trading Partner Agreement and Commentary, 1990 American Bar Association; Mallon p. 24. Mallon states that at the end of 1990s, less than 5% of the world´s companies used EDI while another electronic device, the telefax had become a standard means of transferring information in international trade.

from computer to computer of commercial and administrative transactions using an agreed standard to structure the transaction or message data.

EDI originated in the operations of companies that weredoing business at different locations using automatic data processing. Companies started to move information between their locations and analyse, store and re-utilise that information for internal business use. The next step was to extend the proprietary internal operating systems and templates for formatting information into commercial information.[3]

Once EDI was originated, it became a field, in which international organisations involved in facilitating international trade started to play an essential role alongside industry´s own collective arrangements.In many countries, national bodies of trade facilitation have been founded.[4]

III.1 Some early milestones of e-commerce

Proprietary systems of individual companies were followed by industry standards. Initiatives within industries, particularly in North America, resulted in the development of many complete industry-specific standards in the retail, grocery, transport[5], automotive and chemical industries.[6] Soon it became evident that standardisation had to go further to achieve interactivity between such standards. Problems namely arose e.g. in arranging transport for goods purchased using an industry-specific standard. Information received in connection with a purchase transaction could not be used as such.[7] The needs of the transport interface of the transaction triggered activity with the objective towards creating public standards. This illustrates one of the features of the electronisation of the trade system, the logistical link between the various contractual relationships in a transaction. As will be seen later, there are commercial and legal links as well.

III.1.1 The adoption of the EDIFACT standard

The adoption of a uniform public message standard for EDI transactions was one of the milestones in electronic commerce facilitation in the 1980s.

The United Nations Economic Commission for Europe (ECE) was one of the first bodies active in the field of EDI. The ECE Working Party on Facilitation of International Trade (WP.4) was established in 1961. According to its terms of

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3 Electronic Data Interchange Agreements, p. 11.

4 These include SITPRO in the United Kingdom, DEUPRO in Germany, SIMPROFRANCE in France, NORDIPRO in the Nordic countries and NCITD in the United States.

5 For instance, the railways in North America have had their own proprietary network called R-EDI (Gauthier, ETL 1997, p. 695).

6 Examples of an industry-specific standard are ODETTE in the European automotive industry as well as UCS, VICS and TDCC standards in the US.

7 Electronic Data Interchange Agreements, p. 12.

reference, the Working Party shall "facilitate international trade and transport by promoting rationalisation of trade procedures and the effective use for this purpose of electronic or other automatic data processing and transmission".[8]

Probably the most important achievement of WP.4 has been the development of the United Nations Electronic Data Interchange for Administration, Commerce and Transport (EDIFACT) in 1987. EDIFACT is a standard for the electronic transfer of data in a structured format. The ECE has created a language that can be spoken by traders. As in a spoken language, three elements are necessary: vocabulary constituted by ´common data elements´, grammar constituted by a ´syntax´ and ´standard messages´ which combine data elements and syntax into a structured business message.[9]

Updated UN/EDIFACT directories are issued every year, which contain messages from a wide range of economic sectors. Transport-related messages were obviously among the first ones. The messages are now available in XML form.[10] In 1995, the Working Party on Facilitation of International Trade Procedures recognised that the mandate of UN/EDIFACT work requires the extension of its scope beyond international trade and the acceptance of the universal nature of data structures and concepts.[11]

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8 Terms of Reference of the Facilitation of International Trade Procedures, http://www.unece.org/trade/facil/wp4_tor.htm, visited on 12.2.2000.

9 UNCID, p.8.

10 The Code List of the XML-EDIFACT Repository (http://www.xml-edifact.org/LIB/xml-edifact.03, visited on 15.2.2003) maintained by UNECE WP.4 contains hundreds of items.

11 UN/ECE Trade Facilitation Recommendation 25, http://www.unece.org/cefact/rec/rec25/rec25_1995_r1079rev1.pdf., visited on 28.5.2003). The Recommendation is aiming at co-ordinated actions by governments for the introduction of UN/EDIFACT as a single international standard for the electronic interchange of data (EDI) between public administrations and private companies of all economic sectors worldwide. The recommendation sets out the following definitions:

-Electronic Data Interchange (EDI) is the electronic transfer from computer to computer of commercial and adminmistrative transactions using an agreed standard to structure the transaction or message data.

- An EDI message is an approved, published, and maintained formal description of how to structure the data required to perform a specific business function in such a way as to allow for the transfer and handling of this data by electronic means.

- A UNSM (United Nations Standard Message) means that an EDI message may be referred to as a UN/EDIFACT standardised message only if it complies with the rules and directories of the United Nations Trade Data Interchange Directory (UNTDID), and if it has been approved by the UN/ECE.

-"UN/EDIFACT (United Nations Electronic Data Interchange for Administration, Commerce and Transport) - User application protocol for use within user application systems for data to be interchanged compatible with the *Open Systems Interconnection (OSI)* model. (Nowadays XML standards).

A group of industry representatives, the ´International Transportation Implementation Guideline Group´, developed a set of guidelines for the uniform interpretation and implementation of the UN/EDIFACT format in the maritime industry. (Gauthier, ETL 1997, p. 694).

For a long time, EDIFACT was not applied in the United States, where the communication standard ANSI ASC X12 had been in application.[12] Users were slow to adopt this system. General Motors, which dominates the interchange systems in the automotive industry in North America, replaced ANSI ASC X 12 with the EDIFACT at the end of 1998[13] The ECE Working Party 4 on Facilitation of International Trade Procedures has issued a number of recommendations as regards the possibility of authenticating messages by electronic means rather than by traditional signatures. This work has later for the most part been taken over by other organisations, the European Union and The United Nations Commission for International Trade Law UNCITRAL.

The Working Party has also encouraged governments to adopt international legal instruments in the field of transport to facilitate a move to electronic commerce.[14] As regards legal issues relating to the facilitation of international trade in general, WP.4 referred these issues as early as in 1982 to UNCITRAL.

UNCITRAL considered the legal implications of automatic data processing in international trade a priority item on its work programme in its seventeenth session in 1984. The work of UNCITRAL started in 1985 with a study on the legal value of computer records. This work was based on an international survey on the use of computer records as evidence in court proceedings and was linked to a parallel process within the Customs Cooperation Council to ascertain the acceptability for customs authorities of a goods declaration in a computer-readable form.[15] It resulted in a recommendation by UNCITRAL which was adopted in 1985.[16]

III.1.2 The TEDIS programme of the European Communities

Among other organisations, the European Commission recognised the strategic importance of a rapid and coordinated development of EDI to improve trade relations. The Council adopted the first phase of the TEDIS programme on 5 October 1987.[17] The aims of the programme were, in general terms, to increase

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12 ANSI stands for American National Standards Institute, which is the American member organisation for the International Standard Organisation (ISO). ASC X 12 means the Accredited Standards Committee, X.12 for EDI.

13 Chandler III, p. 650.

14 Notably the 1975 Montreal Protocol No. 4 relating to the Warsaw Convention on International Carriage by Air. Reference is also made the 1978 United Nations Convention on the Carriage of Goods by Sea (the ´Hamburg Rules´) and the UNCTAD (United Nations Commission on Trade and Development) Convention on Multi-modal Transport, which allow for the use of electronic signatures, if permitted by the issuing country. See Chapter VI *post*.

15 Savage & Walden in Walden p. 67.

16 Recommendation on legal value of computer records, adopted at the eighteenth session (1985) of the United Nations Commission on International Trade Law, doc A/CN.9/265.

17 Council Decision 87/499/EEC of 5 October 1987 introducing a communications network Community programme on trade electronic data interchange systems (TEDIS), OJ L 285, 8.10.1987, p. 35.

the awareness of the European industries of the possibilities offered by EDI systems, to create systems which would meet the needs of users and to enhance the use of common standards in data transmission. As regards legal problems, the aim was to seek solutions to such problems that might inhibit the development of trade electronic data interchange and to see to it that restrictive telecommunications regulations cannot hamper its development.

Under the framework of the TEDIS programme, studies were carried out in order to verify the legal obstacles to the development of EDI. The study resulted in the report entitled ´The legal position of the Member States with regard to electronic trade data interchange´aimed to look into the legal framework of the Member States and examine the legislation as well as the commercial practices in order to determine whether there are problems with regard to paper-based documents and hand-written signature requirements.[18]

The survey pointed out provisions in the laws of each member state demanding the creation, delivery, sending or conservation of paper-based documents. It was found that paper documents were, at the time, designed to fulfil legal or administrative requirements in different fields, such as taxation and accounting, customs and administrative declarations and evidential requirements. They concerned both the trade relationship and relationships between commercial and public sectors.[19] It was found, very generally, that there are few requirements applicable to the majority of day-to-day transactions.[20] There were general requirements for the use of paper in producing documents of title. In Italy, commercial and accounting or audit documents, and invoices in particular, had to be on paper. Under Danish law, there was a requirement for paper copies of invoices, although invoices could be sent through EDI.[21]

As regards requirements for evidence, the distinction was made, as already noted, between the admissibility of computer records as evidence in general, and their probative value in particular. As far as the admissibility of computer records was concerned, no important difficulties were thought to be encountered in theory, as there generally has been a freedom to use evidence of any means in commercial disputes. The actual probative value of computer records was considered to be dependent on the appraisal of the judge(s) involved. In the report referred to above, there was a reference to the Luxembourg Civil and Commercial Codes, which provide that the evidentiary value of computer records is equal to written documents, provided that certain requirements, notably in connection with the storage of data, had been fulfilled.[22]

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18 Troye, The European Community and EDI, in ´EDI and the Law´, ed. by I. Walden, London, 1989, p. 92

19 Ibid., p. 91.

20 Anne Troye, Tedis Programme, second phase, legal issues, at the seminar ´EDI/OVT-juridiikan kehitys´, Helsinki 27.11.1991.

21 Ibid. Within the EU, Council Directive 2001/115/EC of 20 December 2001 amending Directive 77/388/EEC with a view to simplifying, modernising and harmonising the conditions laid down for invoicing in respect of value added tax, OJ L 015, 17.1.2002, p. 24, paves the way for new developments; see Chapter VIII.2.1.5., *post*.

22 Ibid.

The study conducted during the first phase of TEDIS also concerned the formation of contracts, especially as regards the place and moment of the conclusion of a contract made at a distance. It was found that most Member States, as well as generally all EFTA countries at the time, applied the ´reception rule´, sometimes with nuances. Only the United Kingdom and Ireland do not apply the reception rule. During the first phase of the TEDIS programme, a draft Model European Interchange Agreement was created to be finalised during the second phase of the programme.

III.1.3 UNCID - a code of conduct for EDI

The technical work carried out in organisations like ECE and CCC was not adequate, since there were legal impediments for the use of EDI. Because of its physical characteristics, the traditional paper document has been accepted as evidence in international commercial transactions, since it is durable and changes or additions are normally clearly visible, whereas the data content of the magnetic medium of an electronic document can be changed at any time, and special devices are needed to verify that changes have been made.

Although electronic documents were regarded as good carriers of information, special techniques needed to be introduced to improve and guarantee the evidentiary and security value of EDI. These techniques must have the following functions: they facilitating the identification of the messages, detecting and correcting errors, guaranteeing the data content and the integrity of the messages, securing the privacy of the interchange by means built into the system and authenticating them in the sense that the correct authorised person has issued the message.

A major step in the legal facilitation of EDI was taken when the ICC adopted the *Uniform rules of conduct for interchange of trade data by teletransmission* (UNCID) in 1987.[23] It was felt that recommendations for governments to facilitate EDI by undertaking an update and overhaul of documentary requirements would take a long time to come into existence, and in the meantime it was necessary to promote the general acceptance of a high level of security in data interchange. A code of conduct was hence seen as "a bridging operation" until national and international legislation and practice would be suitably altered to take account of EDI.

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[23] The International Chamber of Commerce is a non-governmental organisation and has, in addition to the lobbying functions, a tradition to publish standard rules and practices to be incorporated into contracts. It is against this background that the ICC received the task to lead the project, see Savage & Walden in Walden, p. 68.

In the mid 1980s, the ICC had established a joint special committee with participation from other interested organisations and user groups to evaluate and formulate such a set of rules. UNCITRAL, ECE, CCC, the UNCTAD Special Programme on Trade Facilitation (FALPRO), the Organisation for Economic Cooperation and Development (OECD), the International Organisation for Standardisation (ISO), the Commission of the European Communities, the European Insurance Committee and the Organisation for Data Exchange via Teletransmission in Europe (ODETTE) were all represented on this committee, in addition to the various commissions of the ICC. The result of this preparation was published by the ICC as publication No 452.

The original idea of creating one standard communication agreement for various kinds of uses was found to be impracticable, since the different user groups in those days wanted to use different types of agreements. It was therefore felt to be desirable to create a code of conduct to define an accepted level of professional behaviour. As such, UNCID´s principles were to be taken into various forms of communication agreements, based on the needs of the relevant user group. The need to establish communication or interchange agreements was stated in the introductory note of the rules,which already distinguished between the EDI used by defined organisations, and the one used in direct open communication.[24]

UNCID provides a framework under which messages are transmitted. The objective laid down in Article 1 of the document is not to apply to the substance of trade data transfers, except as otherwise provided therein. The rules are intended to apply to trade data interchange between parties using a ´trade data interchange application protocol´[25]. The trade data elements, message structure and similar rules and communication standards used in the interchange should be those specified in the relevant TDI-AP (Article 3).[26]

The rules impose requirements on the parties of a transaction as well as, indirectly, on the intermediaries in transfers. The parties should ensure the correctness, completeness and security of their transfers with the chosen application protocol and should be able to receive such transfers. The parties should instruct their intermediaries to ensure that there is no unauthorised change in transfers requested to be retransmitted and that the data content of such transfers is not disclosed to any unauthorised person.

Requirements are set in the rules regarding the messages and their transfer. The message should contain means of verifying that the message is correct and complete in accordance with the application protocol. It may relate to one or more trade transactions and should contain the appropriate identifier for each transaction. A transfer should not only identify the sender and the recipient, but further include means of verifying the formal completeness and authenticity of the transfer. (Article 6)

As is the case in traditional correspondence by post, the sender may need to have proof that the message has been received, because the receipt has legal effects. As already stated, an offer in a sale of goods transaction under the Convention on International Sale of Goods (CISG) becomes effective when it

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24 UNCID pp. 8-10. The incorporation could occur either through direct inclusion into the text of the agreement or by inclusion in the ´user manual´, which contains all the detailed technical and legal procedures that the trading partners are obliged to follow (Savage & Walden, p. 71).

25 A trade data interchange application protocol (TDI-AP) has been defined in Article 2 to mean "an accepted method of interchange of trade data messages, based on international standards for the presentation and structuring of trade data transfers conveyed by teletransmission".

26 Such as the UN/EDIFACT. UNCID was soon adopted as the legal basis for the UN/EDIFACT standard. See Savage & Walden in Walden, p. 71.

reaches the offeree, and it can be withdrawn, even if irrevocable, if the withdrawal reaches the offeree before or at the same time as the offer.[27] Article 7 of UNCID provides that the sender of a transfer may stipulate that the recipient of a message should acknowledge receipt thereof. Such an acknowledgement may be made through the teletransmission technique used or by other means provided through the application protocol. The recipient of the message is not entitled to act on the basis of the message, until he has complied with the request of the sender. Thus the message does constitute rights for the recipient until the valid request for confirmation of the receipt is complied with. This can be regarded as a substantive provision connected with the requirements of the technique.

Should the sender not receive the requested acknowledgement within a reasonable or stipulated time, he must take action to obtain it. The rules are silent on what kind of action should be taken, but obviously the sender should contact the recipient one way or another. Unless the recipient intentionally or negligently fails to acknowledge, technical problems may have prevented reception. The rules go on to state that if, despite such action, an acknowledgement is not received within a further period of reasonable time, the sender should advise the recipient accordingly by using the same means as in the first transfer or other means if necessary and, if he does so, he is authorised to assume that the original transfer has not been received.

Article 8 stipulates that the sender may request the recipient to advise whether the contents of one or more identified messages in the transfer appears to be correct in substance, without prejudice to any subsequent consideration or action that the content may warrant.

The recipient must also act in a situation in which a transfer received does not appear to be in good order, correct and complete in form, by informing the sender as soon as possible. Furthermore, if a message has been delivered to the wrong recipient, such a recipient should take reasonable action as soon as possible to inform the sender and should delete the information contained in such a transfer from his system, apart from the trade data log.

The parties may agree to apply special protection, where this is permitted, by encryption or by other means, to some or all data exchanged between them. This obvious possibility is, however, amended by a provision according to which the recipient of a transfer so protected should assure that at least the same level of protection is applied to any further transfer (Article 9).

At least as important as the preceding provisions concerning the exchange of messages are the provisions concerning the storage of data in Article 10 of the rules. The storage of data is, of course, important for evidentiary purposes. Each party should ensure that a complete trade data log is maintained of all transfers as they were sent and received, without any modification. The trade data log may be maintained on computers provided that, if so required, the data can be retrieved and presented in a readable form. Each party shall make the necessary

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27 Article 15 of the CISG.

arrangements for the data to be presented as a correct record of the transfers as sent or received. The person responsible for the data processing system of the party concerned or, where applicable, a third party shall be available to certify that the trade data log and the reproduction made from it are correct.

The trade data log should be stored unchanged either for the period of time required by national law in the country of the party maintaining such a trade data log, or for such a longer period as may be agreed between the parties or, in the absence of a legal provision or agreement, for three years.

UNCID is not a legally binding document and its contents do not have a binding legal effect, unless they are incorporated into a contract. As a code of conduct it may still be referred to as a professional standard in disputes regarding negligence. Article 11 of UNCID provides that the ICC may give interpretations regarding the correct meaning of the rules. Similar procedures are used traditionally for the Incoterms and for the Uniform Customs and Practice for Documentary Credits.

The introductory note of UNCID advises that attention be paid to certain matters that are standard concerns in a complete interchange agreement. The first concerns the risk of the interchange failing for some reason. There should be enough concern for the risk, whether allocated between the parties, whether shifted onto the operator, or whether covered by insurance. The liability of the parties for negligence and its limitation may have to be determined.

The problem of timing is also addressed. This means, for instance, the time-limits within which the receivers should process the data. The parties should consider the secrecy of the messages as relating to the substance of the data exchanged. Parties involved in a particular professional field should consider the incorporation of sector-specific rules into the regulatory framework.[28] UNCID does not deal with the vital domain of problems relating to encryption and other security measures including digital signatures. Finally, as in all contractual arrangements, the parties should give a thought as to the applicable law and dispute resolution.

According to *Baum*, the United States EDI community were not familiar with UNCID. A few years after the publication of these rules, their relationship with US practices remained unclear and was mentioned as a potential source of conflict between the US and the rest of the world. Baum saw problems in the presentation of parties´ obligations as absolute requirements, sometimes going beyond the corresponding standards to paper documents, without stating the consequences for the failure to comply with them. The US users were, however, recommended to study UNCID and to apply it to their agreements to some extent.[29]

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28 As an example the banking rules under SWIFT. See Chapter VIII, *post*.

29 Baum in Baum-Perritt, p. 738.

III.2 Closed electronic commerce and interchange agreements

Perhaps the most important operational distinction in electronic commerce is that between closed and open electronic commerce. Closed electronic commerce refers to commerce which is restricted to firms having obtained access to a private network. This access is based on a contractual relationship with the other participants of the network. The communication partners usually use the same, or at least convergent, software, which would rarely be interoperable with other private networks. Open electronic commerce refers generally to a business model in which firms are open to business from all other firms on the Internet.[30] The business messaging may then consist of e-mails or XML messages, or a portal technology is used.[31]

III.2.1 Contract types in closed electronic commerce

Toh See Kiat[32] has identified the following three types of contracts in the context of electronic data interchange or funds transfer. These categories do not have legal significance as such, but are useful tools in approaching the complex contractual network.

A *primary contract* is the underlying trade and services contract, for example a contract of sale. It governs trade or service obligations, the performance of which would require the services of other agents, such as transportation companies or correspondent financiers.

An *ancillary contract* is a contract in ancillary legal relationships, which are formed so as to deliver the promised goods or services and complete the primary contract. An example could be a contract governing the relationship between the banker and his correspondents or the banker and his settlement agencies. An ancillary contract could also be a contract between a trader and the freight forwarder or goods carrier, or the trader and his warehousing agents, or even between the carrier and its stevedores or warehousemen.

A *communications contract*, usually called an ´interchange agreement´ or a ´trading partner agreement´, is designed to create standards and formats as well as to define the obligations and liabilities of parties in respect to communication. This is because traditional rules of communication are based on face-to-face transactions, or contacts made through the mediation of parties immune to suit, such as the postal services. The message carrier has been treated as an agent of one of the communicating parties, who is to bear the loss resulting from the mistakes of the agent.

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30 Guide to Export - Import Basics, ICC Publication No 641, p. 286.

31 The first two cases are sometimes referred to as ´systems-to-systems processing´ whilst portals are used in ´human-to- systems processing´.

32 Toh See Kiat, p. 316.

III.2.2 The purpose of interchange agreements

Interchange agreements have served a dual function. They are intended to provide the technical and legal security for the interchange. The need to have an agreement is obvious in EDI since communication between computers is based on coded data elements, which must be exchanged according to specific interchange rules i.e. syntax. Users of EDI have to agree therefore on a detailed set of technical rules.[33] In order to create a binding legal framework between two or more parties, and to cover the pitfalls that were intentionally left open in the drafting of UNCID, interchange agreements[34] have been used. Interchange agreements have been regarded as a means of creating a safe legal framework comparable to the legal regime that is applicable to the exchange of paper ocuments.[35] Interchange agreements have filled gaps that have existed in legislation with regard to regulating electronic data interchange.

The principal purpose of interchange agreements has been to define the rights and obligations of the parties engaged in the computer-to-computer exchange of data and relating to such exchange only. In Europe, interchange agreements were created for projects involving particular groups. These groups were often industry-specific, like ODETTE for the car industry, or CEFIC for the chemical industry. These groups have developed their own manuals, which have contained an interchange agreement. They contain a framework network operator agreement, and the group is thereby linked to a specific network. The contents of interchange agreements are usually quite similar.[36]

Legally speaking, an interchange agreement could be classified as a distant form of a letter of intent.

III.2.3 The relationship with primary and ancillary contracts

A purist view on interchange agreements excludes all provisions relating to their underlying contractual relationship(s).[37] This has been a typical European approach, while in the United States and Canada interchange agreements have contained provisions regarding the formation of contracts. The different functions of interchange agreements are reflected in the ´EDI trading agreements´ of US jargon.

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33 As stated earlier, Articles 2(d) and 3 of UNCID refer to ´application protocols´ (manuals etc.) as containing the relevant technical rules for the interchange.

34 UNCID calls them ´communication agreements´, while in the US the term ´electronic trading partner agreement´ has been regularly used (Thomsen in Walden, p. 73). According to Baum, a communication agreement is similar to a trading partner agreement, but UNCID reflects European rather than US model agreement approaches (Baum in Baum-Perritt, p.733 note 287).

35 Thomsen in Walden, p.73.

36 Ibid., p. 75.

37 UNCID Art. 8 relating to the confirmation of message content notes the distinction between the exchange of messages and their substantive significance with the phrase "without prejudice to any subsequent consideration or action that the consideration may warrant."

The European legal environment has left the relevant contractual provisions to be governed by the relevant primary and ancillary contracts and legislation. Although national legislators in Europe had done little to facilitate EDI before the mid 1990s, there had not been as many obstacles to its use as there were under US legislation.

The US practice has had to take into account the requirements of the Statute of Frauds. This statute was originally passed in England in 1677 and became part of the law in most states of the US, although in England it already ceased to be applied to contracts for the sale of goods in 1954.[38] The statute lays down two major requirements for contracts of sale with a given minimum level of importance. They have to be in writing and they have to be signed.[39] This caused concern to the American EDI community. There have been attempts to modify this cumbersome provision or to give it a modern interpretation, according to which EDI techniques would satisfy both the writing and the signature requirements.[40]

The differences between the European and American practice of interchange agreements derive from different socio-economic structures and traditions. Covering substantive contractual and technical items in the same contractual framework has its advantages and disadvantages.[41] It is easier to have only one contract on all aspects of a commercial relationship between trading partners, with common provisions on such questions as liability, applicable law and dispute resolution. On the other hand, agreeing on everything in one contract is cumbersome for those who are not used to it and whose legal culture does not require it. However, even if two or more agreements were used, it would be important to avoid discrepant provisions.[42] One technique, used in recent interchange agreements[43], is to reserve space for referencing to substantive conditions, providing, however, which one, normally the text of the interchange agreement, shall prevail in the case of a conflict.

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38 Perritt Jr. in Baum-Perritt Jr., p.336, and Baum in Walden, p. 122. It was applied everywhere in the US except in Lousiana. In New Mexico and Maryland it has not been enacted.

39 "...a contract for the sale of goods for a price of $500 or more is not enforceable by way of action or defence unless there is some writing sufficient to indicate that a contract of sale has been made between the parties and signed by the party against whom enforcement is sought..."(UCC § 2-201(2))

40 See Baum in Walden, pp. 122-138 and Thomssen in Walden, p. 76. Baum calls for an interpretation based on a standard of commercially reasonable security. On the interpretation of the statute and the ABA revision suggestions distinguishing between evidentiary and communicative functions, see Perritt Jr. in Baum-Perritt Jr. pp. 336-341.

41 The advocates of a narrow view of using one contractual framework advance the following arguments in support of restricting oneself to the communication issues. The brevity of the agreement makes it simpler. The class of goods or services traded may vary which may also affect the terms and conditions used due to which it is easier to use the narrow agreement permitting incorporation by reference of any underlying terms and conditions.

The advocates of a broad view consider that all issues ultimately affect the business relationship and the apportionment of risk between the parties. Moreover, as EDI is intended to expedite trade and to be highly machine-processible, it is important to resolve all potential stumbling blocks before commencing electronic trade, including the formation of contract issues. (Baum in Baum-Perritt Jr. p. 51-52).

42 Thomssen in Walden, p. 74.

43 See the RosettaNet Trading Partner Agreement, examined more closely in Chapter IV.8.4.1., *post*.

III.2.4 The European Model EDI Agreement

This study looks more closely into one interchange agreement addressed solely to the needs of EDI and drafted under Community auspices. The aim is to give a general overview of the role and contents of interchange or trading partner agreements in facilitating EDI by way of an example.[44]

At the end of the first phase of the TEDIS programme in 1991, a final draft of the ´European Model EDI Agreement´ was published. The European Commission adopted the the model as its recommendation in October 1994.[45]

The Commission recommendation is targeted to the users of EDI as well as to the Member States. The Commission recommends that "economic operators and organisations conducting their trading activities by EDI use the European Model EDI Agreement and its commentary" as well as that Member States facilitate the use of this agreement and provide the most appropriate means to that end.[46]

The reason for agreeing on a European Model EDI Agreement was to "contribute to the promotion of EDI by providing a flexible and concrete approach to the legal issues raised by the use of EDI, encouraging the cooperation between users for the exchange of EDI messages". Furthermore, it was stated that the use of such an agreement would improve the legal framework by providing a uniform approach to the legal issues and would avoid the need for every undertaking, especially small- and medium-size companies, to draft their own

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44 There have been many other interchange agreements, such as the Standard Electronic Data Association Interchange Agreement (UK), Contrat-type d´interchange EDI du CIREDIT (France), Model EDI Trading Agreement + Short Form (Australia), Norsk TEDIS Interchange Agreement (Norway), FINPRO Model Agreement of Transfer of Data in International Trade (Finland), Automotive Industry Action Group Model Trading Partner Agreement (United States) and the Guideline Concerning Customs-Trader Interchange Agreements and EDI User Manuals of the Customs Cooperation Council (now the World Customs Organisation). For a comparative analysis on these and other interchange or trading partner agreements, see Electronic Data Interchange Agreements, A Guide and Sourcebook, by Amelia H. Boss and Jeffrey B. Ritter, ICC Publication No 517. Paris 1993.

45 Commission recommendation of 19 October 1994 relating to the legal aspects of electronic data interchange, OJ L 338, 28.12.1994, p. 98. An important model for the European Agreement was the EDI Association (EDIA) Standard Electronic Data Interchange Agreement, the 2nd edition of which was published in August 1990. The EDIA Agreement is based on UNCID and follows its example in not covering the substantive law aspects.

46 The Commission recommendation is an instrument of ´soft law´. According to Article 249 of the Treaty, the European Parliament acting jointly with the Council, and the Commission shall make regulations and issue directives, take decisions, make recommendations or deliver opinions. Recommendations and opinions shall have no binding force. Recommendations and other soft law instruments are not, however, without legal effects, see K.C.Wellens and G.M. Borchart, Soft Law in European Community Law, European Law Review Vol 14 No 5 October 1989, p. 267-321.

The Commission recommendation on the European Model EDI agreement was based on Council Decision (91/385/EEC) of 22 July 1991 establishing the second phase of the Tedis programme (Trade electronic data interchange systems), OJ No L 208, 30.7.1991 p. 66. Article 3 of that decision related to the legal aspects of electronic data interchange and referred to the measures proposed in Annex I to that decision. It called for the finalisation of the Model European EDI Agreement, which was one of the results of the work initiated in this field during the first phase of the Tedis programme, established by Council Decision 87/499/EEC, OJ No L 285, 8.10.1987 p.35.

interchange agreement and consequently avoid duplication or multiplication of work.[47] Since the European Model EDI Agreement, built on existing standards as well as on UNCID, is designed and recommended to be the standard agreement for electronic data interchange in Europe and in the relations between Europe and the rest of the world, it is worthwhile to study it in detail. Reference is made here and there, in case of differences in approaches, to the American practice represented, for the purposes of this study, by the Trading Partner Agreement of the American Bar Association.[48]

The European Model EDI Agreement consists of legal provisions which have to be supplemented by technical specifications provided in a technical annex according to the users´ specific needs. It can be adopted by the parties. As a bilateral document it allows the parties to fill in their references and adopt it as such. It can also be used as a multilateral agreement and be adopted by a group of companies, by one or more organisations, by a community of users or by any users group.

Unless otherwise agreed by the parties, the provisions of the agreement are not intended to govern the contractual obligations arising from the underlying transactions effected by the use of EDI (Article 1.3).[49] In order to avoid ambiguous interpretations, the agreement defines the concepts ´EDI´, ´EDI message´, ´UN/Edifact´ and ´acknowledgement of receipt´.[50]

Although the agreement is not intended to deal with contractual obligations as such, it deals with the validity and formation of contracts. These questions are

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47 See the 6th and 7th recital of the recommendation. The need for a standard interchange agreement is stated to be recognised by the UN/ECE WP 4 and by the UNCITRAL, the 11th recital.

48 Model Electronic Data Interchange Trading Partner Agreement and Commentary, Prepared by the Electronic Messaging Services Task Force, Subcommittee on Electronic Commercial Practices, Uniform Commercial Code Committee, Section of Business Law, American Bar Association (1990).

49 The ABA Trading Partner Agreement, on the contrary, states in its recitals that "ABC and XYZ desire to facilitate purchase and sale transactions by electronically transmitting...". The ABA Agreement is intended to be used between commercial partners in connection with US domestic purchase and sale transactions involving goods within the meaning of Article 2 of the Uniform Commercial Code. It is indicated in the commentary that the agreement may be used as a basis for a trading partner agreement in the international context or in the field of services.

Section 3.1 of the ABA Agreement states further that "this Agreement is to be considered part of any written agreement referencing to it or referenced in the Appendix". In the absence of such a written (sales) agreement, the transaction may be subject to the terms and conditions included in the appendix or included in the parties´ standard printed applicable forms identified in the appendix or subject to such additional terms and conditions as may be determined in accordance with applicable law.

50 The starting point for the definition of EDI has been a definition which has been used widely and by the UN/Edifact rapporteurs as well (Art 2.2 referring to the document Introduction to UN/Edifact, UN/Edifact Rapporteur´s Team, April 1991).

EDI messages are stated to be "structured and coded messages, the main characteristic of which is their ability to be processed by computers and transmitted automatically, and without ambiguity and which makes them specific for instance in comparison with other forms of data exchange such as e-mail".

There are various levels of acknowledgement of receipt and parties are advised to indicate the level that is desired.

not covered by UNCID. Parties intending to be legally bound by the agreement expressly waive any rights to contest the validity of the contract effected by the use of EDI in accordance with the terms and conditions of the agreement on the sole ground that it was effected by EDI (Article 3.1). Such a waiver is effective as regards any requirements that the parties can influence, not as regards any mandatory requirements of the national laws concerned.[51] Moreover, each party shall ensure that the concept of an EDI message sent or received is not inconsistent with the law of its own respective country, the application of which could restrict the content of an EDI message, and shall take all the necessary measures to inform without delay the other party of such inconsistency (Article 3.2).

Article 3.3 contains the most relevant provision as regards contract formation by stating the time and place, where the contract is concluded and formed. The commentary states that a majority of Member States shall approve, when parties are not in the presence of each other, the application of the ´reception rule´, which ensures that acceptance takes place at the place and at the time of receipt of such an acceptance by the offeror. Furthermore, Part II of the CISG is referred to as providing for this rule to be applicable to contracts concluded "at distance". The reception rule is to be understood in the context of the European Model EDI Agreement as the rule whereby an EDI message is received at the time and the place where the message reaches the computer of the information system of the offeror.[52]

Article 4 of the agreement is aimed to construe an agreement between the parties regarding admissibility of electronic evidence. As noted before, in most

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51 The ABA Agreement establishes its validity and enforceability as between the parties by stating in § 3.3.1 that "this Agreement has been executed by the parties to evidence their mutual intent to create binding sale and purchase obligations pursuant to the electronic transmission and receipt of Documents specifying certain of the applicable terms".

In addition, the recitals set forth the mutual intention of the parties for valid and enforceable obligations to result from the electronic communication of data in substitution for conventional paper-based documents. The execution and performance of the agreement, together with the performance of the contract of sale transactions, and together with the conduct of the parties in accordance with its terms, should be considered sufficient to show the existence of a contract for the sale of goods. (Comment 3 of the recitals to the agreement).

52 The ABA Agreement does not contain any explicit rule as to when a contract is deemed to be concluded between the parties. However, similar purposes are served by a somewhat different construction:

The ABA Agreement contains a technical receipt clause, which determines when the message is deemed to be received. The receipt requires accessibility by the receiver at its ´Receipt Computer´(§ 4.2). Before that, no obligations are created in the underlying contract. Where a prompt receipt acknowledgement is essential, the agreement may provide that the receiver must review, for instance, his computer twice a day. Furthermore, the ´acceptance clauses´ state the requirements for the legal acceptance of an electronically communicated offer. The agreement provides in § 2.3 that "if acceptance of a Document is required..., any such Document which has been properly received shall not give rise to any obligation unless and until the party initially transmitting such Document has properly received in return an acceptance document". The provision in question changes the traditional American rule that offers and acceptances create obligations when sent, not when received (Baum in Baum-Perritt Jr., p. 60), and this is in line with the European Model Agreement.

countries, there are no mandatory legal provisions concerning evidence in commercial matters. EDI messages shall constitute evidence concerning matters contained therein "unless evidence to the contrary is adduced".[53]

Article 5 sets out standards in relation to the acknowledgement of messages. There is an obligation to process EDI messages as soon as possible after receipt, but in any case, within the time limit specified in the technical annex to be agreed upon. The general rule is that an acknowledgement is not required, unless requested.[54] Such a request can be a general one in the technical annex or an express one of the sender of the message. There is a general requirement asking the acknowledgement to be sent within one business day[55] from the receipt. Like UNCID, the agreement states that the receiver of an EDI message requiring an acknowledgement shall not act upon the content of the EDI message until such acknowledgement is sent.

If the sender does not receive the acknowledgement of receipt within the time limit, he may treat the message as null and void as of the expiration of that time limit. He may, however, initiate an alternative recovery procedure (which has to be agreed upon) to ensure an effective receipt of the acknowledgement. If that procedure fails, the message will be definitely null and void.

Article 6 deals with the overall question of information security with firm wording stating that security procedures and accompanying measures are mandatory for any EDI message. These provisions are designed to protect EDI messages against the risk of unauthorised access, alteration, delay, destruction or loss. The measures include the verification of origin in order to make sure that the message emanates from the correct sender, as well as the verification of integrity in order to make sure that the message is complete and has not been corrupted.[56] There exists, as in UNCID, a good faith obligation for the parties to communicate about any errors in the messaging and to refrain from acting on the basis of erroneous messages.[57]

Article 7 contains provisions on confidentiality and data protection. Firstly, the parties must keep any information confidential, and not use for any unauthorised purposes that information which they have agreed to be treated as confidential or which has been specified as such by the sender. Any information

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53 The ABA Agreement does not have an evidence clause. However, it constitutes a presumption for the communicated ´Documents´ to be ´in writing´ and, where required, to be ´signed´ and constituting an ´original´. This represents the ´functional equivalent approach´ (see Chapter IV.4., *post*).

54 The ABA Agreement, on the other hand, requires the receiving parties "upon proper receipt of any Document to promptly and properly transmit a functional acknowledgement in return". Such functional acknowledgement shall constitute conclusive evidence with the effect that a document has been properly received.

55 That means not being Saturday, Sunday or any declared public holiday in the intended place of receipt of the message.

56 The ABA Agreement requires the parties to use electronic signatures in transmissions (§ 1.5).

57 The ABA Agreement provides that if any transmission is received in an unintelligible or garbled form, the receiving party shall, if possible, notify the originating party. In the absence of such a notice, the originating party´s records of the contents of such document shall prevail.

being in the public domain shall not be considered to be confidential. The requirement of confidentiality extends to any permitted further transmissions of such information. Secondly, there is a provision requiring the respect of the Council of Europe Convention No 108 of 28 January 1981 on automatic processing of personal data in relations with third countries where no data protection law is in force. This provision could nowadays be replaced by a reference to the Community Directive on the processing of personal data and on the free movement of such data.[58] This directive is mandatory law, but contains a reference to the contractual practice between private parties in Article 26(2), which states that data transfers to third countries that do not ensure adequate levels of privacy may be authorised by the Member States, if adequate safeguards result from appropriate contract clauses.[59]

Article 8 sets out requirements concerning the recording and storage of data messages. These provisions are very much a reproduction of Article 10 of UNCID. Articles 9 and 10 of the agreement set out various operational and technical requirements and specifications.

Article 11 concerns the liability of the parties. It excludes liability for "special, indirect and consequential damages", without providing any definition of what is special, indirect or consequential.[60] Moreover, an exemption of liability is made in the case of *force majeure* defined in line with the CISG.

Should a party engage any intermediary to perform such services as the transmission, logging or processing of an EDI message, that party shall be liable for damage arising directly from that intermediary´s acts, failures or omissions (paragraph 3). The allocation of liability between the parties concerning the use of third parties is very much based on the idea that the third party is effectively acting as an agent of the user. Furthermore, it is the party who will use the

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58 Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 on the protection of individuals with regard to the processing of personal data and the free movement of such data, OJ No L 281, 23.11.1995 p.31. There exists also Directive 97/66/EC of the European Parliament and of the Council of 15 December 1997 concerning the processing of personal data and the protection of privacy in the telecommunications sector, OJ C 24 30.1.1998, p. 1.

59 Article 29 of the Directive 95/46/EC sets up a Working Party on the Protection of Individuals with regard to the Processing of Personal Data to study and give recommendations on the level of protection and the adequateness of various safeguarding measures, such as contract clauses. Taking into account the deliberations of this working party, the ICC published on 23 September 1998 ´Model clauses for use in contracts involving transborder data flows´ (http://www.iccwbo.org/home/statements_rules/rules/1998/model_clauses.asp, visited on 15.6.2002). These clauses are intended to assist those who wish to transfer personal data from countries that regulate export of personal data to countries that do not provide protection for personal data that the source country finds adequate. The ICC states it believes that its clauses are appropriate contractual clauses for the purposes of Article 26(2) of Directive 95/46/EC. There are other standard clauses for the same purpose.

The ABA Agreement is slightly more liberal as regards confidentiality since it does impose any confidentiality obligations on the basis of the instructions of the sender. Neither are there any references to data protection standards.

60 However, there is a reference to the report ´The liability of EDI networks operators´ prepared by ´CDID´. I have not been able to trace the origin of the document.

services of a third party service provider and who has the contractual relationship with the service provider who will be in the best position to sue the service provider in the case in which the liability is engaged. However, if a party requires another party to use the services of an intermediary, the party who required such use shall be liable to the other party for damage arising directly from faults of the intermediary. It is considered fairer that the party who imposes on the other party an obligation to use an intermediary should bear the risk for it.

Finally, as in most international contracts, there are provisions concerning settlement of disputes[61] as well as the applicable law. Article 13 invites parties to designate the law governing their agreement. Any such choice of law is stated to be "without prejudice to the mandatory national law which may apply to the parties regarding recording and storage of EDI messages or confidentiality and protection of personal data".

The commentary of the Model Agreement describes the fall-back situation should the parties not designate the law applicable to their interchange agreement. In that case the agreement would fall back on the provisions of the Convention[62] on the law applicable to contractual obligations.

The law governing the contract would be determined at the time of the dispute by determining the law with which the contract is most closely connected. This would be determined by looking at the country where 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 company, its central administration. If the contract is, however, entered into in the course of that party´s trade or profession, that country will generally be the country where the place of business is situated.

Certain remarks should be made about the applicable law. Although the Rome Convention is now generally applied in the Member States of the European Union and the European Economic Area, it does not necessarily always determine the law applicable in the absence of a choice-of-law clause, since the Model Agreement is clearly intended to be used in relations between EU

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61 The Model Agreement recommends settling disputes primarily by negotiation. In addition and particularly if an amicable settlement is not reached in negotiations, the parties are advised to choose between an arbitration clause or a jurisdiction clause. The Model Agreement is fairly neutral about the two methods, and it remains the task of the parties to choose the settlement method. Although there is no fallback provision, it is obvious that a competent court may hear the case in the absence of a valid arbitration clause.

In case of arbitration, parties are invited to choose between one or three arbitrators, and to indicate the appointing authority for arbitrators and the rules to be applied to the arbitration proceedings. The Model Agreement is neutral between ad hoc and institutional arbitration.

It should be borne in mind that the parties also have an underlying commercial relationship, which is normally subject to dispute settlement provisions as well. The dispute settlement system should be very much the same as in the main contract, since there might be a danger that, for instance, two arbitral tribunals should hear a dispute, where, among other things, the validity of a contract is put into question.

62 Convention on the law applicable to contractual obligations opened for signature in Rome on 19 June 1980 (80/934/EEC), OJ No L 266, 9.10.1980, p.1.

countries and third countries as well. The Rome Convention may not be applicable in such relations. In any case, despite the applicable law, the mandatory rules of the national law applying to the parties may come into play. National legislation based on the data protection directive serves as a good example of rules that cannot be derogated from by a contract and which are applied to the parties by the authorities of the European Community Member States.

The characteristic performance of a transaction cannot be easily determined by looking at an interchange agreement alone since the obligations of the parties are very much the mirror images of each other. There would be a strong temptation to look at the performance obligations of the parties in the underlying trade relationship to determine which of them is the performance characteristic of the contract. Furthermore, the questions of the formation and the validity of contracts form borderlines between an underlying substantive contractual relationship and an interchange agreement. The law applicable to these two aspects should be, whenever possible, the same in order to avoid conflicts.

Finally, Article 14 deals with the effect, modifications, term and severability. It is important to note that while an agreement can be terminated by giving at least one month´s notice to the other party, certain rights and obligations of the parties as to the admissibility in evidence, security, confidentiality and protection of personal data as well as to the recording and storage of EDI messages remain in force despite the termination. Should any of the articles of the agreement be deemed invalid, all other articles shall remain in full force and effect.

III.2.5 Interchange agreements and multiple commercial parties

An interchange agreement may be bilateral, or it may be a group or community interchange agreement. It may also link together various groups. One can imagine a situation, where the parties to a contract of sale are parties to an interchange agreement to which also carriers of different modes of transport, as well as the port and other authorities receiving declarations from these carriers, are connected. The goods information, such as goods description, weight and safety precautions, may originally be transmitted as electronic copies of the information.

The contents of the agreement may be the same for all parties but, especially where operators of a different nature are concerned, private amendments may be necessary. A third party service provider can act as a depositary of these amendments to be accomodated.

An example of a group interchange agreement was created to be used in conjunction with the Norsk TEDIS Interchange Agreement[63] in the early 1990s. The group interchange agreement provided that the group approves any bilateral

[63] Published by Norsk TEDIS Solli.

agreement and that an individual group member shall use the agreement as if an equivalent agreement had been concluded bilaterally with each other group member.[64]

Where the number of the parties to a contractual arrangement increases, or where the arrangement is essentially created by a service provider, it is common to establish a special legal framework for the arrangement. At that stage, the arrangement becomes much more than an interchange agreement, although similar features exist. Much attention will be paid later to the *Bolero System*, where the relationship with the arranging organisations[65] is created by service contracts[66], and the relationships of various users are governed by a multilateral contract, the legally oriented *Bolero Rulebook*, which incorporates as an appendix special *Operational Rules* with more technical content. Technologically, however, a separate *Bolero*$_{xml}$ initiative has the objective of creating a simple and robust method for trading partners to exchange data and documents over the Internet without the need for a bilateral data interchange agreement. Similar elements are found in the Bolero contractual network, but the latter is more comprehensive.

A different and slightly less ambitious approach is found in the TEDI Interchange Agreement[67] used with a similar trading platform as the *Bolero System* for dematerialised bills of lading. The agreement provides that participants to the TEDI chain form contracts bilaterally at each level in the trade chain by reference to and employing certain common, standard and required mandatory terms used throughout each link in the trade chain. The parties at each level are free to alter the terms of their contractual rights and obligations on EDI except for the standard terms. The technical specifications and operating rules and repository terms and conditions are other sets of the contractual package brought in by the basic interchange agreement.

III.2.6 Electronic commerce without interchange agreements

The need to use interchange agreements has been said to indicate the relative infancy of EDI.[68] Various groups using EDI cannot connect to each other without going through an elaborate procedure. EDI had lacked an international dimension with the exception of international corporations. A company operating in the United States and in Europe has needed different software on these two

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64 Electronic Data Interchange Agreements, p. 119.

65 Bolero Association Limited and Bolero International Limited, the latter being in charge of the actual operation of the *Bolero System*, see Chapter VIII.7.1.3., *post*.

66 Other possibilities include membership, share ownership or agency arrangements.

67 See Chapter VIII.7.4., *post*.

68 Chandler, ETL 1997, p. 649. The foreword to the UNCID Rules calls the rules an "interim solution" necessitated by the delays inherent in changing existing law and the pressing needs of trade.

continents. Industry or company-specific proprietary software is in use which is incompatible with other systems.[69]

Interchange agreements create an elaborate and rigid legal framework, not necessarily always recognised by national law, at least when it comes to the application of mandatory provisions of law. There is a need to agree on the legal and technical rules of interchange applicable between the parties. More importantly, however, third parties including the VAN service provider are not as such bound by the agreement to which the third party would have to be made privy in order to create a binding effect.

The transition to open electronic commerce generally started with the use of the Internet for other than research and military purposes some ten years ago.[70] The main bulk of electronic commerce today takes apparently place through the Internet, which facilitates electronic commerce also for consumers as well. This is helped by the fact that technically it is possible to do business on the Web confidentially and securely. The Internet provides the basis for technical arrangements between the parties using XML messages, or by conducting business through portals or by communicating by e-mails.

The Internet creates a channel for more sophisticated EDI applications (´Web EDI´). For technical purposes, value-added networks (VANs) are still often needed to establish links between regular commercial partners, and interchange based on a special agreement defining technical and legal details is still useful. Contractual arrangements such as interchange or trading partner agreements are therefore often used even if the interchange takes place through the Web using XML messages. New model contracts are designed to cover many techniques of electronic commerce. Specifications, especially technical ones, are needed for each mode, but the main bulk of legal provisions remains the same.[71]

Retail banking transactions increasingly take place through the Internet.[72] Retail banking services on the Web are still based on a closed system model. Banks normally require their customer to sign an agreement, in which the conditions as well as their methods of use contain elements similar to standard interchange agreements. One of the principal elements of these contracts is the confirmation that electronic messaging is equivalent to communicating through paper documents.

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69 Ibid., Chandler talks here about a "series of technological or proprietary ´ghettos´ that have minimal contacts with other such groups".

70 The Internet had been created for such purposes in 1969.

71 One such contract is the RosettaNet Trading Partner Agreement of 2001, which will be examined in Chapter IV.4.1., *post*.

72 In banking, secrecy and security requirements are of course high. The move towards electronic banking started in the 1980s with the conspicuous example for everyone of digital bank cards that replaced traditional savings books little by little. The first bank to offer online banking services on the net was Wells Fargo in May 1995. For the development of banking infrastructure, especially of that provided by SWIFT, see Chapter VIII. 3. and 4., *post*.

The customer is able to gain access through the portal of the bank. Security is maintained, for instance, through allocating each customer a user-ID and each access to the system has an individual password number together with varying confirmation codes for concluded transactions.[73] In the agreement between the bank and the customer, are provisions regarding liability and other relevant matters relating to the communication.

The move towards open electronic commerce is taking place also in many fields of sales where the Web is not the means of delivery. Flight tickets are increasingly booked electronically although these are already 'e-tickets', the passenger only having to show his credit card when booking in. Customer identification with precontracted user-IDs or other security arrangements is much less onerous than interchange agreements, and the use of the identification codes given by banks pose a real choice for the use of full-fledged digital signatures based on the Public Key Infrastructure. The identification codes can namely be used e.g. in some relations with the Finnish government as well. Also mobile phones can be equipped with identification devices.

While interchange agreements seek to create a legal framework for the interchange, sometimes including substantive provisions as well, the emergence of open electronic commerce has created the need to regulate electronic commerce by legislation. In part, the aim has been to follow commercial developments by providing legislation that facilitates commerce, and in part the objective has been to accelerate the development of electronic commerce by boosting user confidence in electronic trading systems. With new legislation, fewer provisions need to be inserted into contracts. In international trade, contracts for electronic commerce are still needed since not all states have introduced e-commerce laws, and these gaps have to be filled with contractual provisions. On the other hand, legislators seem to have given space to the contractual approach as well.

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73 This is the case for instance with the SOLO Agreement of the Scandinavian Nordea Bank. The bank sends the passwords for access and transaction confirmation to the physical address of the client. The Finnish banks have created, in their sectoral organisation, a common standard for the identification of the customer.

Another method, used by the Belgian Fortis Bank, is to to use a digital device the size of a pocket calculator to give the password numbers for access and for transactions exceeding a certain limit by entering the customer´s personal pin code into the device.

These methods signify simply the electronic identification of the customer which is not usually the subject of electronic signature legislation, see Chapter IV.5. *post*. For electronic identification in the Finnish context, see Sähköisen tunnistamisen menetelmät ja niiden sääntelyn tarve, Liikenne- ja viestintäministeriön julkaisuja 44/2003.

Nordea Finance Finland uses similar techniques in corporate leasing finance applications. The lessees send electronically signed transaction-related annexes, which constitute applications for credit. The technique is largely based on transaction-specific passwords used by the employees of the lessee, but transition to electronic signatures based on public key infrastructure remains an option.

IV THE EMERGING SOURCES OF LAW FOR OPEN ELECTRONIC COMMERCE

This chapter describes the emergence of new electronic commerce law which is also suited to open Internet-based electronic commerce through a portal or the use of electronic mail and XML messages.

As will be seen, the new instruments created deal with contract formation and such fundamentals of legal relationships as authenticating messages and equating electronic forms of information and evidence with paper. Therefore the new instruments contain many aspects common to interchange agreements. The new legislation, for instance, the rules regarding electronic signatures, already has a role to play in facilitating EDI. However, it is arguable that the emergence of electronic commerce conducted over the Internet has finally underlined the need for legislation. Historically, at least, there is a parallel between these two phenomena.

The general legislative framework for electronic commerce is emerging on the basis of work conducted by international organisations, private and public,at the regional level in the European Union and at the national level. In the United States, progress was first made at the state level, then through more federal measures.

Legislators have generally recognised that private or non-state rules have a role to play in electronic commerce, and are encouraging initiatives with this aim. Sometimes public organisations come to suggest soft law options. This happened with EDI when the EU suggested a model for interchange agreements in 1994. In fact, one of the key generators of soft law for international trade, UNIDROIT, is publicly financed. Despite the fact that a balance between different harmonisation methods has not been reached yet, one should recognise that e-commerce law, for which the concept of *lex electronica* is used here, has different components - as the *lex mercatoria* in the field of international trade law in general has.

The concept of *lex electronica* has a general and a more issue- or sector-specific dimension. The rules of contract formation are an example of the first

dimension and the rules purporting to create electronic equivalents for documents of title are an example of the second.[1] One of the assumptions of this study is that there will be little substantive *lex electronica* but that electronic contracting methods and the Internet will underline the need to use harmonised sources of substantive law. The *lex electronica* will then constitute part of the *lex mercatoria*, which will remain as the source of substantive law. Some central sources of substantive *lex mercatoria* will be indicated in Chapter X.3., *post*. As the new system is still emerging, particularly as regards sector-specific provisions, the role of international organisations and different legislative instruments will need another look.

IV.1 International organisations providing global solutions

As already noted earlier, UNECE through its Working Party 4 for trade facilitation has been a key organisation in the field of EDI and computing ever since its foundation in the 1960s and was ultimately transformed into UN/CEFACT at the end of the 1990s. UNCITRAL started its work with EDI and computer questions in the 1980s.

Simultaneously with the development of closed electronic commerce in the form of EDI, the technical and administrative framework for the Internet emerged. In the 1980s, technical coordination of the networks was managed by a set of contracts and ´request for comments´ (RFCs) administered by US government agencies. The RFCs were edited under contract with the US Defence Advanced Research Projects Agency. After the formation of the Internet Society (ISOC) in 1992, the funding of this work was undertaken by the ISOC. Little by little, a set of inter-linked organisations or committees emerged. Technical standards were developed by the Internet Architecture Board (IAB) and the Internet Engineering Task Force (IETF)[2], which also ran the emerging domain name system. The Internet Assigned Numbers Authority (IANA) also operated under contract with the US Defense Advanced Research Projects Agency until 1998 when the Internet Corporation for Assigned Names and Numbers (ICANN)

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1 This is reflected in the structure of the UNCITRAL Model Law on Electronic Commerce presented later in this chapter as regards its general Part I. The first provisions of the sector-specific Part II are presented in Chapter VI, *post*.

2 The IETF is a large, open and international community of network designers, operators, vendors, and researchers concerned with the evolution of Internet architecture and the smooth operation of the Internet. Furthermore, it is the principal body engaged in the development of new Internet standard specifications.

The Internet Engineering Steering Group (IESG) is responsible for the technical management of IETF activities and the Internet standards process. It adminsters the process according to the rules and procedures ratified by the ISOC. Organizations involved in technical coordination of the Internet, ICC Doc. 373-31/5, 2 September 2003, pp. 3-4.

was created to undertake this and other responsibilities with industry funding and a memorandum of understanding with the US Department of Commerce.[3]

One of the organisations with significance to this study is the World Wide Web Consortium (W3C), which develops interoperable technologies (specifications, guidelines, software and tools)[4] to promote the evolution and interoperability of the World Wide Web, which is the face of the Internet.

As regards the legal harmonisation of electronic commerce, both private and public organisations have been involved in this work. The United Nations Commission on International Trade Law UNCITRAL has created model legislation on the functional equivalents of paper documents and electronic signatures and is currently discussing a draft convention on electronic contracting, including the domains of transport law, security rights and arbitration. The UN Convention on Contracts for the International Sale of Goods was prepared under the auspices of UNCITRAL as well, although the very roots of the Convention date back to the time before the Second World War.

The harmonised law of the international sale of goods comprises not only legislative instruments[5] like the UN Convention, but also rules created by semi-public or private organisations which come into play by way of reference in a contract, or sometimes by constituting customary law. This international commercial law has been seen to have detached itself from national laws to the extent that a new *lex mercatoria* has emerged. The UNIDROIT Principles of International Commercial Contracts are often referred to as a source of the new *lex mercatoria*. I will often return to this question later.

However, it should be mentioned that, inspired by Article 7 of the CISG, Article 3 of the Model Law on Electronic Commerce as well as Article 4 of the Model Law on Electronic Signatures, draw the attention of courts and other national authorities to the fact that the provisions of the model laws, while enacted to constitute parts of domestic legislation and therefore being ´domestic´ in character, should still be interpreted with reference to their international origin in order to ensure uniformity in the interpretation of the respective instrument at national level. Moreover, questions concerning matters governed by the model

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3 Ibid., p. 2. The ICC document observes that although these organisations were initially anchored by US government contracts and funding, their structure was essentially autonomous and self-governing. Standards and structures were developed by participants who were mostly volunteers.

In the field of domain names, which are by and large beyond the scope of this study, there operates the Multilingual Internet Names Consortium (MINC).

4 W3C is transforming the architecture of the original Web (HTML, Uniform Resource Identifiers and HTTP) using the foundation of XML.

5 International conventions and model laws become part of national legal systems by way of transposition. Conventions usually contain provisions showing to what extent they are dispositive, i.e. they can be implemented only partly. For instance, the Nordic countries have not implemented part II on contract formation of the CISG. Model laws do not have any imperative character as such, but a state wishing to implement one may also wish to respect the objectives of the model law to promote harmony in international commercial relations. Model laws may give guidelines for their implementation.

laws, which are not expressly settled in them, are to be settled in conformity with the general principles[6] on which these model laws are based.

This study builds on the idea that the legal instruments to be used in electronic commerce will be very much universal, whether or not they are built on existing legal systems or not. Therefore, attention is paid to the initiatives taken by private organisations such as the International Chamber of Commerce and, in a more restricted geographical scope, the American Bar Association, to establish a sound legal framework for electronic contracting.

International organisations working in the field of electronic commerce aim at solutions that are to be adopted globally. Among these organisations one could name the United Nations sub-organisations such as UNCITRAL, UN/CEFACT[7], UNCTAD as well as the World Customs Organisation. The OECD and various sector-specific organisations in the field of transport are also of importance.

IV.2 The European Union and electronic commerce

I have already mentioned that the European Community has already been active in the promotion of EDI between commercial partners as is apparent in the TEDIS programme and the Model Interchange Agreement.

The European Union has attached even more importance to the development of electronic commerce ever since the use of the Internet for everyday purposes started to soar in the middle of the 90s. The Commission released a communication in 1997 to lay down some objectives in the field of e-commerce.[8] The Commission´s initiatives led to a substantial legislative activity and systematic policies to establish an internal market for information society services, to protect consumers and to encourage small- and medium-sized enterprises (SMEs) to use the Internet in their business.

An important objective referred to recently has been to foster dynamism in the European economies and thereby increase their competitiveness. The *e*Europe initiative endorsed at the Lisbon European Summit in March and the Action

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6 The Guide to Enactment of the Model Law on Electronic Commerce gives (on page 26) a non-exhaustive list as to the general principles on which that Model Law is based:
to facilitate electronic commerce among and within nations;
to validate transactions entered into by means of new information technologies;
to promote and encourage the implementation of new information technologies;
to promote the uniformity of law; and
to support commercial practice.

7 Centre for Trade Facilitation and Electronic Commerce working under the auspices of the United Nations Economic Commission of Europe.

8 See A European Initiative in Electronic Commerce, COM (1997) 157 final, 16 April 1997.

Plan[9] endorsed at the European Council in Feira in June 2000 aimed at accelerating the development of the information society in Europe. The *e*Europe Action Plan 2002 purported to stimulate the use of the Internet in major areas, such as transport, health care, schools, technological research, the development of ´e-content´ and the promotion of ´e-government´. The intention is to speed Europe´s transition to the new economy by exploiting the full potential of the Internet.[10] SMEs were encouraged to the use of information technology by the ´GoDigital´ actions.[11]

The initial action plan was followed by the'*e*Europe 2005 Action Plan[12], which aims to stimulate secure services, applications and content based on a widely available broadband infrastructure. As for e-business (comprising e-commerce and restructuring business processes), the Commission sees a need to review legislation in order to extend e-commerce-friendly rules to the offline delivery of goods and services in order to create a level playing field between different trading modes. Importance is attached to such technical aspects as the need for system interoperability[13], uniform standards and multi-platform access.[14] Generally speaking, the policy focus is shifting from promoting e-commerce to a more holistic view of e-business as a whole, which includes not only buying and selling over the Internet but also the productive use of information and communication technology.[15]

For the purposes of this study, one of the most interesting items on the EU agenda is the encouragement of SMEs to use Internet trading platforms, most of which relate to the buying and selling transaction e.g. by online reverse auction, but some of which contain settlement-related functionalities. An expert group

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9 See *e*Europe, Information Society for All, Draft Action Plan prepared by the European Commission for the European Council in Feira 19-20 June 2000, Brussels 24.5.2000, COM 330 final. eEurope 2005 Mi-term Review, COM (2004) 108 final, Brussels 18.2.2004.

10 Verrue, Robert, Director General for the Information Society, European Union initiatives in the field of Internet law, at the Paris International Colloquium in 2001.

11 Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions; "Helping SMEs to Go Digital", COM(2001)136 final, Brussels, 13.3.2001.

12 Communication from the Commission to the Council, the European Parliament, the Economic and Social Committee and the Committee of the regions: eEurope 2005: An information society for all; An Action Plan to be presented in view of the Sevilla European Council, 21/22 June 2002; COM(202) 263 final, Brussels 28.5.2002. See also eEurope 2005 Mid-term Review, COM (2004) 108 final, Brussels 18.2.2004.

13 The Commission has supported the creation of a ´European e-Business Interoperability Forum´ (eBIF). Set up by the European Committee for Standardisation (CEN), the Forum is designed to bring together relevant stakeholders from industry and society to agree on a roadmap on e-business interoperability and to assess ongoing and planned standardisation activities in this field. The first meeting of the Forum took place on 18 February 2004 (Enterprise Europe News Update 2.2.2004).

14 eEurope 2005 Mid-term Review, p. 10.

15 Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions; Adapting e-business policies in a changing environment: The lessons of the Go Digital initiative and the challenges ahead, COM(2003)148 final, Brussels, 27.3.2003, p. 3.

appointed by the Commission has invited the Commission to pay attention to several issues relating to trust and confidence and to promote fair trade on Internet trading platforms.[16]

In order to give a comprehensive picture, I will list the major EU legislative texts in the field of e-commerce, only two of which will be studied more closely *infra*. After the data protection Directives of 1995 and 1997, the purposes of which have already been shortly presented in Chapter III.2.4., *ante*, the first major legislative act to be adopted, at least from the point of view of this work, was the Directive[17] on a Community framework for electronic signatures in 1999.[18] That was followed by directives on legal aspects of electronic commerce as well as on e-money institutions.[19] There have been other important trade-related legislative initiatives from the Commission to the Council and the Parliament. These include directives on distance contracts[20], the distance selling of financial services[21] and electronic public procurement as part of the revision of the existing public procurement directives.[22]

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16 See B2B Internet trading platforms: Opporunities and barriers for SMEs, A first assessment by Maria Perogianni, Enterprise Papers No 13 – 2003, and Report of the expert group on B2B Internet trading platforms, Final report to the Commission, 2003. Annex II of the Report contains a checklist for an assessment of whether a code of conduct sufficiently meets the objectives of fair trade. The *e*Europe 2005 Mid-term Review (COM (2004) 108 final) mentions (on p. 6) that the Commission will prepare a communication on fair trade in B2B Internet trading platforms in 2004 in order to stimulate and facilitate the participation of SMEs.

17 Directive 1999/93/EC of the European Parliament and of the Council of 13 December 1999 on a Community framework for electronic signatures, OJ L 13, 19.1.2000 p. 12.

18 On the EC legislation regarding e-commerce, see Aurelio Lopez-Taurella, A European Community Regulatory Framework for Electronic Commerce, in Common Market Law Review, 38 (2001); 6 pp. 1337-1384.

19 Directive 2000/31/EC of the European Parliament and of the Council of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market (Directive on electronic commerce), OJ No L 178, 17.7.2000, p. 1, and Directive 2000/46/EC of the European Parliament and of the Council of 18 September on the taking up, pursuit of and prudential supervision of the business of electronic money institutions; OJ L 275, 27.10.2000, p. 39.

20 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, OJ L 144, 4.6.1997.

21 Directive 2002/65/EC of the European Parliament and of the Council of 23 September 2002 concerning the distance marketing of consumer financial services and amending Council Directive 90/619/EEC and Directives 97/7/EC and 98/27/EC, OJ L 271, 9.10.2002, p.16.

22 Directive 2004/18/EC of the European Parliament and of the Council of 31 March on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts, OJ L 134, 30.4.2004, p. 114; and Directive 2004/17/EC of the European Parliament and of the Council of 31 March 2004 coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors, OJ L 134, 30.4.2004, p. 1. The author of this study was the secretary of the Council´s Working Party on Public Procurement until February 2002.

E-commerce-related aspects have been under discussion as regards copyright and related rights in the information society[23] and the revision of the Brussels and Lugano Conventions relating to jurisdiction and enforcement of judgements.

A number of non-legislative initiatives have aimed at promoting self-regulation and out-of-court dispute settlement. The Commission has established an alternative dispute settlement network, the EEJ net, in order to utilise and promote dispute resolution mechanisms for resolving consumer-business disputes across borders throughout the EU.

EC legislation in the field of electronic commerce consists mainly of directives. Member States of the Community[24] have to implement or transpose them into their national legislation within the time-period given at the end of each directive, and very often this period is two years. Directives and regulations are imperative instruments, which may be detailed, or which may leave Member States certain freedoms in their implementation.[25]

In a market consisting of now twenty-five national legal systems, directives have a multiple role to play. They provide for the establishment of relevant legal infrastructure relating to services and their providers, but in addition to that they contain stipulations relating to market access, the free circulation of products and relations with third countries. A directive may therefore, at the same time, have an impact on the relationship between commercial actors under contract law, create rules for the relationship between users of information society services and a third party service provider, and may lay down the foundation for the provision of information society services in the internal market.

In international trade, legislation with a global reach is useful for global commercial operators. There is therefore a discrepancy between regionalism, fallen into from time to time by the European Union and the United States alike, and a global approach. Notable global harmonisation has taken place, for instance in international transportation and maritime conventions and in the field of

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23 In the field of intellectual property, there are directives concerning the protection of computer programs (Directive 91/250/EEC, OJ L 122 17.5.1991 p. 42), databases (Directive 97/66/EC, OJ L 24, 30.1.1998, p. 1) and certain aspects of copyright and related rights of the information society (Directive 2001/29/EC, OJ L 167 22.6.2001, p. 10).

24 Directives relating to electronic commerce and the internal market in general are part of the 1st ´pillar´ which consists of legislation adopted in accordance with ´the Community method´ pursuant to the Treaty of Rome establishing the European Community, whereas the European Union was established by the Treaty of Maastrict and is not a legal person but merely a political concept. Therefore directives adopted by the Council and the Parliament are EC directives.

One must mention that the new constitution will change the titles of Community legal acts and uses ´laws´ in lieu of regulations and ´framework laws´ in lieu of ´directives´. The entry into force and the implementation of the new constitution are still unclear.

25 It is a debated issue how detailed the legislation the Community institutions create should be. According to the principle of subsidiarity, which is worded in Article 5 of the Treaty, the Community shall take action in areas which do not fall within its exclusive competence (e.g. trade policy mostly belongs to its exclusive competence), only if and in so far as the objectives of the proposed action cannot be sufficiently achieved by the Member States and can therefore, by reason of the scale or effects of the proposed action, be better achieved by the Community.

intellectual property well before the establishment of the European Communities. Regional legislation can however be reached more rapidly and is often more imperative than than a global solution. Therefore it may easily serve as an interim phase before a global convention is reached.

In the European Union, the need to attain global solutions is recognised in Directive 2000/31/EC on electronic commerce. Recital 59 of that Directive namely states that "despite the global nature of electronic communications, coordination of national regulatory measures at the European Union level is necessary in order to avoid fragmentation of the internal market, and for the establishment of an appropriate European regulatory framework; such coordination should also contribute to the establishement of a common and strong negotiation position in international forums". Recital 61 goes further to state the objective of international harmonisation: "If the market is actually to operate by electronic means in the context of globalisation, the European Union and the major non-European areas need to consult each other with a view to making laws and procedures compatible".

Regional legislation should nevertheless provide an interface for relations with third countries (i.e. the rest of the world). In the case of the European Union, the European Commission may be given a mandate to negotiate international agreements that guarantee wider uniformity than Community directives do.

IV.3 Some central sources for facilitating and regulating electronic contracts

Chronologically, the major public instruments directly addressing electronic commerce in the international sale of goods transactions (and being of a general nature) are the following:

- The UNCITRAL Model Law on Electronic Commerce adopted in 1996.
- The EC Directive on electronic signatures adopted in 1999.
- The US Uniform Electronic Transactions Act adopted in 1999.
- The EC Directive on electronic commerce adopted in 2000.
- The US Electronic Signatures in Global and National Commerce Act adopted in 2000.
- The UNCITRAL Model Law on Electronic Signatures adopted in 2001.
- The UNCITRAL draft convention on electronic contracting (to be adopted possibly in 2005)

In addition to the above list of instruments that have a more general scope, one should mention UNCITRAL´s draft Instrument on carriage of goods by sea, which addresses electronic transport documents for sea carriage and possibly also multimodal transport. One must also mention the launch of the private *Bolero*

System in 1999 which represented the idea of a comprehensive multi-contract trading platform and certain parallel actions mentioned in chapters VIII.7.2. to 7.5., as well as the introduction of the ICC eUCP in 2002 to govern electronic presentations under documentary credits. Important projects have also been launched under the auspices of UNCITRAL relating to the transfer of rights in tangible goods by electronic means and regarding electronic arbitration. Developments on the contract practice side are too numerous to be listed here.

IV.4 UNCITRAL Model Law on Electronic Commerce

UNCITRAL may be credited with a major accomplishment in creating the Model Law on Electronic Commerce which was adopted at the United Nations´ General Assembly in December 1996[26].

The purpose of the Model Law is to offer national legislators a set of internationally acceptable rules as to how the legal obstacles for the communication of legally significant information in the form of paperless messages could be removed. Furthermore, the aim is to create a secure legal environment for electronic commerce. The principles expressed in the Model Law are also intended to be of use for individual users of electronic commerce in the drafting of contractual solutions that might be needed to overcome the legal obstacles to the increased use of electronic commerce.[27]

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[26] General Assembly Resolution 51/162 on 19 December 1996. As of 25 March 2002, legislation based on the Model Law has been adopted in Australia, Bermuda, Colombia, France, the Hong Kong Special Administrative Region of China, Ireland, Philippines, the Republic of Korea, Singapore, Slovenia, the States of Jersey (within the United Kindom) and the State of Illinois within the United States. Moreover, uniform legislation influenced by the Model Law and the principles on which it is based has been prepared in Canada (Uniform Electronic Commerce Act, adopted in 1999 by the Uniform Law Conference of Canada) and in the United States (Uniform Electronic Transactions Act, adopted in 1999 by the National Conference of Commissioners on Uniform State Law) and has been enacted as law by a number of state-level jurisdictions in those countries.

In 1999, the International Chamber of Commerce called on EU countries to implement the Model Law in their legislation. To my knowledge, so far only Ireland and France have done so. In the Nordic countries, however, it seems that legislators consider that the subject-matter is capable of being solved by the interpretation of existing norms in jurisprudence. The report of the committee set up to revise the Finnish Contracts Act (Kom 1990:20) reflects these views. At the time the the report was written, the committee did not see any need for express legislative changes to facilitate electronic contracts under Finnish law.

The above Finnish report notes on p. 60 that the Nordic legal discussion quite unanimously equates electronic records with ´documents´ as required by law.

See the UNCITRAL Web-site: http://www.uncitral.org/english/status/status-e.htm, the latest update 16 March 2004.

[27] Guide to Enactment of the UNCITRAL Model Law on Electronic Commerce (1996) p.15. The guide is intended to help governments, scholars and other interested parties in studying and implementing the Model Law. In the preparation of the Model Law, it was assumed that the draft Model Law would be accompanied by a guide. Due to this, it was decided in respect of a number of issues not to settle a number of issues in the Model Law, but to address them in the guide so as to provide practical guidance.

The Model Law therefore relies on a new approach, referred to as ´the functional equivalent approach´, which is based on an analysis of the purposes and functions of traditional paper-based requirements in view of determining how those purposes and functions could be fulfilled through electronic-commerce techniques.[28]

The Model Law is divided into two parts, one dealing with electronic commerce in general and the other with electronic commerce in specific areas. When the Model Law was adopted, the part covering specific areas consisted only of one chapter that dealt with electronic commerce as it applied to the carriage of goods.[29]

The Model Law does not distinguish between domestic and international transactions, but offers the enacting state the option of limiting the scope of the law to international transactions.

IV.4.1 Electronic commerce not defined

The model law does not define what ´electronic commerce´ means. However, there is a definition of ´electronic data interchange (EDI)´ in Article 2.[30] The Commission had a broad notion of ´EDI´ in mind for addressing the subject-matter for its own purposes. Thus, among the means of communication encompassed in the notion of ´electronic commerce´, there are many modes of transmission based on the use of electronic techniques. Firstly, the notion covers communication by means of EDI defined narrowly as the computer-to-computer transmission of data in a standardised format. Secondly, it covers the transmission of electronic messages involving the use of either publicly available standards or proprietary standards. Thirdly, it encompasses the transmission of free-formatted text by electronic means, including the Internet. Fourthly, in certain circumstances, even the use of such techniques as telex or telecopy could be embraced by the notion of ´electronic commerce´.[31]

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28 Guide to Enactment, p. 18.

29 The Guide to Enactement states on p. 17 that other aspects of electronic commerce might need to be dealt with in the future, and the Model Law can be regarded as an open-ended instrument, to be complemented by future work.

30 ´Electronic data interchange (EDI)´ means according to the definition "the electronic transfer from computer to computer of information using an agreed standard to structure the information", which corresponds to the EDIFACT definition.

31 Guide to Enactment, p.16. The guide notes further that the provisions of the Model Law are intended to apply also in the context of less advanced communication technology, such as telefax. There exists a need to cover a variety of communication techniques that might be used interchangeably. For instance, digitalised information initially dispatched in the form of a standardised EDI message might, at some point, be forwarded in the form of a computer-generated telex or in the form of a telecopy of a computer print-out. A characteristic of electronic commerce is, however, that it covers programmable messages, the computer programming of which is the key difference between such messages and traditional paper-based documents. >>

The Model Law supports the idea of party autonomy. Standard interchange agreements, which have been examined in detail in this study, are examples of innovation within the business community towards creating a legal framework for their operations. The decision to undertake the preparation of the Model Law was therefore based on the recognition that solutions to the legal difficulties raised by the use of modern means of communication are mostly sought within contracts. Party autonomy applies, however, only to Chapter III of the first part, entitled ´Communication of data messages´, which contains provisions on the formation and validity of contracts, the recognition by parties, attribution of data messages, acknowledgement of receipt, as well as the time and place of dispatch and receipt of data messages. The contents of Chapter III of part one are such that they constitute a regular part of interchange agreements or ´system rules´, which the parties can agree to.

Party autonomy is not, however, intended to apply to Chapter II, although enacting states of the Model Law could of course decide otherwise. The drafters of the Model Law thought that the provisions contained in Chapter II (the legal recognition of data messages, incorporation by reference, provision on ´writing´, ´signature´ and ´original´, the admissibility and evidential weight of data messages as well as the retention of data messages) may be regarded as as a collection of exceptions to well-established rules regarding the form of legal transactions. Such well-established rules are normally of a mandatory nature since they generally reflect decisions of public policy.[32]

<< *Hill* (Richard Hill, New paths for dispute resolution in Improving International Arbitration, The need for speed and trust, Liber Amicorum Michel Gaudet, ICC Publication No 598, p. 65 and the references included therein) considers telegrams, telex, telefax and e-mail to be very similar in the technical sense. For each technology, a message is converted to a digital format, then transmitted over a telecommunications network and finally converted into a human-readable form. At transmission, e-mail, telegrams and telex share the feature that they need not be created from a conventional writing and that the printed copy of the transmission is created contemporaneously with the transmission itself. Moreover, a printed copy is always created for a telegram, usually for a telex, but for the e-mail only if the sender requests it. At reception, the only difference is that telegrams and telexes are always printed, and the fax usually is, whilst e-mail is printed only if the recipient requires a print.

The situation, in which an offer is accepted on the Web can be described as follows: The bits comprising the offer are stored on the seller´s computer, transmitted through a telecommunications network to the buyer´s computer and stored there temporarily. When the buyer accepts the offer there is again transmission of information. This also happens when a fax or an e-mail is sent, but in the case of the Internet the ultimate recipient in a way has somehow laid down a basis for the transmission. An electronic offer typically includes some facilities for indicating the buyer´s acceptance and transmitting that acceptance back to the seller. This is most often done in electronic form, and the buyer completes certain blank fields, and then initiates a "submit" or "transmit" function. Thus, a bit stream comprising the offer and resident in the buyer´s computer is modified by the buyer and the modified version is sent back to the seller. This exchange of information is analogous to the exchange that takes place when e-mails or faxes are exchanged.

See also Chapter IX.5.1, *post*.

[32] Guide to Enactment p. 26.

IV.4.2 The general legal recognition of electronic documents

The key component of the Model Law, which is contained in Article 5, is a principle that data messages should not be discriminated against, which means that there should be no disparity of treatment between data messages and paper documents. Article 5 states namely that "information shall not be denied legal effectiveness, validity and enforceability solely on the grounds that it is in the form of a data message". This does not, however, give any extra weight to data messages or to the information contained in them. It merely indicates that the form in which certain information is presented or retained cannot be used as the only reason for which that information would be denied legal effectiveness.

Article 9 of the Model Law establishes both the admissibility of data messages as evidence in legal proceedings and their evidential value in a similar wording to that which Article 5 uses for expressing the principle of the legal validity of data messages in general. The application of rules of evidence shall not lead to a denial of admissibility of a data message on the sole ground that it is a data message. Article 9 stipulates further that information in the form of a data message shall be given due evidential weight and also lists certain aspects[33] to be considered when assessing a data message.

IV.4.3 The ´functional equivalent´ approach

The authors of the model law saw that the legal requirements contained in national laws requiring the use of traditional paper-based documentation to constituted the main obstacle to the development of modern means of communication. In the preparation of the Model Law, thought was given to the possibility of dealing with impediments to the use of electronic commerce by extending the scope of such notions as ´writing´, ´signature´ and ´original´ with a view to encompassing computer-based techniques.[34] It was thought that states adopting the Model Law should not undergo a thorough adaptation of their legislation to remove the ´paper-based´ requirements themselves or to disturb the legal concepts or approaches underlying those requirements.

The Model Law therefore relies, as regards ´writing´, ´signature´ and ´original´ (Articles 6 to 8), on a new ´functional equivalent approach´, which is based on an analysis of the purposes and functions of the traditional ´paper-based´

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33 According to Article 9(2), regard shall be had, in addition to any other relevant factor, to the reliability of the manner in which the data message was generated, stored or communicated, to the reliability of the manner in which the integrity of the information was maintained as well as to the manner in which its originator was identified.

Article 9(1) contains a provision, which is said to be important to common law jurisdictions. The admissibility of data messages shall not be denied on the grounds that they are not in their original form if these are the best evidence that the person adducing them could reasonably be expected to obtain.

34 Guide to Enactment, p. 18.

requirement with a view to determining how those purposes or functions could be fulfilled through electronic-commerce techniques. There is no attempt to define a computer-based equivalent of any kind of document in the Model Law as such. Instead, basic functions of paper-based form requirements are singled out with a view towards providing criteria for data messages to receive the same level of legal recognition as corresponding paper documents.

According to Article 6, the requirement by law for information to be in writing is met by a data message if the information contained therein is accessible so as to be usable for subsequent reference.

Article 7 lays down rules on how to meet a signature requirement in respect of a data message. For reasons of presentation, this article is examined together with electronic signatures later.

Where the law requires information to be presented or retained in its original form[35], that requirement is met by a data message if there exists a reliable[36] assurance as to the integrity of the information[37] from the time when it was first generated in its final form, whether as a data message or otherwise, and, where it is required that information be presented, that information is capable of being displayed to the person to whom it is to be presented. (Article 8)

Article 8 is pertinent to documents of title and negotiable instruments, in which the notion of the uniqueness of an original is particularly relevant. In addition, many other documents used in international trade shall frequently be presented as originals. The Guide to Enactment lists such documents as weight certificates, agricultural certificates, quality or quantity certificates, inspection reports as well as insurance certificates. Without this functional equivalent of originality, the sale of goods using electronic commerce would not be possible since the issuers of such documents would be required to retransmit their data message every time the goods are sold. An alternative would be that parties would have to use paper documents to supplement the electronic commerce transaction.

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35 The requirement of an original may be presented as an obligation, or the law may simply make provision for the consequences of the information not being presented or retained in its original form. In some areas of law, special requirements exist with respect to the registration or notarisation of documents, such as the sale of real estate or family law matters.

36 The standard of reliability required shall be assessed in the light of the purpose for which the information was generated and in the light of all the relevant circumstances (paragraph (3)(b)).

37 The criteria for assessing integrity shall be whether the information has remained complete and unaltered, apart from the addition of any endorsement and any change which arises in the in the normal course of communication, storage and display (paragraph (3)(a)).

IV.4.4 Retention of data messages

Article 10 establishes a set of alternative rules to the existing requirements regarding the storage of information that may constitute obstacles to the development of modern trade. These provisions are relevant, for instance, for accounting or tax purposes, but could also relate to the storage of commercial documents such as bills of lading. But even the retention of court judgements or arbitral awards by competent bodies could benefit from electronic methods.

Paragraph (1)(a) reproduces the conditions established under Article 6 for a data message to satisfy a rule which prescribes the presentation of a ´writing´. Paragraph (1)(b) emphasises that the message does not need to be retained unaltered as long as the information stored accurately reflects the data message as it was sent.[38] Paragraph (1)(c) contains rules on the treatment of certain transmittal information. Such information, which enables the identification of the origin and destination of a data message and the date and time when it was sent or received, shall be retained.

IV.4.5 Acknowledgement of electronic incorporation by reference

The Model Law was adopted in 1996, but was already amended in 1998 when Article 5*bis* on ´incorporation by reference´ was added.[39] This expression is often used as a concise means of describing situations where a document refers generically to provisions which are detailed elsewhere, rather than reproducing them in full.[40] Article 5bis states "Information shall not be denied legal effect, validity or enforceability solely on the grounds that it is not contained in the data message purporting to give rise to such legal effect, but is merely referred to in that data message".

This Article (which in my view is a very special provision in a Model Law of a very general nature)[41] is intended to provide guidance as to how legislation aimed at facilitating the use of electronic commerce might deal with the situation where certain terms and conditions, although not stated in full, but merely referred to in a data message, might need to be recognised as having the same

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38 Usually messages are decoded, compressed or converted in order to be stored.

39 Article 5bis was adopted by the Commission at its thirty-first session in June 1998.

40 Commercial contracts frequently contain an arbitration clause which refers to the rules of a particular arbitral institution. Moreover, abbreviated terms can be used in respect of delivery (covering risks, costs and responsibilities for the transportation of goods) by the use of trade terms (most notably Incoterms 2000) as well as payment terms (such as CAD to mean cash against documents). On incorporation by reference, see also Chapters IV.7.3.2., IV.8.2., and, particularly on transport documents, VIII.2.1.6., *post*.

41 The acceptance of incorporation by reference has, in most jurisdictions, developed in legal practice and legislation has intervened only to prohibit unfair contract terms or practices in some instances. This Article was strongly advocated at least by the International Chamber of Commerce which is strongly influenced in this case, it is submitted, by American regulatory problems and models. Purely technically, this provision would, in my view, belong to an instrument for electronic contracting.

degree of legal effectiveness as if they had been fully stated in the text of that data message. The laws of many states accept this possibility, although consumer protection rules may impose safeguards to this.[42]

The Model Law recognises the need for these safeguards. According to the Guide to Enactment, Article 5*bis* is not to be interpreted as creating a special legal regime for incorporation by reference in an electronic environment. It merely establishes a principle of non-discrimination and is to be construed as making domestic rules applicable to incorporation by reference in a paper-based environment equally applicable to incorporation by reference for the purposes of electronic commerce.

The technique of incorporation by reference is particularly useful in electronic commerce. Instead of using free text in data messages, trading partners can take advantage of extrinsic sources of information, such as databases, code lists or glossaries, by making use of abbreviations, codes and other references to such information. The accessibility of the full text of the information being referred to may be considerably improved by the use of electronic communications. The ´uniform resource locators´ direct the reader to the referenced document by providing ´hypertext links´ which the reader can make use of by clicking the mouse.

Contract law has created rules for determining whether incorporation by reference is sufficiently conspicuous also in respect of the impact of the referenced information on the rights and obligations of the contractual partners. This is the case in particular when consumers are concerned. Even in business-to-business relations a sheer reference to contractual terms not presented in full could be inadequate, if the referenced conditions contain, for instance, terms with unexpected contents.[43] Some of these contract law rules may relate to the substance, but many relate to the means of how incorporation by reference is carried out. For instance, legal rules could require that a reference to a limitation of liability clause should be presented on the first page of a contract document such as a ticket.

In assessing the accessibility in electronic commerce, factors to be considered in the light of the Model Law[44] may include the availability of the information, for instance the hours of operation of the repository and ease of access, the cost of access, matters of integrity such as the verification of the content, the authentication of the sender as well as the mechanism for correcting errors in communication. Moreover, an important factor is the extent to which the term is subject to later amendment, which should be indicated by relevant notices.

The concept of incorporation by reference and the legal requirements for its validity, as compared to the requirement of making the text available to the addressee, are discussed *infra*.

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42 See Chapter VI, *post*.

43 An example of this is the freight forwarder´s general lien clause contained in the General Conditions of Nordic Freight Forwarders giving the freight forwarder lien to the goods under his custody in respect of all his claims, not only those relating to the individual consignment.

44 See the Guide to Enactment, p. 29.

IV.4.6 Basic default rules for interchange

The Model Law includes, in Chapter III of the first part, a number of rules (Articles 11 to 15), which are common to interchange agreements or ´system rules´. The Guide to Enactement uses the notion of ´system rules´ to cover two different categories of rules. Firstly, it could refer to general terms provided by communication networks, and secondly, it could refer to specific rules that might be included in those general terms to deal with bilateral relationships between originators and addressees[45] of data messages.

The provisions of Articles 11 to 15 may be used in several ways. They may be used for concluding interchange agreements, or they may fill the gaps that may exist in contractual terms. More importantly, however, these provisions set a basic default standard for situations where data messages are exchanged without a previous agreement being entered into by the communicating parties. Thus the Model Law paves the way in an important manner for open-network communications.

Article 11 relates to the formation and validity of contracts and provides that an offer and the acceptance of the offer may be expressed by means of data messages.[46] Similarly, as between the originator and the addressee of a data message, a declaration of will or other statement shall not be denied legal effect, validity or enforceability solely on the grounds that it is in the form of a data message.(Article 12)

Article 13 (attribution of data messages) provides rules on what basis the addressee is able to rely on the origin and contents of the data message.[47] A data message can be attributed to the originator in several ways. Firstly, a data message is that of the originator if it was sent by the originator himself. Secondly, a data message is deemed to be that of the originator, if it was sent by a person who had the authority to act on behalf of the originator in respect of that message, or if the message was sent by an information system programmed by, or on behalf of, the originator to operate automatically.

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45 The Definitions of the Model Law (Article 2) give meanings to these terms:

- An ´originator´ of a data message means a person by whom, or on whose behalf, the data message purports to have been sent or generated prior to storage, if any, but it does not include a person acting as an intermediary with respect to that data message.

- An ´addressee´ of a data message means a person who is intended by the originator to receive the data message, but does not include a person acting as an intermediary with respect to that data message.

46 Some domestic laws based on the Model Law, such as the Uniform Electronic Commerce Act prepared by the Uniform Law Conference of Canada, contain more detailed provisions on expression of consent in an electronic environment. Section 20, paragraph (1)(b) of this act expressly refers to "touching or clicking on an appropriately designated icon or place on a computer screen" as a manner of manifesting consent. Official records of UNCITRAL Working Party IV (Electronic Commerce) Thirty-ninth session, New York, 11-15 March 2002, A/CN.9/WG.IV/WP.95, p. 14.

47 This Article has its origin in Article 5 of the UNCITRAL Model Law on International Credit Transfers, which definesthe obligations of the sender of a payment order. (Guide to Enactment, p. 41)

Thirdly, an addressee is entitled to regard a data message as being of the originator, and to act on that assumption, if the addressee properly applied a procedure previously agreed to by the originator for ascertaining whether the data message is of the originator. Similarly, an addressee can act on the assumption that a data message is of the originator, if the data message received resulted from the actions of a person whose relationship with the originator or with any agent of the originator enabled that person to gain access to a method used by the originator to identify data messages as its own.[48]

The entitlement described in paragraph 3 does not apply after the addressee has received notice from the originator that the data message is not that of the originator and has had reasonable time to act accordingly.[49] In a case in which the relationship of a person to the originator has enabled that person to gain access to a method of identifying a message, the addressee cannot act on the assumption of origin after it knew or should have known, had it exercised reasonable care or used any agreed procedure, that the data message was not that of the originator.

In all the above three cases, where the message can properly be attributed to the originator, the addressee is entitled to regard the data message as being what the originator intended to send and to act on that assumption. However, if the addressee knew or should have known, had it exercised reasonable care or used any agreed procedure, that the transmission resulted in any error in the data message as received, it cannot act on the assumption on the contents.

The addressee is thus protected as being in good faith in cases where the message was sent by a person capable of sending it, but not authorised to do so (an employee could be a good example), as well as in cases where errors occur in the transmission. An originator which fails to control the sending of messages, or an addressee which fails to use the agreed authentication procedures to verify the origin of the message, has to bear the consequence of the negligence.[50]

It should be noted, however, that the actual purpose of the Model Law is not, as stated in the Guide to Enactment, to assign responsibility.[51] Contract laws in various legal systems have a wider arsenal of rules for dealing with various shortcomings in the formation of contracts. The Model Law provisions create

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48 Paragraph 3. The method used for identify a message may be a private key used in cryptography.

49 However, if the message had been properly authenticated to have been sent by the originator, it cannot be repudiated.

50 In the United States (on US legislative developments, see 5.3. and 5.6, *infra*), UCC § 2-212, Draft of November 2000, provides that an electronic record or electronic authentication is attributed to a person if the record was created by or the authentication was the act of the person or their person´s electronic agent or the person is otherwise bound by the act under the law.

UCITA § 213 provides that an electronic authentication, display, message, record, or performance is attributed to a person if it was the act of the person or its electronic agent, or if the person is bound by it under agency or other law.

51 Guide to Enactment, p. 41.

rules for the particular hazards created by electronic transmissions. The basic contract law rules should apply in conjunction with the Model Law provisions.[52] Attribution of data messages, for instance, is particularly concerned with some issues of agency law. Moreover, these rigorous rules can be rebutted in some cases such as fraud.[53]

Article 14 contains rules on acknowledgements of receipt. These rules apply only to cases, where the originator has requested or has agreed with the addressee that receipt of the data message be acknowledged. A provision on acknowledgements of receipt is a standard component in interchange agreements. Article 14 creates a presumption that the relevant data message has been received by the addressee if the acknowledgement reaches the originator. This presumption does not, however, extend to the contents of that message.[54]

The Model Law is rather liberal as to the form of the acknowledgement. If no form has been agreed between the parties, the acknowledgement may be given by any communication, whether electronic or not, or by any conduct of the addressee sufficient to indicate to the originator that the data message has been received. The originator may make the data message conditional on the receipt of the acknowledgement. If the time limit (or reasonable time in case no time limit is set) for sending the acknowledgement has passed, the originator has to notify the addressee and to provide the latter a reasonable time to react before the message can be treated as not sent.

Article 15 deals with the time and place of the dispatch and receipt of data messages. These rules are again very detailed and technical, but could have significance in the context of international trade transactions, where for instance documents under documentary credits have to be presented to banks at a certain time and at a certain place. More importantly, these rules have a bearing on when and where a contract is deemed to be concluded, applying the reception rule[55] contained in Part II of the Convention on Contracts for the International Sale of Goods and may even have an impact on the choice of an applicable law.

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52 To illustrate this by an example, let us imagine that an offer for the supply of goods erroneously contains a price of 50.000 euros instead of the correct figure of 500.000 euros. The Model Law would deal here only with a possible error in transmission, whilst the applicable rules would deal with typing errors, as well as the entire consequences of either event for the parties.

53 According to UCC § 2-212, Draft of November 2000, Comment 3, once attribution is established, a person can rebut such attribution by establishing fraud, forgery, or some other invalidating cause.

54 Article 13(5) establishes, as described above, the conditions under which, in case of an inconsistency between the text of the data message as sent and the text as received, the text as received prevails.

55 The use of the reception rule does not deal with the situation of instantaneuous acceptance of an offer. However, a view of significance expressed in a Note by the Secretariat (UNCITRAL Working Party IV (Electronic Commerce), doc A/CN.9/WG.IV/WP.95, para. 61) is that Article 15 would be sufficient to cover both the situation that mirrors the use of traditional mail and the situation of an instantaneous acceptance.

The authors of the Model Law Guide stress, however, that no substantive implications on contract law or private international law are meant.

The Article applies a dual system by defining the time of receipt of a message by referring to the time when the message actually enters an information system, and at the same time defining that the place where the message is deemed to be received may be different.

The general default rule of dispatch is that the dispatch of a data message occurs when it enters (any) information system outside the control of the originator or of the person who sent the data message on behalf of the originator. For receipt, the originator may have designated an information system for the purposes of receiving data messages. Receipt occurs at the time the message enters the designated information system. If no information system is designated, receipt occurs when the data message enters (any) information system of the addressee. Even if an information system were designated by the addressee, receipt occurs when the addressee retrieves the message from another information system.[56] Retrieval is, as I understand it, a technical act, and does not necessarily mean that the addressee becomes aware of the contents of the message. This provision is relatively central in the Model Law since the same question is addressed one way or another in many instruments.[57]

Paragraph 4 defines the places where a data message is deemed to be dispatched or received.This provision follows the approach of the CISG. A data message is deemed to be dispatched at the place where the originator has its place of business, and is deemed to be received at the place where the addressee has its place of business. If the originator or the addressee has more than one place of business, the place of business that which has the closest relationship to the underlying transaction or, where there is no underlying transaction, the principal place of business. Should neither the originator nor the addressee have a place of business, reference is then made to their habitual residence.

IV.5 Electronic signatures

The regulation and facilitation of the use of electronic signatures has been at the top of the agendas of the protagonists of trade legislation and international organisations since an electronic signature has been seen as indispensable for the creation of trust and confidence on electronic communication and documents.

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56 The distinction between designated and non-designated information systems is intended to establish an appropriate allocation of risks and responsibilities between originator and addressee.

57 E.g. national laws implementing the Model Law, see Note by the UNCITRAL Secretariat, doc. A/CN.9/WG.IV/WP.104/Add.2, indirectly Article 11 of the Directive 2000/31/EC on electronic commerce, and some soft law instruments or texts like the First Opinion of the CISG Advisory Council, see *infra*.

IV.5.1 The role of electronic signatures

The concept of an electronic signature has to be looked at from the point of view of information security and law. Combining these two is a challenge which the various drafters of electronic signature legislation have had to rise to. The terminology and definitions may vary. For example, from the information security point of view, a digital signature means the result of applying certain specific technical processes to specific information.

One approach is to look at the historical concept of a signature. ´Signature´ has been defined on many occasions, and a number of definitions are given in legal and literary dictionaries.[58] Under Finnish law, there is no definition of a signature nor of its implications. There are however form requiremens in respect of the sale of land and, in the law of succession, a will of a person has to be signed personally in the presence of two witnesses.[59] Under Anglo-American law, on the contrary, the legal concept of signature exists. In the Uniform Commercial Code of the United States (U.C.C. § 1-201(39)(1992)) is a broad concept covering any mark made with the intention of authenticating[60] the marked document. It should be noted that alongside the traditional handwritten signature exist various types of procedures like stamping or perforation that are also designed to provide certainty. In some cases requiring a ´signature´ of a simple stamp or perforation could suffice whereas in other cases a signature may need to be verified by witnesses.[61]

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58 See Annex I of UN/CEFACT Recommendation 14 (1979), http://www.unece.org/cefact/rec/rec14/rec14_1979_inf63.pdf, visited on 10.6.2003.

59 Outside these situations, Finnish law does not require a signature to render a contract valid. It has, however, been held that when there is a requirement of written form (electronic records will do as well) for a contract, the document has to be signed (the Report of the committee for the revision of the Finnish Contracts Act, Kom 1990:20, p. 58).

60 Guideline 28 of the ABA Digital Signature Guidelines gives a definition of ´authentication´: generally, the process used to confirm the identity of a person or to prove the integrity of specific information. More specifically, in the case of a message, authentication involves determining its source and providing assurance that the message has not been modified or replaced in transit. GUIDEC II of the International Chamber of Commerce defines in its glossary (p. 1) the word ´authenticate´ to mean "to record or adopt a digital seal or symbol associated with a message, with the present intention of identifying oneself with the message". A further clarification is given in the glossary: "In the American usage, the term ´authenticate´ is often used to denote the act of identifying oneself with a message, but in the European usage ´authenticate´ is more associated with the verification of a signature." The concept (to) ´verify a digital signature´ is defined: "In relation to authenticating a given message (digital signature, message and public key), to determine accurately that:

(a) the digital signature was created by the private key corresponding to the public key; and (b) the message has not been altered since its digital signature was created."

61 Guide to Enactment p. 33. Under Anglo-Saxon law, a sale of land is a ´deed´ which has to be "signed, sealed and delivered" in order to be concluded.

Another approach is to look at the functions of a signature.[62] It serves as evidence by authenticating a text by way of identifying the signer with the signed document. When the signatory makes a mark in a distinctive manner, the content of the document becomes attributable[63] to the signer. A signature also has a ceremonial function that calls the signer´s attention to the legal significance of the signer´s act, and it thereby helps to prevent unconsidered engagements. In certain contexts defined by law and custom, a signature expresses the signer´s approval or authorisation of the content of the document, or the signer´s intention that it shall have legal effect.[64] Finally, a signature has a meaning related to efficiency and logistics. A signature on a written document often imparts a sense of clarity and finality to the transaction and may lessen the subsequent need to inquire beyond the face of a document. As an example, negotiable instruments rely upon formal requirements such as a signature for their ability to change hands with ease, rapidity, and minimal interruption.

In a digital setting, a broad concept of signature could include such markings as digitised images of paper images, typed notations (like s/John Smith) or even addressing notations, such as electronic mail origination headers.

From an information security viewpoint, such simple electronic signatures are distinct from the digital signatures described in information security terminology, where they mean the result of applying certain technical processes. Although the concept of a ´digital signature´ is sometimes used to mean any form of computer-based signature, a digital signature is only one type of electronic signature. The recommended best practise of the ICC´s General Usage in International Digitally Ensured Commerce, second version (GUIDEC II), defines a digital signature as

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62 Information Security Committee, Electronic Commerce Division, *Digital Signature Guidelines*, Legal Infrastructure for Certification Authorities and Secure Electronic Commerce, 1996 A.B.A SEC. SCI & TECH, pp. 4-6.

UN/CEFACT Recommendation 14 ´Authentication of Trade Documents by means other than signatures´ (1979) gives (on p. 86) a signature on trade documents three main purposes:

- It identifies the source of the document, i.e. the writer;
- It confirms the information in the documents; and
- It constitutes proof of the signatory´s responsibility for the correctness and/or completion of the information in the document.

Guide to Enactment of the UNCITRAL Model Law on Electronic Commerce lists, in paragraph 53 referring to Article 7, the following functions for a signature: to identify a person, to provide certainty as to the personal involvement of that person in the act of signing and to associate that person with the content of a document. Furthermore, a signature could, depending on the type of document, attest to the intent of a party to be bound by the content of a signed contract, the intent of a person to endorse authorship of a text as well as the intent of a person to associate himself with the content of a document written by somebody else.

63 Attribution of data messages is provided for, as noted *supra*, in Article 13 of the UNCITRAL Model Law on Electronic Commerce. Although a signature is a standard means of attribution, it is not the only one; see the note of the UNCITRAL Secretariat, Doc. A/CN.9/WG.IV/WP.104/Add.3, paras. 8 to 17.

64 The requirements for signature may not be met even if the message is otherwise attributable to the addressor.

> "A transformation of a message using an asymmetric[65] cryptosystem such that the person having the authenticated message and the signatory´s public key can accurately determine (a) whether the transformation was created using the private key that corresponds to the signatory´s public key, and (b) whether the signed message has been altered since the transformation was made".

This concept of digital signature is linked to to public key cryptography, which assures, as becomes apparent from the above definition, two things for commercial actors. Firstly, it assures that their messages are secure and, secondly, that other transacting parties are authenticated. In a given transaction, the sender encrypts the message with the public key of the recipient and digitally signs or authenticates the message with his own private key, and the recipient uses his private key to decrypt the message and the public key of the sender to verify the message (´authentication´).[66] An authenticated message cannot be forged easily. Therefore it binds the signatory and the message cannot be repudiated later.

In conclusion, digital signature technology establishes the basis for the formation of legally binding contracts in electronic commercial transactions since it can provide electronically the same forensic effect as a signed paper message provides. It should be borne in mind that the use of electronic signatures does

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65 An asymmetric cryptosystem, also often termed a ´public key cryptosystem´, is an information system utilising an algorithm or series of algorithms which provide a cryptographic key pair consisting of a private key and a corresponding public key. The keys of the pair have properties to the effect that (1) the public key can verify a digital signature that the private key creates, and (2) it is computationally infeasible to discover or derive the private key from the public key. The public key can therefore be disclosed without significantly risking the confidentiality of the private key.

In other words, using this technology, senders and receivers of electronic messages each possess two keys, a public key and a private key. A public key is shared with anybody, and the private key is never shared with anybody. These two keys correspond to each other so that whatever is encoded with one key can only be decoded by the other. (GUIDEC II, Appendix, What is public key cryptography?)

66 In the encryption process, the sender of the message encodes it with the recipient´s public key, making it impossible for any party other than the one holding the private key to decrypt the message. Encryption protects the message from all parties other than the recipient, without the recipient having to divulge his private key to the sender.

Linked to the sent message, there is an attachment containing a set of data which is compiled by taking the output of a hash function, or digest, of the original data that is encrypted with the sender´s private key. The hash function puts the original data through an algorithm, resulting in a data sequence unique to a particular message but much shorter than the message itself. The resulting digital signature can only be decrypted if the recipient has the correct public key, thereby permitting a recipient to verify the identity of the sender. (The link between the digital signature and the message can be made in many ways: a signature is kept within the message, it is appended or prefixed to it, or it is retained in a separate electronic file or information system).

Some methods of authenticating electronic messages do not employ an asymmetric cryptosystem and are not within the strict definition of ´digital signature´ contained in GUIDEC II. Other means could be digitally scanned images of hand-written signatures, signatures created by means of a stylus and digitising tablet, a name signed using the keyboard, the use of passwords or other techniques such as biometrics for controlling access (GUIDEC II, Appendix, What is public key cryptography?; see also Digital Signatures, A survey of law and practice in the European Union, Cambridge 2000, pp. 6-8).

not as such give any more legal effect to an electronic document than a hand-written signature would do in the case of a paper document. The legal effects of an electronic document have to be assessed in the light of the applicable legal rules.

IV.5.2 When can electronic signatures be regarded as authenticated?

Specific legislation on electronic signatures has emerged, for instance, in the United States and in the European Union, and UNCITRAL as well has adopted a model law dealing with them. It should be noted, however, that the UNCITRAL Model Law on Electronic Commerce has already established in its Article 7 general conditions for the credibility of electronic signatures in Article 7. It establishes namely the general conditions under which data messages would be regarded as authenticated with sufficient reliability in electronic commerce.

Article 7 paragraph(1)(a) introduces the principle that, in an electronic environment, the basic legal functions of a signature are performed by way of a method that identifies the originator of a data_message and confirms that the originator approved the content of that data message. Paragraph (1)(b) of Article 7 then lays down a flexible approach to the level of security. The method used to achieve the aims contained in paragraph (a) of Article 7 should be as reliable as is appropriate for the purpose for which the data message is generated or communicated, in the light of all the circumstances, including any agreement between the originator and the addressee of the data message.[67]

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[67] The Guide to Enactment lists, on pages 33-34, some legal, technical and commercial factors that may be taken into account in determining whether the method used for identification under paragraph (1) is appropriate:
the sophistication of equipment used by each of the parties;
the nature of their trade activity;
the frequency at which commercial transactions take place between the parties;
the kind and size of the transactions;
the function of signature requirements in a given statutory and regulatory environment;
the capability of communication systems;
compliance with authentication procedures set forth by intermediaries;
the range of authentication procedures made available by any intermediary;
compliance with trade customs and practice;
the existence of insurance coverage mechanisms against unauthorised messages;
the importance and the value of the information contained in the data message;
the availability of alternative methods of identification and the cost of implementation;
the degree of acceptance or non-acceptance of the method of identification in the relevant industry or field both at the time the method was agreed upon and at the time when the data message was communicated; and any other factor.

IV.5.3 Early developments in the United States[68]

The American Bar Association has played a pivotal role in enhancing a common regulatory framework for electronic commerce in the United States. Its Model Trading Partner Agreement of 1990 was referred to earlier. In 1996, the ABA created guidelines for digital signatures[69]. These guidelines sought to establish a safe harbour - a secure computer-based signature equivalent, which would minimise the incidence of electronic forgeries, enable and foster the reliable authentication of documents in computer form, facilitate commerce by means of computerised communications as well as give legal effect to the general import of the technical standards for the authentication of computerised messages.[70] The guidelines suggested solutions for various questions relating to electronic signatures to serve as a common framework for unifying principles that act as basis for more precise rules in various legal systems.

In 1995, at the time when the ABA Guidelines were still being prepared, the state of Utah enacted its own Digital Signature Act. This act focused on issues raised by cryptography-based digital signatures. It did not take long before several other states introduced similar laws.[71] By 2001, at least 49 states and the U.S. Federal Government had enacted or were contemplating legislation in the field of electronic signatures.[72]

IV.5.4 EC Directive on electronic signatures

It is easy to see that the emergence of dozens of national statutes regulating the same problems is not inclined towards providing uniformity and may even hamper the development and marketing of new products as confidence in the new systems cannot be built. As regards electronic signatures, the EU could act in a somewhat proactive role, although some Member States already had national legislation in force before the EC Directive. The German law on electronic

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68 Based on Smedinghoff, Thomas J. and Hill Bro, Ruth, Moving with Change: Electronic Signature Legislation as a Vehicle for Advancing E-commerce, The John Marshall Journal of Computer and Information Law, Vol. XVII, No. 3, Spring 1999, p 723, reproduced partly at http://profs.lp.findlaw.com/index.html.

69 Information Security Committee, Electronic Commerce Division, *Digital Signature Guidelines,* Legal Infrastructure for Certification Authorities and Secure Electronic Commerce, 1996 A.B.A SEC. SCI & TECH.

70 The ABA Guidelines, pp. 21-22.

71 Only three states adopted a law based on public key cryptography. Others advanced to a more technology neutral direction admitting, at the same time, that some electronic signatures are more neutral than others. Gregory, p. 6.

72 See also Federal Certification Authority Liability and Policy. Law and Policy of Certificate-based Public Key and Digital Signatures, by Michael S. Baum. U.S. Department of Commerce, Gaithesburg, MD, June 1994. This very comphensive report surveys political liabilities as well as liability and policy issues arising in the operation of a "Federal Certification Authority" infrastructure. A Federal Certification Authority was an illusory concept to cover various certification responsibilities that might be vested on the US Federal Government in the creation of a public key electronic signature infrastructure.

signatures, *the Signaturgesetz*[73], was passed by the German Parliament on 22 July 1997. Similarly, legislation on electronic signatures existed in Italy.[74]

The aim of Directive 1999/93/EC on a Community framework for electronic signatures is to create recognition for and equivalence to electronic signatures within the European Union. The Directive aims at facilitating the use of electronic signatures as well as contributing to their legal recognition. It establishes a legal framework for electronic signatures and certain certification services in order to ensure the proper functioning of the Internal Market.

Member States of the Community shall not make the provision of certification services subject to prior authorisation.[75] Member States may, nevertheless, introduce or maintain accreditation schemes aiming at enhanced levels of certification-service provision.[76] They shall furthermore ensure the establishment of an appropriate system that allows for the supervision of certification-service-providers which are established on its territory and which issue qualified certificates to the public. The Directive also contains provisions aimed at facilitating cross-border certification services with third countries. This could be done by the involvement of a certification-service-provider meeting the Directive´s requirements or through international standards and agreements applicable to certification services. The Commission is given, in Article 7 of the Directive, a task to make proposals to reach such uniformity.

The Directive has a two-tier definition of electronic signature. As described earlier, an electronic signature can exist in many different forms or of which many technologies can be used in its production. The Directive is therefore, in defining an electronic signature, based on the objectives and inherent reliability of the signature.

According to Article 2, an ´electronic signature´ means data in electronic form which are attached to or logically associated with other electronic data and which serve as a method of authetication.[77] An ´advanced electronic signature´ means an electronic signature which meets a number of requirements. First, it is uniquely linked to the signatory[78], secondly it is capable of identifying the signatory, thirdly it is created using means that the signatory can maintain under his sole control and finally it is linked to the data to which it relates in such a manner that any subsequent change of the data is detectable.

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73 Bundesgesetzblatt, I, 1997, p. 1870.

74 Law 59 of 15 March 1997, Supplemento Ordinario alla Gazzetta Ufficiale della Republica Italiana n. 63 del 17 March 1997.

75 A ´certification-service-provider´ is an entity, a legal or a natural person who issues certificates or provides other services related to electronic signatures. Recital 12 of the Directive explains that certification services can be offered either by a public entity or a legal or natural person, if established in accordance with national law.

76 Voluntary accreditation schemes (providing for accreditation similar to ISO quality standards) should not reduce competition for accreditation services and Member States should not prohibit certification-service-providers from operating outside voluntary accreditation schemes.

77 Thus the Directive deals with different kinds of electronic signatures and not only with digital signatures. The word ´authentication´ is used without defining it. For definitions of ´authentication´, see *supra*.

78 ´Signatory´ means a person who holds a signature-creation-device and acts either on his own behalf or on behalf of the natural or legal person he represents.

These two definitions have different legal effects. An advanced electronic signature shall satisfy the legal requirements of a signature in relation to data in electronic form in the same manner as a handwritten signature satisfies those requirements in relation to paper-based data.[79] Moreover, an advanced electronic signature shall be admissible as evidence in legal proceedings. In order to have these effects, an advanced electronic signature has to be based on a qualified certificate[80] and has to be created by a secure-signature-creation device.

An electronic signature (which is not an advanced electronic signature) shall also be recognised to some extent, which may depend on the circumstances of the case. Member States shall namely ensure that an electronic signature is not denied legal effectiveness and admissibility as evidence in legal proceedings solely on the grounds that it is in electronic form or that any of the requirements to make an advanced electronic signature (to be based upon a qualified certificate, to be based upon a qualified certificate issued by an accredited certification-service-provider or having been created by a secure signature-creation device) are not met. Recital 21 of the Directive states that the legal recognition of electronic signatures should be based upon objective criteria and not be linked to authorisation of the certification-service-provider involved.

The Directive does not interfere with the possibility of national law of governing the legal spheres in which electronic documents and electronic signatures may be used. Neither does it affect national rules regarding the unfettered judicial consideration of evidence.[81] As advanced electronic signatures shall be admitted as evidence in legal proceedings, it is the jurisdiction in question, which shall determine what significance should be given to the advanced electronic signature.

Finnish procedural law applies the doctrine of free assessment of evidence. The existence of a valid signature usually counts as evidence of the intention to be bound by the signed text, unless other circumstances such as coercion or forgery are involved. The Directive only requires in this context that an advanced legal signature based on a qualified certificate and created by a secure-signature-creation device shall hold, in respect of electronic data, the same status as a hand-written signature in respect of a paper document.

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79 Recital 17 adds however that the Directive shall not seek to harmonise national rules concerning contract law, particularly the formation and performance of contracts or other formalities of a non-contractual nature concerning signatures. For this reason the provisions concerning the legal effect of electronic signatures should be without prejudice to requirements regarding form laid down in national law with regard to the conclusion of contracts or the rules determining where a contract is concluded.

80 A ´certificate´ means an electronic attestation which links signature-verification data to a person and confirms the identity of that person. A ´qualified certificate´ means then a certificate which meets the requirements laid down in Annex I of the Directive and is provided by a certification-service-provider, who fulfils the requirements laid down in Annex II.

81 Recital 21 of the Directive.

The Directive aims at meeting many objectives. It is designed to create full credibility and a framework[82] for sophisticated products, recognising at the same time that less sophisticated methods need to be given certain significance so that the use of signatures is not hampered by a formal ´straitjacket´. Such a straitjacket may, however, be created by sectoral legislation using the Directive as reference. Furthermore, the Directive gives a role to voluntary accreditation schemes in pursuit of quality, but emphasises that adherence to these schemes is voluntary for the certification-service-providers and tries to make sure that accreditation is not detrimental to competition.

This dualism extends to supervision and liability. There may exist, unless implemented differently by a Member State, different standards in relation to the supervision of certification-service-providers, as the obligation imposed on Member States in Article 3(3) of the Directive concerns only those certification-service-providers which issue qualified certificates to the public.

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82 For repetition and elaboration, an advanced electronic signature is to be equated with a hand-written signature if

- it is based on a qualified certificate; this requires that the certificate meets the requirements of Annex I and is provided by a certification-service-provider who fulfils the requirements laid down in Annex II; and

- it is created by a secure-signature-creation device, which is a signature-creation device that meets the requirements laid down in Annex III.

The Directive contains in the Annexes detailed information about

- requirements for qualified certificates (Annex I), such as the names or identifications of the service provider and the signatory, the signature-verification data which correspond to signature-creation data under the control of the signatory, validity period, limitations on the scope of use or on the value of admitted transactions, as well as an indication that the certificate is issued as a qualified certificate;

- requirements for certification-service-providers issuing qualified services (Annex II), which lays down a detailed list of administrative, financial, technical and contractual measures to be complied with;

- requirements for secure signature-creation devices (Annex III), which are of a general nature and aim to protect the secrecy of the signature-creation-data, which should not be easily derived, which are protected against forgery and which should be protected by the legitimate signatory against the use of others; and finally

- recommendations for secure signature verification (Annex IV), according to which it should be ensured with reasonable certainty i.a. that the signature is reliably verified and the result of that verification is correctly displayed and the verifier can, as necessary, reliably establish the contents of the signed data.

The Directive provides for the establishment of an ´Electronic-Signature Committee´ the tasks of which include the clarification of the requirements laid down in the Annexes.

In the absence of a prior authorisation, the supervision of certification-service-providers plays a more important role.

Each Member State shall ensure the establishment of an appropriate system that allows for supervision of certification-service-providers which are established on its territory (home Member State) and issue qualified certificates to the public. According to Recital 13, Member States may decide how they ensure the supervision of compliance with the provisions of the Directive. Supervision could be done by private-sector-based supervision systems. Moreover, certification-service-providers could apply to be supervised under any applicable accreditation scheme, but they are not obliged to do this.

Furthermore, Member States should designate a public or private body to verify the conformity of secure signature-creation devices with the requirements laid down in Annex III.

The Directive expressly[83] presents as a minimum requirement for Member States that these shall ensure that by issuing a certificate as a qualified certificate to the public or by guaranteeing such a certificate to the public a certification-service-provider is liable for damage caused to any entity or legal or natural person who reasonably relies on the certificate in respect of its contents[84] unless the certification-service-provider proves that he has not acted negligently.

Similarly, there is a presumption that the certification-service-provider is liable for failure to register a revocation of a qualified certificate unless he proves that he has not acted negligently. As is the case with the contents of the certificate, the entity or natural or legal person sustaining damage must have relied on the certificate reasonably in order to be able to recover damages.

A certification-service-provider may limit the use of the certificate, provided that the limitations are recognisable to third parties. Moreover, with similar prerequisites, a limitation can be made on the value of transactions for which the certificate can be used. The Directive provides that the certification-service-provider is not liable outside the limits of use or in excess of the limitation value.

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83 In the case of consumer protection legislation in particular, Member States are considered to have the right to go beyond the otherwise imperative minimum provisions of community directives and impose more stringent requirements than those required by a directive. Sometimes this is expressly stated in the directive, in some cases derogations must be based on aims listed in Article 95(4) of the Treaty of Rome.

84 Article 6 of the Directive stipulates that the information concerning which the liability arises after an entity or legal or natural person has reasonably relied on it as contained in the certificate, is

- the accuracy at the time of issuance of all information contained in the qualified certificate and the fact that the certificate contains all the details prescribed for a qualified certificate;
- the assurance that at the time of the issuance of the certificate, the signatory identified in the qualified certificate held the signature-creation data corresponding to the signature-verification data given or identified in the certificate; and
- the assurance that the signature-creation data and the signature-verification data can be used in a complementary manner in cases where the certification-service-provider generates them both.

IV.5.5 UNCITRAL Model Law on Electronic Signatures[85]

After completing its Model Law on Electronic Commerce, UNCITRAL created a Model Law on Electronic Signatures, which was adopted on 5 July 2001.[86] This Model Law appeared after the two major trading blocs, the European Union and the United States, already had legislation in place on electronic signatures. The Model Law may still have an impact in spreading electronic commerce legislation, for instance, to emerging economies. Moreover, it is a useful reference instrument to other UNCITRAL texts and soft law instruments.

The UNCITRAL Model Law applies to electronic signatures used in the context of commercial activities[87], unless an enacting state might wish to extend its scope outside commercial activities. For comparison, the EC Directive 1999/93 does not apply such a limitation. It follows the approach of Article 7 of the Model Law on Electronic Commerce in the definition of ´electronic signature´[88] as well as in relation to the case-specific relativity[89] of criteria as to when an electronic signature is considered to stand up to the requirements of a signature imposed by the law. However, Article 6(3) of the Model Law on Electronic Signatures lists a number of criteria similar to the characteristics of an ´advanced electronic signature´ envisaged in Article 2 of the EC Directive 93/1999, which are deemed to meet the requirements of the signature in respect of a data message.[90]

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85 See the text of the presentation ´The UNCITRAL´s Model Law on Electronic Signatures (2001)´ by Renaud Sorieul, Chief Administrator, Department of International Trade Law, the UN Legal Affairs Office in the International Colloquium, Internet law: European and international approaches, 19-20 November 2001, Paris, http://droit-internet-2001.univ-paris1.fr/ve/, visited on 9.3.2003.

86 Report of United Nations Commission on International Trade Law on the work of its thirty-fourth session, held at Vienna, from 25 June to 13 July 2001. A final version of the Guide to Enactment of the Model Law on Electronic Signatures was anticipated during the second semester, but appears not to have been released.

87 The Model Law indicates that the term ´commercial´ should be given a wide interpretation so as to cover matters arising from all relationships of a commercial nature, whether contractual or not.

88 According to Article 2 (a) ´Electronic signature´ means data in electronic form in, affixed to or logically associated with a data message, which may be used to identify the signatory in relation to the data message and to indicate the signatory´s approval of the information contained in the data message. The expression ´approval of the information of the message´ is unique to the UNCITRAL Model Laws. It is submitted that it means identifying oneself with the transmission of that particular information rather than approving it generally.

89 Article 6(1) states: "Where the law requires a signature of a person, that requirement is met in relation to a data message if an electronic signature is used that is as reliable as was appropriate for the purpose for which the data message was generated or communicated, in the light of all the circumstances, including any relevant agreement."

90 Article 6(3) states: "An electronic signature is considered to be reliable for the purpose of satisfying the requirement referred to in paragraph 1 if:

(a) the signature creation data are, within the context in which they are used, linked to the signatory and to no other person;

The signature creation data were, at the time of signing, under the control of the signatory and of no other person;

Any alteration to the electronic signature, made after the time of signing, is detectable; and

Where a purpose of the legal requirement for a signature is to provide assurance as to the integrity of the information to which it relates, any alteration made to that information after the time of signing is detectable.

These characteristics are not, however, absolutely necessary as paragraph 4 makes it clear that paragraph 3 does not limit the ability of any person to establish in any other way, for the purpose of satisfying the requirement in a given case, the reliability of an electronic signature. Neither do these characteristics limit the ability of any person to adduce evidence of the non-reliability of an electronic signature.[91] Article 7 then gives the enacting states the opportunity to specify an authority or organ to determine which electronic signatures satisfy the provisions of Article 6 on the criteria for compliance.

Whereas EC Directive 1999/93 lays down requirements for those certification-service-providers that issue qualified certificates (most notably those in Annex II of the Directive), the Model Law also lays down, in addition to requirements for certification-service-providers similar to those in Annex II of the EC Directive[92], requirements for signatories and the relying parties. These provisions may prove to be important in assessing liability in case of disputes.

A signatory must exercise reasonable care to protect the signature-creation data and to inform possible relying parties or service providers if the signature-creation-data has been compromised. Furthermore, it has to make sure that the information taken to a certificate used to support its electronic signature is accurate. (Article 8)

Article 11 lays down an obligation to the relying party to take reasonable steps to verify the reliability of the electronic signature. Furthermore, the relying party must take the necessary precautionary steps in respect of a third party certificate. The Model Law states expressly that a relying party "shall bear the legal consequences of its failure to comply with the above requirements".

IV.5.6 Recent electronic commerce legislation in the United States

At the federal level, a model law entitled Uniform Electronic Transactions Act (UETA) was finalised in 1999. As an American lawyer[93] describes it, UETA is a

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91 Cf. Directive 1999/93/EC which does not expressly state in its Article 5 whether an ´advanced electronic signature´ envisaged therein would be conclusive. The article should be read in conjunction with Recital 21 which states that the legal recognition of electronic signatures should be based on objective criteria, and that the Directive does not affect national rules regarding the unfettered judicial consideration of evidence.

92 The liability regime is not as elaborate, however. According to Article 9(2), a certification service provider shall bear the legal consequences of its failure to satisfy the requirements of paragraph 1 (containing the detailed obligations for certification-service-providers).

93 New E-signature Laws Click Into Action, an Update by Scott D.Patterson on the FindLaw website http://profs.findlaw.com, visited on 27.2.2000.

See also Patricia Brumfield Fry, A Preliminary Analysis of Federal and State Electronic Commerce Laws, http://www.uetaonline.com/docs/pfry700.html, visited on 20.8.2002. Ms Fry was chair of the Drafting Committee for the Uniform Electronic Transactions Act. See also Gabriel, Henry D. The New United States Uniform Electronic Transaction Act: Substantive Provisions, Drafting History and Comparison to the UNCITRAL Model Law on Electronic Commerce at http://www.unidroit.org/english/publications/review/articles/2000-4.htm, visited on 20.8.2002.

template proposed by the National Conference of Commissioners on Uniform State Laws; it has no legal effect unless and until adopted in some form in a given state. The Act took effect on January 1, 2000 and the first state to pass it was California. On 26 August 2002, a total of forty states had enacted UETA.[94]

The underlying purpose of the Act is to ensure that electronic contracts (records and signatures) have the same legal effect as their hard copy counterparts. The Act further provides that if a law requires a record to be in writing, or if a law requires a signature, an electronic record satisfies those requirements.

The Act is designed to facilitate the use of electronic contracting. It only applies to transactions where the parties have agreed to conduct their transaction electronically. Except where an agreement's primary purpose is to authorise electronic transactions, an agreement to conduct a transaction by electronic means may not be contained in a standard form contract that is not itself an electronic record. Nor may standard form agreements be conditioned on an agreement to conduct transactions electronically. Under the Act, if the sender of an electronic record inhibits the printing or storing of that record, the electronic record is not enforceable against the recipient.[95]

The Electronic Signatures in Global and National Commerce Act (´ESIGN´), most of which became effective on October 1 2000, was another milestone on the road to a nationally consistent legal framework for electronic commerce in the United States. It joined the versions that had been adopted or were to be adopted in the individual states of the United States.

ESIGN and UETA apply to transactions among individuals, businesses, and governments[96]; ESIGN only applies to transactions "in or affecting interstate or foreign commerce". Consistently with what has previously been said, both statutes provide - with numerous exceptions - that electronic contracts, signatures and other transactional records "may not be denied legal effect, validity, or enforceability" solely because they are in electronic form. ESIGN is essentially a federal version of UETA. ESIGN can preempt UETA in some situations.[97] Both texts contain provisions of a technical and declaratory nature similar to the UNCITRAL Model Law on Electronic Commerce and the

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94 See the website of Baker & McKenzie: http://www.bmck.com/ecommerce/uetacomp.htm.

95 This is the question of availability of terms which is examined more closely *infra*.

96 Cf. the UNCITRAL Model Law on Electronic Commerce, which is solely concerned with the development of trade and commerce in the private sector; government records are not within its sphere (Gabriel, p. 9).

97 See Smedinghoff 2002, p. 7.

UNCITRAL Model Law on Electronic Signatures.[98] On other matters, UETA and ESIGN refer to other State laws. It has been said that "UETA was drafted to displace as little existing state law as possible and to further the idea that electronic media is on a legal par with paper".[99] ESIGN applies to consumer transactions only under very rigid conditions. However, ESIGN contains certain consumer safeguards provisions that require all critical notices, such as insurance or mortgage cancellations, court orders, product recalls or hazardous material shipments to be on paper.[100]

Both UETA and ESIGN exclude, in identical language, Articles 3-9 of the Uniform Commercial Code, as enacted in any state. Thus neither statute affects paper-based negotiable instruments or rules governing letters of credit.[101]

Both statutes create, however, the concept of ´transferable records´. The provisions of UETA are broader in scope, applying to all documents which would, if on paper, be either promissory notes under UCC Article 3 or documents of title under UCC Article 7, whereas ESIGN solely addresses promissory notes. ESIGN permits the real estate finance industry to take steps to establish an electronic market in debt instruments.[102]

The electronic commerce legislation of the United States generally leaves substantive aspects of contract law to the Uniform Commercial Code. However, the Uniform Computer Information Transactions Act (UCITA) was developed because it was felt that the approach of the ´sale of goods´ transactions embodied in the Uniform Commercial Code was not adequate to address the way in which technology services and items such as software were being sold.[103]

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98 Both acts reinforce the definition of ´signed´ in the Uniform Commercial Code as including ´any symbol´so long as it is executed or adopted by a party with present intention to authenticate a writing". To be enforceable under US law, both E-SIGN and UETA require that an electronic signature possess three elements: it must be a sound, symbol or process; it must be attached or logically associated with an electronic record; and it must be made with the intent to sign the electronic record. Electronic signatures that meet these requirements are considered legally enforceable as substitutes for handwritten signatures for most transactions in the US. Case law shows that even a name typed at the end of an e-mail message by the sender may suffice. (Smedinghoff 2002, p. 12 referring to Shattuck v. Klotzbach, 2001 Mass. Super. LEXIS 642 (December 11, 2001) Furthermore, US law allows a mouse click on an ´I accept´ button on the screen to constitute a signature (Smedinghoff 2002 p. 13 compares this to the definition of a signature in Article 2(1) the EC Directive 1999/93 which requires that the signature constitutes ´data in electronic form´). Operationally, however, the needs of authentication and integrity may require more sophisticated methods of electronic signature than those simply satisfying the formal requirements of signature.

99 Brumfield Fry, p. 4.

100 Baker & McKenzie, E-Law Alert, USA: Electronic Signatures in Global and National Commerce Act, p 1, at http://www.bmck.com/ecommerce/E-SIGN_Act.htm.

101 UCC Article 5 on documentary credits is generally subordinate to contractual arrangements in the form of the Uniform Customs and Practice for Documentary Credits, which are now supplemented by the eUCP (see Chapter VII, *post*). Thus, the ´electronisation´ of documentary credits takes place contractually, which is not limited by the UCC. Moreover, a ´document´ may be in "written or other medium permitted by the letter of credit or ...by a standard practice..." A document may not be oral.

102 Brumfelt Fry, p. 5. On transferable records, see Chapter VI.3.3., *post*.

103 A/CN.9/WG.IV/WP.91, Note by the Secretariat, Working Group IV (Electronic Commerce), United Nations Commission on International Trade Law, Thirty-eighth session, New York, 12-13 March 2001.

In any case, the Uniform Commercial Code has been the object of revision regarding aspects of electronic commerce.[104] This illustrates how electronic contract law may eventually amalgamate into other commercial law, although it is initially drafted as particular legislation.

It has to be stressed that the United States has built its legislation largely on the example given by the UNCITRAL Model Law on Electronic Commerce. In addition, the US has advocated wider international regulation based on the Model Law. According to the programme of action called *Framework for Global Electronic Commerce* put forward by the Clinton administration in the late 1990s, an international model law entitled ´Uniform Commercial Code for Electronic Commerce´ should have been written and passed within two years.[105] Although this time has lapsed, UNCITRAL Working Party IV is currently discussing a draft model law on electronic contracting. Apparently no link exists between the two projects.

IV.5.7 An evaluation of electronic signatures legislation

Electronic signature legislation has been divided into two opposite categories.[106] Minimalist legislation indicates only the general nature of the results to be achieved in using electronic documents, leaving the details to the parties and to the circumstances. In the minimalist approach, the context of the signature is more important for its legal effect than the physical characteristics of the signature itself. The second, opposite approach is to spell out in detail the technology or how at least the technology is to work to create legal effects.[107] This approach stresses the security and integrity of electronic records, and builds on the possibility of using a third party to authenticate an electronic signature. A minimalist approach puts a lot of responsibility particularly on a relying party to decide what kinds of electronic signatures they will accept and for what purposes. The relying party generally bears the risk. On the other hand, advanced electronic signatures are costly.[108]

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104 See Revision of Uniform Commercial Code Article 2 – Sales, National Conference of Commissioners on Uniform State Laws, Draft with Reporter´s Notes, November, 2000, at http://www.upenn.edu/bll/ulc/ucc2/21100.htm, visited on 6.3.2003.

105 Framework for Electronic Commerce, http://www.whitehouse.gov/WH/New/Commerce/read-plain.html, visited in 1997, p. 10.

106 Gregory, Canadian and American Legislation on Electronic Signatures with reflections on the European Union Directive; International Colloquium, Internet law: European and international approaches, 19-20 November 2001, Paris, http://droit-internet-2001.univ-paris1.fr/ve/, visited on 9.3.2003, p. 1.

107 As noted *supra*, the first electronic signature statute in the United States built on the use of digital signatures, i.e. Public Key Infrastructure.

108 See Hindenlang, ´No Remedy for Disappointed Trust – The Liability Regime for Certification Authorities Towards Third Parties Outwith the EC Directive in England and Germany Compared´, The Journal of Information, Law and Technology (JILT), 2002 (1), http://elj,warwick.ac.uk/jilt02-1/hindenlang.html, visited on 12.3.2003. For criticism on the possibilities of electronic signatures in general, see Schneier, Bruce: Secrets & Lies. Digital Security in a Networked World, Wiley & Sons, 2000.

Both approaches are represented in electronic signature legislation, and mixtures exist. Some governments have even been more radical by abolishing the need for signatures altogether or building on closed systems in which parties know each other.[109] Both the United States and Canada have generally preferred a minimalist approach. On the other hand, the UNCITRAL Model Law on Electronic Signatures as well as the EC Directive 1999/93 represent hybrid legislation.

This study will revisit questions of electronic signatures in connection with documentary credits and some trade documents normally presented under them (Chapters VII and VIII, *post*). The law on electronic signatures is very complex, the reason being that legislation purports to be technology neutral and, at the same time, reflects the case-specificity of authenticity standards. An ´advanced electronic signature´ as defined by the EC Directive 1999/93 is only met, if today´s technology is applied, by ´digital signatures´ making use of public key cryptography and infrastructure (PKI).[110] Despite the complications of digital signatures, governments are interested in using them.[111] If introduced generally to international trade and transport, however, the use of digital signatures could be seen as too high and costly a standard for everyday use.

IV.6 The ICC GUIDEC – private guidelines for electronic commerce

It is interesting, in conjunction with the Model Laws and Directives on electronic commerce, to consider a private set of guidelines envisaged as providing guidance for companies, legislators and all relevant circles involved in international trade.

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109 Gregory refers, in connection with the two latter examples, to Ontario, Canada; on this see also Gregory: ´Legal Situation of Electronic Signatures: Ontario Perspective´ (1999), at http://www.euclid.ca/ontsig.html (Gregory's reference 2001).

110 Jos Dumortier in Lodder&Kaspersen, Enapter 3, p. 42. Dumortier mentions that in the framework of EESSI (the European Electronic Signature Standardisation Initiative), a format for advanced electronic signatures, has been described in the ETSI (a standardisation body) technical specification (TS 101 733). This format is based on the existing standard that dominates the e-mail and document security market (Internet specification RFC 2630). It also specifies how time-stamping or trusted archiving services may be used to ensure that the electronic signature remains valid for long periods so that it can later be presented as evidence in case of a dispute. The document defines how the Internet specification RFC 2630 cryptographic message syntax should be used for advanced electronic signatures and defines additional fields and procedures compatible with this syntax to support long term validity. The evidence provided through the use of the ETSI format can prevent the signatory later attempting to deny (in e-commerce terms: to repudiate) having signed a document and can be verified even after the validity of the supporting certificate expires. For recent ETSI standards, see http://www.etsi.org/services_products/freestandard/2004/12-2003_a.htm, visited on 24.9.2004.

111 Gregory, p. 10.

The International Chamber of Commerce published ´a living document´ entitled GUIDEC in 1997. This abbreviation stands for General Usage for International Digitally Ensured Commerce.[112] The proposal to develop international guidelines was put forward within the ICC in 1995 in the context of the organisation´s exploratory work concerning the legal aspects of electronic commerce and on the possibility of establishing an international chain of registration and certification authorities.[113]

The GUIDEC was first published in 1997 and its function is stated to be to "draw together the key elements involved in electronic commerce, to serve as an indicator of terms and an exposition of the general background to the issue". One of the main novelties introduced by the GUIDEC was the replacement of the words ´digital signature´ and ´authentication´ by adopting a specific term ´ensure´.[114]

The first version of GUIDEC aimed to draw together the key elements involved in electronic commerce to serve as an indicator of terms and an exposition of the general background to the issue.

A new version of the guidelines called GUIDEC II was published on 27 November 2001 "to take account of the most recent technological and legal developments". Separate chapters are devoted to electronic contracting and best practices for authentication and certification. Whilst the first GUIDEC set the stage for a principled commercialisation of trust in accordance with business needs, GUIDEC II seeks to do the same for electronic contracting by incorporating principles of fair electronic contracting (abbreviated ´POFEC´)[115].

The purpose of GUIDEC was stated to be "to establish a general framework for the ensuring and certification of digital messages by providing a detailed explanation of ensuring and certification principles, particularly as they relate information system security issues and public key cryptograhic techniques". GUIDEC is organised primarily as an outline for parties involved in public key

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112 It was drafted by the ICC Information Security Working Party, under the auspices of the ICC Electronic Commerce Project (ECP). The ECP is an international multidisciplinary effort to study, facilitate and promote the emerging global emerging ectronic trading system. There were several ICC Commissions participating in the project:

-the Commission on Banking Technique and Practice, Air Transport, Maritime and Surface Transport,

- the Commision on Telecommunications and Information Technologies,

- the Commission on International Commercial Practice, as well as

- the Commission on Financial Services and Insurance.

As noted later, however, the ECP was ultimately amalgamated into the new Commission structure of the ICC.

113 GUIDEC was first drafted and discussed under the name of ´Uniform International Authentication and Certification Practices´ (´UIACP´).

114 The Core Concepts, VI. Glossary of Terms from GUIDEC I defined the term ´ensure´ to mean "to record or adopt a digital seal or symbol associated with a message, with the present intention of identifying oneself with the message". Apparently for this reason, the first GUIDEC did not use the concepts of ´originator´ and ´addressee´, which are used in the UNCITRAL Model Law.

115 GUIDEC II, Chapter Electronic Contracting, p.4.

based systems (meaning ´digital signatures´) but is not technology specific. Thus it could be applied to paper-based as well as other methods of authentication.

GUIDEC II has abandoned the concept ´ensure´ which was, as stated *supra*, introduced by the first version of the GUIDEC to circumvent the different uses of the term ´authenticate´. As said earlier, in the American usage, the term authenticate is often used to denote the act of identifying oneself with a message, but in the European usage ´authenticate´ is more associated with the verification of the signature.[116] GUIDEC II now acknowledges the American version of the term.

GUIDEC is specifically designed to serve in the context of international commercial law and practice between parties operating under the *lex mercatoria*[117]. It attempts to enhance some of the concepts set out in the Digital Signature Guidelines of the Information Security Committee of the Science and Technology Division of the American Bar Association. GUIDEC also "draws upon and extends existing international law treatment of digital signatures in particular...in the UNCITRAL Model Law of Electronic Commerce".

GUIDEC describes the rights and responsibilities of subscribers[118], certifiers[119] and relying parties. Furthermore, it attempts to allocate risk and liability equitably between transacting parties in accordance with existing business practice.

GUIDEC contains 24 definitions, some of which have been referred to in the footnotes of the present study. These are valuable tools for discussions on the subject since a uniform understanding of operative concepts is often almost as important for legal harmonisation as actual harmonised legal rules. For some reason, unfortunately, GUIDEC does not fully consistently build on the terminology used by the UNCITRAL Model Law of Electronic Commerce.

The actual best practices defined in the first GUIDEC were divided into ´ensuring a message´ and ´certification´ (Chapters VII and VIII of the document, respectively).

According to the first point, a message was ensured, as a factual matter, if acceptance evidence indicates the identity of the ensurer and that the message has not been altered since ensured. Ensuring a message may be needed for proceedings in an evidentiary context. The focus of the inquiry is the genuineness of the evidence and its factual linkage to the persons involved in the controversy. It serves often as an indicator of origin. Point 2 stated that "a person must attribute[120] an ensured message to the person who actually ensured the

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116 GUIDEC II, Glossary, p.1

117 The GUIDEC makes, for example, reference to the UNIDROIT Principles of International Commercial Contracts in defining the concept of a ´notice´ (Definition 10).

118 Meaning "a person who is the subject of a certicate" according to Definition 14, The Core Concepts, VI. Glossary of Terms.

119 "A person who issues a certificate, and thereby attests to the accuracy of a fact material to the legal efficacy of the act of another person."

120 The word ´attribute´ means that a person having the ensured message must consider it to be associated with the ensurer in some significant way.

message". Point 3 dealt with the role of an agent in ensuring a message. If an agent ensures a message and represents himself as doing so by authority of a principal, the ensured message is as valid as that of the principal if, under the applicable law[121], the agent had sufficient authority to ensure the message.

IV.7 Regulating electronic contracting

The following fifteen pages will be devoted to describing the legislative efforts that have been taken in the European Union and by UNCITRAL to create rules to govern electronic transactions, contract formation and contracts created by electronic means. This subchapter thereby describes what developments are at the supranational level towards the regulation of electronic contracting. The UNCITRAL Model Law on Electronic Commerce did not complete this task. Its purpose was to create a basic legal infrastructure for electronic commerce. Later legislative efforts either do or not build on it.[122] Moreover, the later legislative efforts deeper into questions of contract formation, and possibly even address to some extent the rights and obligations of the parties in the context of electronic commerce.

The EC Directive on electronic commerce to be presented next focusses, roughly speaking, on enhancing the position of consumers, in addition to addressing the division of tasks between the Member States in the build-up of infrastructure for electronic commerce. The UNCITRAL draft convention on electronic contracting, as I prefer to call it, focusses on business-to-business contracts.

IV.7.1 EC Directive on certain legal aspects of electronic commerce

The Council and the Parliament adopted, in June 2000, a Directive[123] on electronic commerce. The Directive justifies itself in its preamble by serving such needs as the elimination of legal obstacles to the proper functioning of the Internal Market caused by the divergences in legislation and the clarification of the legal uncertainty as to which national rules apply to information society

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121 Although the introduction of GUIDEC states the legal framework to be the *lex mercatoria*, a reference to the applicable law is made.

122 On the US law building on the UNCITRAL Model Law, see Gabriel.

123 Directive 2000/31/EC of the European Parliament and of the Council of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market, OJ L 178, 17.7.2000 p.1.

services Most parts of the Directive apply specifically to the provision of information society services, which limits its relevance somewhat to this study.[124] Furthermore, in order to ensure legal certainty and consumer confidence, the Directive lays down rules to cover certain legal aspects of electronic commerce in the Internal Market. The Directive neither aims to establish additional rules on private international law relating to conflicts nor does it deal with the jurisdiction of courts.

The Directive approximates certain national provisions on information society services relating to the Internal Market, the establishment of service providers, commercial communications, electronic contracts, the liability of intermediaries, codes of conduct, out-of-court dispute settlement, court actions and cooperation between Member States. It is based on the ´Country of Origin´ principle affecting the role of authorities.[125] Attention will be paid here to those aspects more closely relating to contract law. Dispute settlement issues will be dealt with later.

Section 3 of the Directive concerns contracts concluded by electronic means. Article 9(1) provides that Member States shall ensure that their legal system allows for contracts to be concluded by electronic means. Member States shall in particular ensure that the legal requirements applicable to the contractual process neither create obstacles for the use of electronic contracts, nor result in such contracts being deprived of legal effectiveness and validity on account of their having been made by electronic means. There are some exceptions to this obligation: contracts that create or transfer rights in real estate (except for rental rights), contracts requiring by law the involvement of courts, public authorities or professions exercising public authority as well as certain suretyship contracts and contracts governed by family law.

In order to meet this obligation, each Member State is to amend its legislation that contains requirements, in particular requirements as to form,

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124 The Directive defines a ´service provider´ as any natural or legal person providing an information society service. ´Information society services´ are services within the meaning of Article 1(2) of Directive 98/34/EC as amended by Directive 98/48/EC. According to that definition, an ´information society service´ is:

"any Information Society service, that is to say, any service normally provided for remuneration, at a distance, by electronic means and at the individual request of a recipient of services.

For the purposes of this definition:

- ´at a distance´ means that the service is provided without the parties being simultaneously present,

- ´by electronic means´ means that the service is sent initially and received at its destination by means of electronic equipment for the processing (including digital compression) and storage of data, and entirely transmitted, conveyed and received by wire, by radio, by optical means or by other electromagnetic means,

- ´at the individual request of a recipient of services´ means that the service is provided through the transmission of data on individual request."

An indicative list of services not covered by this definition is set out in Annex V of Directive 98/48/EC.

125 On the application of this principle, see Diana Wallis MEP, ´What Links European and International Law – beyond Country of Origin or Destination´, International Colloquium, Internet law: European and international approaches, 19-20 November 2001, Paris, http://droit-internet-2001.univ-paris1.fr/ve/, visited on 9.3.2003.

which are likely to curb the use of contracts by electronic means, as stated in Recital 34 of the Directive. This recital mentions further that the examination of the legislation requiring such adjustment should be systematic and should cover all the necessary stages and acts of the contractual process, including the filing of the contract. The Directive does not go into detail, or refer for instance to the UNCITRAL Model Law on Electronic Commerce, in giving this task to the Member States.

As the predominant part of contract law, especially that relating to contract formation, is regulated by national law, Member States shall decide on their own which parts of their legislation need revision or amendments. At the least this would require having provisions such as those making electronic records admissible as evidence and that give them the same status as paper documents, unless these things were obvious from the outset. Each legal system may have its own approach. The result of this amendment should be to make contracts concluded electronically workable.

The focus of the Directive is on building consumer confidence. Therefore it lays down requirements for the service provider to give information about the conclusion of a contract clearly, comprehensibly and unambiguously, prior to the order being placed by the recipent of the service.[126] This information includes the technical steps to be followed in order to conclude the contract, whether or not the concluded contract will be filed by the service provider and whether it will be accessible, the technical means for identifying and correcting input errors prior to the placing of the order and the languages offered for the conclusion of the contract. Furthermore, the service provider shall indicate any relevant codes of conduct to which he subscribes and information on how those codes can be consulted electronically.

These rules are not applied when two parties who are not consumers agree otherwise. Neither do they apply to contracts concluded through the use of electronic mail.

In Article 10(3), however, there is a requirement which covers business-to-business relationships and the use of electronic mail: contract terms and general conditions provided to the recipient must be made available in a way that allows him to store and reproduce them. This concerns, like the above requirements, the contract between the service provider and the recipient of the information society services, and not the relationship between commercial partners using the Web to conclude their contracts. The parties may obviously need to use the services of an information society service provider to conclude a contract or to perform their obligations thereunder.

Article 11 of the Directive contains provisions[127] as to the placing of the order to obtain information society services. These provisions apply mainly to

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126 Article 10 of the Directive.

127 The service provider has to acknowledge the receipt of the recipient´s order without undue delay and by electronic means. The order and the acknowledgement of receipt are deemed to be received when the parties to whom they are addressed are able to access them. The service provider must make available to the recipient of the service appropriate, effective and accessible technical means allowing him to identify and correct input errors prior to the placing of the order. These provisions do not apply to contracts concluded exclusively by exchange of electronic mail.

consumers and do not have a direct bearing on contracts of sale of tangible goods concluded on the net. However, the Article is important because it establishes an ´accessibility´ requirement by stating that an order and the acknowledgement of receipt are deemed to be received when the parties to whom they are addressed are able to access them.[128]

One of the provisions of great significance for the emergence of the new information services industry is Section 4 on the liability of intermediary service providers. Article 12 bears the straigthforward title ´Mere conduit´ to indicate the role that intermediary service providers have under this legislation. The Article states namely that where an information society service that consists of the transmission in a communication network of information provided by a recipient of the service or the provision of access to a communication network, Member States shall ensure that the service provider is not liable for the information transmitted, on condition that the provider does not initiate the transmission, does not select the receiver of the transmission, and does not select or modify the information contained in the transmission. Transmission and provision of access are said to include the automatic, intermediate and transient storage of the information transmitted in so far as this takes place for the sole purpose of carrying out the transmission in the communication network, and provided that the information is not stored for any period longer than is reasonably necessary for the transmission.

Neither is an intermediary service provider liable for ´caching´ - the automatic, intermediate and temporary storage of that information, performed for the sole purpose of making the information´s onward transmission to other recipients of the service upon their request more efficient (Article 13).[129] This exemption applies with a number of conditions.[130]

Where an intermediary service provider stores information provided by a recipient of the service on a more permanent basis (´hosting´, Article 14), the service provider is not liable for the information stored at the request of a recipient of the service, on condition that the provider does not have actual knowledge of illegal activity or information and, as regards claims for damages, is not aware of facts or circumstances from which the illegal activity or information is apparent. Moreover, an intermediary service provider is not liable where the provider, upon obtaining such knowledge or awareness, acts expeditiously to

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128 The Directive does not make any distinction between designated and non-designated systems as does the UNCITRAL Model Law, see *supra*.

129 Caching improves the performance of the network by reproducing the information in servers closer to the final user (therefore avoiding having to make the connection to the server where the original site is located every time a user request´s access) In view of increasing traffic and limited bandwidth availability, the Internet might effectively collapse without caching.

130 These conditions include the following assumptions: that the provider does not modify the information, that the provider complies with the conditions on access to the information, that the provider complies with rules regarding the updating of the information specified in a manner widely recognised and used by the industry, and that the provider acts expeditiously to remove or disable access to the information it has stored upon obtaining actual knowledge of the fact that the information at the initial source of the transmission has been removed from the network or access to it has been disabled or that a court or an administrative authority has ordered such removal or disablement.

remove or to disable access to the information. This exoneration does not apply when the recipient of the information society service is acting under the authority or the control of the provider.

The above provisions regarding an intermediary service provider´s liability concern liability for the information transmitted or stored. They do not deal other types of liability, for example liability for damage created by system malfunction. As stated earlier, information carriers regularly limit or exclude their liability, at least in cases where there is no negligence on their side.

One of the most significant ideas of the Directive in my view is its emphasis on the role of codes of conduct.[131] Article 16 obliges Member States and the Commission to encourage the drawing up of codes of conduct at Community level by trade, professional and consumer associations or organisations, designed to contribute to the proper implementation of the relevant articles of the Directive. Article 16 contains, in addition, some practical duties to this end. In a rapidly evolving environment, private codes of conduct as well as private rules of reference and model contracts are a quick and flexible method to provide the regulation and guidance required by the business community.

One can conclude that perhaps the most significant contribution of the Directive may be the imperative to introduce functional equivalence between electronic and other, usually paper-based, contracts. Functional equivalence, i.e. full equation, is not mentioned though, although one can infer it. The Community seems to refrain from producing the first 'layer´ of technical communication legislation beyond electronic signatures.[132] It would have apparently been impossible to reach agreement on the Directive should it have interfered with the sphere of private laws of the Member States. Member States evaluate what measures need be taken to implement the obligations of the Directive. It would be therefore useful to stress the importance of the attempts to reach unification on an international level under the auspices of UNCITRAL. This would especially entail attempts to create uniformity in the contract formation of electronic contracts, see *infra*. Could this become a milestone in the creation of harmonised civil law within the European Union? Most Member States already subscribe to Part II of the CISG.

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131 Codes of conduct are typical instruments of ´soft law´, which has a recognised status in Community law and in public international law. For the origin of the concept and the role of soft law in Community law, see K.C.Wellens and G.M. Borchart, Soft Law in European Community Law, European Law Review, Vol 14 No 5 October 1989, p. 267-321. The term is increasingly used in the private law context; a recent ICC/UNIDROIT seminar ´Hard Law/Soft Law´ serves as an example; see also Wilhelmsson, Ole Landon kyydissä kohti eurooppalaista sopimusoikeutta, Defensor Legis No 3/2000, p. 449 regarding the UNIDROIT Principles for International Commercial Contracts as norms of soft law.

An example of codes of conduct is the ´European Code of Conduct for On-Line Commercial Relations´ adopted by EuroCommerce in April 2000. EuroCommerce is the European central organisation for the retail and wholesale industry and has its seat in Brussels. Another Trans-European code of conduct has been drafted for the insurance industry.

For codes of conduct and self-regulation generally, see Chapter X.1.4., post.

132 Recital 34 of the Directive makes a gesture in this direction by stating that it is possible that the acknowledgement of receipt by a service provider may take the form of the online provision paid for. This is still an infrastructural rather than a contractual matter.

IV.7.2 UNCITRAL draft convention on electronic contracting

It is useful to overview the legislative work constantly being carried out by UNCITRAL to see what hangs in the air as regards the forthcoming regulation of electronic contracts at the time of the finalisation of this study in the mid 2004. Although the drafting process is still under way, the discussions are very useful in showing the direction, in which electronic commerce regulation is heading.[133]

At the time UNCITRAL was close to finalising the Model Law on Electronic Signatures, several ideas relating to the future of electronic commerce legislation emerged.[134] At the thirty-third session of the Commission held in 2000 there was a preliminary exchange of views regarding future work in the field of electronic commerce. The Commission focused its attention on three topics. The first deals with electronic contracting considered from the perspective of the CISG.[135] The second topic was online dispute settlement and the third was the dematerialisation of documents of title, in particular in the transport industry.[136] No decision was taken though before the relevant Working Group had examined the topics with a view to making more detailed proposals on the future work.

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133 The most recent documents available indicate that the draft Convention would be ready for adoption in 2005. It is expected that the convention would take shape when Working Party IV (Electronic commerce) meets in October 2004.

134 Note by the Secretariat, doc A/CN.9/WG.IV/WP.95, United Nations Commission on International Trade Law, Working Group IV (Electronic Commerce), thirty-ninth session, New York, 11-15 March 2002.

Support was expressed, at the thirty-second session of the Commission in 1999, for the preparation of an omnibus protocol to amend multilateral treaty regimes to facilitate an increased use of electronic commerce. This idea was based on a recommendation adopted on 15 March 1999 by the Centre for the Facilitation of Procedures and Practices for Administration, Commerce and Transport (CEFACT) of the United Nations Economic Commission for Europe (UNECE). That text recommended that UNCITRAL consider actions necessary to ensure that references to ´writing´, ´signature´ and ´document´ in conventions and agreements relating to international trade allowed for the use of electronic equivalents.

Other items suggested for future work included:

- electronic transactional and contract law,
- electronic transfer of rights in tangible goods,
- electronic transfer of intangible rights,
- rights in electronic data and software (possibly in cooperation with the World Intellectual Property Organisation (WIPO)),
- standard terms for electronic contracting (possibly in cooperation with the International Chamber of Commerce ICC and the Internet Law and Policy Forum (ILPF)),
- applicable law and jurisdiction (possibly in cooperation with the Hague Conference on Private International Law), and
- online dispute settlement systems

135 See doc. A/CN.9/WG.IV/WP.91, Possible future work in the field of electronic contracting: an analysis of the United Nations Convention on Contracts for the International Sale of Goods, Working Group on Electronic Commerce,thirty-eighth session, New York, 12-13 March 2001, Legal aspects of electronic commerce, Note by the Secretariat.

136 For online dispute settlement, see Chapter IX, *post*. For the work not yet really commenced concerning the dematerialisation of documents of title, see Chapters V.8. and VIII.10. and 11., *post*. Examples of the dematerialiasation of documents of title functions created on private terms are the Bolero System and TEDI in Japan, see Chapters VIII.7.1. and 7.4., *post*.

The Working Group came to the conclusion that work towards the preparation of an international instrument dealing with certain issues in electronic contracting be commenced on a priority basis. Three other topics[137] considered by the Working Group also deserved, in its view, further examination. The recommendations of the Working Group were then endorsed by the Commission at its thirty-fourth session in 2001.

The Working Group has commenced work on a preliminary draft of an international convention on electronic contracting.[138] The Working Group took the view that the form of the instrument to be prepared could be that of a ´stand-alone convention´ dealing broadly with the issues of contract formation in electronic commerce.[139] Although the text is still a preliminary draft, and should be examined with caution, it is interesting and worthwile to have a look at the problems and issues as well as the approach suggested in the Note by the

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137 These topics were in liberal order:

- a further study of the issues related to the transfer of rights, in particular, rights in tangible goods, by electronic means and mechanisms for publicising and keeping a record of acts of transfer or the creation of security interests in such goods,

- a comprehensive survey of possible legal barriers to the development of electronic commerce in international instruments, including, but not limited to, those instruments mentioned in the CEFACT survey, and

- a study discussing the UNCITRAL Model Law on International Commercial Arbitration, as well as the UNCITRAL Arbitration Rules, to assess their appropriateness for meeting the specific needs of online arbitration.

138 The draft bears the title

Preliminary draft convention on international contracts concluded or evidenced by data messages (this study uses simply ´draft convention on electronic contracting´ for reasons of convenience) and was first contained in Annex I of the Note of the Secretariat for UNCITRAL Working Group IV (Electronic Commerce), thirty-ninth session, New York, 11-15 March 2002, A/CN.9/WG.IV/WP.95, 20.9.2001. The draft Convention is prepared by the Secretatiat of UNCITRAL following the deliberations in the Working Group during its previous sessions. Revised texts of the preliminary draft convention were prepared by the Secretariat

1) for the forty-first session of the Working Group in New York, 5-9 May 2003, A/CN.9/WG.IV/WP.100.

2) for the forty-second session of the Working Group in Vienna 17-21 November 2003, A/CN.9/WG.IV/WP.103

3)

139 Report of the Working Group on the work of its thirty-eighth session, New York, 12-23 March 2001, A/CN/9/484, para 124.

The plans of the Working Group to create a convention to regulate electronic contracting, as reported by the Note of the Secretariat, have already been commented on by the International Chamber of Commerce, which is contributing to the work of UNCITRAL substantially, but which is itself also one of the ´formulating agencies´ of international commercial law in the form of its uniform rules of reference and model contracts.

The ICC would like to see party autonomy anchored in the convention in the manner it is in the CISG. The interaction between the envisaged electronic commerce Convention and the CISG should be clarified.

The ICC argues that as many contracts are concluded by a mixture of oral conversations, telefaxes, paper contracts, e-mails and web-communication “there is reason to consider having the convention address the applicable legal issues in a media-neutral way”. The ICC agrees, however, with the idea of excluding consumer contracts. >>

Secretariat, as this is thought to be very representative for the state of play in the world at present regarding electronic contracting issues.

In order to define a scope for a legal text, thought has to be given to the type of transactions the law is addressed to. At this stage, no express definition of electronic contracting is provided, but the Working Group has used this notion regarding the formation of contracts by means of electronic communications or ´data messages´ within the meaning of Article 2(a) of the UNCITRAL Model Law on Electronic Commerce. ´Electronic contracting´ is regarded as "a method for forming agreements, not a subset based upon any specialised subject-matter".[140]

Electronic contracts are, as reflected in the report, not fundamentally different from paper-based contracts. Nevertheless, the opinion is expressed that electronic commerce does not fully reproduce the contracting patterns used in contract formation through more traditional means and that some adaptation of traditional rules on contract formation may be needed to accommodate the needs of electronic commerce. The formation of contracts would not include questions relating to the validity of contracts and the legal capacity of the parties.

The Working Group seems to be willing to refrain from dealing with the substantive elements of offer and acceptance or the mutual rights and obligations of the parties under the contract. Substantive law issues would be covered by the applicable law or rules of law.

The Working Group instrument does not limit itself to international sales of tangible goods, but covers any contract "concluded or evidenced by electronic means". It would not cover, however, consumer contracts or contracts relating to the grant of limited use of intellectual property rights[141]. The parties could

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<< The ICC later suggested that it would first, before any convention is concluded, draft a business self-regulatory instrument, which would be either 1) a guidance document, 2) a set of uniform customs and practices, which businesses could incorporate into their contracts, or 3) model clauses or contracts to be used in the electronic medium. The ICC has doubts about the overall feasibility of a convention at this stage, given the rapid developments of electronic contracting practices. The ICC has preliminarily identified the following problem areas:

- When does an offer "reach" the offeree?
- Form requirements as to various notices to be given during transactions
- Mistake risks in an electronic environment.

(The ICC adopted in June 2004 the ´E-Terms 2004´, see *infra)*.

UNCITRAL Working Group IV (Electronic Commerce), thirty-ninth session, New York, 11-15 March 2002, Note by the Secretariat, Comments by the International Chamber of Commerce, doc A/CN.9/WG.IV/WP.96; and Note by the Secretariat containing the ICC task force comments on the draft Convention prepared by the Secretariat for the forty-first session of the Working Group on 5-9 May 2003, doc A/CN.9/WG.IV/WP.101.

See also the Standards and Procedures for Electronic Records and Signatures (SpeRS at http://www.spers.org, visited on 12.9.2003) which has been created in the summer of 2003 by the Electronic Financial Services Counsel (at http://www.efscouncil.org, visited on 12.9.2003).

140 Note by the Secretariat, doc. A/CN.9/WG.IV/WP.95.

141 As referred to by the Working Group as ´licencing contracts´. Not all members of the Working Group agree on the exclusion of these contracts, since the draft convention concerns only contract formation related issues.

incorporate the Convention even if no other connecting factor nor the rules of private international law makes it applicable.[142]

The main rule, however, is that the draft Convention would apply to contracts involving the use of data messages between parties whose places of business are in different states.[143] Article 7 of the draft adds that a party has to indicate his place of business, which can be rebutted.

Article 7(4) of the draft contains a rule according to which the place of the server is irrelevant as regards the place of business.[144] Furthermore, the sole fact that a person makes use of a domain name or e-mail address connected to a specific country does not create a presumption that its place of business is located in such country (Article 7(5)). The UNCITRAL Secretariat has produced a Note analyzing issues relating to the location of the parties.[145]

The issues relating to contract formation could be divided, according to the report, into two categories. One is merely defining the functional equivalence for an invitation to treat as compared to an offer, the timing of communications and the receipt and dispatch of the offer and the acceptance. The second category

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142 The same possibility is granted in Article 1(2) of the UN Convention on Independent Guarantees and Stand-by Letters of Credit. This possibility has significance in arbitration which would generally respect such inncorporation.

As regards ordinary court procedures, this provision has significance e.g. where enforcement of the contract is sought in the courts of a country which is a party to the Convention and the Convention would not be applicable to the contract without incorporation. The courts would thereby generally give the Convention the status of law, although it might have to give way to the mandatory provisions of otherwise applicable law. If the country of enforcement is not a party to the Convention, its courts may still uphold a contractual reference although the provisions of the Convention may not receive the same status as the law does. Again, the mandatory rules of the (otherwise) applicable law may come into application. Furthermore, procedural implications may follow: in English procedure, "foreign" law is generally a matter of fact to be shown by the parties, not law supposed to be known by the judge. It is supposed that a convention incorporated contractually would generally receive this type of status in many jurisdictions.

It should always possible to incorporate international instruments, whether conventions or private sets of rules such as the UNIDROIT Principles for International Commercial Contracts (see Chapter X.4.2., *post*), into private contracts. In the transport world, the famous ´Clause Paramount´ (see Chapter VI.1.3.5., *post*) is an example of how an international convention (the Brussels Convention concerning bills of lading) is incorporated directly, i.e. not necessarily through a domestic law, into a contract. It depends on the *lex causae* as well as on the method of dispute settlement to what extent such incorporation will be respected, and whether such a choice can supersede even its mandatory provisions.

143 Doc A/CN.9/WG.IV/WP.103, p. 3. The wordings as to the communications and contracting are still highly in dispute.

One more possibility offered is that the private international law leads to the application of the law of a contracting state.

144 Therefore the *´lex loci server´* does not apply. The draft Article reads in its most recent form: "The place of location of the equipment and technology supporting an information system used by a legal entity for the conclusion of a contract or a place from which such information system may be accessed by other persons, in and of themselves, does not constitute a place of business [unless such legal entity does not have a place of business [within the meaning of article 5(j)]]". This corresponds to recital 19 of the EC directive 31/2000 on electronic commerce.

145 Doc A/CN.9/WG.IV/WP.104

includes questions such as the treatment of fully automated systems in electronic commerce as well as questions as to what additional rights and obligations the parties using such systems might have.

IV.7.2.1 Can the CISG be used as a foundation?

The Working Group has chosen, at least in its current draft Convention text, to follow the rules on the formation of contracts laid down in Chapter II of the CISG. This Convention applies to contracts of sale only with some exceptions relating to the subject matter sold, whereas the instrument contemplated by the Working Group would extend to all contracts concluded or evidenced by means of data messages, with the notable exception of consumer contracts. Software and licences relating thereto seem to be a grey area in both instruments.

It has to be noted, however, that the principles contained in the Sales Convention have been accepted as being useful beyond the scope of the Convention. An example of this is that they have been used as models for the UNIDROIT Principles of International Commercial Contracts.

In 2001, the Secretariat of UNCITRAL produced an analysis[146] examining the CISG in the light of electronic commerce. The general outcome of the analysis was that the rules of the Convention are, in general terms, also suitable for contracts concluded electronically. However, some of the rules, such as those relating to the effectiveness of communications, may need to be adapted to an electronic system. For instance, Article 20(1) of the Convention states that the "period of time of acceptance fixed by the offeror in a telegram or a letter begins to run from the moment the telegram is handed in for dispatch or from the date shown on the letter or, if no such date is shown, from the date shown on the envelope" whereas the "period of time for acceptance fixed by the offeror by telephone, telex or other means of instantaneous communication, begins to run from the moment that the offer reaches the offeree". It is not obvious whether electronic communications are to be regarded the equivalent of letters or telegrams or whether electronic messages are instantaneous communication.

For some questions, the analysis suggests creating, at least as an alternative, provisions to amend or interpret the Convention in the use of electronic contracting. An example is the definition of the place of business of a party to determine whether the contract in question falls under the scope of the Convention.

Similar conclusions were made already in 1999 by *Eiselen*[147] who thought that "the Convention and its underlying principles are sufficiently robust and flexible to deal with these changes and challenges posed by the new forms of communication and that virtually no change need be made to the Convention" and that "the CISG is a coherent and logical body of law able to to survive and grow in the modern world".

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146 A/CN.9/WG.IV/WP.91.

147 Eiselen, p. 13.

IV.7.2.2 A new set of rules for contract formation?

The solution contemplated in the initial Note by the Secretariat[148] is to produce an additional layer[149] of rules relating strictly to contract formation in the context of electronic commerce concluded through an exchange of electronic messages, and not to reproduce any rules of the Sales Convention especially with any substantive content.[150] In one meeting report[151] of the Working Group on Electronic Commerce, solutions for issues not dealt with in earlier legislative instruments are considered possible, although "every effort should be made to avoid interfering unduly with the legal regime established by those instruments, in particular the UN Sales Convention...".

One of the rules that could be considered important in view of the Secretariat´s note would be a definition as to the time of contract formation. In the early drafts for the Convention, a contract is stated to be concluded at the moment when the acceptance of an offer becomes effective. An offer becomes effective when it is received by the offeree, and an acceptance of an offer becomes effective at the moment the indication of an assent is received by the offeror.[152] The main rule contained in the CISG is that both the offer and the acceptance become effective upon their receipt, more exactly "when they reach the (addressee)".[153] The solution offered in the draft Convention is to back up Article 24 of the CISG with the principles contained in Article 15 of the UNCITRAL Model Law on Electronic Commerce which deals with the time and place of the dispatch and receipt of the data message. The outcome is to be found

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148 A/CN.9/WG.IV/WP.95, paras. 10-12 and 49-52.

149 Author´s own description. All provisions contained in the draft convention in its reported form are not novelties however, since the Working Group is considering reiterating some provisions of the Model Law on Electronic Commerce and Model Law on Electronic Signatures.

150 For instance, criteria as to when a declaration of will can be considered an offer or an acceptance, Articles 14 and 18 of the CISG. These are objective contract formation criteria, in addition to which contract law contains more subjective, ´cognitive´ elements.

151 A/CN.9/509 United Nations Commission on International Trade Law, Thirty fifth session, New York, 17-28 June 2002, Report of the Working Group on Electronic Commerce on its thirty-ninth session (New York, 11-15 March, 2002), para. 27.

152 Draft Article 8, Doc A/CN.9/WG.IV/WP.95, p. 29. There appears to be much criticism against this provision (as evidenced in Doc A/CN.9/528, para. 103). Article 13 as contained in Doc A/CN.9/WG.IV/WP.103 deals with contract formation. Article 13(2) provides two options:

Variant A: "When conveyed in the form of data message, an offer and the acceptance of an offer become effective when they are received by the addressee"; and

Variant B: "Where the law of a Contracting State attaches consequences to the moment in which an offer or an acceptance of an offer reaches the offeror or the offeree, and a data message is used to convey such offer or acceptance, the data message is deemed to reach the offeror or the offeree when it is received by the offeror or the offeree."

I would personally prefer to retain variant A since the reception rule is well-established in electronic commerce. See also the comments in the conclusions of this chapter, *infra*.

153 CISG Article 24 states "for the purposes of this Part of the Convention, an offer, declaration of acceptance ´reaches´ the addressee when it is made orally to him or delivered by any other means to him personally, to his place of business or mailing address". The communication can thus be instantaneous or such that the parties are at a distance.

in draft Article 10 of the suggested instrument. As noted already *supra*, the rule for a designated information system is that receipt occurs when the message enters the system. The draft Article 10(2) builds on this idea but adds a requirement that the message is capable of being retrieved. The message is presumed to be capable of being retrieved "unless it was unreasonable for the originator to have chosen that particular information system for sending the data message, having regard to the circumstances of the case and the content of the data message".[154]

Another reiteration of provisions contained in previous instruments is draft Article 10, which reproduces a rule contained in Article 11 of the UNCITRAL Model Law on Electronic Commerce.

Article 14(1) of the CISG provides that a proposal for concluding a contract that is addressed to one or more specific persons constitutes an offer if it is sufficiently definite and indicates the intention of the offeror to be bound in case of acceptance. This intention is decisive irrespective of the means of communication used. However, Article 14(2) of the CISG lays down a presumption on invitations to treat by providing that a proposal other than one addressed to one or more specific persons is to be considered merely as an invitation to make offers, unless the contrary is clearly indicated by the person making the proposal. This is because the intention to be bound is considered to be lacking.[155]

The Internet makes it possible to address specific information to a virtually unlimited number of persons and current technology permits contracts to be concluded at once. In the view of the Working Group, even advertisements on the Internet would be classified as invitations to treat (draft Article 12(1) of Doc. A/CN.9/WG.IV/WP.103). This rule would apply if a website only offers information about a company and its products, and any contact with potential

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154 A great majority of those some 20 jurisdictions that have implemented the Model Law so far have taken Article 15 almost unmodified. However, the US UETA and the Canadian UECA have modified the above rule so that proper receipt requires that the recipient be able to retrieve the record from the system and that the message be sent in a form that the addressee´s system can process.

Cf. Article 11 of Directive 31/2000/EC on electronic commerce, which requires Member States to ensure that a customer´s order, and the acknowledgement of receipt of the order by the merchant, is deemed to be received at the moment when the parties to whom they are addressed are able to access them. This rule would require the ability the addressee to retrieve the message. It has been pointed out that only the technical possibility of retrieval was relevant, and not the addressee´s availability for retrieving the message. UNCITRAL Doc. A/CN.9/WG.IV/WP.104/Add.2, paras. 26 to 31.

The above cited note by UNCITRAL´s secretariat suggests cautiously (in para, 38) that a presumption of knowledge should be attached to the effective delivery of a message to the addressee´s information system. It would thus be for the addressee to adduce evidence that, through no fault of its own or of any intermediary of its choosing, it could not technically access the message. This language on presumption would make the rule a mixture of the reception and information rules, see Chapter II.7., *ante*.

Cf. also the First Opinion of the CISG Advisory Council and the ICC E-Terms 2004 Article 2, *infra*.

155 Thus advertisements in newspapers or a mere display of goods in shop windows and on self-service shelves are usually regarded as invitations to submit offers.

customers lies outside the electronic medium. Should the website, however, enable the conclusion of a contract through interactive applications, the draft instrument creates, in Article 12(2), the presumption that "unless otherwise indicated by the offeror, the offer of goods or services through automated computer systems allowing the contract to be concluded automatically and without human intervention is presumed to indicate the intention of the offeror to be bound in the case of acceptance."[156]

The Working Group has recently decided to add, as an option, a provision similar to Article 10(1) of Directive 2000/31/EC on Electronic Commerce requiring that a person offering goods or services through information systems accessible to the public should provide means for the storage or printing[157] of the contract terms. This provision is labelled ´availability of contract terms´.[158] In the EC Directive that rule applies between an information society service provider and the user of the information society service. It does not, however, apply between normal traders using electronic communications.

There are a number of issues listed in the Secretariat´s Note that call for attention although these have not so far been reflected as draft provisions in the suggested new instrument. One of them is whether specific rules are required in the context of electronic contracting to clarify the legal regime applicable to agreements reached in ways other than a discernible offer and acceptance.[159]

Other questions of interest that were once listed as items that could be considered by the Working Group are the acceptance and binding effect of contract terms displayed on a video screen but not necessarily expected by a party and the incorporation by reference of contractual clauses accessible through a ´hypertext link´.[160] For incorporation by reference, see further *infra*.

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156 See Note by the UNCITRAL Secretariat: Electronic contracting: background information (Qualification of parties´ intent: offers and invitations to make offers). Note by the Secretariat, A/CN.9/WG.IV/WP.104/Add. 1.

157 Websites cannot easily, as far as I understand, prevent printing of the contents displayed on the screen. Many websites offer, however, the possibility to download or print the text in user friendly form such as the ´.pdf´ form.

158 For the latest version of the provision, see Article doc. A/CN.9/WG.IV/WP.108. For the discussion on it, see doc. A/CN.9/546 paras. 130-135. Some members would like to make the ´making available´ a precondition for the enforceability of the terms, some would like to see the Convention mention that nothing in it requires the terms to be made available.

159 The note concludes that according to a majority of commentators, the CISG covers the agreements reached without resorting to the traditional ´offer-acceptance´ scheme although it does not expressly address them. This matter should therefore "be settled in conformity with the general principles on which it is based" under Article 7(1).

The ICC has expressed its preference for including the text of Article 2(1) of the UNIDROIT Principles of International Commercial Contracts which states that a contract may be concluded either by the acceptance of an offer or by the conduct of the parties that is sufficient to show agreement.

160 Article 15 of the draft A/CN.9/WG.IV/WP.103, page 16, mentions making "the contract terms available to the other party in a way that allows for its or their reproduction". If the text is accessible through a hyperlink, it is normally also available in that way.

IV.7.2.3 The treatment of automated computer systems

Contracts are increasingly formed by or through automated computer systems, which can, within the parameters of their programming, initiate, respond or interact with other parties once they have been activated. These systems are sometimes called ´electronic agents´[161]. The understanding of the UNCITRAL Working Group on Electronic Commerce is that, as a general principle, the person (whether a natural person or a legal entity) on whose behalf a computer was programmed should ultimately be responsible for any message generated by a machine.[162] This should be compatible with the general rule according to which the employer of a tool is responsible for the results obtained by the use of the tool since the tool has no independent will of its own.

A provision has been added to the draft convention to ensure that the actions of automated systems programmed or used by people will bind the user of the system, regardless of whether human review of a particular transaction has occurred.[163] UNCITRAL has already considered the use of automated computer systems in Article 13(2)(b) of its Model Law on Electronic Commerce.

Machines are not as alert about warning a person contracting through them about mistakes or errors as easily as a natural person would be expected to do. Article 16 of the draft Convention deals with errors in electronic communications.[164]

The question of mistakes and errors in contract formation is covered by national law[165], and the UNIDROIT Principles on International Commercial

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161 The term ´agent´, as noted by the UNCITRAL Working Group report, can be used only for purposes of convenience, since there is no analogy between an automated system and a sales agent. The principles of agency law could not therefore become applicable. On electronic agents in the US law, see *supra*.

162 Report of the Working Group at its thirty-eighth session, doc A/CN.9/484.

163 Article 14 (Use of automated information systems for contract formation), of the draft Convention as contained in document A/CN.9/WG.IV/WP.103 is formulated as follows:

"A contract may be formed by the interaction of an automated information system and a person or by the interaction of automated information systems, even if no person reviewed each of the individual actions carried out by such systems or the resulting agreement."

164 There are two variants in Doc. A/CN.9/WG.IV/WP.103, pp. 16-17. Both variants state with nuances that if a person contracting with an automated information system makes an error in a data message, the contract has no legal effect under certain conditions; one of the variants is close to the Canadian UECA. See similar conditions under the US UETA, note 166 *infra*.

165 Such rules may be traditional contract law rules. Finnish contract law, for instance, protects a *bona fide* party relying on a mistake, e.g. a typing error. The existence of *bona fides* means that the person relying on the information neither knew nor ought to have known of the mistake.

In countries where special electronic commerce legislation has been enacted, there may be special rules relating to errors in electronic interchange which can be detected using special security procedures. Section 10(1) of the Uniform Electronic Transaction Act of the United States provides that to the extent that the parties have agreed to use a security procedure to detect changes or errors and one party conformed therewith, but not the other party, and the non-conforming party would have detected the change or error had that party also conformed, the conforming party may avoid the effect of the changed or erroneous electronic record.

Contracts deal with this question to some extent.[166] Some national legislators implementing the UNCITRAL Model Law on Electronic Commerce have included in their laws provisions dealing with errors made by natural persons when dealing with an automated computer system. The Uniform Electronic Commerce Act of Canada and the US Uniform Electronic Transactions Act set forth conditions under which a natural person is not bound in the event that the person made a material error.[167]

As stated earlier, Directive 200/31/EC states in Article 11(2) that a person offering goods or services through automated computer systems shall offer means for correcting errors. It does not, however, deal with the consequences of these errors but leaves that question to be solved by national contract law. The Working Group appears to follow the same path.[168]

But what if an automated system makes mistakes itself? Should these always be at the risk of the person on whose behalf they were programmed and on whose behalf they are operating? The Working Group has recognised that there might be circumstances, such as when an automated system generated erroneous messages in a manner that could not have reasonably been anticipated by the person on whose whose behalf the system was operated. The extent to which a party had control over the software or other technical aspects used in

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166 Article 3.5 (Relevant mistake) of the UNIDROIT Principles provides:

"(1) A party may only avoid the contract for mistake if, when the contract was concluded, the mistake was of such importance that a reasonable person in the same situation as the party in error would only have concluded the contract on materially different terms or would not have concluded it at all if the true state of affairs had been known, and

- the other party made the same mistake, or caused the mistake, or knew or ought to have known of the mistake and it was contrary to reasonable commercial standards of fair dealing to leave the mistaken party in error; or

- the other party had not at the time of avoidance acted in reliance on the contract.

(2) However, a party may not avoid the contract if

- it was grossly negligent in committing the mistake;or

- the mistake relates to a matter in regard to which the risk or mistake was assumed or, having regard to the circumstances, should be borne by the mistaken party."

Article 3.6 (Error in expression or transmission) provides: "An error occurring in the expression or transmission of a declaration is considered to be a mistake of the person from whom the declaration emanated."

167 Section 22 of the Uniform Electronic Commerce Act of Canada; Section 10(2) of the Uniform Electronic Transaction Act of the United States. The latter provides that an individual in an automated transaction may avoid the effect of an electronic record that resulted from an error made by the individual in dealing with the electronic agent of another person if the electronic agent did not provide an opportunity for the prevention or correction of the error, and if, at the time the individual learns of the error, the following conditions are met:

- The individual promptly notifies the other person of the error and that the individual did not intend to be bound by the electronic record received by the other person;

- The individual takes reasonable steps, including steps that conform to the other person´s reasonable instructions, to return to the other person or, if instructed by the other person, to destroy any consideration received as a result of the erroneous electronic record;

- The individual has not used or received any benefit or value from any consideration received from the other person.

168 Note by the Secretariat A/CN.9/548 paras. 14 to 26.

programming an automated computer system could, in the view of the Working Group, be considered to be an element that might be taken into account in reducing the liability of the party on whose behalf the system is working. The extent of liability might also be dependent on the question of to what extent these mistakes could be corrected during the process.[169]

Today´s automated systems work within the structures of their preset programming. However, a question has already been raised by the UNCITRAL Working Group of whether there could one day be ´autonomous computer systems´ where artificial intelligence makes it possible for computers to learn through experience and modify their own programming.[170]

IV.7.3 Adapting the CISG to the electronic age by interpretation

A group of eminent scholars in the field of international trade established in 2003 a ´CISG Advisory Council´ (AC) with German professor Peter *Schlechtriem* as its chairman. The CISG AC is a private initiative which aims at promoting a uniform interpretation of the CISG. The Council is guided by the mandate of Article 7 of the Convention as to the interpretation and application of the Convention with the paramount regard to international character of the Convention and the need to promote uniformity.[171]

The Council does not lay down dogmatic grounds for its authority. However, scholarly opinions are a recognised source of law in many jurisdictions. Even without such recognition in the formal doctrine and practice, scholarly opinions are widely used in dispute settlement, and their impact depends on many factors. Article 7 of the CISG contains a reference to the general principles on which the Convention is based. Obviously the Council consists of many persons who know the drafting history of the Convention and who can testify to the underlying principles and restate them. Moreover, shaping new principles would rival the two existing sets of contract law principles and create confusion.

It is quite clear that analogical interpretation is allowed to be used to fill in gaps in the Convention.[172] For instance, as the first opinion of the Council deals with communication methods which were in existence when the Convention was adopted, it is possible to interpret the provisions of the Convention to cover electronic communications as well.

The ICC has a long-standing tradition of establishing bodies to interpret the instruments it has created. These instruments (e.g. INCOTERMS, UCP, URDG and UNCID) can be categorised as *lex mercatoria* instruments although they are

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169 Note by the Secretariat, Doc A/CN.9/WG.IV/WP.95, para. 78.

170 Ibid., p. 18. For the possibility of consciousness of machines, see the article ´Voidaanko robotille rakentaa tietoinen mieli?´ of Pentti A.O. Haikonen (Nokia Research Center) in Helsingin Sanomat 5 September 2003. Haikonen has also written a book entitled ´The Cognitive Approach to Conscious Machines´(Imprint, Academic, UK, 2003).

171 Mistelis, CISG-AC Publishes First Opinion at http://www.cisg.law.pace.edu/cisg/CISG-AC.html, visited on 2.4.2004.

172 Honnold, §§ 96-102, Eiselen, p. 7.

normally applicable only through incorporation. Interpretations of the UCP and INCOTERMS are issued regularly and are as a rule published in various ways. Such interpretations are normally not the object of incorporation, but give an authoritative view of them. The observance of them can amount to the establishment of a custom.

The first topic to be discussed by the Council was how to interpret the various expressions used by the CISG regarding communications.[173] As noted *supra*, UNCITRAL conducted an analysis of the feasibility of the Convention´s provisions for electronic communications. The draft convention on electronic contracting largely addresses the same issues as the Advisory Council. The Advisory Council does not formally take any position as to the need of a Convention to regulate electronic contracting.

The opinion is based on two working principles, namely those of functional equivalence and the need to establish that there is an agreement between the parties to communicate electronically.[174] The opinion addresses all CISG´s articles which deal with communications between the parties. These articles belong to Part I - Sphere of application and general provisions (articles 11 and 13), to Part II dealing with contract formation (articles 15, 16(1), 17, 18(2), 19(2), 20(1), 21(1), 21(2), 22, 24) as well as the substantive Part III (articles 26, 27, 31, 39, 43, 47, 63, 65, 67, 71, 72, 79, 88(1) and (2). The request was made informally by the ICC, and the Council did not especially address the role of electronic trade documentation in the performance of the contract by the seller. The importance of the opinion warrants closer examination although there is some repetition of what has already been stated.

In the comment part of each individual article-related opinion, reference is made to the corresponding article of the UNCITRAL Model Law on Electronic Commerce. It is not clear whether the AC added these references for the sake of comparison, or whether the Model Law provisions should amend the interpretations of the Council. I read the opinion as derogating from the Model Law in some respects.

The basic rule as to the freedom of form contained in Article 11 applies to electronic communications, and a contract can be concluded by electronic communications. The term ´writing´ includes, in addition to the telegram and telex mentioned in Article 13, any electronic communication retrievable in perceivable form.

In the contract formation Articles 15 to 18, the point of departure of the AC is that the offer, its withdrawal, revocation, or acceptance or rejection, ´reaches´ the addressee, when it enters the addressee´s server. The Model Law talks about an ´information system´ and there are provisions as to the designation of information systems as well as retrieval. In the AC view, a prerequisite for effective communication of the relevant expression of will is that the addressee

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173 CISG-AC Opinion no 1, Electronic Communications under CISG, 15 August 2003, Rapporteur: Professor Christina Ramberg, Gothenburg, Sweden.

174 Jan Ramberg, The First Opinion of CISG Advisory Council, pp. 3-4.
The existence of these principles will be analysed in Chapter X.1.5., *post*.

has consented, expressly or impliedly, to receive electronic communications of that type, in that format and to that address[175].

This requirement of express or implied consent, which also forms part of the draft Convention[176] may be met in several ways. The consent of the addressee may be evident under CISG Article 8, which governs the interpretation of the conduct of the parties. CISG Article 9(1) may also be relevant if the parties have established a practice in their business. Furthermore, CISG Article 9(2) may bring in usages which the parties knew or ought to have known and which in international trade are widely known to, and regularly observed by, parties for contracts of the type involved in the particular trade concerned. The non-retrievability by the addressee due to his internal technical reasons keeps the risk on his side, but the sender bears the risk for erroneous addressing. The term ´notice´ as used by the CISG includes electronic communications as consented to by the addressee. This applies in respect of a variety of articles, many of them in the substantive part of the Convention (sometimes the Convention talks about requests, specifications or other communications, and these enjoy similar treatment following the Opinion).

With regard to CISG Article 18(2) and a couple of other articles, electronical communications can meet the requirements of oral communications with some conditions. The term ´oral´ includes electronically transmitted sound in real time and electronic communications in real time. This important interpretation means that an offer that is transmitted electronically in real time must be accepted immediately unless the circumstances indicate otherwise. The opinion considers chatting[177] in real time over the Internet as instantaneous communication, but e-mail as not.[178] E-mail is generally seen as the functional equivalent of a letter.

The Advisory Council is also discussing a response to the request made by the Association of the Bar of the City of New York Committee on Foreign and Comparative Law to address the question of the parol evidence rule and its relation to the CISG.[179]

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175 The Model Law Article 15 allows parties to designate information systems for the obtaining of messages, but communications can validly be made to other systems and are received when finally retrieved. Obviously the parties can agree on more stringent rules.

See also analyses of CISG Articles 17 and 18 in comparison with the Principles of European Contract Law by Cecila Carrara and Joachim Kuckenburg at http://www.cisg.law.pace.edu/cisg/text/peclcomp17.html, visited on 15.4.2004, and at http://www.cisg.law.pace.edu/cisg/text/peclcomp18.html, visited on 15.4.2004.

176 See Article 8(2) in doc. A/CN.9/WG.IV/WP.108 and doc. A/CN.9/527 para. 108.

177 Chatting is a means of Instant Messaging which allows users to have réal-time keybord conversations with each other. There are basically two standards, the XMPP (Extensible Messaging and Presence Protocol) and SIMPLE (SIP for Instant Messaging and Presence Leverage Extensions; SIP=IETF Session Initiation Protocol). The newer versions of XMPP involve security functions, which make them more interesting for commercial communications. See Nilsson, Instant messaging: business applications and documentary credits, DCI Vol 10 No 3, July-September 2004, pp. 17-18.

178 Cf. Eiselen, p. 8, who considers that since the telex is called an instantaneous method of communication, the same logic can be analogically applied to e-mail, EDI and fax and that these can be considered to be instantaneous as well.

179 Mistelis, CISG-AC Publishes First Opinion.

IV.7.4 Some ICC initiatives

Although legislation on electronic transactions has been created, or is still in the pipeline, the *lex electronica* emerges through contract practice as well. Private law sources such as model contracts for open electronic commerce have been under creation. These are dealt with *infra* in sub-chapter 8.2., but before that I would like to draw attention to some projects and ideas, whether or not they have materialised as ready-made products. This is because sometimes mistakes teach us as much as successes do. Secondly, the time-span has still been relatively too short to see what is ultimately going to work, and what is not.

IV.7.4.1 The ICC ´Uniform Rules and Guidelines for Electronic Trade and Settlement´

In October 1998, the International Chamber of Commerce approached its national committees[180] with a project, the purpose of which was to create ´Rules for Electronic Trade and Settlement´. This project was carried out under the auspices of the ICC Electronic Commerce Project, more particularly its Working Group on Electronic Trade Practices. Although the ICC has now abandoned this project, it is still interesting to learn from what has been reported about it, since the Rules were "intended to apply to the overall electronic process of trade where the entire trade is undertaken electronically".

The first draft[181] contained the draft Rules and trade scenarios. The latter will be examined later together with documentary credits. However, the actual Rules were intended to be applied where they are expressly incorporated within an ´Electronic Agreement´[182], and would have in fact constituted a set of rules comparable to the contents of interchange agreements used in EDI. They contained rules on messaging, message security, confidentiality, recording and storage of messages as well as the validity and formation of contracts (applying the reception rule).

The Rules and the Electronic Agreement would have been governed by the CISG, and to the extent that any issue is not addressed by the CISG, then the law of the country where the seller has its place of business would have applied.[183] Thus, it followed the approach of the ICC Model International Sale Contract. In fact, the draft presumed that the ICC Model Contract would be used as the substantive nucleus of the Electronic Agreement.

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180 The ICC's activities at a national level are conducted through national committees in more than 60 countries representing approximately half of the countries where the ICC has members.

181 ICC Doc ECP WG 1/13, 12/10/1998.

182 Ibid., p. 1. An ´Electronic Agreement´ was set forth to mean a contract entered into through the exchange of electronic messages (defined separately) and concerning one or more electronic trade transactions (also defined separately) where the parties record their agreement to the terms and conditions stated therein, including rights and obligations. This kind of agreement must include at least the value and description of the goods or services as well as the terms of delivery and settlement.

183 The first draft required each party to ensure that the content of an electronic message is not inconsistent with the law of its respective country, the application of which could restrict the content of the communication. Similar provision can be found in the UNCITRAL Model Law on Electronic Commerce.

It is interesting to note that the first draft attempted to combine elements of messaging and contract formation with substantive elements of an Electronic Agreement which was based on the ICC Model Contract. In that way it would have been very much like American trading partner agreements. The Rules contained, in addition to provisions covering contract formation, some other contractual rules such as a *force majeure* clause, as well as a clause interpreting the scope of waivers.

A revised text marked with the words ´final draft´ [184] was produced on the basis of the response in September 1999. That document no longer contained illustrative trade scenarios, and the Electronic Agreement was not described in detail. Apparently the creation of an electronic version of the Model International Sale Contract had in the meantime been separated from this exercise.

Both documents contained rules on what settlement means and how it should be carried out. As defined in both drafts, ´settlement´ means transfer of value, which is the buyer´s task. In the later draft, however, effecting ´settlement´ also included conveying the electronic messages transferring title to the goods. This commercial terminology[185] would not have fitted in with the terminology of the CISG, since the Convention provides that the seller has to ´deliver´ the goods and documents as well as to ´transfer´ property in the goods to the buyer. Using the word ´settlement´ describing both parties´ obligations would be somewhat confusing in a legal context.

The rules were finally never adopted by the ICC. One reason for not finding adequate support for the document is reported to have been that many national committees had questions on the exact purpose of the document.[186] This type of document would, in my view, be useful serving the same purpose as an interchange agreement does in EDI between established trading partners. As the UNCITRAL model legislation remains unincorporated in national law, and is neither formulated, in the first place at least, as practical rules to meet the needs of day-to-day contract formation and communications, there is a need for standard rules for communication to be incorporated into contracts in open e-commerce. The ICC has recently finalised a new instrument entitled the ´ICC E-Terms 2004´, which could serve a similar purpose than the URGETS.

IV.7.4.2 Facilitating incorporating by reference - The ICC E-Terms original

The UNCITRAL Model Law on Electronic Commerce of 1996 was soon amended by adding Article 5*bis* equating incorporation by reference through electronic means by the possibility to use the technique with other methods of

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184 ICC doc ECP 37, 2/9/1999.

185 According to commercial models, a market transaction is divided into several phases: information, negotiation, settlement and after sales (Schmid, B.: Elektronische Märkte, Wirtschaftsinformatik, vol 35 (1993) no 5, p. 467). During the settlement phase, the contract terms agreed upon are fulfilled. Depending on the type of the negotiated product or service as well as the participating partners, the settlement phase can be an initiator of logistical, financial or other transactions. The outcome of this phase is the fulfillment of the contract (Grieger, p. 158).

186 The discussions have been regularly reported in Documentary Credits Insight.

communication. One of the principal proponents of the amendment was the international business community through the International Chamber of Commerce.

The ICC had already practical implications in mind. In 1999, the ICC initiated a project for a repository of terms (´E-terms´) used in electronic contracts. The idea was to make these terms in the ´E-Terms Repository´ available on the ICC website[187] where the accepted terms, having been assigned unique reference numbers, time stamped and digitally signed, would be available to parties for incorporation into electronic contracts. The service was designed with the conviction that "using terms held by a neutral third party vouching for their integrity and authenticity, rather than by one of the contracting parties, greatly enhances legal certainty".[188]

The idea of incorporating legal rules by reference is characteristic of a number of ICC instruments. For instance, the use of trade terms based on INCOTERMS 2000, the use of the model force majeure clause[189], the model retention of title clause[190] for each country and the ICC arbitration clause represent pieces that can be incorporated into contracts, whether electronic or not.

The E-terms were intended to fall under four categories. Firstly, they wwould have included ´proprietary terms´, such as general conditions of an online merchant or service bureau. Secondly, the repository was designed to contain public documents such as the UNCITRAL Model Law on Electronic Commerce. Thirdly, terms of standard e-commerce notices were to be included. These standard notices are promoted with the intention of becoming best practices that facilitate Internet commerce. Finally, the ICC would have promoted its own best practices such as the GUIDEC II or the ICC Guidelines on Advertising and Marketing on the Internet.

The intention of the ICC was to launch the ICC E-Terms Repository with a pilot project in cooperation with a number of user companies. I assume that the project has not been continued in the recent years.[191] In any case, the project is worth noting since they might find use for it elsewhere, for instance, in Internet trading platforms.

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187 The ICC website is http://www.iccwbo.org.

188 ICC Press release ´New service will build confidence in online contracts´, 16.8.1999, http://www.iccwbo.org/home/news_archives/1999/electronic_contacts.asp, visited on 24.9.1999.

189 Force Majeure and Hardship, ICC Publication No 421, Paris 1985, now replaced by ICC Force Majeure Clause 2003/ICC Hardship Clause, ICC Publication No 650, Paris 2003.

190 For such clauses, see Retention of Title (2nd edition), ICC Publication No 501.

191 For documentary credits and related products, the ICC has for some time maintained the ´DEXPRO´, which is an electronic repository of the relevant rules, ICC Banking Commission Opinions as well as journals. It is always possible to classify materials in the repository on the basis of search terms and to reach the relevant laws, rules and case material with one click.

The idea is not novel since, in a similar manner, the rules applicable to Norwegian marine insurance, including laws, conditions and interpretative practice have been collected into one work called a ´Sjøforsikringsplan´.

IV.7.4.3 Increasing the credibility of electronic contracting - POFEC

GUIDEC II of the ICC contains a number of ´Principles of fair electronic contracting (POFEC)´ [192] adopted with a view to set the stage for principled commercialisation of electronic contracting. These principles are merely listed in the document without further elaboration, but are still a valuable contribution to the discussion on electronic contracting systems. In essence, POFEC is similar to the codes of conduct called for by Directive 2000/31/EC, and addressed in more detail in Chapter X.1.4., *post*, but it is more of a guideline than an instrument which companies would expressly adhere to.

According to these principles, and with a view to drafting documents for document processing systems, one should avoid creating situations involving a battle of the forms. Furthermore, one should incorporate external documents sparingly and carefully and avoid any inclusion of inapplicable text. Document type should be used when appropriate, and one should avoid unrecognisable markings on a document. Authenticity should be ensured adequately. Finally, manual intervention and override should be permitted.[193]

Moreover, according to these principles, the legal efficacy of electronic contracting requires addressing how assent is created by a document processing system, how mistakes in a document processing system are dealt with, the availability of the information in human readable form and how information can be used as evidence.

IV.7.4.4 The ICC E-Terms 2004

In June 2004, the ICC adopted a new instrument labelled somewhat confusingly the ICC E-Terms 2004. The present E-Terms are not a repository, but standard terms consisting only of two articles which the parties can incorporate into their contract by reference.[194] The ICC E-Terms 2004 can be seen as a continuation of the URGETS project since in practice the object is the same although the new instrument is much shorter. The prime object is to safeguard the idea that binding contracts can be concluded through electronic means.

According to Article 1 of the E-Terms the parties agree that the use of electronic messages shall create valid and enforceable rights and obligations between them.[195] Furthermore, to the extent permitted under the applicable law, electronic messages shall be admitted as evidence, provided that such electronic

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192 GUIDEC II, Chapter VIII. Principles of fair electronic contracting (POFEC), p. 7.

193 Article 2.21 of the UNIDROIT Principles gives the rule which may be universally accepted that "in case of conflict between a standard term an a term which is not a standard term the latter prevails".

194 The ICC eTerms 2004 will be published on a website, which also contains a parallel product entitled the ´ICC Guide to eContracting´.

195 Cf. Articles 11 to 12 of the UNCITRAL Model Law on Electronic Commerce using a less explicit language as to the parties´ commitments.

messages are sent to addresses and in formats, if any, designated either expressly or implicitly by the addressee.[196] Finally, the parties agree not to challenge the validity of any communication or agreement between them solely on the ground of the use of electronic means, whether or not such use was reviewed by any natural person.

Article 2 of the E-Terms provides that an electronic message is deemed to be dispatched or sent when it enters an information system outside the control of the sender. It is deemed to be received at the time when it enters an information system designated by the addressee. Moreover, when an information system is used other than that designated by the addressee, the electronic message is deemed to be received at the time when the addressee becomes aware of it.[197]

Article 2.3 states further that "for the purposes of this contract, an electronic message is deemed to be dispatched or sent at a place where the sender has its place of business and is deemed to be received at the place where the addresee has its place of business".

The ICC E-Terms 2004 are a skeleton of legal provision that constitute a sound legal regime for electronic contracting and reproduce part of the provisions of the UNCITRAL Model Law on Electronic Commerce, with some deviations indicated in the footnotes.[198]

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196 This provision follows the approach taken by the CISG Advisory Council in its first opinion, *supra*. The benefit of this provision is that it is sufficiently ´mechanical´ and brings therewith legal certainty. However, the existence of an implied consent is sometimes hard to adduce. Moreover, I think that the ICC E-Terms 2004 have taken one step further in requiring the addressee´s consent to the addresses and formats for evidentiary purposes, since the first opinion deals with the legal effects of communications relating to contract formation and various notices required by the CISG. One can argue that the effectiveness of communications in stipulated acts and admissibility in evidence in general are two different things. Many national contract laws impose subjective criteria for the validity of legal acts, and denying all evidentiary value of a notice sent to an undesignated information system would lead to rigid consequences. Cf. also Article 4 of the European Model EDI Agreement, Chapter III.2.4., *ante*, and Articles 5 and 9 of the UNCITRAL Model Law on Electronic Commerce, *supra*.

As regards the stance of the applicable domestic law regarding electronic evidence, I believe that this provision means or should mean mandatory national evidentiary laws (or even *´loi d´application nécessaire´*). There are namely situations where evidentiary requirements of the applicable law may be disregarded. For instance, it is not evident that form requirements for legal acts or the evidentiary value rules of the applicable law are respected in the courts of a different country or in arbitration, especially when the parties´ intention is the opposite, see Chapter II.9., *ante*.

197 These provisions are in line with the UNCITRAL Model Law on Electronic Commerce, with the exception concerning messages sent to an information system not designated by the addressee. In this case the Model Law makes the retrieval of the message by the addressee the critical point, whereas eTerm 2.2. builds on the time when the addressee becomes aware of the message.

I think the UNCITRAL approach should be preferred since communication rules in electronic commerce should be mechanical and be generally based on the *reception theory* rather than on the *information theory*, which involves a cognitive element.

198 It might be in useful to incorporate some other provisions of the Model Law as well, such as Article 13 relating to the attribution of data messages, or Article 5*bis* which equates incorporation by reference through electronic means with incorporation done by other means. Parties could of course agree more specifically, as in the Bolero Rulebook or the TEDI Interchange Agreement, that incorporation by reference be admitted.

The ICC E-Terms 2004 supplement other contract formation rules. Therefore the actual impact of a message´s dispatch or receipt shall be determined by the law applicable to contract formation. This approach is somewhat restrained as compared to the European Model EDI Agreement, which was published ten years earlier, see Chapter II.2.4., *ante*, and which builds on the reception rule as did the drafts for URGETS.

The practical usefulness of a limited set of terms is reduced by the legislative measures to implement the UNCITRAL Model Law on Electronic Commerce or Directive 2000/31/EC on electronic commerce. The contracts being subject to a law or laws allowing electronic contracting do not generally need these provisions, although the E-Terms may slightly help to specify the legal situation. The E-Terms are most useful in jurisdictions, which allow parties to agree on electronic procedures, but where the legal infrastructure is inadequate. Obviously, where the parties intend their contract to be governed by non-state law altogether, the ICC E-Terms 2004 are a useful ingredient of the rules of law.

IV.8 Forming contracts electronically

This study deals generally with the formation of business-to-business contracts concerning the sale of tangible goods. The scope of e-commerce is not, however, limited to contracting. It should be remembered that, while tangible goods are physically delivered to the buyer, electronic communications can be used to carry out the delivery of services or software of which a licence has been acquired by the buyer. The questions relating to electronic delivery are not, however, dealt with in this study.

The movement towards open electronic commerce conducted without the preset interchange agreement referred to earlier has brought electronic commerce into a new era where trade takes place between partners who do not necessarily know each other in advance, and where trust has to be created through third party services in respect of the commercial communication (for instance authentication services) or for the guaranteeing of the payment of the price of the goods.[199]

As soon as national legislation enacting the Model Laws of UNCITRAL or otherwise fulfilling the same tasks is in place, electronic contracting can in principle be effected without any contractual provisions relating to functional equivalence or rules on the formation of contracts. However, since international trade involves, by definition, more than one jurisdiction, the legal framework could be expected to be at least partially inadequate for a long time. Therefore, contractual arrangements should be, in particular when dealing with jurisdictions without an adequate legal framework, more extensive in electronic commerce

[199] A client may be asked to type his credit card number in a blank field in a form contained in a website. As indicated above, there is discussion about whether this can be regarded as an acceptance of an offer (which seems to be the presumption at the moment). In practice, the seller may check the credit card in any case and if it is not valid or its limit cannot cover the price of the purchased goods, the seller rejects the ´acceptance´.

than is the case with traditional paper-based transactions. In some situations, a sheer choice-of-law clause in favour of a jurisdiction well-advanced in electronic commerce issues could suffice.

An ´electronic agreement´ consisting of an offer and acceptance can be made by exchanging e-mails or other forms of electronic messaging such as EDI. An agreement made through the exchange of e-mails is generally as valid as any other agreement, provided the relevant prerequisites (offer, acceptance and intention to be bound as well as, in Anglo-Saxon jurisdictions, consideration) are present.

The way of entering into an electronic agreement throught the Internet is typically to click on the appropriate place on the computer screen after an on-screen licence has been scrolled through by the purchaser. The click or entry onto this area of the screen constitutes an acceptance to be bound by the terms and conditions, and it is after this click that content is downloaded.[200] A web portal may be used to organise the websites of the companies offering their goods for sale through the net. Electronic marketplaces that can be used by several sellers or buyers are a step further away from portals as presented in Chapter II.3.1., *ante*. Electronic marketplaces bring in special contracting techniques such as auctioning. Basic techniques apply in consumer and business-to-business sales, but for the latter the spectre is much wider, starting from the traditional EDI.

Hereafter, some trends and principles are listed to illustrate how forming electronic contracts takes or could take place in practice. The non-exhaustive list omits questions of electronic contracting in special fields such as banking[201] and the public procurement[202] sector, where great steps forward have been or are being taken. No attention will be paid to electronic auctions, which constitute special situations as regards contract formation and sometimes attract questions relating to fair trading practices and competition.

IV.8.1 Party autonomy

Party autonomy is a key principle of the law of international trade. In the facilitation of electronic commerce, it is important to recognise this principle in order to make it possible for the parties to incorporate the necessary provisions for a succesful conclusion of their transaction. This could take place by choosing a jurisdiction with advanced rules on electronic contracting as the law applicable to the contract. The parties could also refer to suitable sets of legal rules which do not constitute a part of the law that would be applicable without such

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200 A ´click-wrap´ contract asks the user to click an area in order to agree to the terms and conditions. The ´click-wrap´ resembles a ´shrink-wrap´, where for instance software licence terms are placed outside a box, the opening of which constitutes acceptance of the terms.

201 See, however Chapters III.2.6., *ante*, and VIII.3. and 4., *post*.

202 The European Union has finalised a legislative package on public procurement, see note 21, supra. Both referenced Directives address ´Dynamic Purchasing Systems´, which essentially means the introduction of electronic procurement. Providing for electronic procurement was namely one of the key objectives of the revision of the public procurement legislation within the EU.

reference. Finally, the parties could build the entire contract on non-state rules of law, often categorised as *lex mercatoria* instruments.

The principle of party autonomy is nowadays recognised throughout the industrialised world, save perhaps the Latin American countries. The principle has found its way into international conventions. Party autonomy in the context of electronic commerce may be understood as relating to form requirements and as to more substantive matters.

The United Nations Sales Convention allows party autonomy by stating in Article 6 that the parties may exclude the application of the Convention or, subject to its Article 12, derogate from or vary the effect of any of its provisions. Article 12, as noted already, relates to form and gives contracting states a right to declare, in accordance with Article 96 of the Convention, that any provisions in Articles 11 and 29 as well as Part II, which establish that no requirement of written form exists, do not apply.[203] Still, the substantive part of the contract may enjoy party autonomy.

The Convention on the Law Applicable to Contractual Obligations concluded in Rome in 1980 provides that where a contract for the sale of goods contains a choice of law clause, the law chosen will apply, except to the extent that the freedom of the choice is restricted by other provisions of the same Convention.[204] The parties´ choice of law to govern their contract need not necessarily be explicit but can also be inferred by the court from the terms of the contract or the circumstances of the case. The Rome Convention permits, however, the choice of a law which has no connection with the contract.[205]

The UNCITRAL draft convention addresses party autonomy in Article 4 which states that "(t)he parties may exclude the application of this Convention or derogate from or vary the effect of any of its provisions..."[206] A general understanding among the drafters seems to be that the principle of party autonomy should not be understood as authorising a party to derogate from mandatory form requirements under national laws or to lower the standards for

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203 Upon ratifying, or acceding to, the Convention, Argentina, Belarus, Chile, Estonia, Hungary, Latvia, Lithuania, Ukraine and the USSR declared, in accordance with the said Articles, 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, would not apply where any party had his place of business in the respective states.

204 The limitation imposed by mandatory laws was mentioned in Chapter II.8., *ante*. See also the 1955 Hague Convention on the Law Applicable to International Sales of Goods (and its revision in 1986) and the Inter-American Convention on the Law Applicable to International Contracts, Art. 11.

Party autonomy is also accepted in the United States, provided at least that the chosen law has some relationship with the parties or the transaction (UCC Section 1-105 for goods, Restatement 2nd for services; see Nimmer, Electronic Contracts: Part I, Computers and Law, April/May 1996, pp. 39-42.

205 Dicey & Morris, The Conflict of Laws, Thirteenth Edition by Lawrence Collins with Specialist Editords, London 2000, Rule 173, 32-064, p. 1219. For the Convention, see also Lando, The EEC Convention on the Law Applicable to Contractual Obligations, Common Market Law Review 24, 2(1987), pp. 159-214.

206 Doc. A/CN.9/WGIV/WP.108, p. 6. See the discussion of the Working Party IV (electronic commerce) regarding this draft article in doc A/CN.9/548, paras. 119 to 124. Exceptions to party autonomy were decided not to be listed in the article.

functional equivalence set out in the convention.[207] The provisions of the convention would be only facilitative and would not affect requirements of special methods of authentication.

IV.8.2 Incorporation by reference

The possibilities for incorporation by reference will expand by the use of the Internet together with relevant commercial rules being stored in public repositories such as the once envisaged ICC E-terms repository or those facilitated by trading platforms. Incorporation by reference in the traditional way could be done by including a relevant abbreviation or noun in the message. In addition, by using the Web, a hypertext link can be established to the relevant set of rules, which are thereby accessible through the Web. The first mentioned situation could be classified as incorporation by reference proper, the second case resembling a situation where the text of the conditions is technically attached to the contract. The UNCITRAL Working Group on Electronic Commerce discusses currently whether to follow the example set by Directive 2000/31/EC in requiring that storage and reproduction of the text incorporated this way has to be made possible.

UNCITRAL and other texts classify contract terms accessible through a hypertext link as being incorporated by reference whereas producing them in a way that allows their storage or printing are categorised as a question of ´making the terms available´. Obviously a text accessible through a link is available for scrutiny whilst storage and printing makes it possible to refer to the terms in dispute situations. I think that there are thus three issues, incorporation of contract terms generally, incorporation by reference, which should have a limited meaning and be restricted to sitations in which the text is not made available to the contracting partner at the exact time of conclusion, and ´making available´, a production which facilitates printing and storage. All these three concepts are technical and must be distinguished from incorporation in substance, which relates to the nature of the terms and may have to meet conscionability requirements.

The acceptability of incorporation by reference is governed by national law unless this gap in the CISG is filled by interpreting the basic provisions of the Convention.[208] More usually, however, national courts fill in the vacuum with judgements based on national law criteria. For instance, in Germany a reference to general conditions is binding for an offeree (i.e. client) only if he can without unreasonable delay familiarise himself with them.[209]

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207 The Working Party is considering allowing Contracting States to make declarations concerning special form requirements under the final article of the convention.

208 See however Perales Viscasillas (on p. 5), who refers to CISG Article 6 (autonomy of the parties), Article 8 (determination of the intent of the parties) and Article 9 (usages and practices). Perales Viscasillas concludes that a incorporation by reference can be express or implied, and where implied, it must be "derived from usages or from practices established between the parties".

209 German law on general conditions of 1976, § 2. Lando, Udenrigeshandelens kontrakter, p. 27.

Scandinavian contract laws generally accept incorporation of contractual terms by reference.[210] English law generally considers the offeree bound by the conditions referred to in the contract he has signed. Should the offeree not have signed the document, the offeree is bound, if he has received a ´notice´ of the conditions. Such notice is considered to be given if the offeree should know that the document contained or referred to standard conditions.[211] French law also accepts incorporation by reference in commercial relationships. However, general conditions do not have binding force under French law,where the offeree did not have, and was not expected to have, knowledge of the existence of the conditions.[212] The approach of French law can be seen e.g. in the stringent jurisprudence concerning transport conditions which will be dealt with later.[213] In Italy, certain contract clauses must be individually initialled to become valid.[214] This obviously makes incorporation by reference practically impossible. Generally speaking, there are great differences in addressing the use of standard terms under domestic contract laws including the problem of the battle of the forms, which makes international harmonisation difficult.[215] One way to alleviate the ambiguity around the possibility of incorporation is to provide for it in framework agreements.[216]

A recent note by the UNCITRAL Secretariat analyses national case law concerning incorporation by reference in electronic commerce.[217] The note reveals that "courts have required a specific act of incorporation and held that the mere existence of such terms in an easily accessible resource like the seller´s website was not sufficient to effectively incorporate those terms into a contract in which they were not otherwise referred to".[218] It is noted that "courts do not seem to have categorically excluded the possibility of of incorporating terms by the mere clicking of an ´I agree´ button on a computer screen".[219] Furthermore, "courts have often required unambiguous demonstration that the accepting party either had an opportunity to actually access and read those terms or that the party was adequately alerted, through a conspicuously placed notice or

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210 See for instance Ramberg & Ramberg 2003, pp. 173-174.

211 Lando, *op.cit*., p. 35 and the sources referred to therein.

212 Lando, *op.cit*, p. 42.

213 See Chapter VIII.2., *post*.

214 Article 1341 of the Italian Civil Code (Codice Civile); A More Coherent European Contract Law, OJ C 63, 15.3.2003, p. 1.

215 Conclusion of the UNCITRAL Secretariat in Doc. A/CN.9/WG.IV/WP.104/Add.4, para.18 . See an overview of the differences in American and European laws in James A. Maxeiner, Standard Terms Contracting in the Global Electronic Age: European alternatives, in the Yale Journal of International Law, vol 28, No. 1 (winter 2003), pp. 109-182.

216 See the Bolero Rulebook and the TEDI Interchange Agreement.

217 Doc. A/CN.9/WG.IV/WP.104/Add.4, pp. 5-6.

218 Reference is made to Hanseatisches Oberlandsgericht Hamburg, Case No 3. 3 U 168/00, 13 June 2002 reported at JurPC-Internet Zeitschrift für Rechtsinformatik, JurPC WebDok 288/2002.

219 See the cases cited in footnote 22 of doc. A/CN.9/WG.IV/WP.104/Add.4.

otherwise, of the existence of those terms and their relevance for the transaction in question".[220] Finally, the note cites jurisprudence regarding electronic auctions, which are conducted over electronic trading platforms and indicates that the conditions of a third party constituting the legal framework of the platform are more easily upheld by courts.[221]

Article 5*bis* The UNCITRAL Model Law on Electronic Commerce does not impose new contractual rules in this respect but simply aligns electronic incorporation with traditional methods. Neither do the UNIDROIT Principles for International Commercial Contracts contain an express provision on the acceptability of and criteria for incorporation by reference. However, they contain, in Article 2.20, rules for the use of surprising terms in standard terms. According to that provision, no term contained in standard terms which is of such a character that the other party could not reasonably have expected it is effective unless it has been expressly accepted by that party.

The technique of incorporation by reference has thus both a technical dimension relating to the question on how the existence and applicability of the terms are brought to the attention of the addressee and a more substantive dimension relating to the contents of the referenced conditions. As jurisdictions have a tendency to protect a weaker party against surprising terms, it is difficult to imagine that incorporation by reference should be enhanced in international legal harmonisation irrespective of the referenced material.

A provision requiring the contract terms to be made available would be rigid and would effectively prevent incorporation by reference, the possibility for which Article 5*bis* of the UNCITRAL Model Law on Electronic Commerce is designed to ensure. My suggestion would be to create an incentive for making the terms available in the described manner by attaching legitimity to terms made available by express provisions.

If the terms are accessible through the link, and can be (as is normal) stored and reproduced, there should be room in business-to-business relations to equate such a presentation with the production of the said terms in physical form. One can argue that Article 10(3) of Directive 2000/31/EC and other provisions calling for the making the contractual terms available in a manner that allows for printing, storage and reproduction actually already elevate the status of said terms up to a level at par with attached paper documents.[222] Furthermore, the general principle of equating electronic records functionally with paper

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220 Specht v. Netscape Communications Corp., Federal Supplement, 2nd series, vol 150, p. 585; Specht v. Netscape Communications Corporation and America Online Inc., United States Court of Appeals for the Second Circuit, 1 October 2002, Federal Reporter, 3rd series, vol 306, p. 17.

221 For example Bundesgerichtshof, 7 November 2001, Case No. VIII ZR 13/01, reported at JurPC- Internet Zeitschrift für Rechtsinformatik, JurPC WebDok 255/2001.

222 Member States implementing this provision have come to different conclusions as regards the consequences of a failure to make the contract terms available. In many Member States, the consequences are administrative, including punitive measures, and in certain cases the failure affects the validity and enforceability of the contract (see doc. A/CN.9/WG.IV/WP.104/Add.4, para. 23. The US UETA provides that a failure to make the terms available makes them unenforceable.

documents normally leads to the same result. Still, a more elaborate equation of terms made available electronically with attached paper terms could be useful in equating e-commerce methods to more traditional measures. A similar equation is actually made in the case of electronic signatures. One can add safeguards such as laying the onus of proof of availability on the party making them available, require conspicuousness and state that this provision does not affect the substance or conscionability of any provisions made available.

As an example, it is difficult for a party to claim that he has no knowledge of transport conditions, if the shipowner publishes its general conditions on the Internet and can prove having done so. A third party service provider, or a business organisation such as the ICC with its once contemplated ´E-terms´ (in their original sense) or an electronic platform, could publish companies´ general conditions and guarantee thereby their (technical) integrity. The Dutch legal practice allows general terms to be published or registered at a chamber of commerce or a commercial court´s office in such a way that a simple reference can be made to it.[223] This practice applied even before such general terms were accessible on the Web.

It should be noted, however, that companies may have relevant marketing material or product information on their Internet sites. If conditions of contract located on the company´s website were generally admitted, an argument could easily be raised about the status of other materials, since these are made deliberately public in the same manner as the terms of contract.

The European Commission has decided to promote the elaboration of EU-wide standard contract terms. For this purpose, it intends to set up a website where companies, persons and organisations can, under their own volition, list information on existing or planned initiatives in this area.[224] This is obviously a policy-oriented site, but may provide a nucleus of a more practically directioned website for reference.

IV.8.3 Battle of the forms

An important problem of contract formation connected with incorporation by reference is the problem of the battle of the forms. It involves an offer or a solicitation of offers that is communicated, where traditional methods of communication apply, on a preprinted[225] form containing contract terms favourable to the form´s author. In a response, the recipient of the preprinted form, instead of accepting the terms contained therein, replies by sending another form containing his own terms. This problem could appear electronically between two sets of contract terms behind a hyperlink.

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223 Troye at the Helsinki seminar on 27.11.1991. Central registries facilitating electronic commerce can also publish the general conditions of their participants, see *infra*.

224 A more coherent European contract law, An Action Plan, OJ C 63, 15.3.2003, para. 87.

225 In the purest sense of the concept of battle of the forms.

There are basically three ways of approaching the discepancy of the offer and the acceptance, at least in the mechanical sense.[226] According to the theory of the ´first shot´, the conflict is resolved by applying unconditionally the offeror´s general conditions communicated to the offeree. The theory of the ´last shot´, on the contrary, builds on the binding nature of the offeree´s conditions, which are the last communicated conditions, provided that the offeror does not protest against them. A third theory purporting to build a consensus between the first two theories is called ´knock-out´ and means the reciprocal cancellation of the conflicting terms.[227]

Contract formation will not, however, be allowed, if the law concerned requires a strict compliance between the offer and the acceptance (the so called ´mirror image´ rule). This rule is found within traditional common law. Most legal systems allow contract formation to take place if there are only minor divergences between the offer and the acceptance. Under Finnish law, for instance, an acceptance of an offer with amended conditions is regarded as a new offer from the offeree, unless the conditions exchanged are so close that the parties ought to regard the offeree´s response as accepting his offer under virtually identical conditions, in which case the offeror has the onus to notify the offeree of his objection.

The United Nations Sales Convention does not deal explicitly with the battle of forms issue, and if it is taken to deal with it, it does so in a traditional manner from a technical offer-acceptance angle.[228] This is the case also with many national legal systems such as the French, Belgian, German and English laws.[229]

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226 In addition to the classical pattern of two declarations of will – offer and acceptance – one can understand the formation of a contract as taking place through performance, even though the content of the contract is incomplete. Another alternative to resolve battle of the forms issues is the good faith principle, which leads to a neutral solution, preventing either party from gaining an advantage by being the first or the last to send a declaration of will. See Perales Viscasillas, p. 4.

227 Delforge in ´Le processus de formation du contrat´, p. 481.

228 Ibid., pp. 525-531. Article 19 provides:

(1) A reply to an offer which purports to be an acceptance but contains additions, limitations or other modifications is a rejection of the offer and constitutes a counteroffer.

(2) However, a reply to an offer which purports to be an acceptance but contains additional or different terms which do not materially alter the terms of the offer constitutes an acceptance, unless the offeror, without undue delay, objects orally to the discrepancy or dispatches a notice to that effect. If he does not so object, the terms of the contract are the terms of the offer with the modifications contained in the acceptance.

(3) Additional or different terms relating, among other things, to the price, payment, quality, and quantity of the goods, place and time of delivery, the extent of one party´s liability to the other or the settlement of disputes are considered to alter the terms of the offer materially.

According to Delforge, CISG Article 19 is perhaps slightly biased towards the ´last shot´ rule and reflects a a relatively strict ´mirror image rule´. See Delforge, *op.cit.* p. 525 note 126. See also Honnold, pp. 182 *et seq*.

229 Delforge in *op.cit*,., p. 483; Schlechtriem, p. 1. For Germany, on the other hand, an important case was the *Schwelfelbrocken* case (WM 1957, 1064 *et seq*.) which led to the result that the steady referral to one´s own terms and conditions despite the actual performance of the contract did not lead to any side prevailing with its term; nevertheless, a contract had been concluded the content of which was to be governed by statutory rules. An important case is also BGH 9.1.2002, reproduced in English at http://cisgw3.law.pace.edu/cases/020109g1.html, visited on 16.4.2004. In this case, the court confirmed that the parties´ contract is valid despite conflicting standard clauses, and that the conflicting terms are void and replaced by the provisions of the CISG regulating the respective subject matter.

French and Belgian jurisprudences are sympathetic to the ´first shot´ theory whilst English jurisprudence based on common law seems to apply a mechanistic ´last shot´ approach[230], and the same goes for German law.[231]

As is the case with Finland, contract formation may be allowed by law, even if the conditions exchanged do not fully match. The Uniform Commercial Code of the United States permits contract formation even though the terms exchanged conflict.[232] Moreover, the UNIDROIT Principles on International Commercial Contracts contain a provision on the battle of the forms with a similar approach. Article 2.1.22 stipulates namely that "where the parties use standard terms and reach agreement except on those terms, a contract is concluded on the basis of the agreed terms and of any standard terms which are common in substance unless one party clearly indicates in advance, or later and without undue delay informs the other party, that it does not intend to be bound by such a contract". The European Principles of Contract Law (Art 2: 209) repeat the same approach, but add that the indication in advance must be done "explicitly, and not by way of general conditions".

As the CISG does not explicitly address the problem of the battle of the forms, there are various schools of thought as to whether and how the Convention should be applied in case of conflicting contract terms. Some commentators think that the regulation of the battle of the forms must be found in the applicable domestic law. Some think that the general principles behind the Convention (referenced in Article 7) should come into play to fill in the gap. Some scholars think that parties performing the contract despite differences in contract forms have implicitly excluded the application of the Convention. There are also those who think that the CISG provisions apply in part. This school of

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230 Butler Machine Tool co Ltd. v. Ex-Cell-O Corpn (England) Ltd. [1979] 1 All ER 965. The ´last shot´ means a positive answer with qualifying additions, which together constitute a new offer.

231 Delforge in *op.cit*, p. 483.

232 U.C.C. § 2-207. Perritt Jr. in Baum-Perritt Jr., pp. 322-323. U.C.C. § 2-207(1) provides that a definite and reasonable expression of acceptance or a written confirmation which is sent within reasonable time operates as an acceptance even though it states terms additional to or different from those offered or agreed upon, unless acceptance is expressly made conditional on assent to the additional or different terms. Moreover, § 2-207(2)(c) provides that additional terms by the offeree become part of of the contract unless notification of objection to them is given within a reasonable time after notice of them is received. Such additional terms do not, however, constitute additions to an original offer, if they alter it materially.

The UCC rules on the battle of forms have been widely criticised and are subject to revision. The draft of November, 2000, for a revised Article 2-207 put the battle of the forms in a larger context of contract interpretation. It states that " (i)f

(i) conduct by both parties recognizes the existence of a contract although their records do not otherwise establish a contract,

(ii) a contract is formed by offer and acceptance, or

(iii) a contract is formed in any manner is confirmed by a record that contains terms additional to or different from those being confirmed, the terms of the contract, subject to Section 2-202, are:

1) terms that appear in the records of both parties;

2) terms, whether in a record or not, to which both parties agree; and

3) terms supplied or incorporated under any provision of the [UCC]."

thought builds on the significance of performance, which turns the problem into a substantive one rather than one relating to formation.[233]

According to *Perales Viscasillas* the legislative history of CISG Article 19 indicates that the battle of the forms is regulated by the Convention. Her view is that the Convention´s rules, despite their rigidity, add predictability. She also refers to the possibility of substantive scrutiny of the winning terms by national courts on the basis of unconscionability.[234] This view does not make it easy to resort to the contract law principles which tackle the question more flexibly and neutrally. If the principles cannot be brought in by virtue of CISG Article 7, the only way to bring them is (express) contractual incorporation. In case the offer and the acceptance differ, and the difference is regarded as material, no contract exists. This leads to the incorporation of the principles being invalid as well.

The possibility of using automated computer systems for making and accepting offers could, in any case, make traditional rules cumbersome or redundant. Computers should not normally permit a contract to be construed unless the terms match, provided that all terms and conditions are exchanged through the electronic system. But this may not be certain. For instance, as illustrated in the literature, should additional terms regarding packaging be included in the free text segment of an electronic message, a computer might simply disregard them, and the result would have to be examined in the light of circumstances. The question may be asked of whether the improperly packed goods could be rejected.

On the other hand, a solution whereby a party is bound by terms which are attached (by a hyperlink etc.) later[235] does not work either since the CISG and electronic commerce practice as reflected e.g. by well-known interchange agreements build largely on the reception rule. Following this rule, a contract may be formed without the addressee having read the non-compliant conditions.[236] Therefore, an international solution should probably still build on UNIDROIT Principle 2.22. Parties using machinery should probably have to bear the risks involved without any new rules for allocating them.

The UNCITRAL Working Party on Electronic Commerce will probably refrain from addressing the question of the battle of forms in the draft convention on electronic contracting.[237] My view is that a universal solution to the mechanistic problem should be dealt with in the convention, since national rules are largely based on jurisprudence and are too divergent, and no view on the relationship between the CISG and the relevant contract law principles has received widespread consent.

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233 For these approaches and references see Perales Viscasillas, pp. 13-15.

234 Ibid., page 17. Perales Viscasillas refers to Article 4(a) which excludes the application of the Convention to questions of validity. Unconscionability does not, however, necessarily relate to validity. The Finnish Contracts Act § 36 gives the courts a right to adjust unconscionable terms, although these are formally valid.

235 For the ´first shot´ and ´last shot´ models, see Ulf Göransson, Kolliderande standardavtal, Uppsala 1988, pp. 25 *et seq*. and Wilhelmsson DL 3/2000, p. 447.

236 CISG 19(2) mentions "without undue delay" in a manner which can be interpreted objectively independent of the addressee being informed of the counteroffer. The logic of the Convention does not support any information theory here.

237 A/CN.9/WG.IV/WP.95, paras. 67-68.

IV.8.4 The use of model contracts

Model contracts prepared by organisations facilitating trade are useful tools in business-to-business transactions. They may be used as such or may be incorporated into a corporations own house conditions. The substantive dimensions of the use of model contracts, e.g. whether they are biased or not, will be dealt with in Chapter X.3.5., *post*. Here, attention will be paid to model contracts in the service of contract formation, or in the establishment of commercial relations in general.

IV.8.4.1 Model contracts governing mainly communications and contract formation

The relationship of exchanging communications through EDI is usually sealed with the use of interchange agreements. Similar contractual arrangements are still useful in other, more open forms of electronic commerce. I will mention two of them as examples of contemporary practice.

UN/CEFACT adopted, as Recommendation No. 31, the Electronic Commerce Agreement (the ´E-Agreement´) in March 2000.[238] The Recommendation notes in its introduction that

> "(t)hough the emerging legal framework of the global marketplace for electronic commerce, once completed, will contribute to the building of trust required for its further development, the use of electronic commerce still raises a number of issues which can be better addressed through a contractual process".

Recommendation 31 builds on the experience gained with the EDI Interchange Agreement.[239] The E-Agreement is said to contain a basic set of provisions which can ensure that one or more electronic commercial transactions, or ´E-transactions´, may subsequently be concluded by commercial partners within an adequate legal framework. Moreover, the E-Agreement aims at addressing all forms of electronic communications, not just EDI. Commercial partners engaged in multiple techniques are recommended to turn gradually to the E-Agreement in lieu of the traditional Interchange Agreement. The E-Agreement is not designed to cover relationships with consumers.

The E-Agreement can be used either for one transaction or for multiple transactions, whereas Interchange Agreements are normally construed to cover multiple transactions in an established business relationship. The nucleus of the Agreement (Chapter 1 of Part I) consists of rules relating to communications[240]

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238 Recommendation No. 31, first edition, Doc. ECE/TRADE/257, Geneva, May 2000.

239 UN/ECE (CEFACT) Recommendation No 26, 1995.

240 The Agreement underlines that parties should agree on the method of communication. The method could be a website, EDI or e-mail or other designated method. The messages could concern e.g. an invitation to treat, an offer, an acceptance, a revocation, an acknowledgement or a notice.

Just as an Interchange Agreement contains many technical specifications, the E-Agreement invites the parties to agree on the names of communication standards, the software used and the third party service providers.

and contract formation, and substantive rules may be added optionally (Chapter 2 of Part I).

The two parts which constitute the agreement are the Instrument of Offer (Part A) and the Instrument of Acceptance (Part B). When a party offers to enter into commercial contractual relationships by electronic means, he sends the Instrument of Offer, which is comprised of rules of communication and contract formation and, in practice, substantive contractual terms, which have to be designated as called for by Chapter 2 of part I. The parties are called the proposer and the accepter. Where the party initially receiving the Instrument of Offer is not satisfied with it, he can amend the Instrument of Offer and return it as a new offer. Once a party wishes to accept an offer he sends the Instrument of Acceptance within a stipulated deadline[241], the exceeding of which makes the acceptance a new offer. This rather mechanical approach to contract formation may eliminate the problem of the battle of the forms to some extent.

The law governing the E-Agreement may be designated by the parties, failing which the law of the establishment of the proposer shall prevail. Should the original proposer, who is actually the the seller offering goods or services, remain the ultimate proposer, the governing law would be close to the approach of the EC Convention on the Law Applicable to Contractual Obligations.[242] Where the buyer makes a counteroffer on, say, communication standards, he becomes formally the proposer whose law prevails, unless otherwise stipulated.

An effort to create a comprehensive Trading Partner Agreement for high technology supplies has been undertaken by several organisations[243] recently. For the sake of simplicity, I will refer to the RosettaNet Trading Partner Agreement (TPA)[244]. The package has the following parts: General Legal Provisions, Non-

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241 The default being 24 hours.

242 The Rome Convention attaches importance to the place of business of the party who does the characteristic performance.

243 The participants are RosettaNet, the European Electronic Component Manufacturers Association (EECA), the European Semiconductor Industry Association (ESIA) and EDIFICE. RosettaNet is an independent non-profit consortium dedicated to the collaborative development and rapid deployment of open Internet-based business standards that align processes within the global high-technology trading network. More than 400 companies are members of the consortium, and the program working group included representatives i.a. from Motorola, Nokia, Sony and Philips Semiconductors. EDIFICE is a standardised electronic commerce forum for companies with interests in computing, electronics and telecommunication. It is a non-profit organisation founded in 1986.

244 See http://www.rosettanet.org >Foundational Programs>Trading Partner Agreements, visited on 21.3.2003. According to a press release (http://www.rosettanet.org > Home > News/Events > 2003 RosettaNet Press Releases > Archive 2001 > Global Industry Organizations Release High Tech Industry´s First Standardized Trading Partner Agreement, 22 October 2001, visited on 21.3.2003) there was a six-week review period in late 2001, after which a final version of the Agreement would be issued by Rosetta Net. Any modifications made after the review period do not appear on the website. It was also indicated that the UN/CEFACT legal team had been connected with the drafting of the TPA.

UN/CEFACT considered the RosettaNet TPA at its Plenary on 12-13 May 2003 (Note for the Press ECE/TRADE/03/N02, Geneva, 14 March 2003).

Disclosure Agreement[245], Appendix 1: TPA Module for Portal Services[246], Appendix 2: TPA Module for XML Services[247], Appendix 3: TPA Module for Electronic Data Interchange (EDI) Services[248]. In the general legal provisions, there is space for referencing to substantive general conditions in order to incorporate those into the contract.

Like the UN/CEFACT´s ´E-Agreement´, the RosettaNet TPA is designed to cover e-commerce beyond EDI[249], but in practice it suits predominantly to permanent business relationships. Moreover, the TPA in question allows for new technology solutions to integrate a TPA into a machine-processable message. This will enable automatic exchanges and negotiations in a systems-to-systems (XML and EDI) approach.[250]

Both the above mentioned model contracts contain, like former interchange agreements, a general clause[251] equating electronic information with that contained on paper. The ´E-Agreement´ contains more provisions relating to contract formation. It defines what constitutes an offer and determines rules on revocation of offers and withdrawals of acceptances in a manner that corresponds to the CISG Part II provisions. Both agreements require for a proper reception to take place in that the message is made accessible or available at the receipt computer.

The RosettaNet TPA requires, as a default provision, an acknowledgement of receipt, whilst in the case of the E-Agreement the default provision for acknowledgement of receipt is that the receiving party shall not be obliged to send one unless the seller requests it. Where such obligation is imposed,

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245 Parties may, by using this agreement, disclose proprietary and confidential information by exchanging information electronically for the purpose of evaluating the feasibility and modality of a possible business relationship between the parties and for the purpose of a possible business relationship which is a consequence of this evaluation.

246 The objectives of Appendix 1 are: (a) To emphasise the obligations of the parties to the agreement in accessing and using the collaborative portal, in particular the obligations to monitor and announce in a timely manner any change about users and their rights and privileges to see or add content, and to use applications in a personalised environment of the collaborative portal; (b) To identify the parties and define the technical means related to the use of the collaborative portal.

247 The objectives of Appendix 2 are: (a) To specify the business framework of the XML transactions and standards that the parties to the agreement are intending to operate and use; (b) to identify the parties and define the technical means for the transport, encryption, digital certificate exchange of XML messages, and support procedures as well.

248 The objectives of Appendix 3 are: (a)To specify the business framework of the EDI transactions and standards that the parties to the agreement are intending to operate and use; (b) To identify the parties and define the technical means and requirements for the transport, security, support and operation for the exchange of EDI messages and to describe security and support procedures.

249 ´Electronic Information Exchange´ is defined as a "(m)eans of Electronic Commerce defined to include, but not limited to, the exchange of messages, documents and data using Information exchange technologies like Electronic Data Interchange, Facsimile, Electronic Mail, and Internet-based Transactions making use of Extensible Markup Language and Portal Technology".

250 Note for the Press ECE/TRADE/03/N02, 14 March 2003. On Straight Through Processing, see Chapter II,2.2, *ante*.

251 The E-Agreement part A Chapter I Section 3.1., Trading Partner Agreement – General Legal Provisions Section 5.

however, the default provision of the E-Agreement is quite liberal because any conduct of the receiving party sufficient to indicate to the sender that the message has been received will suffice. The E-Agreement thus follows the approach of Article 14 of the UNCITRAL Model Law on Electronic Commerce.

Where there is a discrepancy between the message as sent and as received, the RosettaNet TPA presumes in (General Legal Provisions Section 11) the message as sent to prevail, which is a solution opposite to Article 13(5) of the UNCITRAL Model Law. The E-Agreement follows the approach of the Model Law.

The RosettaNet TPA requires that an electronic signature be adopted and used, and a digital signature is one form of it.[252] However, the requirements are relatively flexible. The E-Agreement refrains from addressing the issue completely, even in the particulars to be inserted to identify the parties.

The two above model contracts drafted during the era of open electronic commerce show that there are substantial differences in approach. It is suggested that many divergences could be overcome by resorting more consistently to the provisions of the UNCITRAL Model Law on Electronic Commerce.

There are rules and clauses which are designed to be incorporated into contracts, but which do not constitute entire model contracts. One can mention the ICC E-Terms 2004 and the ´System Rules´ (Articles 11 to 15) of the UNCITRAL Model Law on Electronic Commerce in this context.

IV.8.4.2 Model contracts with substantive contents

As noted earlier, American trading partner agreements contained both interchange-related and substantive provisions. The same patterns may later appear in model contracts used in electronic commerce in general. The ICC E-Terms 2004 is accompanied with a guide containing a list of items that have to be considered when a substantive contract is made.

Model contracts such as UN/ECE Model Contracts for the Supply of Equipment and Machinery Nos 188 or the ICC Model International Sale Contract (Manufactured Goods Intended for Resale) can lay down the foundation for a commercial transaction by way of being incorporated into the contract. Such model contracts may have to be amended by standard rules relating to contract formation or *vice versa*.[253]

The ICC Model Contract consists of Part A (specific conditions) and Part B (general conditions), so that Part A is to be filled in by contracting partners thereby indicating their express choices that replace the provisions in the general

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252 According to the definitions of terms (General Legal Provisions Section 3), an ´Electronic Signature´ means " an electronic sound, code, symbol, or process, attached or logically associated with a contract or other document and executed or adopted by a person with the intent to sign a document". A ´Digital Signature´ is "an Electronic Signature that can be used to authenticate the identity of the sender of a message or the signer of a document, and possibly to ensure that the original content of the message or document that has been sent is unchanged".

253 The UN/ECE Model Contracts have a clause on contract formation.

conditions. The form for specific conditions is also a useful checklist of conditions. The ICC has later made an electronic version of the Model Contract by furnishing the specific conditions form with necessary hyperlinks at the same time recognising that an electronic agreement has to provide, by way of reference or explicitly, contract formation principles together with communications standards.[254]

Very often model contracts contain some kind of *aide-mémoire* assisting in their use and drawing the parties´ attention to problematic issues. As model contracts with substantive contents designed to be neutral between the interests of the seller and the buyer earn a reputation among users, a method should be created to guarantee their integrity in a manner comparable to a letterhead paper. Referencing to a document URL contained in a website maintained by a third party such as a chamber of commerce could help in this respect.

The above examples clearly show, in my view, that electronic commerce calls not only for rules of communication, contract formation and interchange, what could be called the domain of the *lex electronica*, but also for substantive reference points such as substantive international model contracts and uniform rules covering special issues. This need of neutral and well-known sources of substantive law can constitute one more driving force towards a harmonised commercial law – the *lex mercatoria*.

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254 The web version of the Model International Sale Contract is a joint venture between the ICC and a commercial enterprise, Allagraf Limited. The application has been named ´Paction´, and it allows the buyer and the seller to prepare, negotiate and complete sale contracts online. Like many other web contracting facilities, the application guides its user through the procedure. All the communications are made by automated e-mails from the Paction server.

The procedure is as follows:

One party first fills in the application in order to create an initial draft contract to his liking. The application helps the user by asking simple questions, but experienced traders can find shortcuts through the procedure to produce the initial draft. The draft is then released to the counterparty.

The counterparty will have access to a wide range of help facilities to explain the contents and implications of the proposed contract. He can either accept the draft as it is or edit the provisions and make a counteroffer.

Once the counterparty has reacted to the offer made through the system, the originator of the contract receives notification that an amended draft is available. If the offeree has made changes which signify a counteroffer, these are indicated by ´redline´ visual format. The procedure can then be continued by the initiator in a similar manner.

The application keeps track of the process so that once there is a valid acceptance, the application recognises the contract concluded, after which it cannot be edited further by the parties. The parties can then sign the contract online using digital signatures, if they have the capability of doing so. The contract can also be printed and signed manually (I would like to submit that a click on an area on the screen could suffice to prove the intent to be bound without cumbersome signature procedures; it is recognised however that a signature may play a crucial role in some legal cultures). ´Paction´ even retains a secure copy of the contract, which can be resorted to in case of disagreement.

IV.8.5 The use of a central registry

Central contract registries are a useful by-product of electronic trading platforms.

The Bolero Rulebook contains in Rule 3.10 (Ownership and Contracts of Sale) some basic provisions relating to the use of a system that holds a central registry for the conveyance of rights and obligations between contracting partners. Rule 3.10(4) states that, where a contract of sale between users[255] of the Bolero.net is concluded (in whole or in part) by means of a message[256] or by a series of messages, each user agrees that such message or messages shall constitute or evidence the contract concluded between them. However, upon a request from any user entitled to demand the original contract of sale, a contracting user will have to print and sign in writing the message or messages in accordance with any and all formalities required by any applicable law to give effect to the contract.

A central registry may serve as a depository of standard terms and thereby facilitate incorporation by reference. The Bolero System Operating Rules 35 and 36 of Operating Procedures facilitate the publication of users´ documents in ´user support resources´ and determine that a document published in the user support resources is deemed to be available to all users of the Bolero System as required by the Bolero Rulebook section 3.2(1)(b). As the parties are contractually tied to the Bolero Rulebook they are bound by the existence of a document in such a facility, unless national law otherwise applicable to the relationship is very stringent against allowing incorporation by reference.

A central registry may frequently perform the functions of a trusted third party and authenticate messages. A central registry may futhermore be made an agent or trustee of the parties in carrying out actions normally done by the parties.

IV.9 Foreign form requirements and new slegislation

Earlier, in Chapter II.9., the general role of form requirements contained in national law in concluding legal transactions was analysed. The current chapter contains harmonisation measures that have been taken with a view to equating electronic means of communication with paper. This will hopefully change the scene little by little, and parties need no longer to agree on the validity of electronic communications.

When states implement legislation designed to give electronic records the same effects as paper documents by implementating the UNCITRAL Model Law on Electronic Commerce with its ´functional equivalence´ approach, or taking

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255 A person who is enrolled as a user of the Bolero System.

256 Any communication, notice or other information sent through the Bolero System as described in Operating Procedures (appended to the Bolero Rulebook).

otherwise equal measures e.g. by fulfilling the requirements of Directive 2000/31/EC on electronic commerce, form requirements harmful to electronic commerce start to disappear. However, as long as there exist states which continue to maintain problematic requirements in respect of some legal acts, e.g. by insisting, in the case of a transfer of debt, a written notice to the debtor, the basic stance of each jurisdiction to foreign form requirements will likely remain quite similar to what it has been. Little by little, as modern electronic commerce legislation spreads from country to country, courts may start treating foreign form requirements requring traditional written form as anomalies. Moreover, parties will find it increasingly easy to choose a law suited to electronic transactions, unless they decide to refer to non-state rules of law altogether.

IV.10 Conclusions

During the past few years, a new statutory framework for electronic commerce and electronic contracting has gradually emerged, but several aspects still remain in the pipeline.

At the time this study was written, the UNCITRAL preliminary draft convention on electronic contracting was still under preparation. This draft builds largely on the UNCITRAL Model Law on Electronic Commerce and the CISG.[257] Once the draft is finalised, there will be three UNCITRAL instruments dealing with basic contract law issues in place. It is a matter of legislative technique to ensure that these instruments complement one another. Overlap cannot be fully avoided but discrepancy can. Taken together, these instruments should provide a package which would help states to modernise their laws. The European Union does not seem to want to enter into the field of harmonising contract formation. UNCITRAL instruments can do this, just as the CISG has already done in traditional contracting.

There is some cynicism in the air about the role of the possible future convention. I think this instrument could amend the contract formation rules of the CISG and extend them to other fields of contracting. Yes, it would create a dual regime of electronic and other contracting side by side. Still the harmonisation of one very technical layer of contract law could be a way forward. Such provisions could spread their influence to traditional methods of contracting. New provisions could even tackle such controversial issues such as incorporation by reference vs. the making available of contract terms and the battle of the forms in electronic communications. An instrument capable of being incorporated contractually could be a useful piece of necessary rules of law. It is understandable that the lowest common denominator will often prevail in legal harmonisation to guarantee its success. Sometimes, on the other hand, less ambitious goals lead to the marginalisation of the effort.

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257 A note by the UNCTRAL Secretariat states "an international instrument on electronic contracting could not be based on the assuption that the principles of the Model Law have already achieved universal application. It seems, therefore, useful for the new instrument to establish the conditions under which form requirements may be met by equivalent electronic methods." (Doc. A/CN.9/WG.IV/WP.104/Add.3, para. 3)

The international instruments introduced during the past twenty-five years have generally opted for the reception rule in determining when legal effects arise in contractual communications when it comes to contract formation especially. As Eiselen puts it, "in most circumstances it is fairer to both parties to apply an objective test, namely the reception theory rather than the subjective information theory when dealing with indirect forms of communication".

Reception in no way presupposes the information of the addressee. It suffices that the information has reached him or his server. In addition to being evident in Article 24 of the CISG, it has also been a common provision in interchange agreement practice, even in Anglo-Saxon jurisdictions which normally apply the postal rule, and it should constitute the rule in electronic commerce by and large. Contractual communications made by computers require particular attention as to type, format and address (as well as the consent of the addressee). The sender has to be more careful than what he would be when he is sending information with more traditional communication methods. Therefore the risks of errors in communication should normally be allocated to him.

I am referring to contract formation. Article 1.9 of the UNIDROIT Principles of International Commercial Contracts extends the reception rule to notices which relate to the substantive parts of the agreement. There are reasons to derogate from mechanical risk allocation in particular by placing the risk of communication error to the party breaching the contract, which is generally the approach of the CISG. An opposite view has been expressed: "From the point of view of risk allocation, all that is important is who can best prevent the loss. Since only the party who sends the notice can take necessary precautions, it therefore makes sense to place the risk of loss on that party."[258]

In the deliberations of the UNCITRAL Working Party IV (Electronic Commerce)[259], the whole idea of determining when the contract is formed electronically has been challenged by referring to the different approaches in national law as to contract formation. The information rule, which attaches importance to the fact that the addressee is actually informed of the message, which is followed by some national laws, should be respected according to some critics.

I believe it is vital that the draft Convention maintains the reception rule as originally suggested. This kind of harmonisation is desirable, and it is in line with the course of developments in the past twenty-five years. The original suggestion complements Article 24 of the CISG in respect of electronic commerce transactions and brings uniformity to other transactions than sale of goods transactions in a reasonable manner. The fact whether the addressee is actually informed should play no role, as the point when a message is received by the addressee can technically be determined and solved by automation. The point when the addressee is informed is much more difficult to determine.

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[258] Reference to R.Hyland 40 The American Journal of Comparative Law (1992) p. 548, in Bonell 1996 note 15.

[259] See the Report on the forty-first session, 5-9 May 2003, paras 101 to 106.

Finally, the law of contract formation in electronic commerce should not build on cognitive elements since contracts are or will be concluded with or even between machines. How could one determine when a machine is informed of something? Cognitive aspects should come in only when the actual rights and obligations arising out of the contract are at stake, and this could be left to domestic law.

The UNCITRAL Model Law on Electronic Commerce tackled the issue of incorporation by reference cautiously in Article 5*bis* by making an electronic incorporation by reference functionally equivalent to incorporation by reference on paper. This amendment was advocated by the business community, especially the ICC. This possibility should be continuously respected and refrain from imposing the duty of making the contract terms available.

The UNCITRAL draft convention on electronic contracting aims to facilitate e-commerce and is based on the principle of functional equivalence. What the convention could do to enhance functional equivalence and facilitate commerce, again interfering with some traditions of national contract law, is to formally ascertain the legal status of materials made available electronically, usually through hyperlinks.

This could be done by a provision stating that a reference to and inclusion of a hyperlink or an electronic attachment which was ´made available´(i.e. could be stored and reproduced) would constitute the equivalent of an attached paper document. Such a provision would of course be partly repetition of the principle of functional equivalence contained in the Model Law on Electronic Commerce, but would make the case of functional equivalence more concrete as does the whole of electronic signatures legislation.[260] As a statutory safeguard, the burden of proof could be on the referor to prove that the material behind the link was actually available. For this purpose, trusted third parties, such as telecommunications service providers or chambers of commerce, acting as repositories could be resorted to when safety would be needed. Moreover, the hyperlink should be pointed out conspicuously. As regards the traditional notion of incorporation by reference where the terms are not made immediately available during the contracting process, one could refer to the general availability and status of the terms as well as to how well the parties already know the terms on the basis of their prior dealings or otherwise.

Incorporation by reference, or providing a URL hyperlink, is a technicality, and does not look into the detail of the clauses, which may include surprising elements that may not become part of the contract unless expressly agreed upon. Furthermore, where such clauses are not included in the contract, the entire

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[260] Article 6 of the eUCP concerning the examination of electronic records under the Uniform Customs and Practice for Documentary Credits provides that if an electronic record contains a hyperlink to an external system or a presentation indicates that the electronic record may be examined by reference to an external system, the electronic record at the hyperlink or the referenced system shall be the electronic record to be examined. If there is no access to the link or system, the ´documents´ are deemed to be discrepant. See Chapter VII.8.4.5., *post*.

validity of the contract may be put into question. The draft Convention could refer (at least in a future Guide to Enactment) to national law (or refer to or spell out UNIDROIT Principle 2.1.20) in addressing surprising or unconscionable terms and requiring express agreement in respect of these. The technique of ´click-wrap´, for instance, could be used to meet the requirements of having to initial a document, a page or an individual clause.

Finally, a basic provision on the battle of the forms incorporated electronically along the lines of the UNIDROIT Principle 2.1.22 (see *supra*) could be added. The provision should not, however, elevate electronic forms to a higher status and would be able to address the problem when using electronic media.

The law of electronic commerce presented in this chapter is general in nature. To serve international trade, however, substantive aspects of law will have to be considered. In the next three or four chapters, electronic commerce is regarded from the viewpoint of international trade. This will include the various contracts involved, the contracts of sale, transport, insurance and those relating to documentary credit operations and trade guarantees. In that context the question of whether the ´functional equivalence´ approach proposed in the UNCITRAL Model Law on Electronic commerce is sufficient to help overcome all barriers imposed by national law is raised. An alternative is to provide specifically for issues raised by the use of electronic media. This may possibly add new substantive law issues to be resolved.

V AN OVERVIEW OF THE INTERNATIONAL SALE OF GOODS SYSTEM

This study, particularly the following four chapters, follows the structure of a ´tripod´, in which sale, transport and finance legs ultimately join to form a basis for one uniform trading system. This system could be the *Bolero System* or any electronic trading platform designed to accommodate the use of electronic records in lieu of commercial documents such as the bill of lading, and to offer a multi-contract service. My intention is not, however, to promote any commercial solution at the expense of others but just to highlight the possibilities arising from the developments.

The contract of sale and the contract of transport are two essential legs of the tripod, and trade finance in the form of documentary credits is the third. All these legs stand on the legal ground[1] of electronic contracting and the evolving role of electronic trade documentation. The legal rules consist e.g. of the formation of contracts electronically, rules of evidentiary value, the authentication, originality and storage of records, which all have already been analysed in detail.

In order to be complete, one should not, of course, forget the contract of insurance or other ancillary contracts. In any case, when all these and other contractual or documentary components of an international sale of goods transaction are capable of being operated in an electronic environment, complete multi-contract electronic trading platforms can be established on that legal ground. The more stable the legal ground is, the more useful the trading platform becomes. After that, it may become much easier for the operators of these systems to attract subscribers.

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[1] See the Bolero Feasibility Study observations on the role of the private sector in Chapter VIII.9.1.1., *post*.

The contracts involved in the system predominantly serve their original purpose, e.g. the contract of carriage regulates the relationship between the shipper, the carrier and the consignee. However, the contracts have secondary functions as well. The contract of carriage, insurance and even the contract of sale can be used as security for the bank financing the transaction. Moreover, the contracts and documents have common information or data elements, most notably the description of the goods, re-keying of which should be avoided. This saves time and money. The question then arises of whether there could be increased interaction between the contracts included in an electronic trading system to make it work better by eliminating unnecessary conflicts between the various parties. I shall come back to this question later.

In this chapter, I start therefore moving with general questions of electronic contracting and more towards questions concerning international trade and transport, as well as the role of trade documentation in that context. Attention will first be paid to the documentary aspects of the relationship between the contract of sale and the contract of carriage, the transfers of risk and property as well as questions of retention of title and stoppage in transit. There will be an analysis of the role of rights affecting the goods in transit, as well as ways of securing international trade transactions. An overview is also taken of the harmonisation of rights *in rem*.Transport insurance and the documentation relating thereto can be logically presented in the context of the passing of risk.

The next chapter will then examine contracts of transport and their documentary aspects in some detail. Transport documents have multiple roles, one in the delivery obligations under the contract of sale and, where appropriate, the transfer of title and possession, one in evidencing transport contracts, acting as a receipt, and possibly authorising the holder to claim delivery, and a further one representing the goods in documentary payment systems. This ´tripod´ of functions, which does not necessarily follow statutory descriptions, also forms the basis for my presentation. The rough dividing line is that the type and nature of the documents as well as their functions in respect of the contract of transport are examined in Chapter VI, whereas their role under the contract of sale, including proprietary functions, is presented already in this chapter. Some overlapping is inevitable for presentational reasons. The third function of transport and other trade documentation, that relating to finance, is presented and analysed in Chapters VII and VIII.

Negotiable transport documents with their legal functions of transferring title or entitlement to the control and possession of the goods make them essential for electronic trading platforms. If possible, the use of electronic records in lieu of paper documents should be functionally equivalent as regards all contracts involved in a transaction.

V.1 Delivery of the goods and the documents

Article 30 of the United Nations Sales Convention lays down the principal rule of the obligations of the seller under a contract of sale. The seller must deliver the goods, hand over any documents relating to them and transfer the property in the goods, as required by the contract and the Convention.

The ´fall-back´ rule for the delivery of the goods is contained in Article 31. If the seller is not bound to deliver the goods at any other particular place, his obligation to deliver consists in handing the goods over to the first carrier for transmission to the buyer.[2] In practical terms, this means that the buyer would have to contract for carriage, and to bear the costs for such carriage. Moreover, the goods would be at his risk in relation to the seller after the goods are handed over in accordance with the above provision. The term ´delivery´ is to be construed narrowly.[3]

In addition to the goods, the seller has to hand over the documents relating to the goods. Article 34 provides that if the seller is bound to hand over the documents relating to the goods, he must hand them over at the time and place and in the form required by the contract.[4] Should the contract provide for the use of a documentary credit as a method of payment and, at the same time, as the means of handing over the documents, the seller has to deliver documents that are in conformity with the description in the contract of sale and the identical terms of the credit.

In international trade, a practice is said to exist, which links payment, whether on open account, on the basis of a documentary collection or by means of a documentary credit with the ´constructive´ delivery rather than with the ´actual´ delivery.[5] The seller may link the payment and delivery of either the

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2 This rule applies when the contract of sale involves carriage of the goods, which is the situation this study is intended to look at more closely. If the contract does not involve carriage of the goods, and the contract relates to specific goods, or unidentified goods to be drawn from a specific stock or to be manufactured or produced, and at the time of the conclusion of the contract the parties knew that the goods were at, or were to be manufactured or produced at, a particular place, the seller´s obligation to deliver consists in placing the goods at the buyer´s disposal at that place. Finally, in other cases, the seller has to place the goods at the buyer´s disposal at the place where the seller had his place of business at the time of the conclusion of the contract.

3 It means simply the handing over of the goods. In comparison, Article 19(1) of the Uniform Law of International Sales used the French concept ´délivrance´ that "consists in the handing over of goods which conform with the contract" (Honnold, no 210. p. 241).

4 If the seller has handed over documents before that time, he may, up to that time, cure any lack of conformity in the documents, if the exercise of this right does not cause the buyer unreasonable inconvenience or expense. However, the buyer retains any right to claim damages as provided for in the CISG. The provisions of Article 37 apply generally to the cure of defects in documents although it only mentions the goods (Honnold, no 220, p. 250).

5 UN/CEFACT Recommendation No. 12 ´Measures to facilitate maritime transport documents procedures´, second edition, Geneva October 2001, ECE/TRADE/240, 14.-15. pp.3-4. The term ´constructive delivery´ apparently has its roots in English common law. English common law even considers a CIF contract as "not a sale of the goods themselves but a sale of the documents relating to the goods" (Schmitthoff, Export Trade 1986, p. 30).

goods or documents to the other. Article 58 (2) of the CISG provides namely that if the contract involves carriage of the goods, the seller may dispatch the goods on terms whereby the goods, or documents controlling their disposition[6], will not be handed over to the buyer except against payment of price. ´Constructive delivery´ is deemed to be effected by the seller handing to the buyer a ´transport document´ issued by an independent third party, the carrier of the goods.[7] This document may, as shall be explained later, enable the transfer of title between the parties, or it may simply enable the transfer of a right of control over the goods.[8] The seller can in principle require payment at the seller´s place of business. If the payment is to be made against the handing over of the goods or of documents, the buyer must pay where the handing over takes place.

The payment against handing over the documents usually takes place in accordance with preset rules such as the Uniform Customs and Practice for Documentary Credits UCP500 or the Uniform Rules for Collections URC 522. In the case of collections and in three-partite documentary credits, payment takes place normally in the buyer´s country, whereas in the case of a traditional four-partite documentary credit arrangement, in which a local confirming bank is involved, the payment takes place in the seller´s country. Nothing prevents the parties from agreeing on a third country, of course.

The contractual provision is in respect of the delivery of the goods, and to some extent of the handing over the documents, is normally in the form of a trade term. Trade terms such as CIF and FOB have probably existed since the 17th century, and English common law has a great deal of jurisprudence on CIF and FOB contracts, which have been conceptually crystallised over hundreds of years.[9] This jurisprudence takes a stand on, amongst others, what is to be regarded as a valid tender in respect to trade documentation. For instance, a

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6 The CISG was drafted before the discussion on electronic alternatives to trade documentation became active. As Ramberg notes (Konossement och köpavtal, 1991, note 13), the issue of paperless trade has not been observed in some relevant commentaries on the CISG. Honnold (no 217, note 1, p. 249) refers to the Incoterms 1990 A8 which covered electronic documentation. Bianca-Bonell, p. 428, suggests that the words "documents controlling disposition of the goods" should not be interpreted "narrowly or in the strict legal sense of any particular national law".

As has been stated already, the provisions of the CISG were recently analysed by the Secretariat of UNCITRAL with a view to assessing their amenability to electronic commerce. The Note by the Secretariat (A/CN.9/WG.IV/WP.91) does not raise the issue of the contractual delivery of electronic trade documents. The same goes for the first Opinion of the CISG Advisory Council.

One way to interpret the fact that the Convention does not allow adhering states to stick to national form requirements would be to refer to the obligation to interpret the Convention in its international context. When electronic commerce gains ground in international trade, national interpretations imposing form requirements would be against a universal interpretation. Another possibility would be to amend the Convention, but that would presumably draw the process out to some length.

7 Similarly UCC § 2-310(b): "if the seller is authorized to send the goods he may ship them under reservation and may tender the documents of title". Referring to the possibility of delivery effected by documents of title was considered during the preparations of the CISG. This was, however, found to be too complicated for the drafting of other articles (Honnold no 219, p. 250).

8 The sea waybill under the Nordic Maritime Codes has been stripped of that function as well. Still, it remains presumably under the seller´s delivery obligations.

9 For English common law, see in particular Sassoon, CIF & FOB Contracts, 3rd edition, London 1984.

buyer under a CIF contract at English common law has been entitled to require the tender of a shipped bill of lading.[10]

In the international context, in any case, the English common law CIF contract should be seen as a national phenomenon. It is possible that national law in other countries, based either on custom or statute[11], may introduce similar presumptions. Outside the administrative and fiscal contexts, however, national law seldom prescribes requirements as to the delivery of goods and documents on a mandatory basis, but leaves the matter to be decided by the parties. Trade terms used in international trade have been harmonised, and the sooner uniform interpretations of standard trade terms are adopted, the better. Since 1936, the International Chamber of Commerce has published standard interpretations for trade terms.[12] It should be noted that the use of the INCOTERMS has received a formal recognition from UNCITRAL, which recommended their use in 1992. Thus, as the INCOTERMS are a recognised and established part of international trade law, it is my intention to assume that they are followed and base my presentation on that fact. Harmony in international trade can only be achieved by sticking to harmonised practices. In my view, it would therefore be useless to trace existing discrepant local practices in a legal essay on a field where harmony is attainable.

The role of trade terms is to determine the obligations and costs of the seller and the buyer in respect of the delivery of the goods, usually involving carriage of the goods by an independent carrier, and including, where necessary, the insuring of the goods as well as compliance with customs formalities including the payment of relevant duties. As regards the seller´s delivery obligation, which may have implications under national law on the transfer of property and the law applicable, it is not always uncontested that the INCOTERMS really designate the place of delivery according to the contract of sale.[13]

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10 *Diamond Alkali Export Corporation v. Fl. Bourgeouis*, [1921] 3. K.B. 443. This requirement was based on the fact that common law conferred the status of a document of title to a shipped bill of lading.

11 The commercial law of the United States has its own conceptions of FOB terms. Whereas INCOTERMS 2000 envisage the use of the FOB term only in traditional sea carriage, the goods being loaded "over the ship´s rail", the US law knows six different FOB terms relating to various modes of transport. Section 2-319(1) of the Uniform Commercial Code contains fallback terms for the FOB term. FOB as an acronym used to have political connotations during the Clinton administration.

12 Later revisions have taken place in 1953, partially in 1976, in 1980, in 1990, and the latest version is INCOTERMS 2000 (ICC Publication No 560) For INCOTERMS 2000, see also Ramberg, ICC Guide to Incoterms 2000 (ICC Publication No 620) as well as Railas, Incoterms for the New Millennium, ETL, 2000, pp. 9-22.

The ICC gave useful instructions on the proper use of INCOTERMS by publishing a set of guidelines called the´Golden Rules of Incoterms´ in the 1990s.

In the United States, there is a collection entitled ´Revised American Foreign Trade Definitions´, which was adopted in 1941 by a Joint Committee representing, inter alia, the Chamber of Commerce of the US and the National Council of American Importers. Those terms eventually found their way to the Uniform Commercial Code, Sections 230 to 2-235 (Chandler, III in Transfer of Ownership, p. 421). The US business community is not, however, opposed to the use of the INCOTERMS, see Frank Reynolds, INCOTERMS for Americans, New York, 2002.

13 For instance, the Italian courts have been reluctant to give the INCOTERMS that task (Zunarelli in Transfer of Ownership, pp. 206-207). See also Kronke in Internet..., pp. 76-77, and Lando, The 1986 Hague Convention on the Law Applicable to Sales.

If nothing is agreed and by virtue of the relevant conflict of laws rules, Article 31 of the CISG is to be applied, the situation is practically the same as if Ex Works (´EXW´) or, where the sale involves carriage of the goods, Free Carrier (´FCA´) of the INCOTERMS 2000 were applied. Under EXW, the buyer contracts and pays for the carriage and, if needed, for the insurance and, also, takes care of both export and import formalities, which results in that the seller´s duty to hand over documents is very limited. That duty covers only the invoice, the packing list and similar documents. Under FCA, the seller has more documentary duties.

Under the so called ´D-terms´ (Delivered at Frontier or ´DAF´, Delivered Ex Ship ´DES´, Delivered Ex Quay ´DEQ´, Delivered Duty Unpaid ´DDU´, Delivered Duty Paid ´DDP´), as well as under the ´C-terms´ (Carriage Paid to a destination ´CPT´, Carriage and Insurance Paid to a destination ´CIP´, Cost and Freight ´CFR´ and Cost, Insurance and Freight ´CIF´), the seller has to contract for the carriage, and in CIP and CIF the letter ´I´ indicates that the seller has to insure the goods as well.

On the contrary, in the case of Ex Works ´EXW´ and the ´F-terms´ (Free Carrier ´FCA´, Free Alongside Ship ´FAS´ as well as Free On Board ´FOB´) the buyer has to contract at least for the main carriage. Under the F-terms however, the seller has obligations in respect of transport documentation.

The ´C-terms´ are particularly useful in connection with documentary credits, since the seller is able to fulfil his obligations at his own end before the main carriage takes place. Thus the seller delivers the goods to the carrier, either "over the ship´s rail" (the terms CFR and CIF) or simply "to the carrier" in his terminal (the terms CPT and CIP)[14]. The seller is responsible for export formalities, but not for import formalities and duties.

To illustrate the contractual obligations to deliver trade documentation imposed by a trade terms agreed on by the parties, one may have a look at the traditional CIF terms. According to Point A1 of CIF INCOTERMS 2000, the seller must provide, in addition to the goods, the–commercial invoice or its equivalent electronic message, in conformity with the contract of sale, as well as any other evidence of conformity[15] which may be required by the contract of sale. In addition, Point A3(b) provides that the seller must obtain, at his own expense, cargo insurance as agreed in the contract, such that the buyer or any other person having insurable interest in the goods shall be entitled to claim directly from the insurer and provide the buyer with the insurance policy or other evidence[16] of insurance cover.

Finally, according to Point A8, the seller must, at his own own expense, provide the buyer without delay with the usual transport document for the agreed port of destination. This document, which can be, for instance, a

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14 The terms ´CPT´ and ´CIP´ are suitable to all carriages whereas ´CFR´ and ´CIF´ are recommended for traditional sea carriages, where loading and unloading take place "over the ship´s rail".

15 On such evidence, see Chapter VIII.6.7., *post*.

16 Interestingly, INCOTERMS2000 does not mention the possibility that an insurance policy or other evidence of an insurance contract could be in electronic form. For this issue, see *infra*.

negotiable bill of lading, a non-negotiable sea waybill or an inland waterway document, must cover the contract goods, be dated within the period agreed for shipment, enable the buyer to claim the goods from the carrier at the port of destination and, unless otherwise agreed, enable the buyer to sell the goods in transit by the transfer of the document to a subsequent buyer in the case of a negotiable bill of lading, or by notification to the carrier e.g. in the case of a sea waybill. When such a transport document is issued in several originals, as is the case with negotiable bills of lading, a full set of originals must be presented to the buyer. Although any of these originals, as will be seen later, will give its holder independent rights as against the carrier, the seller is not entitled to indorse different originals separately. In a situation in which the surrender of one original to the carrier makes other originals void, the holders of such other originals have a recourse against the seller.[17]

Point A8 of CIF INCOTERMS 2000 adds, as every Incoterm ever since the publication of the INCOTERMS 1990 as a rule does, that where the seller and the buyer have agreed to communicate electronically, the transport document referred to may be replaced by an equivalent electronic data interchange (EDI) message. This applies naturally only between the seller and the buyer since the Incoterms only govern this relationship and constitute a part of the contract of sale and are incorporated by reference. The availability and use of electronic transport documentation calls for a separate agreement between the carrier and the shipper. Since a valid tender of electronic records as commercial documents requires the assent of the buyer as the primary consignee of the goods, there is no need to require his approval for the issue of an electronic transport document in the first place. The same applies to every new buyer who enters into the position of a consignee or indorsee of a transport document. However, as the buyer as consignee or indorsee is not, as a rule, obliged to accept an electronic transport document, there is not much use for an electronically issued transport document, unless the new buyer being the next in the chain accepts such an issue.

The documents to be delivered by the seller to the buyer are defined in the contract of sale. The definition can be a simple reference to a trade term, which imposes standard requirements. Parties may modify these requirements. When documentary credits are used, documentary requirements are especially elaborate.[18]

INCOTERMS 2000 contains provisions relating to most documentary obligations that arise in connection with an international sale of goods transaction. However, the drafters of the next revision might wish to consider amending the text to be more all-embracing.[19]

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17 Under the relevant rules applicable to documentary credits (see Chapter VIII. 6.3., *post*), the seller has a similar obligation. A counter-argument is that the buyer, when the seller´s obligations are clearly written in INCOTERMS 2000, should insist on his rights to get all the originals and, failing to do so,has waived his rights.

18 The ICC Model International Sale Contract (Manufactured Goods Intended for Resale), ICC Publication No. 556, contains in Part A, General provisions, a checklist of documents regularly used in documentary credits.

19 Point A 1 of each term could, in my view, be a catch-all term and read as follows: "The seller must provide the goods and the commercial invoice, or its equivalent electronic message, in conformity with the contract of sale, (...) any (...) evidence of conformity, or any other documents which (...) are required in these terms or by the contract."

The goods and documents delivered must be in conformity with the contract of sale. The non-conformity of the goods constitutes, according to the CISG, a breach of the contract, which gives the buyer the remedies provided for in Articles 45 to 52 of the CISG. If the goods do not comply with the terms of the contract, the buyer may reject the goods to the extent this is allowed in the Convention.

Trade law, including the CISG and trade contracts, are comprehensive on the consequences of the non-delivery or non-conformity of the goods. But what happens if the documents to be tendered fail to meet the criteria imposed on them by the contract, the terms of a letter of credit, or a legal instrument of national law or INCOTERMS 2000?

Generally speaking, the buyer may also reject the documents, if these are clearly not in accordance with the terms of the contract, with the requirements of laws and regulations or with the practise in the particular trade. If the buyer is entitled to claim a negotiable transport document to be tendered in the case that he is to sell the goods further, a non-negotiable sea waybill is not a valid tender.

The Incoterms are silent about the consequences of not acting in accordance with them. Similarly silent are the terms of the contract. Legislation, which normally remains a secondary source of law as regards the positive obligations of the parties, has to be looked into, when interruptions in a contractual relationship take place. The CISG gives the seller certain rights to remedy deficiencies in the documents. Article 34 of the Convention provides namely that where the seller has handed over the documents before the time stipulated in the contract, he may, up to that time, cure any lack of conformity in the documents, if the exercise of this right does not cause the buyer unreasonable inconvenience or expense. However, the buyer retains any right to claim damages as provided for in the convention.

Although the Convention is very comprehensive as to the consequences of the seller tendering non-conforming goods, it appears to be silent about the consequences of the seller tendering non-conforming documents.[20] Article 39 states that the buyer must notify the seller of a lack of conformity within a reasonable time after discovery. On this score, the English text refers to the lack of conformity "of the goods". One can ask as did Bernard *Audit*[21]:

> "Does this restriction mean that Article 39 is inapplicable if the non-conformity appears in the documents instead of the goods – although delivery of documents is closely associated in the Convention with delivery of the goods themselves?"

Audit raises the conflict between different language versions of the Convention. The French text namely is not as restrictive and speaks of *défaut de*

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20 English common law gives a CIF buyer the independent right to refuse non-conforming goods on the one hand and non-conforming documents on the other. "The right to reject the documents arises when the documents are tendered, and the right to reject the goods arises when they are landed and when after examination they are not found to be in conformity with the contact" (as observed by Devlin J. in *Kwei Tek Chao V. British Traders and Shippers Ltd, [1954] 2 Q.B. 459 and 481*).

21 Audit, p. 8.

conformité in general terms. Moreover, *Honnold* has supported a wider interpretation of this provision.[22]

Any major discrepancy between the documents and the requirements as to them may lead to the application of Article 49 (1) whereby the buyer may declare the contract avoided if the failure of the seller to perform any of his obligations under the contract or the convention itself amounts to a fundamental breach of the contract.

There is a clear-cut line in the convention between non-delivery of the goods and the delivery of non-conforming goods. In the case of non-delivery, the buyer may fix, pursuant to Article 47(1) of the convention, an additional period for the seller to perform his obligations. This provision only mentions the goods. However, given that in certain cases there cannot be any access to the goods by the buyer without conforming documents such as a document of title, it is submitted that at least in cases where the documents do not at all perform their commercial or statutory function, there is either a non-delivery in terms of a ´constructive´ delivery or a fundamental breach of the contract.[23]

In cases where documentary credits are used, the buyer imposes documentary requirements becoming terms of the credit which usually form part of the contract of sale. The banks acting as intermediaries have to verify whether these requirements are met. The banks have very little leeway in this respect. The doctrine of strict compliance[24] leads to the banks rejecting the documents which do not appear, on their face, to be strictly in conformity with the terms of the credit. The commercial practice is that a majority of first tenders of documents are defective and have to be corrected by the seller. Should this, however, not be accomplishable, then a fundamental breach of the contract of sale is imminent.

V.2 Passing of risk

The significance of the passing of the risk is that the loss of or damage to the goods after the risk has passed to the buyer does not discharge him from his obligation to pay the price, unless the loss or damage is due to an act or omission of the seller (Article 66 of the CISG). As to the consequences of the seller´s risk, Article 36 of the CISG provides that the seller is liable in accordance with the contract and the convention for any lack of conformity which exists at the time when the risk passes to the buyer, even though the lack of conformity becomes

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22 Honnold, Uniform Law for International Sales (1987) at 280 § 256.

23 To illustrate further the distinction English common law makes between the delivery of goods and the delivery of documents one can mention that English common law treats the delivery of an appropriate insurance document to cover the goods when in transit as an essential condition of a CIF contract and the buyer would be entitled to refuse the acceptance of uninsured goods even when they have arrived safely at the port of destination (*Diamond Alkali Export Corporation v. Fl. Bourgeois [1921] 3 K.B. 443*)

24 see Chapter X, *post*.

apparent only thereafter.[25] Similarly, the seller may become liable for non-delivery[26] if the goods are completely lost and cannot be replaced in due time[27].

Furthermore, the party who bears the risk also has an insurable interest in the goods, and transport insurance can be effected in his favour.[28] In the absence of an insurance cover, the party bearing the risk must try to recover the losses he has sustained from the carrier, if the damage has been attributable to the carrier´s negligence to the extent provided for by the rules applicable to carrier´s liability.[29] The right of action against the carrier may arise in contract or in tort, depending on the jurisdiction and the contractual framework.

Articles 67 to 70 of the CISG contain more detailed provisions as to the passing of risk. In practice, however, the moment when the risk passes is normally determined in accordance with the INCOTERMS, according to which the risk usually passes at delivery.[30] As the INCOTERMS deal with the division of costs as well, one could say that unexpected costs not relating to official formalities generally fall on the party bearing the risk. Thus, if the cargo has to contribute to a general average, the payment of the contribution falls on the party bearing the risk.

As the passing of risk does not appear to have any direct bearing on electronic commerce, there is no need to present the rules on the passing of risk in greater detail.[31] It is submitted, in any case, that questions relating to the passing of risk have been very satisfactorily solved in the contract practice by

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25 The seller is also liable for any lack of conformity which occurs after the time of the passing of the risk which is due to a breach of any of his obligations.

26 The consequences for non-delivery and lack of conformity are somewhat different under the United Nations Sales Convention. However, in contract practice their treatment may be becoming more similar to eavh other, see e.g. the ICC Model International Sale Contract, General Conditions, Articles 10 and 11.

27 A delayed delivery usually attracts special remedies under law and standard contracts.

28 When trade terms CIP or CIF are used, the seller contracts for insurance cover in favour of the buyer, but this obligation is minimal since failing any express agreement to the contrary, the cover only has to be the minimum cover of the Institute Cargo Clauses of the Institute of London Underwriters. Institute Cargo Clauses C, which is the minimum cover, is however inadequate for most cargoes.

29 See Chapter VI.1.2., *post*.

30 The terms intended for carriage by conventional vessels (FOB, CFR and CIF) require the seller to deliver the goods on board the vessel at the port of shipment. However, the risk passes to the buyer slightly before that, namely when the goods pass the ship´s rail.

Irrespective of the use of INCOTERMS, Article 68 of the CISG usefully adds that the risk in respect of goods sold in transit passes to the buyer from the time of the conclusion of the contract. However, if the circumstances so indicate, the risk is assumed by the buyer from the time the goods are handed over to the carrier who issued the documents embodying the contract of carriage. It might therefore be advisable to use the original trade term (which the seller used as the buyer of the goods in the preceding sale) in resale. When goods are sold afloat, it is normally impossible to examine the goods, and the seller cannot be held liable for damages occurring after their shipment. Should the seller know about a loss of or damage to the goods, this would apparently amount to a fundamental breach of the contract.

31 For the rules of transfer of risk in national law, see Gunnar Lagergren, Delivery of the Goods and Transfer of Property and Risk in the Law on Sale, Stockholm 1953. See also Berndt von Hoffmann, Passing of Risk in International Sales of Goods, in International Sale of Goods, Dubrovnik Lectures, Edited by Petar Sarcevic and Paul Volken, New York, 1986, pp. 265-304.

referencing to the acronyms of the INCOTERMS, thus incorporating by reference a number of relevant rules affecting the rights and obligations of the parties. Such referencing serves as a model for incorporating other provisions relating to the contractual relationship.

It should be mentioned, however, that the rules on the passing of risk relate operationally to the rules covering the carrier´s liability in the sense that the the party having sustained the loss on the basis of the distribution of risk should be entitled to sue the carrier for the latter´s fault or neglect. The case may then be based, at least theoretically, either on contract or tort law. One of the main reasons for the revision of the English 1855 Bill of Lading Act was that it required that the property in the goods pass to the indorsee under the contract of sale, before the indorsee could sue the carrier in contract. Problems arose particularly in connection with bulk shipments.[32] The transfer of property takes place in principle by indorsing a document of title, which mkese the issue partly documentary. In the context of electronic documentation such a requirement would cause even more problems than in the traditional paper document environment. Fortunately, the 1855 Act has now been replaced by the 1992 Carriage of Goods by Sea Act according to which the right to sue is no longer tied to the transfer of property.

V.3 Cargo insurance

Only two Incoterms, the ´C´ terms ´CIF´ and ´CIP´, contain an obligation on a party in the contract of sale to insure the goods. Under those terms, "the seller must obtain at his own expense cargo insurance as agreed in the contract, such that the buyer, or any other person having an insurable interest in the goods, shall be entitled to claim directly from the insurer and provide the buyer with the insurance policy or other evidence of insurance cover".[33] In other cases, the party bearing the risk, and having therefore insurable interest in the goods, can insure the goods to the extent he deems it necessary. It should be mentioned that even a CIF or CIP buyer needs to protect himself since those Incoterms only require the seller to provide insurance cover in accordance "with minimum cover of the Institute Cargo Clauses (Institute of London Underwriters) or any similar set of clauses"[34]. In addition, the seller shall, when required by the buyer, provide at the buyer´s expense war, strike, riot and civil commotion risk insurance where procurable.

Cargo insurance has to be distinguished from the carrier´s liability insurance. Shipowners´ liability is, as a rule, insured with protection and indemnity (P&I) clubs. Generally speaking, carriers in all modes of transport, but especially in sea

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32 See *Leigh and Sillivan Ltd. V. Aliakhmon Shipping Co. Ltd. [1985] 2. W.L.R. 289*.

33 CIF INCOTERMS2000 A3(b) and CIP INCOTERMS2000 A3(b).

34 Ibid.; This minimum cover corresponds to Institute Cargo Clauses C. Sometimes, however, commercial custom has modified this obligation by presuming that the seller procures insurance in accordance with Institute Cargo Clauses A (i.e. all risks).

transport, can exonerate themselves from liability or extensively limit their liability. The cargo insurer, after having indemnified the merchant, claims recovery from the carrier, who is defended by a P&I club[35], on the basis of subrogated rights.

V.3.1 The legal rules applying to insurance documentation

There are international requirements as to insurance documents that have to be delivered by the seller to the buyer. The requirement of CIF and CIP INCOTERMS 2000 is, as noted above, "the insurance policy or other evidence of insurance cover". This would seem to indicate that the insurance document need not be transferable. The Uniform Customs and Practice for Documentary Credits UCP500 and the International Standard Banking Practice ISBP contain express requirements as to the form and contents of an insurance document. These will be examined later in Chapter VIII.6.4.

In addition to international rules relating to insurance documents, national law requirements have a role to play. Such requirements may also be based on a local custom. In international trade, the cargo insurance conditions established in the London market, the Institute Cargo Clauses 1982, are applied extensively.[36] Even INCOTERMS 2000 expressly refers to the Institute Clauses. These Clauses are, by an express reference, subject to English law and practice. This choice of law clause could be construed to apply only to the interpretation of the clauses, or it could apply to the entire transport insurance contract. In any case, the approach of English law on insurance documentation is of importance to electronic commerce, in part since the *Bolero System* is subject to English law.

English law on marine insurance is largely based on the 1906 Marine Insurance Act. Section 22 of the act provides that, subject to the provisions of any statute, a contract of marine insurance is inadmissible in evidence, unless it is embodied in a marine policy in accordance with the Act. Furthermore, a marine policy must be signed by or on behalf of the insurer, and in the case of a corporation a corporate seal may be sufficient.[37] A marine policy is legally

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35 Many P&I clubs operate under English law. Under English law, direct action against the liability insurer of the tortfeasor or negligent contractual partner is not allowed.

36 An estimate has been made that in two thirds of cargo insurance covers issued in international trade, the Institute Clauses are applied. During the current revision process of the ICC Uniform Customs and Practice for Documentary Credits some opinions have even been are expressed that the use of the Institute Clauses should be mandatory. For the Institute Clauses, including those for cargo, for war, or for strikes, see N.G. Hudson, The Institute Clauses Handbook, 3rd edition London 1999. There are similar Institute Clauses for air transport.

37 Section 24.

relevant because it contains express warranties.[38] Furthermore, a broker may exercise a lien over a marine policy.[39] It has not been decided whether, for the purposes of the Marine Insurance Act, there must be a formal policy in existence containing the statutory particulars, or whether any document containing these particulars is admissible under section 22 and can be sued on under English law.[40]

The Marine Insurance Act knows a ´floating policy´, which is a policy describing the insurance in general terms leaving the name of the ship or ships and other particulars to be defined by subsequent declaration. The subsequent declaration or declarations may be made by an indorsement on the policy or in any other customary manner. This type of policy, which is often described as ´open´, is used in cargo insurance. All shipments, which come within its terms, are automatically covered by the insurance, provided that the declarations thereunder are duly and properly made.[41] Where evidence of insurance under such policies is required, for example in connection with documentary credits, the practice is for a ´certificate of insurance´ to be issued in respect of the consignment.[42] In English practice, an insurance certificate or other document entitling the assured or transferee to demand the issue of a policy is regarded as the equivalent of a formal policy by implied agreement of the parties, unless their contract stipulates that the seller shall tender a formal policy. The decisive criterion is that the document tendered entitles the holder at any time to demand the issue of a formal policy.[43] The American practice, on the other hand, is that the seller can invariably tend an insurance certificate in lieu of an insurance policy.[44]Another method of insurance, akin to a floating policy, is to use an ´open cover´ which is an agreement whereby the underwriter undertakes to insure all shipments or interests of the assured for certain voyages or trades, either at specified rates of premium or at rates to be arranged. The underwriter is notified by the assured when the shipments are made of the interests attaching to the cover, and policies are then issued from time to time, as and when required.[45]

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38 Under English law in general, the breach of a condition in a contract may give rise to repudiate the contract whilst the breach of a warranty entitles only to damages. In English marine insurance law in particular, however, warranties are contractual conditions that must be precisely complied with, otherwise the insurer is discharged from liability as from the date of the breach. The Marine Insurance Act implies the warranties of seaworthiness and legality. Other (express) marine insurance warranties must be included in, written upon, or incorporated by reference into, the marine policy pursuant to section 34 of the Act.

39 Section 53(2) of the Act.

40 Arnould I, Chapter I para. 14 and Arnould III, Chapter 2 para. 13. For the form and contents of marine insurance policies and other documents such as slips, see Arnould III Chapter 3.

41 Templeman on Marine Insurance, p. 5.

42 Ibid. p.6.

43 Schmitthoff, Export Trade Eighth edition, 1986, p. 35.

44 Ibid.

45 Templeman on Marine Insurance, p.10. Arnould I (Chapter I para. 165) describes the difference between an open cover and a floating policy. First, unlike a floating policy, an open cover has no more legal effect than a ´slip´, and consequently policies must be issued in respect of all shipments declared. Secondly, the sum insured in a floating policy is reduced by the value of each shipment declared until the sum insured is exhausted, whereas an open cover is not usually subject to any aggregate limit of liability, but is underwritten on the basis of a maximum limit shipped by any one vessel.

A statutory requirement exists for a marine policy to specify the name of the assured, or of a person who effects the insurance on his behalf. When the trade terms CIF or CIP are used, the seller effects insurance in favour of the buyer. When the CIF term is used, the seller bears the risk until the goods pass the ship´s rail[46], at which point the risk passes to the buyer. At the same time, the principal insurable interest passes to the buyer[47] In the practice of cargo insurers, trade terms, most notably those following INCOTERMS 2000, are used to indicate in whose favour the insurance contract has been written. The two C-terms bringing about insurance obligations for the seller, ´CIF (named port)´ and ´CIP (named destination)´, presuppose that the seller effects insurance for the buyer´s benefit and that the risk passes to the buyer already at the seller´s end before the main carriage. The other Incoterms do not require a party to insure for the other party´s benefit.

A transferable insurance policy may be used when goods are intended to be traded. The use of such a quasi-negotiable document recognised by the insurer makes it clear that the insurance covers the assignee´s interest in the goods.[48] The assignment of an insurance policy, which may become relevant when goods are sold in transit, is usually effected by indorsement (in blank) and delivery or in any other customary manner. The relevant thing, however, is to show that the intention to transfer the benefits of or rights under the policy to the person to whom it was delivered. An assignee of the policy may by Section 50(2) sue in his own name.[49] This English law approach may not, however, be shared by everybody in the international trading community. Outside the rigid English statutory approach, which has been greatly alleviated by practice[50], there is

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46 CIF INCOTERMS 2000, Point A.5.

47 The seller may have an insurable interest even after since insurable interest can also be defeasible or contingent.

For an example of this, see Templeman on Marine Insurance, pp. 116-117.

48 In Sweden, for instance, cargo insurance conditions are said to exclude Article 54 of the Swedish Insurance Act (Lag 1927:77 om försäkringsavtal), which would automatically extend the insurance cover to third parties´ interests. Conversely, in Denmark and Norway persons deriving an interest in the goods from the assured may also be protected without explicit stipulations in the individual policy. (Johnsson in Transfer of Ownership, pp. 389-390, Selvig, Cargo Insurance, pp. 80-81).

Under Anglo-Saxon law, attention has to be paid to how the policy is drafted and transferred since the doctrine of privity of contract prevents the insurance moving with the goods as is the case with many civil law countries. As *Mallon* noted on 24 November 2003, US cargo policies usually include a broad assureds clause whilst English policies do not. English practice builds on an assumed transferability of insurance certificates in lieu of policies.

49 Arnould I Chapter I para. 30. Templeman on Marine Insurance, pp. 76-77. However, it should be noted that the Marine Insurance Act draws a clear distinction between the marine policy and the marine insurance contract, and the terms are not interchangeable. This means, for example, that the statutory dispensation allowing assignment applies only to the policy and not to the underlying contract. (Law Commission 2001, p. 31).

50 *Mallon* observed that a custom has grown up and appears to be acceptable to business interests of the indorsement of insurance certificates as if they were negotiable instruments. He added, referring most certainly to the English law position, that this practice is not watertight. For the treatment of insurance certificates under English law, see Arnould I Chaper VI, para. 166 and the references contained therein.

nothing inherent in the concept of an insurance policy to make it more transferable than other sorts of insurance documents. Therefore the quality of transferability has been added, in some cases, to insurance certificates as well.[51]

V.3.2 Electronic insurance documents

The possibility of using electronic insurance documents in international trade is tied to the use of a formal policy. The Bolero Feasibility Study[52], conducted on the legislation of some eighteen jurisdictions, suggests that insurance policies commonly have to be in writing, but insurance certificates generally do not. Furthermore, very frequently assignments of insurance policies have to be in writing.[53] Therefore the use of electronic insurance documents could be enhanced if the use of a written policy and its written indorsements could be avoided.

As regards English law, the Law Commission has analysed the need for revision of the Marine Insurance Act 1906. The Commission´s report concluded that there is no requirement for a marine policy to be in writing and, even if such requirement were to be inferred from the wording of the Act, that it would preclude the use of electronic insurance documents. Neither does the signature requirement preclude the use of an electronic document. Furthermore, the requirement to write down express warranties can be met through electronic media as well.[54]

On the other hand, the Law Commission concluded that it is uncertain whether the requirement for an indorsement for an assignment of a policy is met by using an electronic medium. The Law Commission notes "(a)n indorsement usually refers to something which is written or printed on the back of a document. It is difficult to apply this concept to an electronic document". Moreover, the Law Commission concluded that "the fact that section 53(2) provides that a marine policy is capable of being subject to a lien suggests... that a tangible object is required and that an electronic document will not therefore suffice". These two problems led the Law Commission to conclude that a marine

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51 One of the ICC Banking Commission´s unpublished queries related to a question of indorsement of an insurance certificate. Usually the benefiary having taken the insurance cover indorses the certificate to his order. Therefore a negotiating bank would only need to indorse the document further if it had been made the party assured in the insurance document, or if the beneficiary had indorsed the document to the bank expressly.

52 Bolero Feasibility Study, 1999, p. 73, at http://www.boleroassociation.org/downloads/legfeas.pdf, visited on 4.8.2003. For the *Bolero System* and the Feasibility Study, see Chapter VIII.7., *post*.

53 Ibid., p. 13.

54 Law Commission 2001, p. 32.

insurance transaction cannot be entirely electronic and that Marine Insurance Act 1906 has to be revised in this respect.[55]

The Bolero Feasibility Study suggests that many formalities can be overcome by using third party beneficiary insurance contracts. This means that the insurance is expressed to be for the benefit of all who have an interest in the goods. These parties must have an insurable interest in the goods. Alternatively the seller may insure for himself and as an agent on behalf of the buyer. The solution suggested in the Feasibility Study is, of course, ingenious, and illustrates at the same time the benefits of governments implementing electronic commerce legislation.

It should be added that insurance policies for goods will initially be outside the *Bolero System*. However, the Bolero System may record the policy, as well as copies of insurance certificates, for information purposes and presentation under letters of credit.[56]

In trade conducted between regular business partners, insurance certificates are often unused and are replaced by monthly declarations to the insurance company in charge of goods dispatched. Therefore the question of the form of insurance documents is particularly interesting in the context of documentary credits. The requirements for insurance documents imposed by the Uniform Customs and Practice for Documentary Credits UCP500 and the recent International Standard Banking Practice will be examined in Chapter VIII.6.4., *post*.

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55 Law Commission 2001, pp. 32-35. The Commission has outlined some options or principles to guide the reform:

- The reform of the Act should dispense with the rule that the contract for marine insurance is only enforceable once it is embodied in a (paper) marine policy;
- The reform must enable the marine insurance contract to continue to fulfil its essential role in the future;
- One option is to dispense with the marine policy as a legal document under the Act;
- Another option is to retain the marine policy as a legal document under the Act, but defining it to include an electronic equivalent;
- Both options would effectively do away with the broker´s lien;
- A further reform of the Act to allow the assignment of marine insurance contracts or electronic marine policies would be needed. The assignment mechanism to be adopted should be the subject of discussion with the insurance market;
- This further reform, and the assignment mechanism chosen, should be considered with regard to the role of marine insurance in international trade (for example the interaction with UCP500);
- The first option would do away with the statutory requirement that the policy specify the subject matter of the contract and the identity of the assured, and mean that a marine insurance warranty would be enforceable if it formed part of the marine insurance contract, which could be entirely oral;
- The second option would maintain the minimal content requiremens for the marine policy, and allow marine insurance warranties to be recorded in an electronic marine policy; and finally
- The signature requirement of section 24 of the Act would apply to an electronic marine policy, and statutory signature requirements could be met by electronic signatures available in the market.

56 Bolero Feasibility Study, 1999, p. 73.

V.4 Transfer of the property in the goods

The transfer of the property in the goods is a key issue of electronic commerce since property passes frequently by the indorsement of a bill of lading, which is a document of title.

The CISG does not regulate the transfer of property and neither does INCOTERMS 2000. One reason for this is that both the International Chamber of Commerce and the United Nations realised that issues of ownership, title, possession and other proprietary rights were far too complicated, and that national reservations regarding these issues were likely to prove too difficult an obstacle to the adoption of these sets of rules.[57] Recently, however, UNCITRAL and Comité Maritime International CMI have begun an extensive study on these issues.[58] At the same time, proprietary rights are being studied by a group of scholars doing informal background work with a view to creating draft articles for a suggestion on a European Civil Code. With these prerequisites in mind, proprietary rights affecting movable goods can probably not be dealt with satisfactorily in this individual study, although these are of core importance to electronic commerce as well. It is hoped that the text can still illustrate the problems and the existence of a variety of solutions thereto.

In the absence of international regulation of substantive proprietary rights in the sale of goods, answers to these these questions have to be sought from national laws. The year 1999 marked the publication of an excellent compilation of contributions by national correspondents on law relating to the transfer of property in 19 countries entitled *Transfer of Ownership in International Trade.*[59]

The first difficult question is to determine the law applicable to questions of ownership (conflict of laws). The possibilities could vary from the *lex fori* to the *lex contractus* relating to the contract of sale, and further to the *lex situs* (or the *lex rei sitae* used concurrently) of the goods or *lex carta sitae* of the document of title. If the law applicable were one of the two last mentioned laws, the question could arise of whether the law applicable would change constantly e.g. during the haulage of the goods through multiple Continental European jurisdictions (*res in transitu*).[60] The first question is, however, whether the parties can choose the law

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57 As expressed in the Introduction of ICC Publication No 546., p. 1.

58 Ibid., p. 2.

59 Transfer of Ownership in International Trade, edited by Alexander von Ziegler, Jette H.Ronoe, Charles Debattista and Odile Plégat-Kerrault (Kluwer/ICC, the Hague 1999, ICC Publication No 546). See also Hans Hoyer, International Sales and Security Interests with an Outline of Conflicts Laws, in International Sale of Goods, edited by Paul Volken and Petar Sarcevic, New York, 1986, pp. 401-442.

60 To complicate the matter even more, what if the goods are in a vessel carrying a ´convenience flag´? Is the flag state their *situs*? Furthermore, what could the situs be of oil in a pipeline crossing many countries? Oil in a pipeline can be pledged in many jurisdictions.

applicable to the transfer of ownership and other proprietary rights. There appears to be variation or uncertainty in national laws in this respect.[61]

The substantive law in question may address, in addition to the basic question of the transfer of ownership from the seller to the buyer, some ancillary issues such as the proprietary role of transport documents, rights to such documents, the effect of retention of title clauses[62], the right of stoppage in transit and proprietary interests such as liens held by third parties. It would be ideal if only one single law would govern such a diversity of issues. This may not necessarily be the case.[63]

The transfer of property is also a contractual obligation created under the applicable sales law, e.g. Article 30 of the CISG. Its contractual dimension has to be distinguished from the proprietary aspects of the transfer of property including any external liens, which the sales convention does not govern.

In contrast to the CISG, there are rules relating to the transfer of property in national sales laws. In most jurisdictions are general presumptions in this respect. The English Sale of Goods Act 1979 gives the intention of the parties a predominant role.[64] Under French law, transfer of ownership takes place when promises are exchanged, regardless of whether they are oral or written.[65] Belgium, Luxemburg and Italy follow the same approach.[66] If the transfer of property takes place by consent without delivery, it is not necessarily enforceable against third parties, however.

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61 In France, for example, some writers and the courts seem to have the view that parties cannot choose other laws than that of the *situs* to govern the transfer of ownership (Plégat-Kerrault in Transfer of Ownership, pp. 160-161).

Moreover, suggestions were made in France in the 1970s that parties could choose the law applicable to the pledge of the goods. The French courts, however, have maintained the view that French law is exclusively applicable to security interests in property located in France (*Société Kantoor de Mas c/ Société des Automobiles Ravel, Suprème Court, 24 mai 1933*, Revue critique de droit international privé 1934, p. 142, Plégat-Kerrault in Transfer of Ownership, pp. 171-172).

In Germany, the same discussion exists as well; see Wilhelm, para 303, page 179, who thinks that the situs rule cannot be regarded as mandatory. Moreover, Wilhelm (referring to Stoll, RabelsZ 32 (1968), 450 and 461) states as follows:

"Würde man bei Fällen mit auslandsbezug eine Disposition der Parteien über das materielle Sachenrecht auf dem Wege einer Parteivereinbarung über das auf eine sache andwendbare Recht zulassen, würde ´durch die Hintertüre´ der *numerus clausus* dinglicher Rechte durchbrochen".

For the *numerus clausus* of rights in *rem*, see Chapter VIII.10.1, *post*.

62 For retention of title, see *infra*.

63 See Chapter VIII.3.4.1., *post*.

64 Section 17(1) provides "Where there is a contract for the sale of specific or ascertained goods, the property in them is transferred to the buyer at such time as the parties to the contract intend it to be transsferred". Subsection (2) adds that

"For the purpose of ascertaining the intention of the parties regard shall be had to the terms of the contract, the conduct of the parties and the circumstances of the case."

65 Code Civil s. 1583.

66 Drobnig in Towards a European Civil Code, p. 487. Art. 1376 of the Italian Civil Code.

Under German law, mutual consent must be accompanied by the delivery of the goods to the buyer.[67] This approach also applies in Greece, the Netherlands and Scotland.[68] Moreover, under German and Dutch laws, there must be a real agreement to transfer property, which does not follow *ex lege* from the contract of sale.[69]

Under US law, the place and time of the seller completing his performance by the physical delivery of the goods or the execution of the contract is relevant in the absence of an agreement by the parties.[70] Under Swedish law, ownership is said to pass gradually from the seller to the buyer from the time of entering into the contract of sale until the completion of the transaction, when the buyer receives a complete, unencumbered and unrestricted title to the goods.[71]

Division is regularly made in national statutes between the sale of specific goods and the sale of unascertained or future goods by description.[72] I will illustrate how this distinction is made in national law. As regards unascertained goods, English law requires that goods are ascertained (separated) and appropriated (designated to the buyer) in order for the property to pass to the buyer. Ascertainment of cargo in bulk had caused problems, but a law reform in 1995 made it possible to create ownership in a specified quantity of goods in an identified bulk.[73] French law requires in principle the identification of goods (which means that the goods are both ascertained and separated). When a bulk cargo contains cargo destined for different buyers, identification could only take place after discharge. However, the French Supreme Court has decided that property in such cases already passes at the loading of the goods.[74] United States law requires generally that goods are identified in the contract. The parties are free to define how and when the goods are identified. One may have title to part of a cargo in a tank, although no segregation has taken place.[75]

The passage of property regularly takes place through the use of documents of title, which matter is examined in more detail *infra* and later in this study.[76]

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67 BGB Section 929, 1st clause. Actual delivery (the transfer of possession is not, however, always required).

68 Drobnig in *op.cit.*, p. 501.

69 Drobnig in *op.cit*, pp. 504-510.

70 Chandler, III in Transfer of Ownership, p. 421.

71 Johnsson in Transfer of Ownership, p. 367, Lagergren, p. 62.

72 See eg. Section 18 of the English 1979 Sale of Goods Act and Sections 1583-1586 of the French Civil Code (under French law, distinction is made between *corps certains* and *choses de genre*).

73 See the Sale of Goods (Amendment) Act 1995 and Debattista in Transfer of Ownership, p. 137.

74 *Sup. Cour, 13 fev 1978, Bull. Civ. IV. No 59*, Odile B. Plégat-Kerrault in Transfer of Ownership, p. 164. French courts to some extent are thus aligning the transfer of property with the passage of risk (*res perit domino*).

75 Chandler, III in Transfer of Ownership, pp. 420-421.

76 See Chapter VIII.3.4.1., *post*.

V.4.1 Other rights *in rem* involved in international sale transactions

In addition to the transfer of ownership between the seller and the buyer, there are different rights *in rem*[77], security or proprietary interests that affect the goods in international sale of goods transactions. There exist also rights *in rem* in respect of the documents representing the goods. Such rights may be held by the parties to the contract of sale, or they may be held by third parties. There may be concurrent property rights in the goods. The goods may be legally owned by the buyer, but they may be pledged to a bank financing the purchase. Third parties such as the creditors of a buyer gone bankrupt may take his place. The goods will then become an object of conflicting claims.[78]

These rights are based on national law and contractual arrangements and would require a comprehensive survey in order to be presented more adequately. Even definitions may not match. Each jurisdiction has namely developed its own system of rights *in rem,* which are far less harmonised than contract law. In an international context, especially where the goods are in transit, national jurisdictions may apply different conflict of laws rules to rights *in rem*. It is also possible that differ aspects of rights *in rem* are governed by different laws. For instance, the creation and acquisition of rights *in rem* may have to be regarded under one law, and the content of the right under another law.[79] As there are different rights *in rem* in different jurisdictions, the powers they give may different substantially. Sometimes a limited right *in rem* can even enjoy better protection than full ownership.[80]

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77 Each jurisdiction has its own system of rights *in rem*. Generally speaking, however, a right *in rem* is available against the world at large (*ultra partes*), whereas a right *in personam* applies in a given relationship (or *inter partes*). Jurisdiction relating to property may likewise take place *in rem*, e.g. where it relates to an arrested ship, or *in personam*. This is the case under English law.

Under Finnish law, which together with other Nordic laws has its closest roots in German law, a distinction is made between the law of property (Sachenrecht) and the law of obligations (Obligationenrecht). The Finnish law on property has often made a distinction between static and dynamic protection offered by law to the right in question. The static protection relates to the possibility to resort to procedural measures in order to enforce the right. The dynamic protection applies in situations where various rights collide. The static protection forms a basis for the *numerus clausus* principle, according to which there is only a given number of rights limited by law applying to the world at large (*ultra partes*). See Tepora in Juhlajulkaisu Simo Zitting, pp. 290-307.

For the German law on property, see e.g. Wilhelm, Sachenrecht, de Gruyter Lehrbuch, Berlin 1993. For French law, see e.g. Larroumet, Christian, Droit civil, Tome 2, Les Biens, Droits réels principaux, 3e édition, Paris 1997.

78 According to Article 4 of the European Insolvency Regulation the law of the state of of the opening of the proceedings will determine the priority order of various rights and claims. However, foreign rights *in rem* and retention of title clauses have been given in the Regulation the status of a creditor who can execute his claims separately.

79 In Italy, the law of the country of destination determines the acquisition of the right whereas the law of the transit country governs the content of the right, see Zunarelli in Transfer of Ownership, p. 204.

80 In France, a freight forwarder has a statutory lien on the goods under thecharge to secure the payment of freight and fees. The lien grants the freight forwarder´s claims a status which ranks above that of an unpaid seller even if the seller can invoke a retention of title clause, but this requires that the freight forwarder did not know about the clause (Code Civil section 95, Plégat-Kerrault in Transfer of Ownership, p. 174).

Some general remarks may be made in any case. Firstly, rights *in rem* serve many functions. They may aim for full ownership, or they may be security rights[81] invoked only in case of default. Secondly, ownership is to be distinguished from possession, which may be either physical or non-physical (regularly called *constructive possession* or *indirect possession*). The latter case means that the goods are actually in the custody of a third party. The effects of the transfer of physical possession (*traditio*) can be achieved in the latter case e.g. by giving notice to the person holding physical possession of an assignment or by indorsing a document of title relating to the goods (*traditio longa manu*).

Under English law, a rule of double possession arises from the *bailment* where the bailee has actual or physical possession whilst the bailor has *constructive possession*. In commercial transactions, shared possession is very typical. If A holds possession for himself or for a third party and later undertakes to hold it for B, this undertaking is known as an *attornment*. A person can attorn in advance by issuing a warrant or other document of title by which he undertakes to surrender the goods to whoever is the holder of the document. Delivery of the document (with any necessary indorsement) thus puts the deliveree in constructive possession.[82]

Under German law, an assignment of the right of possession can take place where goods are in the custody of a third party. As a legal consequence, constructive possession is transferred to the acquirer and ownership of the goods passes as well.[83] The same result is achieved if the transferor orders the bailor to hold possession on behalf of another person, and the bailor follows this order.[84]

The right of pledge is generally an accessory right *in rem* to secure a particular debt.[85] Pledge is a classical form of possessory security. The term ´possessory´ indicates that the pledged corporeal items are not held by the debtor but by the secured creditor or, otherwise, by a third person.[86] The pledge of the goods is an important security right for the bank that carries out documentary credit operations.[87] By a pledge the bank ensures that it has a contingent proprietary right to claim delivery of the goods from the carrier if its customer, the buyer as the applicant, fails to pay the sum due under the credit.[88]

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81 For conflict of laws relating to security rights affecting movable property, see Kaarina Buure-Hägglund, Irtaimiin esineisiin kohdistuvat reaalivakuudet kansainvälisen yksityisoikeuden kannalta, Vammala 1978.

82 Goode, Commercial Law, pp. 61-63.

83 Thorn in Transfer of Ownership, p. 186; the relevant provisions are sections 931, 398 and 870 of the Bürgerliches Gesetzbuch.

84 Ibid.

85 Zwitser in Transfer of Property, p. 259.

86 Drobnig in *op.cit*, p. 512.

87 The importance of the pledge of goods as a commercial security is probably less than the relationship between the customer and the bank as security. Gutteridge and Megrah (eighth edition 2001 at 256) note that the increased use of non-negotiable transport documents has not led to increased litigation revealing the existence of any problems in relation to security.

88 Debattista in Transfer of Ownership, p. 149.

Theoretically speaking, the pledge of the documents must be distinguished from the pledge of the goods. Naturally, the documents are relevant because they provide constructive possession over the goods, which nobody else can then claim.[89] The pledge of the goods themselves, however, makes it possible for the pledgee to enforce or liquidate the debt owed to him through selling the goods.[90] Unless the bill of lading is made to the order of the paying bank, the possession of the document is relevant for the maintenance of the pledge.[91]

Again, national law adds diversity to the legal nature or operation of a pledge. Dutch law, for instance, makes a distinction between possessory and non-possessory pledges.[92] Where a possessory pledge is involved, the actual possession must be transferred either to the pledgee or to a third party. For the non-possessory pledge, a registration requirement prevails. Documents of title may also become objects of pledge. An exception is a non-possessory pledge on negotiable instruments to order, which the Dutch law does not allow. The pledgee of the document of title also has also a right of pledge in respect of the goods represented by the document.[93] In France, on the contrary, a non-possessory pledge is not possible. Moreover, a contract of pledge has to be concluded in writing.[94] Romanic jurisdictions generally impose certain form requirements on pledges.[95]

A possessory pledge is normally possible through a third party that is in custody of the goods. The use of a non-possessory pledge with its administrative requirements (such as in the Netherlands) is therefore not necessary. Constructive or indirect possession can namely be established through the use of documents of title, or legal arrangements such as the *attornment* of English law. It is normal that the carrier must acknowledge that he holds possession on the account of the pledgee at least where no document of title is used.

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89 The pledge of documents of title is meant here; where documents delivered to the charge of the bank are not documents of title, there is no pledge of goods under English law unless the bank is named as consignee in the document (Gutteridge and Megrah, p. 256).

90 Under English law, the secured party, as the pledgee of the secured property, is said to have a ´special property´ in the secured property. It indeed empowers him to sell the secured property, in the event of a default in the performance of the secured obligations or on giving notice to the security provider. However, the secured party´s special property under a pledge does not constitute real or proprietary rights in respect of the secured property. It only confers rights *in rem* on the secured party, which are wider than those conferred by a contractual lien, see *infra* (Ali, pp. 101-102).

91 English legal system uses ´trust receipts´ or ´letters of trust´ to secure the pledgee´s position when the bank gives away the possession of the documents (Debattista in Transfer of Ownership at 149-150).

92 This is, of course, against the basic definition of pledge, *supra*. However, the concept of pledge has detached from its original meaning, and many Continental jurisdictions use pledge terminology in a non-possessory context as well. Under English common law, on the contrary, pledge is narrowly limited to possessory security. Its non-possessory sibling is the ´charge´ since the rules governing charges are akin to but not consciously derived from the possessory pledge (Drobnig in *op.cit*, pp. 516-517).

93 Articles 3:236 to 3:238 of the Dutch Civil Code, Zwitser in Transfer of Property, pp. 259-260.

94 Plégat-Kerrault in Transfer of Ownership, p. 172. On the other hand, French law may accept pledges to portions of e.g. oil or grain cargoes (*choses de genre*), although these are not easily identifiable (Affaki, Revue de Droit International 3, 2000, p. 663 et seq.).

95 Drobnig in *op.cit*, p. 513.

Many legal systems admit the possibility of granting a pledge to future goods. The US Uniform Commercial Code (§ 9-204 (1) and (3)) knows the possibility of granting security on the goods that the debtor will own in the future. The same applies according to the Dutch[96], English and Swiss laws, as well as for the laws of those twenty-six Central and East European states which have adopted the EBRD Model Law on Secured Transactions 1994.[97]

As regards electronic commerce, attention has been paid to the form requirements of pledges of cargoes. The Bolero Feasibility Study 1999 concludes that "it would seem that possessory pledges are universally available by means of acknowledgement by the carrier, there ought to be no public registration requirements by virtue of the use of Bolero".[98] The study estimates that in a substantial number of jurisdictions, no writing is required for the carrier´s acknowledgement.

A special type of proprietary right affecting the goods in transit is the carrier´s or freight forwarder´s lien over the goods. The nature of lien rights differs from jurisdiction to jurisdiction. In the next few paragraphs, the concept of carrier´s or freight forwarder´s lien is used to signify a variety of rights, e.g. pledges, ´liens proper´ and retention rights.

In some cases the right entitles its holder to sell the goods for the correponding claims and sometimes the holder can simply withhold the goods until his claims are satisfied, or until a time bar stipulated for the exercise of the right has expired. According to one view, pledge differs from lien in that, where payment is not effected, it gives the creditor has access to sell the goods without a previous judgement or execution.[99] At the other end of the carrier´s or freight forwarder´s rights in respect of goods are the rights of retention or withholding of the goods without any right to sell them. In any case, the rights in question are either statutory or contractual. Sometimes these rights may even rank ahead of ownership rights protected by retention of title clauses, which is the case in France.

There are rights related to a carrier´s lien in various service and work contracts. For instance, Nordic laws give parties having possession of the goods and having performed work with or on the goods under a contract a right of retention.[100] The possession of the goods is generally important to the exercise of the carrier´s lien rights, but often physical possession is too cumbersome to work with, and the carrier may have to store the goods. Under French law, the sea carrier has to apply an order of deposit from the courts, and likewise obtain a further order to sell the goods to satisfy his claims.[101] French law grants the

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96 Burgerlijk Wetboek, Book Three, Article 231.

97 Affaki, Journal du Droit International 3, 2000, p. 6. For the Model Law, see *infra*.

98 The Bolero Feasibility Study 1999, p. 95.

99 Ronøe in Transfer of Ownership, p. 123.

100 Johnsson in Transfer of Ownership, p. 388.

101 See Section 2102 of the French Civil Code regarding a sea carrier´s lien, which requires the intervention of the court.

freight forwarder a possessory lien, which enables him to withhold the goods and claim ownership of those goods which represent a value equal to the amount of his claim.[102]

A special lien relating to the documentation of international trade is an English broker´s lien over a marine insurance policy.[103] It is to be noted that the exercise of lien under present English law is seen to presuppose a tangible instrument.[104]

The Finnish Maritime Code gives the carrier a lien in respect of general average contributions, certain expenses advanced on behalf of the cargo owner, and freight.[105] The carrier may further retain the goods and refuse to deliver them even against surrender of a bill of lading, provided that the bill contains an indication that the freight is payable by the consignee.[106]

As said, liens are also created contractually. As the terms of the lien may be onerous to the shipper, consignor and consignee, there are often form requirements as to its incorporation. A good example in this context are the General Conditions of the Nordic Association of Freight Forwarders[107]. These Conditions provide that the forwarder has rights to the goods that are in his possession as security for all costs incidental to the goods, even for previous claims. This provision is sometimes categorised as a pledge although it serves the same function as the carrier´s statutory lien.[108] Being of an onerous character, the incorporation of this clause into the contract of carriage may require special attention.[109]

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102 Odile B. Plégat-Kerrault in Transfer of Ownership, p. 174.

103 According to section 53(1) of the English Marine Insurance Act 1906, the broker is generally directly responsible to the insurer for the premium. There can be two separate liens: the first is a particular lien over the policy for unpaid premiums and charges, the second a general lien covering any outstanding balances due to the broker in relation to the insurance business. (Law Commission 2001, p. 31 note 5).

104 Law Commission 2001, p. 32; the Law Commission anticipates however (p. 32 note 12) that some form of electronic functional equivalent of a lien may be devised and sanctioned by law in the future.

105 See e.g. Chapter 3, section 9 and Chapter 13, section 20 of the Finnish Maritime Code.

106 In a converse situation, the bill contains a note ´freight prepaid´. Where no bill of lading has been used, the consignee is responsible for the freight, if the consignee was notified of the claims upon delivery or he realised or ought to have realised that the carrier had not received payment (Chapter 13 section 19 of the Finnish Maritime Code).

107 The latest version as abbreviated in Finnish and Swedish is PSYM/NSAB 2000.

108 Ronøe in Transfer of Ownership, p. 124. Under Danish law, a practical difference between a lien and pledge is that a statutory lien for freight applies against the shipper and the consignee irrespective of the transfer of property, whereas a pledge requires that the pledgor has property in the goods at the time the goods are handed over to the freight forwarder.

109 See Chapter IV.8.2., *ante*, and Chapter VIII.2.1.6., *post*.

The Bolero Feasibility Study 1999 does not consider liens comprehensively because "the subject is too detailed".[110] In any case, it is worth noting that liens affect the rights of the consignee to obtain the goods from the carrier even where these rights are supported by the possession of a bill of lading or, alternatively, by an entry in the *Bolero Title Registry*. As some contractual liens require express attention in their incorporation, it might be useful to consider recording them in electronic trading platform repositories and not simply attempting to incorporate them by reference.

Where the law applicable to property or security rights is generally connected to the situs of the goods, rights of a foreign origin may not match the legal concepts of the country of situs. The latter may take an admissive or a restrictive stand to rights alien to its own legal order. In Germany, foreign rights *in rem* unknown to German property law have to be transposed into a closely related right *in rem* under German law. Courts in Germany are said to find a German ´functional equivalent´ to the foreign property right.[111] In contrast, French courts tend to take a prohibitive view in respect of the non-possessory pledge admissible in the Netherlands.[112]

It is sometimes said that different legal systems come to more or less similar results by applying different ways and concepts.[113] Rights *in rem* seem to constitute a notable exception to this general observation. The legal requirements for an effective pledge and security, proprietary rights or rights *in rem*, in whatever way these are classified under national law, are not harmonised and vary from country to country. The tendency of many national courts to refer to the *lex situs* makes this disharmony more critical to electronic commerce, where contractual arrangements such as the *Bolero System* are made to create security or property rights. As *Affaki* puts it, security rights in tangible goods are subject to a

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110 Bolero Feasibility Study, p. 48. For liens under English law, see Ali, pp. 91-98. According to Ali, there are contractual liens and non-contractual liens. Non-contractual liens include common law liens, equitable liens and non-statutory maritime liens. Common law possessory liens include the carrier´s lien the subset of which is the shipowner´s lien for freight. A common law lien is a possessory lien which does not carry with it the power of sale of the goods. A vendor´s statutory lien pursuant to section 39(1) of the Sale of Goods Act 1979 (UK) is also possessory. Non-statutory maritime liens include damage liens, salvage liens and liens for seamen´s wages. These are non-possessory security interests arising from the operation of law. Non-statutory maritime liens confer rights that can be enforced solely through the judicial process of arrest of ship.

Contractual liens further extend the protection of the secured party. Parties may e.g. agree that the secured party´s right of possession is to be accompanied with a contractual power of extra-judicial sale, but this may qualify the right to constitute a pledge which has been made subject to special requirements. Moreover, non-statutory maritime liens override contractual security agreements.

111 Thorn in Transfer of Property, p. 193.

112 *Supreme Court, 3 mai 1973*: Revue Critique de Droit International Privé 1974, p. 100. In that case goods were pledged to the bank but they remained in the possession of the debtor. Such a pledge did not give the creditor any right against third parties. Plégat-Kerrault in Transfer of Property, p. 172. Affaki (Revue de Droit International 2000,3, pp. 691-692) believes that French courts would not give effect to an English trust receipt, which is given by the debtor to make it possible for him to maintain possession of the pledged goods.

113 E.g. Professor Hugh Beale expressed this idea at the seminar ´The Future of European Law´ at the University of Helsinki on 10 June 2003.

depeçage situation: the *lex causae* is applied to determine the existence of the creditor´s right *in rem* whilst the *lex situs* is applied to determine the form and contents of the right.[114]

UNCITRAL Working Group VI (Security Interests) is currently discussing a draft legislative guide on secured transactions, which would contain provisions on conflict of laws relating to security rights in tangible property, including goods in transit.[115]

V.4.2 The role of a document of title[116]

The point of using negotiable instruments is that they permit the indorsee or other holder of the document to sell the goods during transit or to pledge the goods as security. Property or other rights such as indirect or constructive possession may be transferred without notice to the issuer of the document (in the case of a negotiable instrument, the debtor). The transfer of title (ownership, property) to the goods in transit is primarily a matter for the contract of sale between the parties. The parties may provide expressly or by implication[117] that the title passes when the bill of lading, primarily a transport document, is exchanged for value, i.e. negotiated. As a document of title[118], the bill of lading

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114 Affaki, Revue de Droit International, 2000.3, p. 700.

115 At the present stage of discussions preference is expressed, in the case of non-possessory security interests, for the *lex situs* of the tangible property, except for ´mobile´ goods, in the case of which the creation and publicity of a non-possessory security right would be governed by the law of the state in which the grantor is located. As regards goods in transit, the law of the place of destination would be decisive provided that the goods are moved to that place within a certain time limit. See docs A/CN.9/549 paras. 22 to 26. and A/CN.9/WG.VI/WP.9/Add.7. paras. 32 and 33.

116 Due to the dual role of negotiable transport documents (usually bills of lading), part of the analysis relating to documents of title is placed in Chapter VI.3.4.1., *post*. See also Chapters VIII.10. and 11., *post*.

117 There may be pre-established rules for the interpretation of what the intention of the parties may be. Where the English Sale of Goods Act applies, and the bill of lading is made to the order of the seller or his agent, the seller is presumed to have preserved the right of disposal. However, where the bill is made to the order of the buyer or his agent, or there is an agreement that payment is made under the terms ´cash against the documents´ (which is similar to a documentary collection arrangement), there is a presumption that property is intended to pass on shipment or, in the latter case, on payment against the documents. See also Serutton 1996, paras. 96-97.

118 There are documents of title other than the bill of lading. National law determines which documents constitute documents of title or how they are created. For instance, under English law, the expression ´document of title´ shall include any bill of lading, dock warrant, the warehouse-keeper´s certificate, and the warrant or order for the delivery of goods, and any other document used in the ordinary course of business as proof of the possession or control of goods, or authorising or purporting to authorise, either by indorsement or by delivery, the possessor of the document to transfer or receive goods thereby represented. (Factors Act section 1(4)). There is, however, a separate common law regime of documents of title, which is more restrictive. Todd states (Todd 1998, p. 106) that documents of title within the meaning of the Factors Act do not necessarily transfer constructive possession of the goods represented by them, which is the quality of common law documents of title. Therefore, documents of title must be established by custom, and ´any bill of lading´ is not a document of title under English law. According to Payne & Ivamy, p. 93, "it has never been settled... whether delivery of a bill of lading which is marked ´non-negotiable´ transfers title at all". Furthermore, even if negotiability were provided on the document, it may still not qualify, as seems to be the case with some bills issued by freight forwarders, see Chapters VI.1.3.2 and VI.3.4.1., *post*. >>

gives the buyer the right to obtain the goods against its surrender, or to sell them further by making an indorsement and delivering or simply delivering the bill. Most transfers of bills of lading are full transfers relating the sale of the complete cargo represented by the bill of lading. The transfer may, however, be made with reserve, or it may be partial. In complex situations of apportionment, ship´s delivery orders are useful.[119]

Later in Chapters VI and VIII, attention will be paid to the fact that bills of lading usually are issued in several originals. Each of them has, as a rule, the relevant characteristics of a document of title.[120] Procedural rules exist for carriers to be applied in such situations.[121] For the buyer claiming delivery, the existence of other originals poses the threat of adversarial claims. Therefore documentary credit practice and INCOTERMS 2000 require the seller to present a "full set" of originals of the bill.[122]

Constructive (or indirect) possession may be held through a document of title, when the goods are under the control of a third party[123] such as the carrier. Constructive possession can also be transferred, with or without property in the goods, by transferring the bill of lading also when the goods are in the custody of a third party (*traditio longa manu*).[124]

The bill of lading and other documents of title have, in addition to their functions under the contract of carriage, functions relating to certain proprietary rights in respect of the goods carried. These functions are related to the contract of sale, the contract of transport, or to credit agreements.

All jurisdictions presented in the work *Transfer of Ownership in International Trade* seem to recognise That property in the goods may be transferred by transferring the bill of lading to the buyer. The picture in this respect is, however,

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<< One can distinguish the issue of a document of title within the meaning that it produces proprietary or security effects, which is meant above or within the meaning envisaged in Article 1(b) of the Hague-Visby Rules, which introduce binding transport liability rules in cases where the goods are covered by "a bill of lading or any similar document of title". See Chapter VI.3.4.2., *post*.

119 Under English law, ship´s delivery orders are not documents of title. This is not necessarily the case in other jurisdictions, e.g. Dutch law gives the ship´s delivery order that status (Art. 8:482 of the Dutch Civil Code).

120 However, where goods are delivered at a place other than the destination, all originals must be presented (provided e.g. by the Finnish Maritime Code Chapter 13 Section 52). Copies, naturally, do not have the status of a document of title (Todd 1998, p. 129). On the other hand, documents of title play a role under presentations (for value) under documentary credits, and there are particular rules as to what constitutes an original document under them, see Chapter VIII.6.2., *post*.

121 See e.g. the Finnish Maritime Code, Chapter 13 Section 53. Among competing holders of bill of lading originals, the fastest wins. Bill of lading conditions usually state that when one of them is accomplished, others stand void. The carrier can safely deliver to any such holder at a destination. The seller is the one that becomes ultimately accountable for the losses of the right consignee who came too late, not the carrier.

122 See Uniform Customs and Practice for Documentary Credits UCP500 Art.23(a)(iv).

123 Third party relations must be separated from agency. An agent can namely hold the goods or the document of title on behalf of the principal. A ´factor´ under English law has authority to sell, pledge, or raise money on security of the goods or documents of title to the goods (Factors Act 1889, section 1(1)).

124 Selvig, Grenseland, p. 51.

not without complexities. For instance, German law requires several preconditions for an effective transfer of property in the goods to take place. First, the document of title must be transferred by way of a transfer agreement and indorsement. Second, there must be mutual consent between the transferor and the transferee (buyer) that the property in the goods shall pass. Third, the document of title must be delivered to the transferee. Finally, the issuer of the document of title, which is the carrier, must have the goods in his possession in order to create an effective transfer of property.[125]

In any case, the use of the bill of lading therefore generally helps to avoid the problems that would be created by the use of conflicting laws based on the casual *situs* of the goods. The use of a document of title often defines the law applicable even as regards the goods in transit. For instance, under Dutch law, the property in the goods is determined by the *lex carta sitae* of the document, wherever the goods themselves may be located.[126]

For a bank involved, inter alia, in a documentary credit transaction, a document of title makes it possible to obtain security over the goods as a pledge for its advancing sums as credit. The purpose of the credit transaction is not to gain property in the goods themselves. A document of title is useful in pledge arrangements, since its use usually facilitates security transfers[127], including a non-possessory pledge without registration. Under English law, a bank receiving and paying for documents tendered under a letter of credit holds a pledgee´s interest in the goods represented by a bill of lading. The requirements for an effective pledge, however, are not clear but may depend on how the front of the bill is completed.[128]

Moreover, a bill of lading puts, in many jurisdictions, the possessor or pledgee of goods in transit in a better position than a possessor or pledgee without a bill of lading, because the holder of a document of title enjoys a better position against third parties.[129]

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125 Thorn in Transfer of Ownership, p. 190; see further Schnauder, Sachenrechliche und wertpapierrechtliche Wirkungen der kaufmännischen Traditionspapiere, NJW 1991, pp. 1642-1649.

126 Zwitser in Transfer of Ownership, p. 254.

127 In England, the deposit by the security provider of a document of title to the secured property with the secured party, *prima facie* constitutes sufficient evidence of the intention of the parties to create an ´equitable mortgage´ over the secured property in favour of the secured party. Like a pledge, such an equitable mortgage does not require a security agreement. A security transfer effected by a deposit of title documents is thus an acceptable alternative to a security agreement (Ali, 3.53, p. 65). Consequently, should an electronic recording system offer functions equivalent to documents of title, these systems would benefit from legislation granting electronic records the status of a document of title; see Chapters VI and VIII, *post*.

128 Gutteridge and Megrah, seventh edition (1979) take, on page 212, the view that for a pledge to exist under English law, the bill of lading must be made out either to shipper´s order or to the order of the paying bank. The same approach is taken in the eighth edition of the same work (2001 by Richard King) on pages 252-254. The opposite view is taken by Jack, on page 252 at para. 11.4., where he contends that the pledge is effective whether or not the bill is made out to shipper´s order, bank´s order or buyer´s order. See also Debattista in Transfer of Ownership, pp. 148-149.

129 G.J. van der Ziel, Main Legal Issues Related to the Implementation of Electronic Transport Documentation, ETL, 1997, p. 719.

V.4.3 Retention of title

Sales contracts invariably contain retention of title clauses, the effect of which is to reserve the title to the goods to the seller until they have been fully paid for. Another objective for the seller is to obtain protection against the other creditors of the buyer. What kind of protection the retention of title clause gives to the seller against third parties depends normally on the jurisdiction of the buyer.[130]

National laws are even more divergent when it comes to the extent in which the retention of title also covers, for example, a claim for the purchase price which arises upon the resale of the sold goods by the buyer or over products made from the sold goods.[131] The extensions of the right of retention contained in national laws could even cover all the buyer´s outstanding indebtedness against the seller, not only claims regarding the purchase price on the specific goods delivered.[132]

The effect of the retention of title clause is that the buyer cannot effectively sell the goods further before he obtains title to the goods himself. The stringent obligation to pay the price of the goods may, however, be relieved by trade credit merchanisms, where the buyer is protected by an irrevocable payment undertaking by a bank.[133]

Retention of title clauses are regular parts of international contracts of sale. Each jurisdiction has its own rules as to what kinds of clauses are admitted and how far these apply as against the creditors of the buyer. National law may also contain form requirements as to retention of title clauses. This is the case under the Swiss law, pursuant to which retention of title clause is operative only if it has been recorded in the public register of the transferee´s domicile.[134] Such rules come into play when the validity of foreign retention of title clauses is assessed. The tendency of the courts to stick to the *lex situs* makes the rules at the location of the goods relevant.

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130 For the treatment of retention of title clauses in various jurisdictions, see Retention of Title (2nd edition), ICC Publication No 501 and Transfer of Ownership in International Trade, ICC Publication No 546. For retention of title clauses in the Nordic countries, see Tepora, Omistuksenpidätyksestä (Über den Eigentumsvorbehalt, On the retention of title), Vammala 1984.

When the European Union tackled late payments in Directive 2000/35/EC of the European Parliament and of the Council of 29 June 2000 on combating late payment in commercial transactions, OJ L 200, 8.8.2000, p. 35, the Commission had proposed making retention of title mandatory law, but the outcome in Article 4 was only that "Member States shall provide in conformity with the applicable national provisions designated by Private International Law that the seller retains title to the goods until they are fully paid for if a retention of title clause has been explicitly agreed between the buyer and the seller before the delivery of the goods".

131 The former type of extension seems to be valid in France and Germany, and the latter, only in Germany; see Communication from the Commission to the European Parliament and the Council: A More Coherent European Contract Law, An Action Plan, Brussels 14 March 2003, OJ C 63, 15.3.2003, p. 8.

132 Ibid; these clauses are called ´all-monies´ clauses and are effective in the UK and in Germany.

133 Chapter VII.1.4., *post*, explains that so called ´back-to-back letters of credit´ are used, for instance, in situations of consecutive sales in transit.

134 Article 715 of the Swiss Code Civil, von Ziegler in Transfer of Ownership, p. 405.

For instance, the Federal Supreme Court of Germany had to determine the validity of an Italian clause which was not developed according to the form requirements of Italian law.[135] As the Italian form requirement was not met, the retention of title clause was held to be effective only *inter partes*. However, as soon as the goods reached Germany the clause also took absolute effect with regard to third parties and especially the creditors of the buyer.[136] French law also makes a distinction between legal effects *inter partes* and as against third parties. French courts will respect a clause in a contract referring to German law based on the extensive scope of retention of title provided therein, but do not grant security to the seller to the same extent against third parties.[137]

The European Insolvency Regulation stipulates in Article 7 that the opening of insolvency proceedings against the purchaser of an asset shall not affect the seller´s rights based on a retention of title where at the time of the opening of the proceedings the goods are situated within the territory of a Member State of the European Union other than the state of the opening of the proceedings. Moreover, the opening of insolvency proceedings against the seller of the goods after their delivery shall not constitute grounds for rescinding or terminating the sale and shall not prevent the purchaser from acquiring title where at the time of the opening of the proceedings the asset sold is situated within the territory of a Member State other than the state where the opening of the proceedings occurs.

The above stipulations are minimum rules respecting retention of title clauses. The state opening the proceedings may give further protection. The stipulations indirectly recognise the status of the *lex situs* of the goods in determining property law questions. It is submitted that the private international law rules of the *lex situs* ultimately determine the question of which law will decide the validity of the retention of title clause.

A different approach to retention of title clauses is found in the United States. Retention of title is generally not permitted under the Uniform Commercial Code. Thus, the only effective way for the seller to retain title is to retain a negotiable bill of lading. Title may still pass under the contract, and the seller´s right is reduced to a security interest. A buyer purchasing the goods for value can defeat the retention of title or a security interest.[138] Generally speaking, US law gives more priority to rights represented by negotiable instruments and, perhaps, abstraction in general.

V.5 Stoppage in transit

One of the areas where the regime for contracts of sale on the one hand and that for contracts of carriage on the other are in conflict, is a situation in which the

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135 Bundesgerichtshof 2.2.1966, Entscheidungen des Bundesgerichtshofs in Zivilsachen 45,95, 98.

136 Thorn in Transfer of Ownership, p. 191.

137 Plégat-Kerrault in *op.cit.*, pp. 167-168.

138 Chandler, III in *op.cit.*, pp. 424-426.

law gives the seller the right to interfere with the carrier´s delivery obligations under the contract of transport.

In addition to retention of title clauses, sales laws frequently give the seller a right called stoppage in transit (or *in transitu*) in certain adverse circumstances, usually the insolvency of the buyer.[139] In the CISG, the right for stoppage in transit is provided for in Article 71. Paragraph 1 of this article provides that a party may suspend the performance of his obligations if, after the conclusion of the contract, it becomes apparent that the other party will not perform a substantial part of his obligations as a result of a serious deficiency in his ability to perform or in his creditworthiness, or his conduct in preparing to perform or in performing the contract.

Paragraph 2 adds that where the seller has already dispatched the goods before the grounds described in the preceding paragraph become evident, he may prevent the handing over of the goods to the buyer even though the buyer holds a document which entitles him to obtain them.[140] Paragraph 2 states namely that it relates only to the rights in the goods as between the buyer and the seller. How should this provision be interpreted?

In preparing the CISG, several comments were made that suggested that the provisions imposing obligations upon the carrier conflicted with those of municipal and international law concerning the carriage of goods. The UNCITRAL Secretariat accordingly proposed that paragraph 2 be augmented to include the sentence "the foregoing relates only to the rights in the goods as between the buyer and the seller and does not affect the obligations of carriers and other persons". This wording was then adopted in substance.[141]

Ramberg notes that the duties of the carrier in these situations are therefore wholly outside the scope of the CISG and must be resolved primarily according to the rules relating to the contract of carriage.[142] Therefore, an independent carrier is not affected by this provision and is able to release the goods to the buyer who surrenders the bill of lading. The only possibility for the seller in such a situation is to try to get a court injunction restraining the carrier from releasing the goods against the bill of lading.[143]

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139 The right of stoppage in transit has its origin in Anglo-Saxon law (Tiberg, p. 548). It is not part of the laws of e.g. Germany or France as regards domestic sales (Karsten, p. 192, and Plégat Kerrault, p. 169, in Transfer of Ownership).

However, in France and Switzerland, for instance, the right of stoppage does not arise from sales law, but from debt collection or bankruptcy law (Plégat Kerrault, pp. 169-170, and von Ziegler, p. 406).

The implementation of the CISG has spread a uniform idea of stoppage in transit to these countries and is now applied to international sales contracts.

140 It is generally understood that the goods must be in the custody of an independent carrier or similar party. If the goods are in the hands of a representative of the buyer, the right of stoppage does not apply.

141 Bennett in Bianca-Bonnell, 517.

142 Ramberg 2000, p. 45.

143 Ibid.

If the seller still retains the relevant copy or copies of the transport document, the exercise of the right of stoppage in transit is, of course, much easier. The transport document need not be a document of title, since many other transport documents give the holder of the consignor copy or a duplicate the right to exercise control over the goods whilst in transit. Strictly speaking, however, the seller as the shipper exercises in such a case his right of controlling the goods and not of stoppage in transit. Should the seller have waived the right to control the goods, e.g. in systems where this is effective under law by using a ´NODISP´ type clause, he can no longer exercise control. He can still resort to stoppage in transit, but as said this requires the involvement of courts, unless transport laws give effect to the CISG provision in a way which allows interference with the contract of carriage.[144]

The limits of stoppage in transit have been treated differently among national laws. Provisions on stoppage in transit have even found their way to the Nordic Maritime Codes, which is a relatively exceptional approach. The problems relating to stoppage in transit will be revisited in Chapter VIII.9.2., *post*, as an example of a potential point of conflict between the contracts of sale and transport.

It should be further noted that where stoppage in transit in its proper meaning comes into play through the application of sales law, it is frequently treated as a matter falling under the *lex contractus*. However, where national insolvency law or procedural measures are invoked to use the right of stoppage, as is the case in Switzerland, the buyer (debtor) must have his seat or domicile in the country.[145]

V.6 Trade security arrangements and banks

In the preceding parts of this chapter, property and other rights in the goods have been covered in some detail. What makes these rights so important in international trade is that they provide security for the commercial parties of the transaction, the seller and the buyer, but also for the middlemen in ancillary contractual relationships, the carrier protected by the lien, and the banker advancing money in trade finance protected by the pledge. In the next few paragraphs, an attempt is made to list the ways to secure the bank that is to advance money. The list is not exhaustive, but is given for the purpose of distinguishing those security methods where the goods sold play a role via indirect or constructive possession, which brings in the trade documents, which itself are also objects of proprietary rights.

In addition, the bank, like the principal parties to the transaction, may find security in the contracts involved, i.e. the rights based on the contract of sale and the contract of transport, as well as by being holders of the negotiable

144 US law confusingly gives the carrier receiving a stoppage order a right to require the presentation of an original negotiable instrument. US law therefore makes transport documents more instrumental.

145 Von Ziegler in Transfer of Ownership, p. 406.

instruments or documents of title issued. All these forms of security have electronic commerce implications, as analysed in the Bolero Feasibility Study 1999.

In a sale of goods transaction, property in the goods passes from the seller to the buyer. Other parties may be protected by various security rights. It is not right, however, to generalise that security rights are always something less than full ownership. In fact, many transactions are in the form of ´title finance´. These forms of security include retention of title clauses, the factoring of receivables, financial leasing, hire purchase and the discounting of bills of exchange accepted in trade transactions. Some jurisdictions, however, recharacterise these transactions as security interests.[146]

I shall skip here export credit guarantees and credit insurance, which are also of great significance in respect of securing the use of demand guarantees in some cases. Retention of title, which has already been dealt with, is also a very important security measure for the seller.

In some countries, goods sold form parts of security arrangements, where a universal corporate charge exists in favour of a bank over all the assets of its client. This charge also includes the goods sold, as long as they form part of the property of the client, e.g. on the basis of a retention of title clause. This kind of a ´floating charge´ is known in English-based jurisdictions.[147] It is also found in Finnish[148] and Swedish laws.

The largest proportion of security in relation to international trade takes place through the use of documentary credits, at least where buyers are concerned.[149] The buyer of the goods requests his bank to issue a letter of credit to the seller, after which the confirming bank in the seller´s country confirms the letter of credit by undertaking the personal responsibility to pay the seller against production of the documents. The banks involved assume risks until they are compensated for the sums they have advanced, but are protected by the pledge of the documents and of the goods themselves through indirect or constructive possession. In a documentary credit transaction, the seller is normally provided an irrevocable undertaking by a bank to pay against any stipulated documents, which constitutes a security undertaking for him.

The seller may also use documentary collections, where the seller´s bank holds the documents and delivers them to the buyer or the buyer´s bank against payment. The documents serve as security for the seller until payment is made against them, which is normally the time of the ´constructive delivery´. Unless either bank advances money as a credit undertaking, there is no function for the

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146 Bolero Feasibility Study 1999, p. 80.

147 See Ali, para 4.100 et seq, pp. 114-129. The floating charge is said to ´crystallise´ when the floating charge converts into a fixed charge. On crystallisation, the security provider´s licence to deal with the secured property ceases and the secured property is brought within the control of the secured party.

148 See Yrityskiinnityslaki 24.8.1984/634

149 For documentary credits, including standby letters of credit as well as demand guarantees and documentary collections in particular, see Chapter VII, *post*.

documents as security for the bank. Like with documentary credits, the documents represent the goods, which are thereby used as security for trade finance.

Documentary credits are related to independent demand guarantees and standby letters of credit as regards many basic features such as the independent nature of the undertaking of the bank as well as the standard of examining the documents triggering the payment, be it a regular payment or a payment only in case of default. However, as no commercial documents are used, the goods do not serve as a security for the transaction unless other arrangements are made. There are guarantees or standbys designed to protect the seller´s or the buyer´s interests, as the case may be.

Bills of lading may also be used in seller finance transactions. The seller draws a bill of exchange on the buyer for the price and indorses the bill to his bank in return for payment. This is effectively a sale of the price to the bank, which is called factoring. A security assignment may take place as well. The obligations on the bill of exchange are secured by a pledge of the goods as well as by an assignment of the contract of carriage, which takes place by indorsing the bill of lading to the bank at the same time as delivering it to the bank.[150] Factoring transactions concern transfer of receivables in general, and not necessarily those represented by negotiable instruments.[151]

In forfaiting, however, the bank purchases a debt expressed in a negotiable instrument such as a bill of exchange or a promissory note. The forfaiting bank requires a security, which is usually an aval on the instrument as such or a separate bank guarantee. The forfaiter will often re-negotiate the negotiable instruments which he has purchased by way of a forfaiting transaction in order to raise funds or to spread the risk. If the forfaiter is involved in documentary credit transactions, he will often receive the document to be forfaited through its documentary credit collection system. Documents of title change hands in this context as well. Bills of lading are transmitted to the importer´s bank with instructions that they must only be released against acceptance of the bill of exchange or signature of the promissory notes plus the ´per aval´ indorsement or the issue of the letter of guarantee by the importer´s bank, according to the previous arrangements with the forfaiter.[152] It is possible to use the bill of lading, the goods represented and the transport contract evidenced by the bill as additional security.

Banks may also have security over any negotiable instruments issued for the price of the goods or may simply purchase these documents. As no attempt has

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150 Bolero Feasibility Study 1999, p. 77. Export factoring is divided into disclosed and undisclosed factoring. Under English law, disclosed factoring is subject to form requirements, must be in writing signed by the seller as the assignee and must be absolute. In addition, an express notice is given to the buyer as debtor (s. 136 of the Law of Property Act 1925). Usually the notice is given in the invoice (Schmitthoff, Export Trade, eighth edition 1986, p. 387).

151 For factoring, see also Chapter VII.12., *post*. There exists a United Nations Convention on the Assignment of Receivables in International Trade from 2001 as well as a 1988 UNIDROIT Convention on International Factoring (Ottawa).

152 Schmitthoff, Export Trade, eighth edition, pp. 389-391.

been made to create a framework for negotiable instruments, except for the UETA provisions for ´transferable electronic records´[153], there is no method to carry out forfaiting transactions electronically or to use negotiable instruments as securities other than by using their traditional form and applying traditional formalities.

In addition to the goods and documents, banks may require security over contracts. When the bank has security over the contract of carriage, it is guaranteed that it has direct rights against the carrier for loss of or damage to the goods. It is doubtful how useful this right is, since carriers are able to limit their liability substantially according to transport legislation. Therefore a contractual arrangement whereby the proceeds of cargo insurance compensation are awarded in favour of the bank would be more useful. In any case, the *Bolero System* in its initial form already covered the electronic transfer of the contract of carriage in favour of the bank.[154]

Moreover, a bank financing the buyer may have security over the contract of sale, which confers on the bank direct rights against the seller for defects in the goods and for injury caused by the goods to third parties or for damage to property. A bank financing the seller assumes security over the contract of sale with a view to gaining rights against the buyer and rights to the goods under a possible retention of title clause. It is imaginable that the bank would exercise the right of stoppage in transit in lieu of the seller.

In Chapter IV, contracts of sale were analysed especially with formation of contract aspects in mind. Another aspect to be considered is the procedure for the transferring of contracts e.g. for security purposes. The Bolero Feasibility Study 1999 does not consider this form of security to be very vital. An assumption is, however, made in that study that it is not possible in any jurisdiction to create security over the contract of sale by the indorsement and delivery of a document of title.[155]

V.7 Summary of the transfer of rights in tangible goods at present

Many preceding parts of this chapter have included analyses of the transfer of rights *in rem* from a country to country perspective. One could summarise that the methods for transfer of property interests in tangible property are generally based on two legal concepts, the principle of consent and the principle of delivery. Additional related methods are registration and symbolic delivery.

The legal systems that apply the principle of consent may simply allow property to pass if there is a sales agreement between the seller and the buyer.

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153 See Chapter VIII.3.3., *post*.

154 This is possible under section 3.5.1. of the Bolero Rulebook 1999. See also the Bolero Feasibility Study 1999, p. 78.

155 Bolero Feasibility Study 1999, p. 100.

Other systems put the emphasis on the intention of the parties, which has to be demonstrated clearly. Sometimes the law requires that in order to be enforceable against third parties, the transfer is registered in a registry system, or that the goods are actually delivered to the transferee.

Registration of the transfer of property rights serves to ensure legal certainty especially when the achieved ownership cannot be shown by the transfer of possession. Registration also often helps to create effect against third parties, even if the transfer is valid between the parties themselves. Registration has a role to play in respect of the transfer of shares or other securities issued by companies where traditional securities issued on paper are not used.[156] In this way, registrations are used to transfer rights to both tangible and intangible property.

Property rights are also transferred by way of delivery. The concept of delivery is also based on consent but requires the physical delivery of the asset to the transferee as well. Therefore two stages are seen where consent appears. First, there is an underlying contractual undertaking to transfer property. Second, the consent appears when goods are delivered. The validity of the contract is usually a prerequisite for the validity of transfer by delivery. The validity of the delivery may, however, be detached from the validity of the contract.[157]

Delivery is also the means of transferring rights in negotiable instruments or debts expressed therein. The delivery may be simply physical, i.e. from bearer to bearer, but often an indorsement is used.[158]

Delivery can be symbolic in the sense that indirect or constructive possession is transferred. Title is transferred together with indirect possession and means of controlling the goods and of claiming delivery. A document of title such as a bill of lading is used in such symbolic delivery.[159] In most jurisdictions, transferring security interests in tangible goods and in intangible property requires some formalities, e.g. that the transfer is in writing.[160] An agreement to provide security may have to be supplemented by a method of making it public.

Even if granting security interests is valid between parties, it may not be enforceable against third parties such as the creditors of the debtor. Following the formalities in full may then create *perfection* for the security and make it valid also *ultra partes*.[161] As regards tangible goods, the transfer of possession is often a means for the perfection of security interests. Possession is a means to give publicity to the security right. The possession can again be indirect, e.g. a bailee

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156 Registrations have a role to play in paperless stock trading. Following the same models, electronic registries can reproduce the functions of documents of title, see Chapter VIII.11., *post*.

157 The principle applied here of ´abstraction´ applies under German law, see *supra*. UNCITRAL doc A/CN.9/WG.IV/WP.90, para 15.

158 An indorsement in blank being a special case.

159 The UNCITRAL report (doc A/CN.9/WG.IV/WP.90, in paras. 17 and 18) uses the notion of ´symbolic delivery´ in the context of the transfer of property rights, whereas the notion of ´constructive delivery´ is used in the context of seller´s obligations under a contract of sale, see *supra*.

160 UNCITRAL doc A/CN.9/WG.IV/WP.90, para 20.

161 On perfection of security interests under English and some Commonwealth jurisdictions, see Ali, Chapter V.

holds the goods for the benefit of the possessor. When goods are represented by a document of title, the possession of such a document perfects security rights in it and simultaneously in the goods represented by it.[162] This makes documents of title particularly useful.

Perfection and publicity may also be attained through registration. A UNCITRAL Secretariat study indicates that modern legislation usually accepts the idea of the registration of non-possessory security interests as a means of giving publicity.[163] Registration makes it easier for third party creditors to verify the economic situation of the debtor. As will be seen in Chapters VI and VIII, *post*, registration is a means of replacing the functions of a paper bill of lading. The question will then be raised of to what extent security rights such as pledges should be registered as well. In addition to the legal requirements imposed by applicable law, rights affecting the goods could be recorded on a contractual basis to serve the needs of transparency.

V.8 Legal harmonisation and rights in the goods[164]

As already observed, property rights in the goods in the context of international sale of goods transaction law has become the object of interest of international organisations regulating international trade. A few efforts in this regard will be mentioned here to give a general picture, although some of these efforts have already been referred to earlier in the text.

UNCITRAL considers rights in tangible goods to be one of its priority areas. At its thirty-third session in 2000, as already noted in Chapter IV.7.2., *ante*, the Commission discussed future work in the field of electronic commerce. One area, in which the involvement of the Commission was suggested to be useful was the "dematerialisation of documents of title", the others being electronic contracting from the point of view of the CISG as well as online dispute settlement.[165]

After contemplating the issues, the Commission finally agreed in 2001 that work to be carried out by the Working Group could involve several topics in parallel, as well as initiate preliminary discussion on the contents of the possible uniform rules on certain aspects of the above three topics.[166] The ball then went back to the Working Party. Its suggestion for a future work order was later endorsed by the Commission at its thirty-fourth session, in 2001.[167]

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162 Ibid., para 23.

163 Ibid, doc A/CN.9/475., para 38.

164 See also Chapter VIII.11.2., *post*.

165 Doc A/CN.9/528, para. 1.

166 Official Records of the General Assembly, Fifty-fifth Session, Supplement No. 17 (A/55/17), paras. 384-388.

167 Ibid., Official Records of the General Assembly, Fifty-fifth Session, Fifty-sixth Session, Supplement No. 17 (A/56/17), para 293.

Pursuant to the above, UNCITRAL is prioritising the creation of an international instrument dealing with certain issues in electronic contracting, which instrument has already been examined in this study.[168] However, the secretariat of the organisation has been entrusted with the preparation of needed studies which are to consider three other topics, one of which is "a further study of the issues related to transfer of rights, in particular rights in tangible goods, by electronic means and mechanisms for publicizing and keeping a record of acts of transfer on the creation of security interests in such goods".[169] In a Note by the Secretariat[170], an analysis was made of the various legal issues that arise in connection with developing an electronic equivalent to paper-based documents of title and other negotiable instruments. Working Group IV on Electronic Commerce agreed to recommend to the Commission (which recommendation was endorsed by the Commission at its thirty-fourth session, in 2001) that the secretariat be requested to study further the issues of the transfer of rights by electronic means, in particular rights in tangible goods, as well as and mechanisms for publicising and keeping records of acts of transfer or the creation of security interests in such goods. As stated, the study should also examine the extent to which electronic systems for transferring rights in goods could affect the rights of third parties. Furthermore, the study should consider the interface between electronic substitutes for the documents of title and financial documentation used in international trade, by attending to efforts currently under way to replace paper-based documents, such as letters of credit and bank guarantees with electronic messages.[171]

The work in this field, in which cooperation with the Comité Maritime International was sought, had not led to any results by the summer of 2004.[172] The documentation indicates that the draft Convention on Electronic Contracting discussed within Working Group IV (Electronic Commerce) is receiving priority in the distribution of the organisation´s resources. A question arises, however, about the relationship between this work plan and other projects under the auspices of UNCITRAL.

The question arises because Working Group III on Transport Law is currently preparing a draft Instrument for the carriage of goods [wholly or partly][by sea][173], which will create electronic equivalents for negotiable paper transport documents that presently function as documents of title.

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168 See Chapter VI.7.2.2., *ante*.

169 Doc A/CN.9/528, para. 3, Doc A/CN.9/484, para. 134. The other topics, in respect of which exploratory tasks were vested on the Secretariat were as follows:

- A comprehensive survey of possible legal barriers to the development of electronic commerce in international instruments; this survey has been completed (Note by the Secretariat of 14 February 2002, A/CN.9/WG.IV/WP.94), see in detail Chapter XII.2.2., *post*. This survey was discussed at the fortieth session of Working Group IV (Electronic Commerce) on 14-18 October 2002.

- A study discussing the UNCITRAL Model Law on International Commercial Arbitration, as well as the UNCITRAL Arbitration Rules, to assess their appropriateness for meeting the specific needs of online arbitration (this belongs to the domain of Working Group II in charge of international arbitration, see Chapter IX, *post*).

170 Doc A/CN.9/WG.IV/WP.90.

171 Doc A/CN.9/484, para 93.

172 See however UNCITRAL doc A/CN.9/WG.IV/WP.90.

173 See Chapter VI.3.2., *post*.

As documents of title are principally used in connection with the use of transport documents, the primary features of documents of title in transferring property and indirect possession also vis-à-vis third parties should be adequately dealt with in this instrument. Creating electronic documents of title with such effects requires, in my view, statutory interference. Encouragingly, the plenary of the UN Commission for International Trade Law (UNCITRAL) has urged Working Groups III and IV to coordinate their work on dematerialised transport documentation.[174]

Later, in Chapter VI, attention is given to the question of how documents of title are established in different jurisdictions and what the characteristics of a document of title are as compared to negotiable instruments. Such questions have not been a target of harmonisation measures so far, and diversity seems to prevail in this respect. A convention-based notion of an electronic document of title with minimum characteristics common to the understanding of the business world might help to spread the use of this instrument.

It should be added that UNCITRAL has two other Working Parties involved in questions relating to property or security rights in the goods, both of which have at least an indirect bearing on such rights in tangible goods. Working Group VI (Security Interests) was given the task at the thirty-fourth session of the Commission in 2001 "to develop an efficient legal regime for security rights in goods, including inventory". In the longer term, it was felt, a flexible and effective legal framework for security rights could serve as a useful tool to foster economic growth. The Commission held that the task of the working group should be interpreted widely "to ensure an appropriately flexible work product, which should take the form of a legislative guide". This was needed because national policies in this area varied substantially, the divisions related in particular to privileged, secured and unsecured creditors.[175] The work involves security rights over tangible goods and covers such important issues as the conflict of laws relating to such goods, the treatment of goods represented by a document of title vis-à-vis other security rights. The work of the group is presently accessible in the form of a draft Legislative Guide on Secured Transactions.[176]

Working Group V (Insolvency Law) is currently preparing, for similar reasons as the working group discussing security interests, a draft Legislative

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174 Official Records of the General Assembly: Fifty-seventh Session, Supplement No. 17 (A/57/17), para. 224.

175 Doc A/CN.9/531, paras. 1-8, Official Records of the General Assembly: Fifty-sixth Session, Supplement No. 17 (A/56/17), para. 357; Fifty-seventh Session, Supplement No. 17 (A/57/17), paras. 202-204.

176 See a sample of the latest documents: A/CN.9/549, A/CN.9/WG.IV/WP 9/Add. 7 and A/CN.9/WG.IV/WP.13.

For the legal harmonisation of security interests, see the presentation entitled ´Development of Standards for Security Interests´, initiated by Pascale de Boeck and completed by Thomas Laryea, Counsel, IMF Legal Department, held at the Seminar on Current Developments in Monetary and Financial Law, Washington, D.C., 7-17 May, 2002, http://www.imf.org/external/np/leg/sem/2002/cdmfl/eng/index.htm, visited on 25.11.2003.

Guide on Insolvency Law.[177] In 1997, UNCITRAL adopted a Model Law on Cross-Border Insolvency[178]. Results in this regard have been achieved at a regional level in the European Union, where three regulations[179] were passed in 2000-2001 regarding insolvency law. The purpose of the Insolvency Regulation and its sister-regulations, one for credit institutions and one for insurance undertakings, is to coordinate the application of insolvency laws roughly in the same manner as the Brussels and Lugano Conventions (now a regulation) have done as regards jurisdiction and the recognition and enforcement of judgements in civil and commercial matters. The state of the opening of the insolvency proceedings and its law determines most matters such as the priority order of various claims. However, certain rights not related to that state, such as retention of title to the goods in a different state, enjoy a separate status.

It is worth noting that an academic Study Group on a European Civil Code has a sub-group discussing the transfer of property in movable goods. At the time this work was finalised, there were, to my knowledge, no published results of the work of the study group. Due to the status of *lex situs* in many countries as the applicable property statute, the results of the Study Group would have to be codified to gain wider effects.[180] The contractual way of tackling rights *in rem* has obvious limitations.

Finally, one should take note of the EBRD Model Law on Secured Transactions[181], which the European Bank for Reconstruction and Development has drafted with the intention of utilising it it used in the former socialist states of

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177 The latest document available from this study prepared by Working Group VI is the report from its thirtieth session on 29 March-2 April 2004, Doc A/CN.9/551.

178 UNCITRAL Model Law on Cross-Border Insolvency, General Assembly resolution 52/158 of 15 December 1997. This Model Law has been implemented in a few countries, including Japan, South Africa and Mexico.

179 Council Regulation (EC) No 1346/2000 of 29 May 2000 on insolvency proceedings, OJ L 160, 30.6.2000, p. 1. Directive 2001/17/EC of the European Parliament and of the Council of 19 March 2001 on the reorganisation and winding-up of insurance undertakings, OJ L 110, 20.4.2001, p. 28. Directive 2001/24/EC of the European Parliament and of the Council of 4 April 2001 on the reorganisation and winding-up of credit institutions, OJ L 125, 5.5.2001, p. 15. For Insolvency Regulation 2000/1346/EC, see Koulu, Konkurssi Euroopan unionissa, Jyväskylä 2000.

For insolvency issues relating to cross-border payment and securities settlement systems, see Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement finality in payment and securities settlement systems, OJ L 166, 11.6.1998, p. 45. For the treatment of such securities as collateral, see Directive 2000/47/EC of the European Parliament and of the Council on financial collateral arrangements, OJ L 168, 27.6.2002, p. 43.

These Directives opt for the law of the jurisdiction where the relevant book entry account is held to govern proprietary and security interest effects. This sets a useful analogy for electronic documents of title systems, where the law could be made that of the place of registry as well, but one has to bear in mind that there is a strong traditional connecting factor: the *lex situs* or *lex rei sitae* governing the proprietary or security interest of the goods relates to the goods themselves and generally not to the documents or equivalent electronic records representing the goods. See also Chapter VIII.11.2., *post*.

180 The Commission Action Plan ´A more coherent European contract law´ (OJ C 63, 15.3.2003, p.11) mentions that ´A common frame of reference´ envisaged by the Action Plan should cover "credit securities on movable goods", but does not mention transfer of property rights. The common frame of reference will, however, be established later.

181 Available at http://www.ebrd.org/pubs/index.htm, visited on 4.4.2004.

Central and Eastern Europe. This Model Law operates generally with the concept of ´security interest´. One can also note, for the purposes of this study, that the rules of priority rank a possessory charge over negotiable instruments below 1) a security interest arising by operation of law, which secures amounts due for services rendered in relation to the secured property, and 2) a purchase money security interest. The possessory charge over negotiable instruments takes, however, priority over other claims, which are honoured through applying time priority.[182]

V.9 Transfer of contractual rights and obligations

Although the emphasis in the sale of goods is on the transfer of rights in tangible and movable goods, the transfer of contractual rights such as those based on debt instruments has some significance for the purposes of this study as well. This is because property and security rights exercised through a document of title are an alternative to direct contractual rights. An electronic medium based on a registry serves both purposes, and both types of rights are in a way ´dematerialised´.

This study generally omits the treatment of intellectual property rights, since they are more relevant to the use of Internet content production as well as to the identification of commercial parties by domain names. However, a presentation on the transfer of rights relating to tangible goods would be incomplete without a mention that such goods, in regard to technology in particular, are frequently sold under the condition that intellectual property rights remain with the seller.[183]

The consent of the parties is in many systems sufficient for the transfer of intangible property. Special rules are often found, however, in respect of the assignment of receivables. For instance, an assignment to a bank is a common way to finance the credit granted to a customer. While an assignment may be valid and binding on the assignor and the assignee, it does not bind the debtor, unless he has acquired knowledge of the assignment. Legal systems differ as to whether a notice to the debtor is required, or whether any other act results in the debtor acquiring knowledge of the assignment.[184] Registration often has a role in the assignment of receivables. Some jurisdictions have namely established a system of filing information about assignments of trade receivables for the purpose of providing evidence of title to the receivables, notice about assignment to interested third parties or a method of determining priorities.[185]

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182 Ali, paras. 10.06 -10.13, pp. 295-297. This also seems to be the present approach in the UNCITRAL draft Legislative Guide on Secured Transactions. One can also mention in this context the UNIDROIT draft Convention on International Interests in Mobile Equipment.

183 For instance, in the ICC Model International Sale Contract (Manufactured Goods Intended for Resale), Article 2.2. of the General Conditions provides that "(u)nless otherwise agreed, the Buyer does not acquire any property rights in software, drawings etc. which may have been available to him. The Seller also remains the exclusive owner of any intellectual or industrial property rights relating to the goods".

184 UNCITRAL doc A/CN.9/WG.IV/WP.90, para. 12.

185 Ibid., p. 6.

The UNIDROIT Principles of International Commercial Contracts 2004 introduce new rules of law regarding assignments. Chapter 9 of the new volume covers the assignment of rights[186], the transfer of obligations[187] and the assignment of contracts[188]. The new rules are a useful component of transnational legal rules that can be incorporated into contracts. The evolution of

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186 Chapter 9 Section 1 of the Principles deals only with transfers by agreement from the ´assignor´ to the ´assignee´ , including transfer by way of security of the assignor´s right to payment of a monetary sum or other personal performance by a third person (´the obligor´). Legal transfers or transfers by mergers are not covered. Transfers made through the use of negotiable instruments, documents of title or financial instruments are not covered, unless they are transferred by a normal assignment and not under special rules relating to such instruments.

A right is assigned by mere agreement between the assignor and the assignee, without notice to the obligor. The consent of the obligor is not required unless the obligation in the circumstances is of an essentially personal character (Article 9.1.7).

However, until the obligor receives a notice of the assignment from either the assignor or the assignee, he is discharged by paying the assignor. After the obligor receives such a notice, he is discharged only by paying the assignee (Article 9.1.10).

Where the assignee gives the notice, the obligor may request reasonable proof of the assignment. Adequate proof includes any writing emanating from the assignor and indicating that the assignment has taken place (Article 9.1.12).

A right to non-monetary performance may be assigned only if the assignment does not render the obligation significantly more burdensome (Article 9.1.3). Moreover, transfers from the assets of the assignor to those of the assignee remain subject to third party rights. Third party rights are in some instances governed by mandatory rules of the otherwise applicable law, more particularly the law of bankruptcy.

The assignment of a right transfers to the assignee not only the assignor´s rights to payment or other performance but also rights securing performance of the right assigned.

The assignment of a right to other performance is ineffective if it is contrary to an agreement between the assignor and the obligor limiting or prohibiting the assignment. Nevertheless, the assignment is effective if the assignee, at the time of the assignment, neither knew nor ought to have known of the agreement (Article 9.1.9). This rule decreases the importance of negotiable instruments since other rights can also be validly transferred to an innocent third party.

As will be discussed in Chapters VIII.8, VIII.10 and 11, *post*, electronic registries are used to carry out functions in the storage and transfer of equity, documents of title and other instrument-related rights. Registries could be used in transferring contractual rights which are not represented by instruments. My observation later is that the registration of rights and facts effectively prevents the indorsee invoking rules of acquiring rights or goods in good faith.

Registration is therefore a useful function in connection with contractual rights as well.

For assignment issues in international trade, see also the United Nations Convention on the Assignment of Receivables in International Trade from 2001.

187 In contrast to the assignment of rights, a transfer of an obligation by an agreement between the original obligor and the new obligor requires the consent of the obligee (Article 9.2.3). The obligee may either discharge the original obligor or retain him on board for situations in which the new obligor does not perform properly. If nothing else is agreed, the original and the new obligor are jointly and severally liable (Article 9.2.5).

Discharge of the original obligor also extends to any security of the original obligor given to the obligee for the performance of the obligation, unless the security is over an asset which is transferred as part of a transaction between the original and new obligor (Article 9.2.8).

188 In an ´assignment of a contract´, the assignor´s rights and obligations arising out of a contract are transferred. The parties are ´the assignor´, the ´assignee´ and the party other than the assignor or the assignee, called ´the other party´. The assignment of a contract requires the consent of the other party (Article 9.3.4), who may discharge the assignor or retain the assignor as an obligor in case the assignee does not perform properly. If nothing else is agreed, the assignor and the assignee are jointly and severally liable.

internationally recognised legal rules for transfers of contractual rights and obligations is creating an alternative to the development of a framework based on instruments such as documents of title. If electronic registrations are used to record rights and obligations, these two approaches will become more similar to each other at least in operation.

The assignment of rights or contracts need not be made if the contract is made directly in favour of a third party beneficiary. Chapter 5, section 2 of the UNIDROIT Principles 2004 of international commercial contracts contains general principles on third party rights. Contracts for the issuance demand guarantees and transport insurance contracts are examples of contracts made in favour of a third party beneficiary. Traditional Anglo-Saxon contract law contains the doctrine of consideration, which is founded on the idea that "the essence of contract is not promise but bargain, the exchange of equivalents".[189] This doctrine does not fit in with international trade law instruments such as documentary credits or demand guarantees, in which the bank undertakes to pay to a third party beneficiary without any consideration, and is usually disregarded.[190] The new UNIDROIT Principles now elevate this possibility into a general principle of international contract law.

V.10 Rights and obligations of the parties of a contract of transport

The role and operation of transport documents in the law of transport will be discussed in detail in the next chapter. Transport documents, whether documents of title or waybills, have multiple roles to play as they have functions both under the contract of transport and under the contract of sale, especially when documentary credits are used. They have a further role in trade finance. Transport documents ideally need therefore such qualities that they can be used in a contract of sale involving payment against documents in a manner that advantages and disadvantages are divided between the parties of the sale transaction more or less in the same way as they would be divided in a direct sale from the seller to the buyer.[191] Under documentary credits, the said functions of transport documents, together with an insurance document, have the impact that the obligations of the seller and the buyer are met simultaneously.[192]

However, a brief account is given in this subchapter on the principal aspects of the relationships between the shipper of a sea carriage or a consignor in other

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189 Goode, Commercial Law, p. 84.

190 Goode describes the confusion and approaches to the problem *ibid*., pp. 658-659.
For the potential problems caused by Anglo-Saxon law third party beneficiary contracts, in the context of the TEDI electronic bill of lading system, see TEDI Interchange Agreement (with annotation) http://www.tediclub.com/english/pdf/IA-English_Ano.pdf, visited on 18.7.2004, p. 28. For TEDI in general, see Chapter VIII.7.4., *post*.

191 Selvig, p. 44.

192 Pasanen, pp. 17-18. In German doctrine, the simultaneous performance of obligations of the seller and the buyer is called the *Zug-um-Zug* principle.

modes of transport, the carrier, and the legitimate receiver, i.e. the party surrendering a properly indorsed negotiable bill of lading or a named consignee in connection with other types of transport documents. The idea is to stress the interaction between the contract of sale and contract of transport and to make thereby ´a bridging operation´ to the next chapter, which examines transport law and transport documents.

As will be explained in the next chapter, The UNCITRAL Model Law on Electronic Commerce establishes, in Part II Chapter 1, functional equivalence between electronic transport documents, including documents of title, and their counterparts on paper. A detailed non-exclusive list of actions between the three parties is given as the scope of the relevant provisions in the Model Law.[193] These listed actions represent a good deal of situations in which the three parties are involved with each other. Some of these contacts involve documentation, some do not.

The shipper is, in principle, entitled to receive a transport document from the carrier, and in sea transport especially a bill of lading. This document evidences the conclusion of the contract of carriage, and acts as a receipt of goods delivered to the carrier. International transport conventions contain detailed provisions as to the manner goods are to be identified in the transport document.[194]

The carrier´s task is to discover clear defects in the goods. However, the carrier does not verify the specification of the goods under the contract of sale, and neither is he expected to see the contract of sale. The buyer can protect himself by organising a commercial pre-shipment survey of the goods. Such

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193 See Chapter VI.2.1., *post*.

194 Article III paragraph 3 of the Hague-Visby Rules provides "After receiving the goods into his charge the carrier or the master or agent of the carrier shall, on demand of the shipper, issue to the shipper a bill of lading showing among other things – The leading marks necessary for the identification of the goods as the same are furnished in writing [emphasis by the author] by the shipper before the loading of such goods starts, provided such marks are stamped or otherwise shown clearly upon the goods if uncovered, or on the cases or coverings in which such goods are contained, in such a manner as should ordinarily remain legible until the end of the voyage.

a) Either the number of packages or pieces, or the quantity, or weight, as the case may be, as furnished in writing [emphasis added] by the shipper.

b) The apparent order and condition of the goods.

Provided that no carrier, master, or agent of the carrier shall be bound to state or show in the bill of lading any marks, number, quantity or weight which he has reasonable grounds for suspecting not accurately to represent the goods actually received, or which he has no reasonable means of checking".

Furthermore, paragraph 5 of Article III adds "(t)he shipper shall be deemed to have guaranteed to the carrier the accuracy at the time of shipment of the marks, number, quantity and weight, as furnished by him, and the shipper shall indemnify the carrier against all loss, damages and expenses arising or resulting from inaccuracies in such particulars".

See also Article 16 of the Hamburg Rules. The distinction between ´received for shipment´ and ´shipped´ bills of lading is disregarded in this context. For the sea and other transport conventions, see Chapter VI, *post*.

surveys are not normally done, but in case of bulk trade are more frequent.[195] The survey should obviously take place before the risk passes to the buyer.

As between the shipper and the carrier, the description of the goods and their condition in the transport document can be countered by adducing evidence to the contrary. However, a negotiable bill of lading acts furthermore as a document of title along with possible variations brought by national law. The carrier has to deliver the goods against the surrender of the bill of lading. When indorsed to a person acting in good faith, the contents of the bill of lading generally become conclusive, and the carrier cannot invoke any agreement between himself and the shipper.[196]

Should the goods not be in conformity with the description in the bill or should they be delayed, the indorsee or consignee can claim damages from the carrier. The right of suit is established in legislation or in jurisprudence and can be based on either contractual or tortious liability. Notice of damage has to be given to the carrier in writing after the goods are delivered to the consignee, or if the loss or damage is not apparent, within a few days. Thereafter the suit has to be brought against the carrier within the stipulated time-limit relating to prescription in the relevant transport convention.[197] Should the goods be lost or damaged, the carrier can limit his liability.[198] However, should the carrier deliver the goods to a person not authorised to receive the goods, the carrier is liable and cannot, it is generally accepted, limit his liability.

Indorsing a negotiable transport document to the consignee transfers to him rights under the contract of carriage. In addition, as analysed *supra*, a document of title can transfer property rights under the contract sale. But under the contract of transport itself, the consignee exercising rights generally also incurs liabilities as against the carrier.[199]

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195 From an interview of Heikki *Vaara* on 25 February 2004, A measurement is taken at both ends of the carriage; in the sugar trade, a commercial survey takes place usually at the place of discharge.

A commercial survey has to be distinguished from pre-shipment inspection which is organised to meet the requirements of authorities, see Chapter VIII.6.7., *post*.

196 Article III paragraph 4 states "(s)uch a bill of lading shall be prima facie evidence of the receipt by the carrier of the goods as therein described in accordance with paragraph 3(a), (b) and (c). However, proof to the contrary shall not be admissible when the bill of lading has been transferred to a third party acting in good faith". As the shipper is deemed to have guaranteed the information as against the carrier by virtue of paragraph 5, the carrier in any case remains primarily liable against the *bona fide* indorsee of the bill anyhow. Articles 16 and 17 of the Hamburg Rules contain similar provisions.

According to *Ramberg* (Ramberg 1991, pp. 360-361), there is a discrepancy between the concept of a ´third party´ and the role of a FOB buyer, who is the party contracting with the carrier, but not the shipper. Such a buyer as the consignee, but also as a contracting party, may be protected by the provisions as a ´third party´. Article 16.3 of the Hamburg Rules has clarified the situation by adding that third party includes the consignee. In UNCTAD/ICC Rules for Multimodal Transport Documents, however, the notion of ´third party´ has been eliminated altogether.

197 Article III paragraph 6 of the Hague-Visby Rules, Articles 19-20 of the Hamburg Rules.

198 For sea carriage, see Articles IV and IV*bis* of the Hague-Visby Rules and Part II of the Hamburg Rules.

199 This matter is expressed clearly [albeit is still contested and in square brackets] in Article 60(2) of the draft Instrument on the Carriage of Goods [wholly or partly][by Sea], see Chapter VI.2.2., *post*.

The shipper is obliged to inform the carrier of the dangerous nature of the cargo and incurs liability for his failure to do so. There are, furthermore, requirements in respect of the marking of dangerous cargo.[200] The carrier has a lien (which means a pledge, lien or right of retention or any similar right stipulated in national law or in the contract of carriage) on the goods for freight and need not deliver the goods before obtaining payment. The consignee may become liable for freight to the extent provided for in national law.[201] In an ideal world, such liability is in conformity with the obligations allocated to him as the buyer under the trade term forming part of the contract of sale.

The party designated by law, which is usually based on the possession of the relevant transport documents, can give instructions to the carrier, e.g. relating to the direction of the goods. The exercise of this right of control may vary somewhat depending on the mode of transport and the transport document used. The party entitled to give instructions need not necessarily be a party under a contractual relationship with the carrier, such as the shipper or the charterer, but can be, in certain cases mentioned in the next chapter as the consignee. The transport document issued may be used to pledge the goods to the bank, which is named as the consignee, and which then is entitled to give instructions to the carrier. The duty of the carrier to comply with such instructions may be strengthened by practices whereby the carrier confirms any such instructions. In the *Bolero System*, which uses an electronic Title Registry, as well as under the CMI Rules for Electronic Bills of Lading, the acknowledgements given by the carrier are of legal significance as they constitute rights.[202]

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200 These are the so called IMO (=International Maritime Organisation) codes.

201 For instance, Chapter 13 Section 19 of the Finnish maritime code states: " (i)f the goods are delivered against a bill of lading, the consignee incurs by receiving the goods an obligation to pay freight and the carrier´s other claims according to the bill of lading". Section 46 of the same chapter adds that the bill of lading must include information about the amount of freight, if payable by the consignee, or indication that freight is payable by him, as well as any other conditions for the carriage and delivery of the goods.

As regards other transport documents than the bill of lading, Chapter 13 section 19 of the Finnish Maritime Code states that "the consignee is obliged to pay freight and other claims according to the contract of carriage only if the consignee was notified of the claims upon delivery or he realised or ought to have realised that the carrier had not received payment".

202 See Chapters VI and VIII, *post*.

VI TRANSPORT DOCUMENTS AND E-COMMERCE

In most cases it is probably true that transport documents are the most important documents in connection with an international sale of goods transaction, at least considering their legal functions. Documentary credits would be practically useless if there were no document of title symbolising and transferring indirect possession of the goods or if there were no transfer of the right of control in respect of certain transport documents. The principal role of transport documents relates, however, to the contract of transport.

VI.1 Transport law and transport documents

This chapter attempts to examine the main features of transport law, in particular the role of transport documents in connection with contracts of carriage. It will be seen that transport law is even more divided as to the role of documentation than is general sales law involving the transfer of property and security rights. The role and significance of documentation varies from one mode of transport to another, inside certain modes of transport, and from one jurisdiction to another. Generally speaking, the role of transport documentation within the framework of contracts of transport is in decline, given the reduced use of traditional bills of lading and the tendency to strip non-negotiable transport documents of their function of transferring the right to control the goods.

VI.1.1 International transport conventions

As the aim of this study is to describe the possibilities and obstacles of moving towards electronic contracting in the sale of goods involving carriage of the goods in which electronic letters of credit are used, it is not my intention to go into minute detail of substantive transport law. On the other hand, transport

documents and especially those having the character of a document of title are undoubtedly the most relevant – and problematic – documents used in the legal relationships in relation to letter of credit. Therefore, an overview of the mosaic of transport conventions and various transport documents addressed therein as well as their role in practice is necessary.

International transport is regulated by a number of conventions and regimes based mainly on the mode of transport, although attempts have been made to create a single legal framework for combined (multimodal) transport.

Carriage of goods by sea is covered by three principal international convention regimes, which are usually called the Hague Rules of 1924, the Hague-Visby Rules of 1968 and the Hamburg Rules of 1978. The Hamburg Rules differ from their predecessors in that they govern the rights and obligations of the parties to a contract of carriage regardless of whether or not a bill of lading has been issued, although some jurisdictions, such as Nordic countries, may have made exceptions as to the previous regimes, extending them to certain carriages taking place without the use bills of lading. The most important sea trading nations adhere either to the Hague Rules[1] or to the Hague-Visby Rules[2]. The Hamburg Rules have been adopted by 28 countries, which do not, however, represent major shipping nations. Moreover, there are countries outside these three systems. Therefore, already in maritime transport there are four principal liability regimes in operation.

In road transport, the CMR Convention[3] is adhered to widely in Europe, which Convention applies to every contract for the international carriage of

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1 The most important example of adherents of the original Hague Rules, but not the Hague-Visby Rules is the United States. For the carrier´s liability system established by the Hague Rules, see Hoppu,Esko: Rahdinkuljettajan tavaravastuusta, Helsinki 1966**.** An example of a ´Clause Paramount´ referring to the Hague Rules may be found in the ´General Paramount Clause´of ´Conlinebill´ (Liner terms approved by The Baltic and International Maritime Conference - BIMCO):

> *"The Hague Rules contained in the International Convention for the Unification of certain rules relating to Bills of Lading, dated Brussels the 25th August 1924 as enacted in the country of shipment shall apply to this contract. When no such enactment is in force in the country of shipment, the corresponding legislation in the country of destination shall apply, but in respect of shipments to which no such enactments are compulsorily applicable, the terms of the said Convention are applicable."*

2 The Hague-Visby Rules were approved in the form of a Protocol amending the 1924 Convention and signed at Brussels on the 23rd of February 1968. The Hague-Visby Rules have raised the limits of the carrier´s liability per unit. The 1979 Visby Protocol brought the Special Drawing Rights in use.

The Hague-Visby Rules are more widely applied than the traditional Hague Rules. For instance, all Nordic countries, even after revising their Maritime Codes in the 1990s, still adhere to the Hague-Visby Rules. In the United Kingdom, the Hague-Visby Rules are enacted through the 1971 Carriage of Goods by Sea Act.

The Hague-Visby Rules apply on a mandatory basis to the contract of carriage in cases where the contract of carriage is covered by a bill of lading or any similar document of title, in so far as such document relates to the carriage orf goods by sea. Where the bill of lading is issued pursuant to a charterparty, the Hague-Visby Rules apply from the moment at which such bill of lading or similar document of title regulates the relations between a carrier and the holder of the bill. (Article I (b) of the Rules)

3 The acronym CMR stands for *´Convention relative au contrat de transport international des marchandises par route´*, or in English ´Convention on the Contracts for the International Carriage of Goods by Road, which was signed at Geneva in 1956. The 1978 CMR Protocol was introduced to replace the gold franc used in liability provisions by Special Drawing Rights.

goods between two countries, at least one of which is a contracting state. This Convention contains a provision (Article 2.1) concerning a sea-leg in an international road carriage, which is in practice applicable to ´roll on roll off´ traffic. Moreover, one international convention relates to the transport of goods by rail, the CIM Convention[4], which is embodied in the Convention on International Carriage by Rail, the COTIF Convention[5] signed at Berne in 1980.

In air transport, the basic Warsaw Convention[6] of 1929, designed to set limitations on the liabilities of airline carriers resulting from injury to passengers or their baggage or from damage to cargo, has been amended by the Hague Protocol of 1955.[7] A supplementary convention, which was signed in 1961 at Guadalajara in Mexico, aims at the unification of certain rules relating to international carriage performed by a person other than the contracting carrier. The Warsaw Convention was further amended by Protocols Nos 3 and 4, which were signed in Montreal in 1975, and the latter Protocol is of relevance since it concerns cargo and postal items and the raising of the limits of liability in respect of them. In 1998, the United States ratified Montreal Protocol No 4, which is important since US trade accounts for some 20% of total international air traffic. Protocol No 4 was then also implemented in Europe.[8]

Yet, in air transport as well there remain several liability regimes in operation. The carriage may be governed by the original Warsaw Convention, it may be governed by the amended Convention, by the Montreal Protocol, or it may be a non-convention carriage.

In May 1999, a new Convention for the Unification of Certain Rules for International Carriage by Air was signed in Montreal.[9] This Convention aims at modernising and consolidating the Warsaw Convention and related instruments and applies to all international carriage of persons, baggage, or cargo performed by aircraft for reward. This Convention is not yet in force. However, it has gained adherence since the Member States of the European Union decided to ratify the Convention by the end of 2002. Greece was the first to do this.

In addition to the Conventions made for each specific mode of transport, an attempt has been made to create rules for multimodal (´door-to-door´) transport. The United Nations Convention on International Multimodal Transport of Goods

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4 The acronym CIM stands for *´Convention internationale concernant le transport des marchandises par chemin de fer´*. Over 30 European administrations have joined this Convention.

5 The acronym COTIF stands for *´Convention relative aux transports internationaux ferroviaires´*. There has been a revision of the COTIF-CIM (the Uniform Rules Concerning the Contact for International Carriage of Goods by Rail, Appendix B to the Convention Concerning International Carriage by Rail, as amended by the Protocol of Modification of 1999).

6 Convention for the unification of certain rules relating to international air carriage.

7 The Hague Protocol entered into force in 1963.

8 Thus, the entire convention is called ´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 signed at The Hague on 28 September 1955 and by Protocol No. 4 signed at Montreal on 25 September 1975.

9 For the text of the Convention, see OJ L 194, 18 July 2001, p. 39.

was adopted in Geneva in 1980 but has not entered into force. Furthermore, the United Nations Convention on the Liability of Operators of Transport Terminals in International Trade, which was signed in 1991, has not entered into force either. It would cover the liability of independent transport operators, with the application of the provisions of the Convention being subsidiary to other transport conventions so that damage covered by virtue of provisions applicable to the liability under maritime transport[10] would not be covered by the terminals Convention.

VI.1.2 Main approaches to the carrier´s liability

Transport documents presented under documentary credits each contain or refer to a particular liability regime, which is normally based on international conventions or contractual arrangements amending the scope of mandatory conventions. Liability issues generally are a central obstacle in the way of electronic transport documents, since if there are doubts about a carrier´s eventual liability regime. Then their liability insurers, the protection & indemnity (P&I) clubs, may refuse to accept their use, a problem which has occurred.[11]

Although it is not necessary to present each of those regimes in detail in this part of the study, which focusses on documentary requirements, the rights and obligations created under these regimes for the parties of a transport contract, including the holder as pledgee of a transport document, have great significance for the parties. This explains very much the conservatism as regards streamlining transport conventions.

The principles under which the carrier is liable for loss of or damage to the goods under his custody or for delays in delivering them, differ substantially depending on the mode of transport used. Likewise, the quantitative limits of carrier´s liability differ from one another. Furthermore, the different regimes have different provisions for notice periods and prescription. As'*Schmitthoff* has put it, "the continuance of this legal tower of Babel is indefensible in modern circumstances, in which the multimodal transport plays an almost dominating role in the international transport of goods...".[12]

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10 The 1994 Maritime Code of Finland extends the mandatory application of carrier´s liability to container terminals in lieu of the ´tackle-to-tackle´ limits of the Hague-Visby Rules. However, Finnish and other Nordic Marime Codes make it possible for the carrier to decrease his liability by defining his duties as to when he takes the goods into his charge and when they cease to be in his charge, see Honka, pp. 34 et seq.

11 Transport documents may affect the applicable convention regime and the absence of paper documents might be seen to jeopardise the limitation or exoneration system, or to bring in uncertainties about delivery to the correct person. A legislative approach equating electronic transport documents could help in lowering resistance.

12 Schmitthoff, Export Trade, Eighth edition, 1986, p. 526.

The grounds for carrier´s liability vary, generally speaking, from objective liability (air transport[13]) to strict liability with force majeure exceptions (road transport under the CMR Convention[14], rail transport), to liability for negligence with a reverse burden of proof or presumed fault or neglect (the Hague and Hague-Visby Rules for maritime transport), or to ordinary liability for negligence (sea passengers).[15]

The Hamburg Rules differ, in addition to slightly increased limits of liability, from both the Hague-Rules and the Hague-Visby Rules in that the carrier no longer is exempt from liability for errors in navigation or fire.[16] The Hague and Hague-Visby Rules are a result of a historical fine-tuned commercial balance of interests. A rapid breakthrough of the Hamburg Rules, which would be much

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13 The carrier of goods by air is automatically liable for destruction or loss of, or damage to or delay of cargo if it occurs during the carriage by air. The carrier has the right to use specified defences if he can, but he cannot contract out of liability or for a lower limit of liability.

The carrier is not liable if he proves that he and his ´servants´ or agents have taken all necessary measures to avoid the damage or that it was impossible for him or them to take such measures. Furthermore, if the carrier proves that the damage was caused or contributed to by the negligence of the injured person the carrier may be exonerated wholly or in part.

14 Under the CMR Convention, the carrier is relieved from liability if the loss, damage or delay was caused by the wrongful act or neglect of the claimant, by the instructions of the claimant, or by the instructions of the claimant given otherwise than as a result of a wrongful act or neglect on the part of the carrier, or by inherent vice of the goods, or through circumstances which the carrier could not avoid and the consequences of which he was unable to prevent. (Article 17(2)). If the carrier wishes to rely on the last mentioned ground for relief, it is not sufficient for him to show that he did not act negligently; he has to show that the loss could not be avoided.

15 Following the presentation by Dr. Lena *Sisula-Tulokas* at a seminar organised by the Finnish Section of the ICC on 17.11.1993. See also Sisula-Tulokas, Kuljetusoikeuden perusteet, Helsinki 2003.

16 Article IV Paragraph 2 of the Hague-Visby Rules provides that "neither the carrier nor the ship shall be responsible for loss or damage arising or resulting from inter alia [there are 18 points all in all listed from (a) to (q) on the list of ´excepted perils´]

"(a) act, neglect or default of the master, mariner, pilot, or the servants of the carrier in the navigation or in the management of the ship; or

(b) fire, unless caused by the actual fault or privity of the carrier".

Point (q) states the most general of the ´excepted perils´, which relieves the carrier from liability resulting from "any other cause arising without the actual fault or neglect of the agents or servants of the carrier, but the burden of proof shall be on the person claiming the benefit of this exception to show that neither the actual fault or privity of the carrier nor the fault or neglect of the agents or servants of the carrier contributed to the loss or damage".

The shipowner cannot rely on the ´excepted perils´ if he has not carried out his obligation under Article III, rule 1 to exercise due diligence to make the ship seaworthy and thes non-fulfilment of the obligation causes the damage, nor can he do so if the vessel makes a deviation not permitted by Article IV Rule 4. (Payne & Ivamy 1985, pp. 186-187, and 1989, pp. 112-116)

Under the Hamburg Rules, the carrier is liable for loss resulting from loss or damage to the goods as well as from delay in delivery if the occurrence which caused the loss, damage or delay took place while the goods were in his charge unless, the carrier proves that he, his servants or agents took all the measures that could reasonably be required to avoid the occurrence and its consequences.(Annex I, Art 5(1))

more in line with the liability provisions applicable to other modes of transport, cannot be predicted at the moment.[17]

The United Nations Convention on International Multimodal Transport of Goods of 1980 would apply, should it enter into force, to carriages made using more than one mode of transport. The grounds for the Multimodal Transport Operator´s liability as well as its limits are very close to those in the Hamburg Rules.[18] However, if it is known during which type of carriage the goods have been damaged and if the maximum liability required by the legislation applicable to that mode of transport is higher than that given in the MTO Convention, then the rules providing for higher compensation shall apply. This is often called the ´network liability principle´[19], according to which the liability network for the relevant mode of transport shall apply, while however, introducing a general fall-back liability provision for situations where it is not known at which stage of transportation the damage occurred.

As already mentioned in Chapter V.3., *ante*, given the possibilities for the carrier to limit his liability for loss of or damage to the goods, the party who suffers the loss or damage after the risk has passed to him has better a chance of

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17 The reason why the Hamburg Rules have not had success is mainly because the insurance industry has opposed them. It is thought that a sound commercial balance already exists at the moment. If the carrier´s liability were to be increased by taking away some excepted perils and increasing amounts, this would lead to increased recovery costs, which is thought to be too costly. Insurance companies can tackle the situation through insurance conditions or risk prevention directives to their clients. (Ramberg 1993, pp. 189-190)

It also seems that the UNCITRAL draft instrument on the carriage of goods by sea under preparation will discard part of the outcome of the Hamburg Rules and maintain nautical fault and fire exceptions.

18 Article 16 of the Convention provides that the multimodal transport operator shall be liable for loss resulting from loss of or damage to the goods as well as from delay in delivery if the occurrence which caused the loss, damage or delay in delivery took place while the goods were in his charge, unless the multimodal transport operator proves that he , his servants or agents or any other person referred to Article 15 of the Convention took all the measures that could reasonably be required to avoid the occurrence and its consequences.

19 As this Convention is not yet in force and applicable, the idea of a network liability principle has been introduced through standard terms. The ICC Rules for Combined Transport Documents (ICC Brochure 298, 1975) was created for this purpose and was replaced by the UNCTAD/ICC Rules for Multimodal Transport Documents, ICC Publication No 481, which came into effect on 1 January 1992. The purpose of these Rules is well-defined in its foreword: "In the absence of an international convention applicable to multimodal transport, the UNCTAD/ICC Rules for Multimodal Transport Documents are intended to avoid a multiplicity of different regimes governing such transportation and to provide a private transport contract with a uniform legal regime." The Rules are designed to fill the gap existing in the regime due to the delay in the entry into force of the United Nations Convention on Multimodal Transport of 1980, but they differ from the Convention essentially in that they are based on the Hague Rules and the Hague-Visby Rules approach that the carrier´s liability is based on the presumed fault and the two fundamental defences for the carrier, namely nautical error and fire, are expressly mentioned. Multimodal transport and a uniform set of rules for the entire carriage, albeit based on network liability, serve the idea of a managed supply chain.

For early applications of the ´network liability´ principle, see Grönfors, 1991, pp. 33-47.

The UNCTAD/ICC Rules have been incorporated into the general conditions of two major combined transport documents, namely the freight forwarders´ FIATA Bill of Lading and the ´COMBIDOC´ published by the Baltic and International Maritime Commission (BIMCO).

recovering any amount lost from his transport (cargo) insurance. This insurance may be taken by the party bearing the risk under the transportation, or a contract may be taken by the seller in favour of the buyer (CIP and CIF contracts). The transport insurer then has a possibility to recover from the carrier or his liability insurer, by way of subrogation, at least part of the amount indemnified to the assured. Particularly in shipping, liability insurers are mutual protection and indemnity (P&I) clubs.

A document evidencing transport insurance, a policy or an insurance certificate, regularly forms part of the documentation to be presented under documentary credits.

Another cause of liability, which is more relevant when the application of electronic documents is used, is the carrier´s liability for the delivery of cargo to an unentitled consignee. The carrier may become liable for not requiring the presentation of a bill of lading.[20] This form of liability has remained outside transport conventions (apparently because the carriers have never consistently challenged the existence of their liability, and the number of problem cases has supposedly remained very low as compared to the number of cargo claims), but some principles have been established in legal literature.[21] Generally speaking, the carrier´s liability for delivery to an unentitled person is strict, especially if it is intentional.

It seems to be very difficult to make changes in liability regimes that would simplify their patchwork nature. Their fragmentary nature is relieved by the use of transport documents that cover the entire carriage door-to-door by resorting to the network liability approach. Still, all reforms that make the substantive law of contracts of carriage more uniform would certainly help to improve the acceptability of e-commerce in the field of transport, although no direct link exists between the two issues.

VI.1.3 The types and functions of transport documents

When cargo is delivered for shipment in maritime transport, a bill of lading or a non-negotiable sea waybill is issued.[22] In other modes of transport, the transport documents are, as a rule, non-negotiable. Negotiable instruments can, however, be issued for multimodal transport and, in theory, for air transport as well.

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20 The person requesting delivery without a bill of lading may issue a security or an indemnity for the damages the carrier may have to pay to the correct consignee (Scrutton 1996, art.151).

21 According to the Nordic doctrine, the carrier cannot limit his liability for this *´utlämnings/utleveringsansvar´*; see Sjur Brækhus, Bortfrakterens ansvar for utlevering av last till ulegitimert mottager, Arkiv for Sjørett, Vol. 2 (1955), pp. 144-149 and 152-156; Selvig Grenseland p. 79, Honka, pp. 138 et seq., Wetterstein 1983, p. 118 and Falkanger-Bull, p. 297. The discussion on the subject seems to be more scarce in English or French textbooks.

22 Without prejudice to attempts at creating a paperless carriage, such as those made by the Atlantic Container Line.

Negotiability need not necessarily lie on a statutory basis but can be, it is submitted, created by contractual provisions (in civil law countries) or by an established custom (in England).[23]

VI.1.3.1 The bill of lading as a document of title

The role of the bill of lading as a document of title representing the goods and transferring various property and security rights has already been dealt with in detail in Chapter V.4.2., *ante*. It is, however, necessary to examine the bill of lading in greater detail.

To start the discussion of the bill of lading, one may look into the definition of the bill of lading which is contained in Article 1(7) of the Hamburg Rules[24] and which has also been taken on board by UN/CEFACT Recommendation No. 12 ´Measures to facilitate maritime transport documents procedures.[25] A bill of lading is said to be

> *"...a document which evidences a contract of carriage and the taking over or loading of the goods by the carrier, and by which the carrier undertakes to deliver the goods against surrender of the document. A provision in the document that the goods are to be delivered to the order of a named person, or to order, or to bearer, constitutes such an undertaking"*.

The shipper may demand a bill of lading immediately when the goods are received into the charge of the carrier.[26] Bills of lading are frequently issued in several originals. This was useful at the time when mailing was insecure, but may create problems, if the originals are in different hands. In the port of destination marked on the bill, a single original is sufficient to legitimate its holder to claim the goods from the carrier. If the goods are delivered against one original, this original is ´accomplished´ and other originals stand void.[27] In other ports, however, a full set of originals has to be presented. Moreover, if the exporter sells under a letter of credit, he normally hands over (presents) all originals of the bill, together with other required documents, to the bank.[28]

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23 See the country report for the Netherlands by Richard Zwitser in Transfer of Ownership, p. 239.

24 United Nations Convention on the Carriage of Goods by Sea, 1978.

25 UN/CEFACT Recommendation No. 12 second edition, Geneva October 2001, ECE/TRADE/240, p. 12.

26 Hague-Visby Rules Art 3(3), Hamburg Rules Art. 14(1). Scrutton 1996, art. 32.

27 Schmitthoff, Export Trade, p. 256. The various parts of the bill are forwarded by the consignor to the consignee e.g. by air mail or courier. Sometimes the vessel will even carry the shipping documents by storing one original which, together with other shipping documents, accompany the ship in the ship´s bag. The original bill is then given to the addressee representing the consignee. The bill will then be forwarded to the ship´s agent who will thereafter issue a ´delivery order´.

For background and on attempts to get rid of three originals, see Grönfors, 1991, pp. 20-21.

28 If this bank is an advising or negotiating bank, it will send the documents via air mail to the issuing bank. See Chapter VII, *post*.

The bill of lading is a receipt by the shipowner acknowledging that goods of certain particulars are shipped or at least received for shipment, as the case may be. It also evidences a promise to carry the goods to a certain destination and to deliver them upon presentation of an original bill of lading.[29] A bill of lading is not the contract, but rather evidences the terms of the transport contract. In the hands of an indorsee in good faith, however, it is the only evidence.[30] Thus, if the carrier makes no reservation in respect of any damage to the goods already visible at the time he receives them, he becomes liable to compensate for these damages to the consignee.[31] However, if the carrier enters his reservations on the bill, the bill is ´claused´ and not a ´clean´ bill.

As the bill of lading evidences the terms of the transport contract, there may or may not be a pre-existing contract document in respect of the cargo, such as a charterparty[32] or a booking-note.[33] If there is a charterparty, the terms of the contract of carriage are defined in it and the bill of lading frequently incorporates them by referring to the charterparty. In the hands of other parties than the shipper, however, the bill evidences the terms of the contract of carriage.[34]

Finally, a bill of lading is a document of title. It enables the consignee to dispose of the goods after an indorsement[35] and delivery or delivery of the bill of lading. The carrier undertakes to deliver the goods against surrender of the document. The carrier is neither entitled nor obliged to deliver the goods unless an original bill of lading is surrendered. Should the carrier deliver the goods without it, this would be regarded as a wilful breach of his obligations and he would become liable to the legitimate consignee without any possibility to limit

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29 Falkanger-Bull, pp. 237-238.

30 This applies by virtue of the Hague-Visby Rules. Falkanger-Bull, p. 292. Scrutton 1996, Art. 30.

31 Such a bill of lading shall be prima facie evidence of the receipt by the carrier of the goods as therein described. However, proof to the contrary shall not be admissible when the bill of lading has been transferred to a third party acting in good faith. Article III paragraphs 3 and 4 of the Hague-Visby Rules, Article 16 of the Hamburg Rules.

32 Charterparties are used to hire an entire vessel for a certain period of time (time-charters) or for a certain voyage or voyages (voyage charter). There are also demise (bare-boat) charterparties. The shipowner may issue, or may be required to issue, bills of lading for the goods loaded or received for shipment under charterparties. The Hague and Hague-Visby Rules as well as the Hamburg Rules do not apply mandatorily to charterparties and apply to charterparty bills of lading only from the moment the bill of lading regulates the relations between the carrier and the holder of the bill.

33 In liner shipping, the shipping line issues a booking note to signify that a space has been booked on board a ship for a shipper. The booking note regularly refers to the applicable conditions of carriage and is therefore also of significance in evidencing the contract. A mate´s receipt is given to the shipper when he delivers the goods to the ship or terminal.

34 Wetterstein 1984, p. 28.

35 Goods shipped under a bill of lading may be made deliverable to a named person, to a name left blank or to bearer, and in the first two cases may or may not be made deliverable to ´order or assigns´. Under English law, bills of lading making goods deliverable ´to order´ or ´to order or assigns´ are by mercantile custom negotiable instruments, the indorsement and delivery of which may affect the property in the goods shipped. This is the custom of merchants (or *lex mercatoria*) which was recognised as being part of English law in the special verdict in the case *Lickbarrow v. Mason (1794) 5 T.R.. 683*. In this verdict, bills of lading were for the first time recognised as transferable documents of title, the word ´negotiable´ meaning merely transferable. >>

his liability.[36] The carrier would therefore need, in order to protect his interests, a guarantee from the consignee who did not produce an original bill of lading for the delivery.

Perhaps the principal purpose of the bill of lading is to enable the person entitled to the goods represented by the bill to dispose of the goods by selling them while they are in transit. By mercantile custom, possession of the bill is in many respects equivalent to possession of the goods, and the transfer of the bill of lading has normally the same effect as the delivery of the goods themselves. The delivery of the goods sold in transit takes place by transferring the bill of lading (´constructive delivery´).[37] Moreover, the goods are pledged by handing over the bill to the pledgee.[38] However, the transfer of the bill does not

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<< Indorsement is effected either by the shipper or consignee writing his name on the back of the bill of lading, which is called an ´indorsement in blank (*blanco)* ´or by his writing ´Deliver to X or order, Y´ which is called an ´indorsement in full´ (Scrutton 1996, Art. 94).

By mercantile custom, an indorsement and delivery of a bill of lading transfers such property as it was the intention of the parties to the indorsement to transfer (Scrutton 1996, Art. 95, referring to the case *Sewell v. Burdick (1884) 10 App.Cas. p. 74*). The inference that an assignment of property is contemplated will be weaker from an indorsement in blank than from one in full (Scrutton 1996, Art. 94, referring to the same case, p. 83). The decision in Sewell v. Burdick has made it clear that that the effect of the indorsement of a bill of lading depends entirely on the particular circumstances of each indorsement and that there is no general rule that indorsement passes the whole legal property in the goods (Scrutton 1996, Art. 96).

In addition to indorsement, a negotiable instrument may also be transferred (under Anglo-Saxon law) by assignment. An assignment is a separate deed affixed to the document. (ICC Doc ECP WG 1/13, 12/10/98, p. 59).

According to the Hamburg Rules (Article 1(7)), there should be a provision in the bill of lading or other document of title, according to which the goods are to be delivered "to the order of a named person, or to order, or to bearer". The Nordic Maritime Codes have followed that path, but added that "a bill of lading made out to a named person shall be considered an order bill of lading unless it contains a reservation against transfer by terms such as "not to order" or similar (e.g. the Finnish Maritime Code 1994 Chapter 13 section 42(2)).

Schmitthoff (Export Trade, Eighth Edition, 1986, pp. 492-493) uses the term ´quasi-negotiable´ which is said to reflect the views of some English authorities, and which implies that the bill itself shall contain all the essential terms of the contract of carriage and an indorsee or other holder of the bill shall be able to gather the terms from the document itself. However, as compared to a bill of exchange, which is negotiable unless otherwise stated, a bill of lading is negotiable only if it is made negotiable by writing the word ´order´ in the consignee box of the bill of lading form and stating the ´Notify Party´ thereto. Secondly, a holder of the bill of lading cannot acquire a better title than his predecessor possessed, whereas the holder in due course of a bill of exchange is entitled to the benefits arising from a bill of exchange obtained through fraud before a *bona fide* indorsement. (Schmitthoff, Export Trade, pp. 275-276). Whereas the transfer of a bill of of exchange transfers the ´ownership´ of a debt, a bill of lading passes merely indirect possession of the goods, and the property passes only where this is the intention of the parties, see the Bolero Feasibilility Study 1999.

Thus, when the word ´negotiable´ is used in relation to a bill of lading under English law, it merely means ´transferable´. (*Kum v. Wah Tat Bank Ltd [1971] 1 Lloyd´s Rep 439 at 446*; Payne-Ivamy 1985 p. 81, Scrutton 1984, art. 92, p. 185).

36 Falkanger-Bull, p. 297. There would not be any P&I coverage either.

37 It is possible to transfer the bill partially, by resorting to the use of several originals, one transferred to the buyer of part of the cargo and another representing the remainder.

38 Schmitthoff, Export Trade, pp. 289-290. Bull-Falkanger 1982, p. 238. Under English law, the possession of the document of title establishes ´constructive possession´ over the goods.

necessarily imply the transfer of the property in the goods, since this depends on the intention of the parties, or the applicable law may provide otherwise.[39]

A difference can be found in the treatment of the bill of lading in common law countries and a number of civil law countries. For instance, under the Scandinavian Maritime Codes a *bona fide* holder of a stolen bill of lading can acquire a better title than his predecessor, since the real owner of a stolen bill of lading may not be allowed to take it back by vindication from the purchaser in good faith, and he may also be prevented from taking the goods back at a later stage.[40] Moreover, in many civil law countries a negotiable bill of lading is a negotiable instrument, ´a document of credit´ (or a ´credit instrument´), similar to a check or bill of exchange. If a bill of lading is drawn up in accordance with legal requirements, it is considered to be complete evidence by all parties concerned as well as between such parties and third parties such as underwriters and indorsees. [41]

In the French doctrine, for instance, a bill of lading is not a document of title (*titre de propriété*) because the rights which are transferred with it are of credit (*titre de créance*) and not ownership.

Thus, under French law, a bill of lading gives its holder the right to claim delivery of the goods described therein just as a bill of exchange gives its holder the right to demand a sum of money.[42] Many writers do not emphasise the difference however.[43] The essence should be that the document as such does not

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39 Under English law, problems were created by the 1855 Bill of Lading Act, which provided that "every consignee of goods named in the bill of lading, to whom the property in the goods therein mentioned shall pass upon or by reason of ...consignment or endorsement, shall have transferred to him and vested in him all rights of suit, and be subjected to the same liabilities in respect of the goods as if the contract contained in the bill of lading had been made with him" (emphasis added). Therefore the rights to suit were tied to the property to the goods, which caused undesired consequences, see the case ´Aliakhmon´ (*Leigh and Sillivan Ltd. V. Aliakhmon Shipping Co. Ltd. [1985] 2. W.L.R. 289*).

The 1855 Bill of Lading Act was, however, repealed by the 1992 Act, under which this problem no longer arises.

40 Norwegian Maritime Code § 306. Røsæg, ´Electronic Bills of Lading - sophisticated toys or workable solutions?´, at a Seminar in Maritime Law Autumn 1994, Scandinavian Institute of Maritime Law, University of Oslo, 19.10.1994.

41 Luis Cova Arria, Legal Obstacles to the Implementation of the Electronic Bill of Lading in Civil Law Countries, European Transport Law, ETL, 1997, p. 709.

42 Ibid., p. 710, see also Martine *Remon-Gouilloud*, Droit Maritime, 2nd ed., Paris 1993, p. 356 and the 1st ed., Paris 1988, p. 313. See, however, *Rodière*, Traité général de droit maritime, affrêtements & transports, tome II, Les contrats de transport des marchandises, Paris 1968, no 480, p. 109, who thinks that the assimilation of a bill of lading with e.g. a bill of exchange is a fundamental error. According to Rodière, different writers tend to emphasise either the causal aspect (the connection with the relationship behind it) or the abstract aspect (freedom from the *causa*) of the instrument. Much of this literature is decades old. The problem seems to be partly theoretical. It is alien for modern generations of lawyers to operate with established concepts from which legal effects are then deduced (*Begriffsjurisprudenz*). For Belgium, see Putzeys-Rosseels no. 503, page 283: "Le connaissement n´est pas un titre de propriété: il confère un titre à la délivrance de la marchandise, sans que l´on ait à rechercher la cause de cette possession".

43 See, for instance, Plégat-Kerrault in Transfer of Ownership, p. 167; Lamy Transport, tome 2 (point 443), simply uses the term ´titre représentatif de la marchandise´ as does Rodière 1991, no 348, pp. 266-267. See also the case *Cour de Cassation de France, 1.10.1985, Cooppérative Agricole d´Esternay v. Margarine Verkaufs Union*, ETL 1986.I. pp. 91-101, which uses the term ´titre de propriété´ for an inland bill of lading.

necessarily give its holder all proprietary rights, since, for instance, retention of title clauses may affect the position of the holder of the bill.

Moreover, this argumentation does not take into consideration that the term ´document of title´ is at least indirectly used in both the Hague-Visby Rules and the Hamburg Rules, although without defining its precise meaning.[44] These Rules do, however, expressly give a bill of lading a number of legal effects. The countries adhering to these Rules must give the bill of lading at least these effects, but may treat it differently in other respects. The question of whether a bill of lading with relevant characteristics is a negotiable instrument or a ´document of credit´ comparable, among other things, to a bill of exchange depends on the applicable domestic law.

VI.1.3.2 Main types of bills of lading

The difference between a *´clean´ bill of lading* and a *´claused´ bill of lading* has already been explained *supra*. The carrier does not have to examine the goods thoroughly. It suffices to state the apparent order and condition of the goods.[45] In any case, a clause stating any deficiency in or damage to the goods reduces the value of the bill.[46]

The goods to be shipped may be received by the carrier at a terminal (or quay) or on board the ship. In the latter case, an *´on board´ bill of lading* should be issued; in the former case, a *´received´ bill of lading* is to be issued. Again, an ´on board´ bill of lading is more valuable than a ´received´ bill of lading, since the latter does not prove that the actual shipment has already been carried out.[47] The actual shipment may namely have a bearing on the liabilities of the parties. The use of ´received´ bills of lading has increased since a container bill of lading issued at an inland loading depot of the container shipping line is invariably a ´received´ bill of lading.

A *charterparty bill of lading* is a bill which incorporates, by reference, some of the terms of the charterparty, so that the terms might have effect against the consignee or an indorsee of the bill. On the contrary, if the bill issued under a charterparty does not incorporate the terms of the charterparty into the contract, it is not a charterparty bill of lading in the technical sense.[48]

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44 Article III (7) of the Hague-Visby Rules and Article 15(2) of the Hamburg Rules. It is submitted that the notion is used to define the scope of the conventions.

45 Article III, paragraph 3(c) of the Hague-Visby Rules and Article 15 paragraph 1(c) of the Hamburg Rules.

46 Shipowners may be asked by shippers to disregard the faults in the goods delivered for shipment by offering ´back letters´ for compensating the shipowners any losses they might incur by not clausing the bill properly. ´Back letters´ are, however, considered to be illegal.

47 Schmitthoff, Export Trade, p. 277.

48 Schmitthoff, Export Trade, p. 273. Another question is the role of the bill of lading for goods on a chartered ship. *Prima facie*, the bill of lading in the hands of the charterer is merely a receipt for the goods. However, in the hands of an indorsee from the charterer, the bill of lading must be considered to contain the contract as between the indorsee and the shipowner. (Scrutton 1996, Articles 34 to 36).

A *blank back bill of lading* is a bill of lading which does not contain the transport conditions on the reverse side of the bill of lading form, but merely refers to them. The conditions are either supposed to be known to the parties[49] or can be inspected at the office of the shipowner.[50]

A *through bill of lading* is a bill of lading which evidences a contract of carriage from one place to another made in separate stages of which at least one stage is sea transit and by which the issuing carrier accepts responsibility for the carriage as set forth in the document.[51] A through bill of lading is used where the sea-carriage forms only part of the complete journey, and goods have to be carried by several land or sea carriers. In this case, one can speak of a *combined transport bill of lading*. The shipper contracts only with one carrier, who is responsible for the entire journey although he does not perform the carriage entirely by himself. It is possible that the carrier sub-contracts each leg of the carriage.

As against the shipper and the consignee, there is, however, only one liability regime, although this may contain elements of several regimes through the application of the ´network liability´ principle. Through bills of lading are also used where the sea transit itself is divided into separate stages to be performed by different shipowners by a process of ´transhipment´. A through bill of lading can cover on-carriage by air. In current use, a through bill of lading, a combined transport bill of lading or a ´received´ bill of lading are, at least by custom, treated as transferable documents of title.[52]

A combined transport bill of lading could more generically be called a *combined transport document*[53], as there is no legislation in force that would guarantee its status as a document of title however it is labelled. The best example of such a document is the FIATA Combined Transport Bill of Lading

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49 For instance, many general conditions of carriage used in the Baltic Sea and the North Sea are based on the ´North Sea Standard Conditions of Carriage´ created by a regional shipowner´s conference. Some shipowners add their own variations in a separate part ´Special and Local Clauses´.

50 Modern information technology eases incorporation by reference or making the terms available. See Chapter VIII.2.1.6., *post*.

51 UN/CEFACT Recommendation No. 12 second edition, Geneva October 2001, ECE/TRADE/240, p. 12.

52 Scrutton 1996, Art 181: "But it is submitted that there would now be little difficulty in establishing that all three types of document are by custom treated as transferable documents of title. For the same conclusion in Scandinavian law, see Selvig, p. 6. In Germany, the law was unclear as to through bills of lading until the 1998 law reform, which led to the adoption of the ´Gesetz zur Neuregelung des Fracht-, Speditions- und Lagerrechts´ (Transportrechtsreformgesetz – TRG) of 25.6.1998, BGBl I, 1588. Herber, NJW 1998, p. 3300.

According to Todd (Todd 1998, p. 128), however, English law unequivocally gives only a ´shipped´ bill of lading the status of a document of title. He does not conclude such custom to exist in respect of other documents. In Belgium, a ´received for shipment´ bill is not in principle negotiable (Putzeys-Rosseels, no 517, p. 290).

53 The Baltic and International Maritime Conference (BIMCO) has published a number of transport document and charterparty forms. For multimodal transport, there is the COMBICONBILL form (revised in 1995) and the MULTIDOC 95 form.

(FBL)[54], which in its title states that it is ´negotiable´. The FBL is issued by a freight forwarder, and there exist other transport documents issued by freight forwarders.[55]

Todd[56] argues, obviously referring to English law, that although combined transport documents can be either negotiable or non-negotiable, even a negotiable combined transport document may not be a document of title without proof of custom. According to him, no such custom yet exists. Consequently, even a negotiable combined transport document might not transfer constructive possession or property in the goods to the holder of the document, and a negotiable combined transport document may well obtain security which is inferior to that provided by a shipped bill of lading. The authors of *Schmitthoff´s Export Trade* (Tenth Edition, 2000) argue[57] that the ´negotiability´ of the FIATA documents merely means assignability of the rights under the contract of carriage but not transfer of obligations. Moreover, the FIATA Combined Transport Bill of Lading is not a document of title, but contractually the surrender of the duly indorsed document is a condition precedent for the delivery of the goods. The author has not come across analyses of the status of the FIATA bill of lading in other jurisdictions.[58]

A container bill of lading is used by shipping lines which engage in combined transport. They are subject to the Hague-Visby Rules in respect of the sea leg of the carriage, insofar as these Rules would be applicable otherwise. All container bills of lading tend to adopt the network liability system, and they usually provide that, when the stage where the loss of or damage to the goods cannot be ascertained, the liability of the carrier shall be determined by the Hague-Visby Rules.[59]

A *house bill of lading* is issued by a freight forwarder who consolidates several cargoes belonging to different owners or forming the subject-matter of different export transactions in one consignment shipped under a *groupage bill of lading* issued by the carrier to the forwarder. A house bill of lading is not a bill of lading legally since it is not a document of title, at least under English law.[60]

A *straight bill of lading* is a bill of lading completed in such a way that delivery is to be made to the named consignee only. Accordingly, it is not a transferable or negotiable document of title which can be used to transfer title to or possession of

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54 FIATA is the international freight forwarder´s federation "*Fédération internationale des associations de transitiares et assimilés*". FIATA has published standard conditions, last revised in 1992 (incorporating the 1991 UNCTAD/ICC Rules for Multimodal Transport Documents) governing the FIATA Multimodal Transport Bill of Lading.

55 A *Forwarder's Certificate of Transport (FCT)* contains a clause according to which the goods are only released against the surrender of the document. Strangely, the party issuing the document – the freight forwarder – does not assume carrier´s liability.

A *Forwarder's Certificate of Receipt (FCR)* is a non-transferable document issued by a freight forwarder who, unlike in FCT, assumes carrier´s liability.

56 Todd 1998, p. 149.

57 On page 280.

58 For instance Lamy Transport, tome 2, point 469, page 321, mentions only the negotiability of the FBL under French law.

59 Schmitthoff, Export Trade, p. 320.

60 Ibid., p. 498.

the goods. The term ´bill of lading´ is confusing in this context because it is mostly used to signify a negotiable instrument.[61] It would be easy to align a non-negotiable bill of lading with sea waybills (see *infra*), but the fact that the bill must be surrendered makes it a compromise between a negotiable bill of lading and a sea waybill.[62] The attachment of the mandatory liability regime based on the Hague-Visby Rules may be critical.[63]

As regards transport documents in the United States[64], there are two types of bills of lading, negotiable and non-negotiable. A negotiable bill of lading must be consigned to bearer or to order or to the order of a named consignee, it must be stamped ´original´ and surrendered in exchange for the goods (´order´ bill). A non-negotiable bill of lading (which may be called straight bill, waybill, sea waybill, air waybill and so on) is made out to a named consignee, requires no originals and need not be surrendered.[65] A non-negotiable bill of lading can only be assigned and cannot be negotiated (transferred for value by delivery or indorsement). A negotiable bill of lading is effective for the transferring of title. A non-negotiable bill of lading is effective in transferring the right of control (see *infra*).[66]

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61 Under English law, a ´non-negotiable bill of lading´ is known, whereas in civil law countries this is a misnomer, since bills of lading are by definition negotiable.

62 In fact it is unique for the bill of lading that the delivery must take place against its surrender (see Grönfors 1982 § 151, p. 278)

In a recent case before the English courts, ´The Happy Ranger´ [2002] 2 Lloyd´s Rep. 357, the bill of lading appeared to be a straight bill – the consignee box showed only a named consignee and did not contain the words ´to order´. Nevertheless, the face of the bill contained, in another body of text, the printed words "consignee or to his or their assigns". It was held that the bill was negotiable. So there seems to be a presumption of negotiability in case of doubt in English law.

63 See the case RAFAELA S [2003] 2 Lloyd´s Rep. 113. Chapter VI.3.4.2., *post*.

64 The United States remains a party to the original Hague Rules. The Carriage of Goods by Sea Act (COGSA) 1936 incorporates the rules in relation to outward and inward shipments. The Federal Bill of Lading Act 1916 (The *Pomerene Act*) applies to export shipments and interstate shipments whether by vessel, rail, truck, or aircraft, when a bill of lading, negotiable or non-negotiable, is used. A proposed revision of the Pomerene Act would also extend it to import shipments subject to the COGSA. Interestingly, the Pomerene Act regulates the relations between the shipper and the carrier, between the carrier and the consignee, and even between the shipper (seller) and the consignee (buyer).

The United States did not enact the Hague-Visby Rules. Thereafter came the Hamburg Rules in 1978. Both sets of rules have their supporters in the US. The US government, through staff members of the Department of Transportation, the US Senate and the House of Representatives, have indicated that the US would not take action until or unless all circles of the US maritime industry agreed on the course of action to be taken. In the meantime, the Maritime Law Association of the United States formed a working group to attempt to look for a consensus amongst the various segments of the US maritime industry. In May 1996, the US MLA produced a draft COGSA. The suggestion has advanced to a legislative process but has not yet resulted in enacted law. The MLA suggestion contains elements of the Hague, Hague-Visby and Hamburg regimes, see Force in Honka, p. 373, and US COGSA update by Chester Hooper, The MaritimeAdvocate.com, Issue 16, September 2001, http://www.maritimeadvocate.com/i16_cogs.php, visited on 22.8.2003. See also Senate Draft COGSA 1999 [Staff Working Draft] September 24, 1999, http://tetley.law.mcgill.ca/maritime/cogsa99.htm, visited on 22.8.2003. See also the US approach in respect of the UNCITRAL draft Instrument on the Carriage of Goods [wholly or partly [by Sea], *infra*.

65 George F. Chandler, III in Transfer of Ownership, p. 418.

66 Ibid., p. 423. Chandler, III mentions that, under US law, a non-negotiable bill of lading is a ´document of title´ within the meaning of the Hague and Hague-Visby Rules, which I understand to mean its transport law functions.

VI.1.3.3 Non-negotiable maritime transport documents

In sea-carriage, non-negotiable *sea waybills* or *liner waybills* are also used, especially for fast liner routes in the Baltic Sea and the North Sea, in cross-Atlantic trade as well as in certain areas of the Far East. Sea waybills are always practical when the goods are not sold during the transit and where the goods usually reach their destination so quickly that a requirement to produce an original bill of lading would slow down the logistical process as the mail might come in later than the goods themselves. Sea waybills were first introduced in the late 1960s.

In the international context, UN/CEFACT has defined, in its Recommendation No. 12 entitled 'Measures to facilitate maritime transport documents procedures'[67] the sea waybill to be a "(n)on-negotiable document which evidences a contract for the carriage of goods by sea and the taking over or loading of the goods by the carrier, and by which the carrier undertakes to deliver the goods to the consignee named in the document".

The shipper or the consignee may receive the same protection as regards the carrier's liability afforded by the Hague-Visby Rules as if a bill of lading were used since transport conditions invariably incorporate these Rules.[68] Many countries have extended the application of their maritime laws to cases where a bill of lading is not issued.[69] The Hague and Hague-Visby Rules do not know sea waybills, but they are addressed in Article 18 of the Hamburg Rules, which may serve as a model for modern sea transport legislation in other respects than its liability regime. This Article does not mention the sea waybill expressly, but addresses "a transport document other than bill of lading".

The sea waybill is a non-negotiable document that constitutes evidence of the contract of carriage and of the receipt of the goods by the carrier. The condition of the goods as received is also evidenced by the document. This evidence, however, does not become conclusive, not even as against a *bona fide* consignee.[70] Article 18 of the Hamburg Rules (which are thought to reflect the contemporary concept of sea waybills, although the relevant Convention is not in force), states namely that "such a document is prima facie evidence of the conclusion of the contract of carriage by sea and the taking over by the carrier of the goods as therein described". The sea waybill also contains the name of the consignee to whom the carrier undertakes to deliver the goods. The sea waybill is not a document of title and it cannot be used to transfer property rights in the goods. The sea waybill need not be presented for taking delivery of the goods; the carrier tenders delivery to the named consignee, who needs only to prove his identity.

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67 UN/CEFACT Recommendation No. 12 second edition, Geneva October 2001, ECE/TRADE/240, p. 12.

68 In carriages between Nordic countries, the issue of a bill of lading has not been a precondition for the application of the Rules.

CMI (Comité Maritime International) adopted in 1990 'Uniform Rules for Sea Waybills', see *infra*.

69 For instance Finland, Norway, Sweden Denmark, France and the United Kingdom.

70 This is provided expressly, for instance, in the UK Carriage of Goods by Sea Act 1992, Section 2(5), and in the Finnish Maritime Code, Chapter 13 Section 59.

As said, the advantages of the waybill relate to time. If the bill of lading is used, goods frequently arrive at a destination before the bill of lading, and the goods have to be released by the carrier against security. With a waybill, the transport industry may find it easier to avoid liability for delivery to an unauthorised person. Moreover, waybills are not issued in duplicates, which fact makes document handling easier. If, however, the buyer wants to sell the goods further whilst they are in transit, or he needs a document of title for security, a replacement is not possible. For the seller, a waybill may be a disadvantage since the seller loses a useful instrument against which payment can be demanded.

The use of the waybill has facilitated the use of its electronic alternatives. A D*ata Freight Receipt* of the *Atlantic Container Line*[71] was a pioneer project to replace paper-based transport documentation. Once the consignor has agreed to the loading information, an electronic representation of a waybill, which is called DataLading, passes through ACL´s computer system from the loading port to the discharge port. The consignor receives a receipt, which is not a waybill *per se*.[72] Similarly, the consignee receives a notice of arrival on paper.

In order to meet the seller´s concerns of maintaining some control of the goods until they are paid and in order to make it possible to use the ´Data Freight Receipt´ in documentary credits and documentary collections, professor Kurt *Grönfors* introduced the *Cargo Key Receipt*, which is still a waybill, but which contains a ´NODISP clause´.[73] With this clause, the bill can be drawn up in the name of the financing bank acting as consignee, and this named party retains the power to dispose of the goods in favour of one other person. This person could be the actual buyer, if this buyer pays for the goods. Should he not pay, the goods may be disposed of otherwise.

A special type of document issued by an individual shipping line represents a competitive edge for the operator and does not extend to other parties of the operation of a multimodal carriage, such as a road haulier, unless special arrangements are made.[74]

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71 An affiliate of Compagnie Générale Maritime, Cunard Steam-Ship Company Ltd., Intercontinental Transport (I.C.T.) B.V. Swedish American Line and Wallenius Line. A data freight receipt was also used by *Intercargo*.

72 However, such a receipt is a transport document other than a bill of lading envisaged in Article 18 of the Hamburg Rules, constituting a *prima facie* evidence of the conclusion of the contract of carriage by sea and taking over by the carrier of the goods described therein.

73 The clause is added to the carrier´s ´SECURITY´ declaration which means that he holds the consignment as specified in the receipt in security and as collateral for the bank named as consignee.

74 Grönfors, 1991, pp.75-76; Alan Urbach, Electronic Presentation and Transfer of Shipping Documents in Goode (ed.) Electronic Banking – the Legal Implications, pp. 114-115. For the Cargo Key Receipt, see also Grönfors, Cargo Key Receipt and Transport Document Replacement, Gothenburg, 1982.

Should the bank not desire to be named as the consignee, the actual consignee could be inserted in the waybill, and the bank would gain a lien on the goods through a clause such as: "Delivery of the Goods represented by this waybill can only be made against written authority to do so from the X bank who has lien on these goods" (Grönfors, 1991, p. 76).

VI.1.3.4 Some other transferable documents

A *ship´s delivery order* is a direction to the carrier to deliver to the holder of the document the amount of cargo mentioned in it. [75] Delivery orders are often used in situations where parts of bulk consignments are sold or resold whilst the goods are in transit, but where the use of bills of lading is not possible.[76] The English Carriage of Goods by Sea Act of 1992 defines the ship´s delivery order to be "any document which is neither a bill of lading nor a sea waybill but contains an undertaking which is given under or for the purposes of a contract for the carriage by sea of the goods to which the document relates, or of goods which include those goods; and is an undertaking by the carrier to a person identified in the document to deliver the goods to which the document relates to that person".[77] Despite this wording, delivery orders are transferable, since the goods are to be delivered to the holder or to the order of a named person.[78]

Sometimes transferability functions are added to arrival notices which are sent to the consignee to allow him to put an agent in his place or to warehouse receipts.[79] Depending on the case, the carriage and the period of carrier´s liability may already have ended.

VI.1.3.5 The form of the bill of lading and the waybill

The relevant provisions in the Hague-Visby Rules do not expressly state that the bill of lading for the carriage of goods by sea must be written on paper or manually signed. The same goes for the Hamburg Rules. However, both Rules, when imposing on the carrier the duty to ´issue´ a bill of lading upon the demand of the shipper, refer to the concept of ´document of title´.[80] As this concept is not defined in the Rules themselves, it has to be apparently defined in accordance with the law of the country where the bill is issued. On the other hand, Article 1(8) of the Hamburg Rules, which spells out the definitions of the Rules, expressly states that "writing includes, inter alia, telegram and telex". Taking into account that the Hamburg Rules were agreed upon in the 1970s, such non-exhaustive wording could easily be interpreted as including electronic records that are able to be authenticated. However, the Bolero Feasibility Study notes that "although the Hamburg Rules make provision for electronic signatures on bills of lading, this is subject to whether an electronic document can constitute a bill of lading at all by national law".[81]

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75 Todd 1998, p. 137.

76 Ibid.

77 Section 1(5) of the Act. Delivery orders may also be issued by a merchant, who addresses them to a shipowner requiring him to deliver to the order of a named person, in which case the carrier attorns it to this person.

For the concept of *attornment* under English law, see Chapter V.4.1., *ante*.

78 Law Commission No 196: Rights of Suit in Respect of Carriage of Goods by Sea, London, 1991, para. 5.26, Todd 1998, p. 138.

79 A *FIATA Warehouse Receipt (FWR)* gives a right to claim the goods that a freight forwarder has taken into his custody for storage. The right may be transferred by an indorsement on the reverse side of the document (Ramberg 1993, p. 183).

80 Article III (7) of the Hague-Visby Rules and Article 15(2) of the Hamburg Rules.

81 Bolero Feasibility Study 1999, p. 44.

As the national laws may differ in this respect, electronic bill of lading schemes such as the CMI Rules for Electronic Bills of Lading (Rule 11) provide that parties may waive any requirements based on national law requiring a bill of lading to be in writing. As will be mentioned later, all jurisdictions may not, however, admit such waivers.[82]

The Hague-Visby Rules and the Hamburg Rules both provide that a bill of lading has to be signed by the carrier or his representative. Article 14(3) of the Hamburg Rules states 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".[83] This possibility corresponds to the ´International Standard Banking Practice for the examination of documents under documentary credits´ relating to the Uniform Customs and Practice for Documentary Credits UCP500.[84] In some national laws, additional requirements may be imposed.[85]

As regards sea waybills, few provisions on them are found in international conventions, but some national laws contain minor formal requirements. These relate mainly to the information (data) content of the document. For instance, Chapter 13 Section 59 of the Finnish Maritime Code stipulates that a sea waybill shall contain particulars of the goods received for carriage, the contracting shipper, the consignee and the carrier, the conditions of carriage and the freight and other costs to be paid by the consignee. The carrier has a duty to inspect the particulars and to make reservations as in the case of the bill of lading. Finally, a sea waybill shall be signed by the carrier or any person acting on his behalf. The signature may be made by mechanical or electronic means. Contrary to what is provided for in the case of bills of lading, there is no obligation to furnish a sea waybill. Therefore, when the shipper abstains from requiring a bill of lading, this gives the carrier an opportunity to issue a sea waybill or to go electronic completely.[86]

UCP500 contains form requirements for sea waybills similar to ocean bills of lading. There are trade facilitation models for the appearance of sea waybills and bills of lading following the UN Layout Key.

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82 See Chapter VIII.4.2.2. *post*.

83 Under English law, which applies the Hague-Visby Rules, there is now a possibility introduced by the Carriage of Goods by Sea Act of 1992 (repealing the 1855 Bills of Lading Act) that the Secretary of State may by regulations make provision for the application of the Act to cases where a telecommunications system or any other information technology is used for effecting transactions corresponding to

(a) the issue of a document to which the Act applies,

(b) the indorsement, delivery or other transfer of such a document, or

(c) the doing of anything else in relation to such a document.

84 ISBP Points 39-42., ICC Publication No. 645.

85 French law has abolished the duty of the shipper to sign the bill in order to verify that he has seen the transport conditions. Yet, the jurisprudence may follow that old rule. See Chapter VIII, *post*.

86 There appears to be a practice in a large number of cases not to require the issue of any transport documents. This type of ´dematerialisation´ may not be well received by P&I clubs for evidentiary reasons.

VI.1.3.6 The Clause Paramount and the Himalaya Clause

Sea transport conventions transposed into national law mandatorily apply to carriages starting from the the country where a bill of lading is issued, and in many countries such as the Nordic countries and France they apply to all carriages except those where a charterparty is used. All other carriages, whether a bill of lading or a sea waybill is issued, are invariably evidenced by a transport document incorporating the Hague Visby Rules[87] in the contract of carriage by a Clause Paramount. Reference is made to the law which implemented the international agreements concerning the said Rules expressly or abstractly. Another possibility is that the transport document incorporates the said international agreements directly without incorporating any national law as such.

The said rules apply, in most cases, mandatorily anyhow. Furthermore, their role is to protect the weaker party, who is the shipper or the consignee. Therefore the incorporation technique for the Hague or Hague-Visby Rules is usually not an issue. On the contrary, where exoneration or exception clauses are inserted into the contract of carriage, attention is often paid to the form of its presentation, and incorporation by reference meets even more thorough scrutiny.

A Himalaya Clause is designed to extend the protection of the contractual carrier´s exemptions to the actual carrier as well as to independent stevedores and similar parties who are not parties to the contract of carriage and cannot thus benefit from exemption clauses. At times, a Himalaya Clause commits the shipper to not suing the unprotected party. Under English law, a Himalaya clause may invoke form requirements, since the clause may create a trust of the benefit of the clause or may be a third party beneficiary contract.[88] In the latter type of situation, an attempt to dispose of the beneficial interests in the contract of carriage attracts the requirement[89] of written form.[90]

VI.1.3.7 Transport documents in land and air transport[91]

The CMR provides that the contract of carriage by road shall be confirmed by a *consignment note*. The consignment note has to be made out in three original copies signed by the sender and the carrier. The first copy (´duplicate´) is handed to the sender, the second accompanies the goods, and the third is retained by the carrier. The consignment note is not a negotiable instrument nor a document of

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87 The same goes for the original Hague Rules or the Hamburg Rules.

88 See Article 5.2.3. of the UNIDROIT Principles of International Commercial Contracts 2004.

89 Section 53(1)(c) of the English Law of Property Act 1925.

90 The Bolero Feasibility Study 1999, p. 48.

91 Questions relating to transport in inland waterways are not treated here. One can simply note the existence of the Budapest Convention on the Contracts for the Carriage of Goods by Inland Waterways, 2000 (abbreviated the CMNI). Transport documents issued by freight forwarders were mentioned in the context of bills of lading, *supra*.

title. However, it is prima facie evidence of the making of the contract of carriage, the conditions of the contract and the receipt of the goods by the carrier.[92] The provisions of the Convention are not tied to the issue of a consignment note. Article 4 of the CMR Convention states namely that

> *"The contract shall be confirmed by the making out of a consignment note. The absence, irregularity or loss of the consignment note shall not affect the existence or the validity of the contract of carriage which shall remain subject to the provisions of this Convention."*

Moreover, the consignment note functions as a record of the carrier´s reservations. The carrier has to make his reservations on the note when he has not been able to check the goods. Otherwise, there will be a presumption that he has been able to check the goods. Such reservations will not, however, bind the sender unless he has expressly agreed to be bound by them.[93] In any case, the absence of such reservations creates a presumption that the goods and their description appear to be in good condition when the carrier took over them, and the number of packages, their marks and numbers corresponded with the statement on the consignment note.[94] The question arises of whether a legal presumption can be held against the carrier if the consignment note is not issued. In some countries, courts interpret this provision against the carrier.[95]

In railway carriage between the signatory countries of the CIM Convention, an international CIM *through consignment note* is issued to the consignor. There is a special form to be used and the waybill consists of two parts. One of them follows the goods, usually only in the sense that it is sent by the railway administration to the station of destination and is handed over to the recipient. The other is given to the consignor. A rail waybill is not a document of title. Article 1 of the CIM Convention provides that the rules apply to consignments under such a consignment note. One view of this matter holds that where a through consignment note is not issued, the Convention does not apply.[96]

In air carriage governed by the original Warsaw Convention, the document of carriage is called the *air consignment note*. It is not a document of title. The carrier has the right to require the consignor to draw up an air consignment note and to require a separate one for each package. Each air consignment note must be in three original parts and must be handed over with the goods.[97]

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92 Article 9(1).

93 Article 8(2) of the CMR Convention.

94 Article 9(2) of the CMR Convention.

95 According to the Bolero Feasibility Study 1999 (p. 46), this seems to be the case in France and Germany.

96 Bolero Feasibility Study 1999, p. 47 (for England), UNCITRAL doc A/CN.9/WG.III/WP.29. The 1999 version of the COTIF-CIM instead provides in Article 6.2 similarly to CMR Article 4 that the absence, irregularity, or loss of the consignment note does not affect the existence or validity of the contract, which would remain subject to the COTIF-CIM.

97 The first part is marked "for the carrier" and signed by the consignor; the second part is marked "for the consignee" and is signed by the consignor and accompanies the goods; the third part is signed by the carrier and handed to the consignor after the goods have been accepted for carriage. Furthermore, the consignor must furnish the consignee with the additional information and information necessary for customs and police purposes. Schmitthoff, Export Trade, p. 330.

In air carriage that is governed by the amended Warsaw Convention, the document of carriage is called an *air waybill*. The provisions of the original Convention relating to the air consignment note apply to the air waybill under the amended Convention. The particulars to appear therein are however somewhat different. It is stated expressly in the amended Convention that nothing therein prevents the issue of a negotiable air waybill. Additionally, an air consignment note can be negotiable.

Montreal Protocol No. 4 amends Article 5 of the Warsaw Convention with the effect that an air carrier can substitute an electronic message for an air waybill without losing the benefit of the limitations of liability in the Convention. The consignor must give his consent to this substitution. Even in this case, the air carrier must give a signed receipt for the cargo, unless the consignor waives his rights.[98] The Montreal Protocol was signed during the early days of EDI in the 1970s.

The Montreal Convention of 1999 that consolidated and modernised previous instruments provides in a similar manner that "any other means which preserves a record of the carriage to be performed may 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 cargo receipt permitting identification of the consignment and access to the information contained in the record preserved by such other means".

Further to the above convention-based transport documents, there exists a common form of air waybill used by members of the International Air Transport Association (IATA) for interline and online carriage, and also by non-members who either participate in interline carriage involving IATA members or wish to adopt the international standards set by IATA members. The format of this waybill is designed to facilitate the production of a air waybill copy which can easily be transmitted by electronic means. The IATA waybill follows the mandatory provisions of the relevant convention, but has legally independent provisions concerning non-convention carriage.

Whilst the possession of a bill of lading after due indorsements entitles its holder to receive the goods from the carrier, the possession of a waybill does not have such effects but the carrier has to hand over the goods to the consignee mentioned in the waybill. Neither does the information taken in the waybill constitute a similar ground for liability to the consignee as the information taken in a bill of lading does. A waybill merely constitutes evidence of a transport contract and of the receipt of the goods by the carrier.[99]

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98 It is unclear whether the consent could be implied or whether it should be given in writing, e.g. in an interchange agreement. It seems to be the tendency of the air freight industry to require a signed document showing receipt of the goods. See Peter Jones, The US ratifies Montreal Protocol No. 4 in Forwarders Legal Guide, release 23 October 1998, http://www.forwarderlaw.com/feature/fiatfe23.htm, visited on 10.7.1998.

99 Grönfors 1991, pp. 58-59. At the national level, there can be provisions on the negotiability of other documents than maritime bills of lading. In Germany, a carrier can issue a negotiable loading note (Ladeschein) in all modes of transport (§ 363 II HGB). The loading note can apply to a combined transport as well (Herber NJW 1998, p. 300).

VI.1.3.8 Right of control

When a bill of lading has been issued, the right to control[100] the goods during the transport belongs to the party who has all originals (the´full set´) of the bill of lading. This right of control is relevant for the parties to a transaction, a further buyer or a bank financing any of the transactions. In addition to providing the right of control, the bill of lading has proprietary effects as described in Chapter V, *ante*.

In land and air transport, however, the consignor is entitled to control the goods if he can present the consignor´s copy (or, in rail transport, the ´duplicate´) of the consignment note.[101] Therefore, as long as the goods have not arrived at their intended final place of destination, a change of the ´actual consignee´ can be made by delivering the duplicate to the new purchaser of the goods combined with a written notice to the carrier who is to deliver the goods in transit to a new person.[102]

For the buyer, or a subsequent buyer, acquiring the possession of the consignor copy of the consignment note protects him against the seller (as the consignor), who can no longer control the goods, irrespective of whether it would be otherwise justifiable to do so or not. Moreover in this case, the carrier becomes liable to the correct consignee if he fails to require the presentation of the consignor copy when goods are being controlled by him during the transit.

The CMR Convention builds on the assumption that a consignment note is issued. It would, indeed, be strange if a legal framework were built on the possibility that its provisions are not observed outside pure sanctions. Electronic trading systems replicating the functions of electronic transport documents attempt to dispense with the requirements of written transport documents. If there are too many legal functions tied to the possession of a piece of paper, users are left with uncertainty when that piece of paper is not used. It is thus impossible to say up to what point the sender is able to use his right of control in cases where a consignment note is not used in international land transport.[103]

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100 A good description of the right of control of the goods is contained in Article 53 of the ´Draft instrument on the Carriage of Goods [by Sea] under preparation within the UNCITRAL Working Group on Transport Law (annexed to Note by the Secretariat, A/CN.9/WG.III/WP.32, pp. 5-68; for the Draft Instrument, see *infra*)

According to that draft provision, the right of control of the goods means the right under the contract of carriage to give the carrier instructions in respect of these goods during the period of its responsibility. Such right to give the carrier instructions comprises rights to:

(a) give or modify instructions in respect of the goods that do not constitute a variation of the contract of carriage,

(b) demand delivery of the goods before their arrival at the place of destination,

(c) replace the consignee by any other person including the controlling party, and

(d) agree with the carrier to a variation of the contract of carriage.

101 The same goes for the Forwarder´s Certificate of Receipt (FCR), the possession of which entitles the holder to give instructions to the carrier (Ramberg 1993, p. 183).

102 Grönfors, 1991, p. 28. According to Grönfors, it is also possible to exercise the right of control at the place of destination as long as the consignee remains passive.

103 See the analysis in the Bolero Feasibility Study 1999, p. 46.

The right to control the goods is also relevant as a ´security´ for a bank financing the sales transaction. Many banks accept duplicates of land and air waybills as security during the transport, usually provided that banks are named as consignees. Using their right of control, they ultimately give the carrier instructions for the ultimate consignee. The right of control remains with the shipper until he waives the right or when goods have arrived at their destination. The right of control may not be transferred as such; however, the right to stand as consignee or to name somebody else as consignee serves the same function.

The use of a sea waybill is not yet based on any convention that is applied widely. A notable effort to regulate the use of sea waybills was the adoption and promulgation of the CMI Uniform Rules for Sea Waybills.[104] It is therefore not clear to what extent the shipper´s right of control exists when the waybill is issued. In most jurisdictions the exercise of the right of control seems to be possible and in France the right even belongs to parties other than the shipper.[105] Thus, subject to the provisions of the applicable law, the shipper is entitled to change the name of the consignee at any time up to the moment that the consignee claims delivery of the goods after their arrival at the destination.[106]

Another question is whether, where statutory provisions are absent, the possession of a shipper copy is a prerequisite for the exercise of the right of control. It would be unfounded to limit the shipper´s contractual rights in the absence of statutory provisions.[107] The matter of the right of control was decided not be be dealt with in the Hamburg Rules.[108] However, the revision of the Nordic Maritime Codes in the middle of the 1990s addressed this problem. The right of control is given to the shipper, unless he has waived this right (e.g. by a NODISP Clause), until the consignee has used his right to obtain the goods. The right of control is not tied to the possession of any copy of the waybill.[109] As the right to control the goods is relevant to banks, the exercise has also been

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104 UN doc TRADE/WP.4/INF.116, TD/B/FAL/INF.116, 9.7.1991.

105 UN/CEFACT Recommendation No. 12: ´Measures to facilitate maritime transport documents procedures´, (second edition, Geneva October 2001, ECE/TRADE/240), 26, p. 5). The Bolero Feasibility Study 1999, p. 40. In France, a cumbersome procedure (huissier) may and shall be used to transfer the right to control the goods during transit (Article 1690 of the Code Civil; see Rodière, Droit Maritime 11e édition, 1991).

106 UN/CEFACT Recommendation No. 12, p. 5.

107 Under US law, a non-negotiable bill of lading has functions in respect of transfers of the right of control and the use of the right of stoppage in transit (Chandler, III in Transfer of Ownership, p. 423).

108 Grönfors 1991, p. 54.

109 See for instance Chapter 13, Article 58(2) of the 1994 Maritime Code of Finland and HE 62/1994, p. 56. The relevant provision may also be interpreted so that it suffices that the consignee uses any rights belonging to him. Articles 44 and 56 of Chapter 13 of the the Code in effect entitle the shipper to obtain a bill of lading at a later stage, until the consignee claims the goods at the place of destination.

In the absence of ties connected with a duplicate or a consignor copy, should the shipper wish to transfer the right of control to a new party, this has to be done by contractual clauses (Grönfors 1991, p. 55).

organised contractually without a duplicate of the waybill (see the Cargo Key Receipt, *supra*).[110] Another way to solve the matter contractually is to incorporate the CMI Rules for Sea Waybills into the transport conditions.[111]

VI.2 Electronic transport documents

The legality of electronic transport documents is obviously vital for an electronic documentary credit system to succeed since the documents presented under a credit almost without exception have legal functions, which are important to the parties of a documentary credit transaction. As has been previously stated, the delivery of the transport document amounts to a ´constructive delivery´ under the contract of sale, and the document has functions in relation of title, possession or control of the goods, and, as such, is valuable for the bank as security. In addition to functions relating to the execution of the contract of sale, transport documents have the role of evidencing the contract of transport and being evidence of the quantity and condition of the goods, amongst other things.

Few legislative projects, intentions or reservations have been involved in creating electronic transport documents. The most important is obviously that carried out under the auspices of UNCITRAL Working Party III (Transport Law), see *infra*. As negotiability is a characteristic typical to other commercial documents such as bills of exchange, the provisions of the US UETA regarding transferable electronic records are also of interest. In parallel with certain public interest arising in this matter, the private sector and professional organisations have created their own initiatives.

Historically, it would be logical to start with private sector initiatives as some of these certainly preceded the acts of legislators just as interchange agreements and EDI preceded electronic commerce legislation. However, the use of electronic transport documentation based on private initiatives did not start on a scale comparable to the use of EDI. Moreover, parts of the discussion of electronic transport document systems are placed in Chapter VIII.7., *post*, since the systems are used for other types of documents as well. Therefore, the order I have chosen is to put legislative attempts first and private initiatives thereafter.

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110 Grönfors 1991, p. 56.

111 These Rules provide in Article 6 (Right of Control) that the shipper can irrevocably renounce such right and transfer the right of control to the consignee by a notation on the sea waybill at the time of issue. One such notation reads:

"Upon acceptance of this waybill by a bank against a letter of credit transaction (which acceptance the bank confirms to the carrier) the shipper irrevocably renounces any right to vary the identity of the consignee of the goods during the transit".

The CMI Rules for Sea Waybills generally consider the arrival at the port of destination to be the point of the transfer of the right of control.

VI.3 Legislative approaches to electronic transport documents

Electronic transport documents have not been an object of comprehensive legislative efforts yet. The situation may, however, change when international instruments are drafted to address the issue. Creating detailed legislation requires, in turn, practical experience of the problems. Experience will have to be gained through pilot projects operating on a contractual basis in areas which have been governed by legislation for the last century.

VI.3.1 UNCITRAL Model Law on Electronic Commerce (Part II)

As already noted, the UNCITRAL Model Law on Electronic Commerce of 1996 contains two parts. Part I, which has already been presented in detail, deals with electronic commerce in general. Part II deals with electronic commerce in specific areas and covers for the moment only carriage of goods. It may, however, be amended in the course of developments in other specific areas. Therefore, the provisions on the carriage of goods appear as Chapter I of Part II of the Model Law. Part II is, however, intended to contain only sector-specific provisions, whereas the general rules of electronic commerce such as Article 6 (writing), Article 7 (signature) and Article 8 (original) apply to transport documents equally.

Chapter I of Part II is made up of two Articles: Article 16 lists some actions[112] "in connection with, or in pursuance of, a contract of carriage of goods", which

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[112] These actions include, but are not limited to

(a)

(i) furnishing the marks, number, quantity or weight of goods;

(ii) stating or declaring the nature or value of goods;

(iii) issuing a receipt for goods;

(iv) conforming that goods have been loaded;

(b)

(i) notifying a person of the terms and conditions of the contract;

(ii) giving instructions to a carrier;

(c)

(i) claiming delivery of goods;

(ii) authorising release of goods;

(iii) giving notice of loss of, or damage to, goods;

*(d)*giving any other notice or statement in connection with the performance of the contract;

*(e)*undertaking to deliver goods to a named person or a person authorised to claim delivery;

*(f)*granting, acquiring, renouncing, surrendering, transferring or negotiating rights in goods; and

(g) acquiring or transferring rights and obligations under the contract.

are covered by Chapter I of Part II of the Model Law. Article 17 generally applies the functional equivalence approach to transport documents.

Article 17(1) provides that where the law requires that any action referred to in Article 16 be carried out in writing or by using a paper document, that requirement is met if the action is carried out by using one or more data messages. This applies whether the requirement of written form or the use of a paper document is in the form of an obligation or whether the law simply provides consequences for failing to carry out the action in writing or failing to use a paper document.

These provisions establish functional equivalents, not only of written information about the actions referred to in Article 16, but also of the performance of such actions through the use of paper documents. The transfer of rights and obligations through the transfer of written documents, in particular, needs a functional equivalent in the electronic world. Where there is a requirement for a written contract of carriage or requirements for indorsement and transfer of possession of a bill of lading, these will be replaced by equivalent data messages and their use in an appropriate manner.[113]

There is, however, a specific rule in paragraph 3 of the same Article relating to the use of documents of title. Paragraph 3 provides in a rather abstract and complicated manner that "if a right is to be granted to, or an obligation is to be acquired by, one person and no other person[114], and if the law requires that, in order to effect this, the right or obligation must be conveyed to that person by the transfer, or use of, a paper document, that requirement is met if the right or obligation is conveyed by using one or more data messages, provided that a reliable method is used to render such data message or messages unique[115]". Paragraph 4 clarifies that for the purposes of paragraph 3, the standard of reliability required shall be assessed in the light of the purpose for which the right or obligation was conveyed and in the light of all the circumstances, including any relevant agreement.

Paragraphs 3 and 4 are intended to ensure that a right can be conveyed to one person only, and that it would not be possible for more than one person at any point in time to lay claim to it. This requirement is called in the Guide to Enactment the ´guarantee of singularity´. This guarantee has to be an integral element of procedures whereby rights or obligations are conveyed by electronic

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113 The Guide to Enactment of the Model Law states on page 50 that "it was felt in the preparation of the Model Law that the focus of the provision on the actions referred to in Article 16 should be expressed clearly, particularly in view of the difficulties that might exist in certain countries for recognizing the transmission of a data message as functionally equivalent to the physical transfer of goods, or to the transfer of a document of title representing the goods".

114 The Guide to Enactment stresses on page 50 that "one person and no other person should not be interpreted as excluding situations where more than one person might jointly hold title to the goods. For example, the reference to ´one person´ is not intended to exclude joint ownership of rights in the goods or other rights embodied in a bill of lading."

115 The word ´unique´ is used in the sense that a message purporting to convey any person´s right or obligation should not be used by, or on behalf of, that person inconsistently with any other data message by which the right or obligation was conveyed by or on behalf of that person.

methods instead of using paper documents. This guarantee would consist of technical security devices built in a communication system used by the trading community.[116]

The ´guarantee of singularity´ is further complemented by paragraph 5 which states

> "Where one or more data messages are used to effect any action in subparagraphs (f) and (g) of Article 16, no paper document used to effect any such action is valid unless the use of data messages has been terminated and replaced by the use of paper documents. A paper document issued in these circumstances shall contain a statement of such termination. The replacement of data messages by paper documents shall not affect the rights or obligations of the parties involved."

Just as it is important to ensure that the same data message is not used twice, it is equally important to secure that no two media can simultaneously be used for the same purpose. No system based on electronic equivalents of bills of lading can work if the same rights could at any given time be embodied both in data messages and in a paper document.

Paragraph 5 also envisages a situation in which a party having initially agreed to engage in electronic communications has to switch to paper communications where it later becomes unable to sustain electronic communications. The Model Law is silent on how the termination should be carried out. The Guide to Enactment suggests, however, that enacting states might wish to indicate, for example, that, since electronic commerce is usually based on an agreement between the parties, a decision to ´drop down´ to paper communications should also be subject to the agreement of all interested parties. Otherwise, the originator would be given the power to choose the means of communication unilaterally.

An alternative suggestion put forward by the Guide to Enactment to the enacting states is that since paragraph 5 would have to be applied by the bearer of a bill of lading, it should be up to the bearer to decide whether it preferred to exercise its rights on the basis of a paper bill of lading or on the basis of an electronic equivalent of such a document and to bear the costs for his decision. This approach has been applied in Rule 3.7 (Switch to Paper) of the Bolero Rulebook and in Section 2.10 of the TEDI Interchange Agreement.[117]

Transport documents in the form of electronic records, the possession of which is recorded in a registry, cannot become functionally fully similar to their counterparts on paper, since information in the registry is not tangible as a negotiable paper instrument is. Since electronic records exist only in singular form, no rules are needed for collisions between the rights of holders of individual copies of bills of lading. In the paper-based world, there is a statutory guarantee of singularity, although bills of lading are issued in multiple

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116 For the practical applications of this in the *Bolero System*, see Chapter VIII.7.1.4, *post*. See also Section 2.10. of the TEDI Interchange Agreement, available with annotation at http://www.tediclub.com/english/pdf/IA-English_Ano.pdf, visited on 18.7.2004.

117 See Chapters VIII.7.1.4 and VIII.7.4., *post*.

originals.[118] The Nordic Maritime Codes[119] contain prerogatives for the carrier confronting multiple claims based on individul originals. In addition, contract practice tries to resolve the problem of singularity for paper bills of lading.[120] Neither does one need rules for documents lost when electronic registries are used. Systems may, however, break down, which would create complications unless adequate technical precautions are used.

VI.3.2 A new instrument for transport law

At its twenty-ninth session in 1996, the United Nations Commission on International Trade Law considered a proposal to include in its work programme a review of current practices and laws in the area of the international carriage of goods by sea, with a view to establishing the need for uniform rules where no such rules existed and with a view to achieving greater uniformity of laws.[121]

It was noted that the growing use of electronic means of communication in the carriage of goods aggravates the consequences of the application of "fragmentary and disparate" laws on the carriage of goods by sea constituting an obstacle to the free flow of goods and increasing the cost of transactions. The Secretariat was finally given the task to solicit views from governments and relevant international organisations. This approach already met, however, some opposition at the starting point.[122]

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118 It is usually a commercial practice to issue multiple originals. However, in France, the law requires at least two originals, and the import authorities of some countries may have their own requirements.

119 E.g. section 53 of Chapter 13 of the Finnish Maritime Code.

120 Article 23 (iv.) of the Uniform Customs and Practice for Documentary Credits UCP500 (see Chapter VII., *post*) requires that if the bill has been issued in more than one original, a full set of originals as so issued must be presented to the bank.

Furthermore, in relations with the carrier, bills of lading contain texts rendering the remaining originals void if one original is surrendered. Such text could be formulated as follows:

"One original Bill of Lading must be surrendered duly indorsed in exchange for the goods or delivery order. IN WITNESS whereof the master of the said Vessel has signed the number of original Bills of Lading stated below, all of this tenor and date, one of which being accomplished, the others to stand void". (Ramberg 1991, p. 360, note 5).

121 Official Records of the General Assembly, Fifty-first Session, Supplement No. 17(A/51/17), para. 210 and Note by the Secretariat, A/CN.9/WG.III/WP.21.

122 It was said that the continued coexistence of different treaties governing the liability in the carriage of goods by sea and the slow process of adherence to the 1978 Hamburg Rules made it unlikely that adding a new treaty to the existing ones would lead to greater harmony of laws. As the Note by the Secretariat, A/CN.9/WG.III/WP.21, para. 4, states, "Indeed, there was some danger that the disharmony of laws would increase". As stated earlier, there are four liability regimes applicable to carriage of goods by sea: 1. no convention, 2. the Hague Rules, 3. the Hague-Visby Rules and 4. the Hamburg Rules. If a new convention, to which everybody could not immediately avail, were added, there would be five regimes (in addition to the problems caused by multimodal transport).

VI.3.2.1 Work of CMI as the basis

The UNCITRAL Secretariat has been able to benefit from a fruitful cooperation with the Comité Maritime International (CMI). This organisation of transport lawyers is composed of 52 maritime law associations and is dedicated to the international uniformity of maritime law. CMI was instrumental in the development of electronic commerce in producing the 1990 CMI Rules on Electronic Bills of Lading (see *infra*) and by organising an important colloquium on maritime electronic commerce at its centenary anniversary in Antwerp in June 1997, the fruits of which are widely exploited in this study.

At the thirty-first session of UNCITRAL in 1998, the CMI welcomed the invitation made by the UNCITRAL Secretariat to solicit views of the sectors involved in the international carriage of goods and to prepare an analysis of that information.[123] The CMI informed that it had sent a questionnaire to its member organisations covering a large number of legal systems. The relevant CMI working group had identified numerous interfaces between the different types of contracts involved in international trade and transport of goods, such as sales contracts, contracts of carriage, insurance contracts, letters of credit, freight forwarding contracts and a number of ancillary contracts.[124] The CMI working group intended to clarify the nature and function of those interfaces and to collect and analyse the rules currently governing them. An international subcommittee would be created to analyse the data and find a basis for further work towards harmonising the law in the area of the international transport of goods.

The CMI reported that "the enthusiasm encountered so far in the industry and the provisional findings about the areas of law that needed further harmonisation made it likely that the project would be eventually transformed into a universally acceptable harmonising instrument". The CMI had had in mind that, at a later stage, its field of study would include a re-evaluation of principles of liability to determine their compatibility with a broader area of rules on the carriage of goods.[125]

VI.3.2.2 UNCITRAL Working Group on Transport Law

At the thirty-fourth session of UNCITRAL in 2001 a report requested by the UN Commission was presented by the Secretary General.[126] The report suggested that work could usefully commence towards an international instrument, possibly having the nature of an international treaty, that would modernise the law of

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123 Doc A/CN.9/WG.III/WP.21, para. 7.

124 See e.g. Intermodal Liability Statement by the Comité Maritime International, dated 14 January 1999, at http://www.bmla.org.uk/annual_report_1998/intermodal_liability.htm, visited on 22.8.2003. Cf. the notion of ´ancillary contracts´, which has been used in Chapter III, *ante*, to denote contracts other than communications contracts and primary (sales) contracts.

125 Doc A/CN.9/WG.III/WP.21, para. 8.

126 Report of the Secretary General, A/CN.9/497. See Fifty-fourth Session, Supplement No 17(A/54/17), Fifty-fifth Session, Supplement No 17 (A/56/17, paras 319-345) as referred to by the Note by the Secretariat, A/CN.9/WG.III/WP.21, paras. 19-23.

carriage, take into account the latest developments in technology including electronic commerce, and eliminate legal difficulties in the international transport of goods by sea that were identified by the Commission. The Commission further decided to establish a ´Working Group on Transport Law´ to further the project. It was expected that the Secretariat would prepare for the working group a preliminary working document containing drafts of possible solutions for a future legislative instrument, with alternatives and comments, which were under preparation under CMI.[127] The Commission decided that the working document to be presented to the working group should include issues of liability.[128]

The secretariat has since then prepared, on the basis of its mandate, a draft instrument on transport law presently entitled Instrument on the Carriage of Goods [wholly or partly][by Sea].[129] It would be beyond the needs and possibilities of this study to go into all the details of the draft Instrument. Generally speaking, the draft Instrument recognises the fact that in addition to a traditional maritime regime based on a ´port-to-port´ principle, there is a need to "go ashore" by providing for a multimodal regime based on a ´door-to-door´ principle, but how exactly this would be done is not yet certain.[130] However, some attention should be paid to the attempts to align electronic records with transport documents on paper.

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127 This would mean that the CMI actually had the incentive and some burden of the preparation. One could draw a parallel to the foundations of the UNCITRAL, which was established after the New York Convention on International Arbitration, and although its creation had been originally suggested by the International Chamber of Commerce, it saw daylight under the auspices of the United Nations. These are examples of fruitful cooperation between private ´formulating agencies´ and the public legislator.

A very recent example of this type of cooperation can be found in the Regulation of the European Parliament and of the Council on the application of international accounting standards adopted on 6 June 2002, Regulation (EC) No 2002/1606 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards adopted, OJ L 243, 11.9.2002, p. 1, whereby the Commission is given rights to adopt international accounting standards prepared by a private body International Accounting Standards Committee, IASC. Frequently, when the private sector produces the end result in international rule-making, the questions of copyright and charges arise, as private bodies finance themselves by the income accrued from the outcome of their work.

128 This means that a decision shall be taken whether to maintain nautical fault and fire under excepted perils.

129 The first version was in Doc. A /CN.9/WG.III/WP.21, on pp. 9-70 and one of the very latest documents carrying the present title is A/CN.9/WG.III/WP.36. Square brackets indicate that decisions as to the scope have not been taken yet; see also the next note.

130 This dualism has later been criticised by Canada, which considers it to be too ambitious. According to Canada, a ´land leg´ should be made an option for contracting states. (For Canada´s suggestions, see A/CN.9/WG.III/WP.23, Preliminary draft instrument of the carriage of goods [by sea], Proposal by Canada, Note by the Secretariat). Sweden suggests, generally speaking, the coordination of the liability regime of the draft Instrument with existing liability regimes on land transport (Doc A/CN.9/WG.III/WP.26). Italy, again generally, would like to do away with the network liability principle (Doc A/CN.9/WG.III/WP.25). The United States supports a door-to-door regime on a uniform liability basis as between the contracting parties, subject to a limited network exception as well as the liability limits set out in the Hague-Visby Rules. Finally, as part of an overall package, the United States also supports the retention of almost all the carrier´s exemptions now contained in Article 4(2) of the Hague and the Hague-Visby Rules (Doc A/CN.9/WG.III/WP.34, paras 5, 10 and 13). >>

VI.3.2.3 Electronic contracts of carriage

The Note by the Secretariat mentions that the draft Instrument takes into account the needs of electronic commerce which means the need to remove obstacles to electronic transactions. It purports to be applied to all contracts of carriage, including those concluded electronically. To reach this goal, the draft Instrument is said to be medium neutral as well as technology neutral. This means that it can be adapted to all types of systems, not only those based on a registry. It is drafted to suit systems operating in a closed environment (intranets) as well as those operating in an open environment (the Internet).

In the draft Instrument, negotiable and non-negotiable transport documents are consistently presented in tandem with non-negotiable and negotiable electronic records which play a similar role as their paper equivalents. However, in order to lay down and illustrate the functions of electronic records, the draft instrument contains a number of detailed provisions on their use. The draft Instrument does not operate solely on the basis of functional equivalent provisions which would put the burden on the reader to figure out what they mean in practice. This seems to be a good approach. The principal provisions dealing with electronic records and communication will be presented next.

´Electronic communication´ and ´electronic records´ have been defined in the draft Instrument.[131] Futhermore, there are definitions for a ´negotiable electronic

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<< The Secretariat has invoked (in Doc A/CN.9/WG.III/WP.29, para 28) the possibility that whilst the actual maritime transport would be covered by a convention, the ancillary land carriages could be governed by model uniform rules.

A ´contract of carriage´ within the meaning of this Instrument is a contract under which a carrier, against payment of freight, undertakes to carry goods wholly or partly by sea from one place to another.

It is also interesting to recognise the starting point of the work. In the course of the discussions in the CMI subcommittee, it had namely been noted that although bills of lading are still used, especially where negotiable documents were required, the actual sea carriage of goods actually represents a only relatively short leg of an international carriage of goods. In container trade, even a port-to-port bill of lading would involve receipt and delivery at some point not directly connected with the loading onto or discharge from the ocean vessel. Moreover, in most situations it is not possible to take delivery alongside the vessel. Furthermore, where different modes of transport are used, there are often gaps between the mandatory regimes applying to the various modes of transport involved. (A /CN.9/WG.III/WP.21, paras. 9 to 13)

131 Articles 1(n) and 1 (o), respectively (version A/CN.9/WG.III/WP.32, 26.8.2003).

1 (n): ´Electronic communication´means "communication by electronic, optical, or digital images or by similar means with the result that the information communicated is accessible so as to be usable for subsequent reference". Communication includes generation, storing, sending, and receiving.

1.(o): ´Electronic record´ means information in one or more messages issued by electronic communication pursuant to a contract of carriage by a carrier or a performing party that

(a) evidences a carrier´s or a performing party´s receipt of goods under a contract of carriage, or

(b) evidences or contains a contract of carriage, or both.

It includes information attached or otherwise linked to the electronic record contemporaneously with or subsequent to its issue by the carrier or a performing party.

An important aspect of the definition is that an electronic record is apt to include information added after the issuance of the record. This information could cover electronic signatures logically associated with an electronic record as well as an electronic indorsement which could be attached or logically associated with the electronic record.

record´ and for ´non-negotiable electronic records´.[132]

Articles 3 to 6 of the draft Instrument deal with the specifics of electronic communication. Article 3 lays down the general principle of functional equivalence between electronic and paper communication and is based on the consent between the parties to communicate electronically.[133] However, such consent is not envisaged in Chapter I of Part II of the UNCITRAL Model Law on Electronic Commerce.

As it is expected that for a certain period there is a need for a provision dealing with a switch between a paper document and its electronic equivalent and the other way around, there are provisions in Articles 4.1 and 4.2 to establish rules on this.[134]

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132 Art 1.13: ´Negotiable electronic record´ means an electronic record

(i) that indicates, by statements such as ´to order´ or ´negotiable´ or other appropriate statements recognised as having the same effect by the law governing the record, that the goods have been consigned to the order of the shipper or to the order of the consignee, and it is not explicitly stated as being ´non-negotiable´ or ´not negotiable´, and

(ii) is subject to rules of procedure as referred to in Article [6], which include adequate provisions relating to the transfer of that record to a further holder and the manner in which the holder of that record is able to demonstrate that it is such holder.

Art 1.15: "Non-negotiable electronic record means an electronic record that does not qualify as a negotiable electronic record".

133 Article 3(1) provides: "Anything that is to be in or on a transport document in pursuance of this instrument may be recorded or communicated by using electronic communication instead of by means of the transport document, provided the issuance and subsequent use of an electronic record is with the express or implied consent of the carrier and the shipper".

134 Article 4.1 provides, "If a negotiable transport document has been issued and the carrier and the holder agree to replace that document by a negotiable electronic record,

(a) the holder shall surrender the negotiable transport document, or all of them if more than one has been issued, to the carrier; and

(b) the carrier shall issue to the holder a negotiable electronic record that includes a statement that it is issued in substitution for the negotiable transport document, whereupon the negotiable transport document ceases to have any effect or validity."

Accordingly, Article 4.2 provides, "If a negotiable electronic record has been issued and the carrier and the holder agree to replace that electronic record by a negotiable transport document,

(a) the carrier shall issue to the holder, in substitution for that electronic record, a negotiable transport document that includes a statement that it is issued in substitution for the negotiable electronic record; and

(b) upon such substitution, the electronic record ceases to to have any effect or validity."

The shipper may be interested in obtaining an electronic record, if he can use it in his commercial transaction (supposing also that the shipper is the seller). This requires actually the consent of the indorsee and even of the banks involved, should documentary credits be used. There are, therefore, a number of parties interested in the form of the information. In the light of the alternative approaches suggested in the Guide to Enactment of the UNCITRAL Model Law on Electronic Commerce, two possibilities exist as to who could decide the form of the presentation of information, and which form applies then to the later stages of the documentary process. The two approaches are namely that 1. all interested parties agree to the change of form or 2. that the bearer decides in which form he presents the ´document´. Given that the legal instruments facilitating electronic commerce generally presuppose the consent of the parties for the use of electronic records, the bearer would have to, in each case, obtain an agreement from each indorsee or party to whom the record or document is presented. ´Dropping down´ to paper would not normally cause as many problems as transforming the document into electronic media.

The Bolero System (see Chapter VIII.7.3., *post*) gives the holder the right to determine the switch to paper. Apparently slightly different rules are needed in more open trading.

Article 5 makes it clear that certain communications between the parties which are referred to elsewhere in the draft Instrument can be made electronically provided that the parties so agree.[135]

Article 6 provides that the use of a negotiable electronic record is subject to rules of procedure agreed between the carrier and the shipper or the holder. The rules of procedure shall be referred to[136] in the contract particulars and shall include adequate provisions relating to the transfer of that record to a future holder, the manner in which the holder of that record is able to demonstrate that it is such holder and the way in which confirmation is given that delivery to the consignee has been effected or that the negotiable electronic record has ceased to have any effect or validity pursuant to the relevant provisions[137] in the draft Instrument.

The approach using rules of procedure has been adopted in the Bolero System, where the Rulebook (see Chapter VIII.7.1.2, *post*) constitutes the applicable rules of procedure between all interested parties, not only between the carrier, shipper and the bearer.[138]

The use of electronic records instead of transport documents is a matter of agreement between the carrier and the shipper pursuant to Article 3. The consignor or, in the case of negotiable documents, the shipper, is entitled to receive a transport document.[139] It may be recalled that the Hague, the Hague-Visby and the Hamburg Rules give the shipper a right to obtain a bill of lading. In line with this, Article 33(b) provides that if the carrier and the shipper have agreed to the use of an electronic record, the shipper is entitled to obtain from the carrier a negotiable electronic record, unless they have agreed not to use one, or it is the custom, usage or practice in the trade not to use one. The status of negotiable transport documents (bills of lading) is therefore reduced, since a carrier could refer to a custom, e.g. in short-sea shipping, not to use negotiable transport documents.

There are requirements in Article 35 of the draft Instrument very much in conformity with existing transport laws, according to which a transport document shall be signed by the carrier or a person having authority from the carrier.[140] Correspondingly, an electronic record shall be authenticated by the electronic signature of the carrier or a person having authority from the carrier. An electronic signature within the meaning of the draft Instrument is "data in

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135 "...the use of such means is with the express or implied consent of the party by whom it is communicated and of the party to whom it is communicated. Otherwise it must be made in writing". (It should be noted that ´in writing´ includes electronic means of communication pursuant to the UNCITRAL Model Law on Electronic Commerce with the systemacy of which subsequent legislative instruments of UNCITRAL should be in syncrony).

136 Thus they need not be incorporated in full.

137 Such as Article 4(2) of the draft concerning the replacement of a negotiable electronic record by a negotiable transport document.

138 See also TEDI Interchange Agreement.

139 According to Article 33, a consignor is entitled to obtain a transport document or, if the carrier so agrees, an electronic record. However, the contracting shipper is given the right to control the entitlements (negotiable documents or electronic records).

140 See however, Chapter VIII.6.2.1., *post*.

electronic form included in, or otherwise logically associated with, the electronic record and that is used to identify the signature in relation to the electronic record and to indicate the carrier´s authorisation of the electronic record". This definition is taken from the UNCITRAL Model Law on Electronic Signatures of 2001. The definition is for electronic signatures generally, not for any advanced or sophisticated form of electronic signature, and must be read in conjunction with Article 6(3) of the Model Law which requires that the electronic signature must be appropriate for the purpose for which the data message was generated or communicated.[141]

The document of title character of a negotiable electronic record is stipulated in Article 49(a)(ii), which states that, without prejudice to the provisions of Article 10.1 of the duty of the consignee to accept delivery, the holder of a negotiable electronic record is entitled to claim delivery of the goods from the carrier after they have arrived at the place of destination, in which event the carrier shall deliver the goods at the time and location mentioned in Article 46(7)(3) to such holder if that holder demonstrates in accordance with the rules of procedure mentioned in Article 6 that he is the holder of the electronic record. Upon such delivery, the electronic record ceases to have any effect or validity.

As regards the right of control, the difference between the use of a negotiable electronic record and a case where no negotiable record is issued is regulated by Articles 53 to 58. Where no negotiable electronic record is issued, the controlling party is entitled to transfer the right of control to another person, upon which transfer the transferor loses his right of control. The transferor or the transferee shall notify the carrier of such transfer (Article 54(b)). The presumption is that the shipper has the right of control in the first place (Article 54(a)). What is essential is that the right of control is not tied to transport documentation, unless this is negotiable.

However, where a negotiable electronic record is issued, the holder is the sole controlling party and is entitled to transfer the right of control to another person by passing the negotiable electronic record in accordance with the rules of procedure[142], upon which transfer the transferor loses its right of control. In order to exercise the right of control, the holder shall, if the carrier so requires, demonstrate, again in accordance with the rules of procedure, that he is the holder. Any instructions to the carrier as referred to in Article 53 (b), (c) and (d) given by the holder upon becoming effective in accordance with Article 155 shall be stated in the electronic record.

Chapter 12 (Transfer of Rights, Articles 59 to 62) of the draft Instrument is said to represent a novel approach in relation to maritime conventions. Namely, two principal reasons were given for the inclusion of a chapter on transfer of rights. First, the provisions are there to ensure that coherence would be reached

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141 See Chapters IV.3.3., *ante*, and VIII.6., *post*.

142 Rules of procedure as referred to in Article 2.4.

throughout the Instrument in terms of the issue of the liability of the parties.[143] Second, there is a need to set out the necessary rules to accommodate the electronic communication component of the draft Instrument.[144]

The reason for the inclusion of Chapter 12, at least as far as the arguments relating to electronic commerce are concerned, was to respond to problems that had been encountered in the preparation of the UNCITRAL Model Law on Electronic Commerce specific to bills of lading, and the notion of functional equivalence. At the time when the Model Law was prepared it was concluded that the law of bills of lading was insufficiently codified in an international instrument to be able to accommodate an electronic record functionally equivalent to a paper-based bill of lading.[145] It was felt then that the development of rules regarding paper transport documents would facilitate the development and use of electronic records.[146]

Article 59 of the draft Instrument provides that if a negotiable transport document is issued, the holder is entitled to transfer the rights incorporated in such document to another person, (i) if an order document, duly indorsed either to such other person or in blank, or (ii) if a bearer document or blank indorsed document, without indorsement, or (iii) if a document made out to the order of a named party and the transfer is between the first holder and such named party, without indorsement.

The transfer of rights incorporated in an electronic record by a holder is carried out by passing the electronic record in accordance with the rules of procedure referred to in Article 6, irrespective of whether the record is made to order or is to the order of a named party (Article 59.2). As will be noted in Chapter VIII.7.1.3., *post*, the *Bolero Rulebook*, which constitutes an example of such rules of procedure, replicate the functions of the paper world and creates electronic equivalents to even ´bearer´ instruments.

Where no negotiable transport document or no negotiable electronic record is issued, the transfer of rights shall be effected in accordance with the provisions of the applicable law (Article 61). The same Article provides, however, that such transfer of rights may be effected by means of electronic communication. A transfer of the right of control cannot be completed without a notification of such transfer to the carrier by the transferor or the transferee.

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143 Article 12.2.2. provides that a holder who exercised a right under the contract of carriage also assumed any liabilities under that contract, but to the extent they were ascertainable pursuant to that contract. If no right were exercised, no liability would arise. A mere transfer of rights by a person who is not the shipper, or a shift from a paper negotiable instrument to a negotiable electronic record, or vice versa, would not be regarded as exercising any right within the meaning of the above provision.

144 Report of Working Group III (Transport Law) on the work of its eleventh session (New York, 24 March to 4 April 2003), Doc A/CN.9/526, para 128.

145 The draft Instrument refrains from using the notion of a bill of lading, however.

146 Ibid., para 129. Discouraged by the complexity of the issue, some voices at the meeting called for the deletion of Chapter 12 altogether. It was made clear, however, that this would constitute an impasse for the development of electronic transport documents.

VI.3.2.4 Conclusions

It is, of course, premature to build on an instrument, which has only started to be drafted relatively recently and which may not necessarily lead to a breakthrough. Still, the existence of the project is very important for the development of electronic commerce in maritime transport and, perhaps, for the ´door-to-door´ transport with a sea leg. The problems discussed illustrate the problems that remain in the way of the statutory regulation of electronic transport documents. The progress so far gives rise to a few observations and conclusions.

Firstly, the issues discussed cross the frontiers of the UNCITRAL Working Group structure, and, at the same time, possibly involve several contractual relationships. A negotiable transport document, or an electronic record, generally substitutes for a bill of lading used as a document of title. Therefore it has significance in transferring proprietary or security rights between the parties to a sales contract and their banks. In the UNCITRAL structure, this other function of a negotiable transport document is largely covered by Working Group IV (Electronic Commerce). The plenary session of UNCITRAL has invited Working Groups on Transport Law and Electronic Commerce to join forces in the creation of dematerialised transport documentation.[147] It would be useful if trade law and proprietary aspects were also covered in the work.[148] This would facilitate the application of a single law for sophisticated multifunctional trading platforms.

Secondly, the terminology used calls for attention. The abolition of the notions of bill of lading and waybill may be detrimental to the acceptance of the convention. Such notions are covered by national jurisprudence, which can supplement statutory provisions, unless these are very elaborate. Even the *Bolero System* attempts to create an equivalent of a bill of lading (which is named Bolero Bill of Lading). Moreover, the draft Instrument refrains from using the notion of ´document of title´, unlike the Hague-Visby Rules. The term may be theoretically improper for many Latin jurisdictions. Under English law, however, documents of title are established by custom or by statute. Custom may take a long time to establish. Therefore the term bill of lading, or an equivalent description, could be added to save the industry from some uncertainty.

Moreover, certain modern instruments dealing with security rights such as the 1994 EBRD Convention discussed in Chapter V.8., *ante*, build on the concept of document of title and give the rights represented by it priority over rights recorded in a registry, and security rights represented by documents of title do not need a separate act of perfection. Documents of title are therefore useful instruments even in a modern context. In addition to the desirable use of the term, certain minimum characteristics could be listed in a legislative text.[149]

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147 Report of Working Group III (Transport Law) on the work of its eleventh session, Doc A/CN.9/526, para 15.

148 In comparison, the CMI Rules on Electronic Bills of Lading 1990 (see *infra*) do not cover the proprietary aspect of bills of lading.

149 One could of course, in line with the rephrasing, alternatively use the concepts ´Document/electronic record (or messages) representing the goods´. Its function could be the transfer of rights, in particular through indirect possession, in the goods to the extent provided for by the applicable law and express or implied contract or custom, with legal effects also as against parties other than the issuer or holder in due course.

It may be argued that an instrument ultimately becoming a maritime or multimodal transport law convention is not the right place to solve or address problems relating to transfer of property in the goods, which is a matter for the legal regime for contracts of sale. Conversely, one could not see the point in regulating the two aspects of the same instrument in different legislative texts, the implemention of which would not necessarily coincide at the national level. As most national laws already recognise that parties may transfer property in the goods by negotiating a document of title, the creation of a functional equivalent for a paper document of title by a statutory declaration might be helpful.[150] Moreover, it may help to wipe away the ambiguity that is connected to the use of negotiable multimodal transport documents. This applies, of course, only if the convention will become a door-to-door transport convention. As regards creating legitimacy for transferable electronic transport documentation, a compulsory door-to-door regime would be very useful indeed.

The term ´negotiable´ has been used within the meaning of transferring rights and liabilities under the contract of carriage. Under current English law, at least, the term is not appropriate for bills of lading. The Working Group is considering the alternative ´transferable´.[151] Yet the the term ´negotiability´ torn out of the national legal system context is not accurate either. National law normally provides the extent to which a person can gain a better title than the predecessor. What would be, using the earlier example, the position of a *bona fide* indorsee of a stolen negotiable transport document? In the electronic world, the presumption rules relating to the attribution of data messages could constitute a limit to which the uniform rules could extend.[152] Reference to national law could be made as regards the legal effects of negotiability in other respects than those (minimum) effects that might be provided in the Instrument.

The role of the rules of procedure, in which details of the use of electronic negotiable instruments would be regulated, may need to be specified. The rules of procedure need to contain "adequate provisions relating to the transfer of that record to a future holder, the manner in which the holder of that record is able to demonstrate that it is such holder, and the way in which confirmation is given that delivery to the consignee has been effected, or the negotiable electronic record has ceased to have any effect or validity". Industry would have to create such a system. The Bolero Rulebook and other contracts constituting the Bolero legal framework, the contracts making up the TEDI contractual structure, and

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150 This is, of course, done already in Part II.1. of the UNCITRAL Model Law on Electronic Commerce, see *supra*, but that is only a model law and its transport articles have apparently not been implemented as yet. The *Bolero Rulebook* addresses the transfer of property by making the transfer of a Bolero Bill of Lading a functional equivalent of a transfer of a paper document of title in respect of the transfer of property: such property transfer may result from the application of national law or from an (also implied) agreement by the parties (see Chapter VIII.7.1.4. - 7.1.7., *post*). For questions relating to transfer of property rights, see Chapter V, *ante*, and further elaboration in Chapter VIII.10. and 11., *post*.

151 Draft Instrument on transport law; Annex to doc A/CN.9/WG.III/WP.21, para 13.

152 There is a protection for a *bona fide* addressee in some cases, see Article 13 of the UNCITRAL Model Law on Electronic Commerce, Chapter IV,4.6., *ante*.

partly also the CMI Rules for Electronic Bills of Lading already constitute examples, but others may follow.[153] It is impossible to impose very precise technical requirements for the rules of procedure, because then the rules would not be technologically neutral. However, there could be a list of elements that the rules should contain. For instance, adequate prerogatives could be provided for the liability framework, confidentiality and privacy.

I shall add some more questions without trying to answer them myself. In the *Bolero System*, the parties have given a pre-established consent to follow the rules of the system by adhering to the Rulebook. Others cannot use the system. This might not be useful if e.g. a purchaser of tangible goods is only a casual user of electronic trading platforms. Or, more importantly, there may be a number of platforms with similar functions, and a company is a member of only one of them. In this way, and I refer mainly to the descriptions of the bill of lading under English law (see *supra*), an electronic negotiable instrument created pursuant to the envisaged rules of procedure is really ´quasi-negotiable´. An interface with non-members is lacking. It would be ideal if a statutory legislative instrument could help to create systems that would be applicable against the world at large and legal and commercial terms could be defined facilitate interconnection between various platforms around the world.

Even in the present situation the exclusivity based on a contractual relationship is not absolute. Parallels could be drawn to the position of a consignee, or an indorsee of a bill of lading, under the traditional paper-based system. A quasi-contractual relationship is established.[154] In electronic bill of lading systems, the contractual framework is created partly to establish legal rights and obligations between the parties in the absence of an adequate statutory framework and partly between the system and the user, which may also have commercial reasons. If it is necessary to hold a new party bound by the contractual terms, techniques to carry this out, such as ´click-wrap´ adherence could be developed. One idea would be to define by law the status of a mere consignee who does not use the system actively. Another method would be to create contractual terms especially addressed to passive users, which would be adhered to by way of incorporation when claiming delivery.[155]

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153 See Chapters VIII.7.1. to 7.5., *post*.

154 See Ramberg 1991, p. 360, and the literature referred to therein. Under U.S. law, when the transfer of rights based on the contract of transport is made, either based on the negotiation of a negotiable bill of lading or by assignment of a non-negotiable bill of lading, the consignee becomes the third party beneficiary of the contract of carriage, taking over the remaining rights of the shipper, without taking on the shipper´s liabilities (Chandler, III in Transfer of Ownership, p. 424).

155 TEDI Interchange Agreement section 2.3 (Related Transactions) tries to tackle this problem by providing that "...each Party shall make commercially reasonable efforts to ensure that...all Third Parties to any such related transactions that it enters into with respect to any Shipment are subscribers..." and that such Party maintains in effect the Interchange Agreement and other contractual documents of the system.

VI.3.3 National law and electronic transport documents or documents of title

The Carriage of Goods by Sea Act of 1992 of the United Kingdom is a piece of modern national maritime transport legislation, in which the issue of electronic transport documentation has been given some thought. In comparison, the Nordic[156] Maritime Codes, which were revised as late as 1994, are silent about electronic transport documents as well as about undocumented carriage.[157]

The main objective of the Act was to remedy some basic problems relating to the 1855 Bills of Lading Act. In particular, the consignee´s right to sue the carrier in contract (as opposed to suing in tort) for his fault or neglect, without the previous imposition of a requirement that property in the goods should have passed to the consignee (indorsee) to entitle him to sue, was introduced. In addition, the Act includes in its scope most marine bills of lading as well as sea waybills and ship´s delivery orders whilst the 1855 Act concerned only ´shipped´ bills of lading.

Provision for electronic documentation is made in section 1(5), according to which the Secretary of State may by regulations make provision for the application of the Act to cases where a telecommunication system or any other information technology is used for effecting transactions corresponding to (a) the issue of a document to which the Act applies, (b) the indorsement, delivery or other transfer of such a document, or (c) "the doing of anything else in relation to such a document".

Section 5(1) of the 1992 Act provides that ´information technology´ includes any computer or other technology by means of which information or other matter may be recorded or communicated without being reduced to documentary form.

Todd[158] criticises these provisions for, as far as I understand, their superficiality. No guideline is given as to the type of electronic documentation that ought in principle to be covered. According to Todd, it would be sensible to allow only electronic documentation which performs a similar function to the other documentation covered by the Act. The documentation would then represent an undertaking and receipt by the carrier, and this undertaking could be transferred to further holders without the carrier necessarily being further involved.

Furthermore, Todd thinks that the provisions in Section 1(5) (a) and (b) seem to assume the transmission of a single computer-generated document from trader to trader. However, the practice seems to be the use of a central registry, or

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156 ´Nordic countries´ usually refers to Finland, Sweden, Norway, Denmark and Iceland, but here reference is made to Finland, Sweden, Norway and Denmark.

157 A Finnish commentary on the Code published in 1997 notes, "This is surprising from the point of view that electronic information has been in use for a great number of years and it is a relevant commercial method in transport logistics in the Nordic countries" (Hannu *Honka* in Honka, p. 115).

158 Todd 1998, pp. 247-248.

involving the carrier at each stage of the transaction, which is presupposed with the use of the CMI Rules for Electronic Bills of Lading.[159]

The US Uniform Electronic Transactions Act of 1999 introduced a new concept of ´transferable record´. That concept covers electronic equivalents of both promissory notes and documents of title.[160] Transferable records within the meaning of the UETA are based on Section 16 establishing the criteria for the legal equivalence of electronic records to notes (Article 3) or records (Article 7) under the Uniform Commercial Code. The essential criterion for such equivalence is that the electronic record can be seen to grant control over the record. This ´control´ serves as the substitute for the delivery, indorsement and possession of an analogous paper instrument. Section 16(b) allows for control to be found so long as "a system employed for evidencing the transfer of interests in the transferable record reliably establishes [the person claiming control] as the person to whom the transferable record was issued or transferred". It is essential that the system be shown to reliably establish the identity of the person entitled to payment.[161]

According to Section 16(c), a system satisfies Section 16(b) requirements, and a person is deemed to have control of a transferable record, if such record is created, stored and assigned in such a manner that

> "(1) a single authoritative copy of the transferable record exists which is unique, identifiable, and except as otherwise provided in paragraphs (4), (5) and (6), unalterable;
>
> (2) the authoritative copy identifies the person asserting control as the person to which the transferable record was issued; or the authoritative copy indicates that the transferable record has been transferred, the person to which the transferable record was most recently transferred;
>
> (3) the authoritative copy is communicated to and maintained by the person asserting control or its designated custodian;
>
> (4) copies or revisions that add or change an identified assignee of the authoritative copy can be made only with the consent of the person asserting control;
>
> (5) each copy of the authoritative copy and any copy of a copy is readily identifiable as a copy that is not the authoritative copy; and
>
> (6) any revision of the authoritative copy is readily identifiable as authorised or unauthorised."

Section 16(d) of the UETA creates the same rights of a holder for the party exercising control of a transferable record as the party would have as a holder of a negotiable document or instrument. It is further provided that the requirements of delivery, possession and indorsement are not necessary to obtain or exercise

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159 See *infra*.

160 Both the UETA and the ESIGN statutes cover equivalents of promissory notes, whereas only UETA addresses equivalents of documents of title.

161 As analysed in UNCITRAL doc A/CN.9/WG.IV/WP.90 para 89.

any of the rights of a transferable record. These terms are obviously used in their physical connotation without trying to create equivalent procedures in the electronic world.

Control requirements imposed by Section 16 may be satisfied through the use of a trusted third party registry system, but a technological system which meets such exact standards would apparently also be permitted.[162]

The electronic records envisaged are, in fact, related to real (immovable) property collateral, yet they may serve as an example for goods and trade-related documents. A transferable record is defined as an electronic record that would be a note[163] under the law of negotiable instruments or a document under the law of negotiable documents if the electronic record were in writing, and if the issuer of the electronic record has expressly agreed that the electronic record is subject to the Act.[164] With a transferable record, obligors have the same rights and defences as equivalent obligors under equivalent transferable records under the laws of negotiable instruments and negotiable documents.[165]

Gabriel[166] reports that the concept of a transferable record was adopted at the meeting of the Drafting Committee for the UETA after a long and spirited debate. The major proponents of transferable records pointed out that electronic instruments and documents of title allow more efficient transfer and easier storage and access. One argument against transferable records is that they infringe on the existing and clear US law of negotiable instruments and documents. Moreover, a transferable record does something radical for electronic commerce legislation at its initial stage by namely creating a new substantive right. The general provisions of the UETA would not constitute a sufficient basis for the determination of who has the right in the transferable record. As transferable records are created by contractual arrangements, the criticism may deal with the status of third parties.

The UETA does not establish technological standards for the creation and preservation of transferable records. That is left to the parties involved as well as to the development of the technology. What the UETA does is simply provide the statutory vehicle for a situation where the parties can develop the minimal standards necessary to create, transfer and validate transferable records.[167] By the end of 2000, no such system appeared to fully meet the stringent UETA requirements.[168]

Such standards would not be solely technical, but would apparently also consist of legal provisions determining the rights and obligations of the parties. As legal rules would be created outside statutory legislation, new parties to whom such transferable records were transferred, would have to adhere to the legal framework by signing in to a ´rules of procedure´ or similar private instrument.

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162 Ibid., reference is made here to the official commentary of the UETA.

163 The Act covers only two party promissory notes, and not three party drafts (bills of exchange).

164 Section 16(a) (1)-(2) UETA (1999), Gabriel, p. 6.

165 Section 16(e) UETA (1999).

166 Gabriel, p. 6.

167 Sections 16 (b) and (c) UETA (1999), Gabriel, p. 6.

168 UNCITRAL doc A/CN.9/WG.IV/WP.90 para 94.

According to *Brumfelt Fry*[169], several questions relate to transferable records which cannot be answered until further developments occur. The first question is whether industry will eventually accept the invitation to establish systems to control the records, which would lead to the emergence of markets. Another question is the potential loss of flexibility. The comments on Section 16 of the UETA reveal that whilst the concept was designed as an initial effort to support private initiatives, it was done with the thought that further legislation probably would be required once some experience had accumulated. Brumfelt Fry anticipates problems in the efforts to develop a more complete statement of the rights and obligations of participants in such potential markets.

Problems are also anticipated in the creation of standards for transferring and maintaining such rights. Meeting such standards will require a carefully designed and supervised set of systems and practices. According to one view[170], the key element will be data integrity. Courts evaluating the control of a transferable record may be expected to focus on the systemic protections – e.g. the division of labour, the complexity of backup systems, activity logs, the security of copies stored offsite to verify content – which make it difficult to tamper with the record without detection.[171]

Where a transferable record is created by way of legislation, it becomes possible to create and transfer a negotiable instrument using electronic messages. As noted in the Bolero Feasibility Study 1999, it may be possible to replicate the main functions of a bill of exchange contractually. In many jurisdictions, however, the transfer of debt requires giving notice to the debtor or even public registration of debt transfer.[172]

A legislative reform is also pending in the United States, which would amend the Carriage of Goods by Sea Act of 1936 to allow for electronic communications in particular.[173]

The traditional negotiable instruments used in international trade have been originally established by commercial custom. In England, courts recognised this custom. In the United States, however, most states gave the bill of lading the status of a negotiable instrument only in 1909.[174] Therefore a legislative method for producing changes in the use of commercial instruments already has a tradition in the US.

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169 Brumfelt Fry, p. 5.

170 UNCITRAL doc A/CN.9/WG.IV/WP.90 para 94, referring to the article by R. David Whitaker, "Rules under the Uniform Electronic Transaction Act for an Electronic Equivalent to a Negotiable Promissory Note", The Business Lawyer, vol 55 (November 1999), p. 449.

171 Ibid.

172 Bolero Feasibility Study 1999, p. 79.

173 See Senate Draft COGSA 1999 [Staff Working Draft] September 24, 1999, http://tetley.law.mcgill.ca/maritime/cogsa99.htm., visited on 22.8.2003, Section 2(b) of the draft ´Special Rule for Electronic Communication´ provides: "

> "Whenever in this Act a notice, claim, or other communication is required to be made in writing, it may be transmitted in written form on paper transmitted by an electronic medium, including electronic data interchange and other computerized media of transmission."

174 Chandler, III in Transfer of Ownership, p. 423.

In theory, custom could also legitimise the use of transferable electronic records. It is, however, difficult to imagine how a commercial custom based on new techniques could establish itself within such a time-frame that would satisfy the accelerating requirements of modern society.[175]

English law requires an established custom in order for a transport document to constitute a document of title, unless it is a shipped bill of lading.[176] *Todd* assumes that the English common law would not regard an electronic bill of lading as a document of title. However, an electronic document (record) could become a document of title with proof of custom, but as Todd points out, "customs take a long time to establish: legislation may well be the best solution to the...problem".[177]

The problem in creating legislation for negotiable instruments operating in electronic form is how to strike a balance between certainty and predictability on the one hand, and neutrality towards technology and innovation on the other. With precise provisions comparable to those dealing with electronic signatures, public trust could be achieved more easily. However, specificity could hamper development and be a legal tightrope.

VI.3.4 The role and form of transport documents and conflict of laws

I have described the various functions of transport documents in contracts of sale and contracts of carriage as well as form requirements imposed by law. Although many features are unified by international conventions, states may adhere to different conventions or implement them in different manners. Therefore the main features of conflict of laws relating to transport documents must be examined after a substantive insight into the rules.

VI.3.4.1 Documents of title and conflict of laws

The use of documents of title in the relations between the shipper, the carrier, the consignee and the indorsee are defined in the Hague-Visby Rules, and even more explicitly in the Hamburg Rules. Both Rules use this concept. However, national law may still influence the treatment of documents of title.

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175 See also Bolero Feasibility Study 1999, http://www.boleroassociation.org/downloads/legfeas.pdf, visited on 4.8.2003.

176 Todd defines some characteristics for a document to be able to constitute a document of title under custom:

1. It is part of the essence of a document of title that it can be negotiated, which means that a non-negotiable document can never be a document of title.

2. A preliminary document intended to be given up for another document, such as a mate´s receipt, cannot become a document of title. However, if there is evidence that a mate´s receipt becomes the last document issued in practice, custom may make it a document of title. (Analogy could, in my view, be found in marine insurance, where a certificate of insurance gives a right to obtain a policy, but practice may already have added the feature of transferability to certificates; obviously marine insurance documents are not documents of title since they relate only to indemnification.)

177 Todd 1998, p. 168.

Firstly, national law may amend the effects in the above mentioned relation to the extent permitted by the Rules. An example already mentioned is that in the Nordic countries a *bona fide* indorsee of a stolen bill of lading can claim delivery of the goods and keep them whereas under English law such an indorsee can not.[178]

Secondly, national laws have completely different approaches as to what constitutes a document of title. In England, documents of title are established by commercial custom,[179] which requires in practice a considerable period of time for a new document of title to be established. The custom need not be universal, but can be a custom in a particular trade or a region.[180] In the Netherlands, on the contrary, statute law provides several examples of documents of title, which all can be negotiable as well. In addition to bills of lading, the ship´s delivery order and the combined transport document are expressly mentioned in law as documents of title.[181] However, the system is open and it is up to the intentions of the parties to create a document of title.[182] Where parties wish to name such a document as a bill of lading, there are, however, requirements as to the contents. In any case, such a liberal approach is of course also more favourable to the creation of electronic equivalents of documents of title. Such equivalents would have legal effects not necessarily limited to relations *inter partes*.

As regards the law applicable to the document of title, one has to distinguish between the law applicable in particular 1) to the constitution of a document of title, 2) to its transfer and 3) to the proprietary effects of the document. The document may be issued in country A, indorsed in country B and represent goods seized for the seller´s debts in a transport terminal in country C. Without trying to give any full account, the following represents some national approaches to the question of the applicable law in each case. One can note that the pitfalls of *depeçage* are close. The advantages of an electronic system that could cover the constitution, transfer and effects of an electronic equivalent of a document of title are obvious. As regards transport law aspects, however, the requirements of mandatory national transport laws make it impossible to submit all aspects of a document of title to be governed by one law.

The first mentioned law, the law applicable to the constitution of the instrument, is normally also critical as regards the form requirements and the possibility of establishing electronic equivalents. Swiss law gives significance to the choice-of-law clause inserted in the document. If the document fails to designate a governing law, the law of the state in which the issuing party has its

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178 Schmitthoff, Export Trade, pp. 275-276. Norwegian Maritime Code Section 306; Finnish Maritime Code Chapter 13 Section 56. As for England, see also section 24 of the Factors Act 1889, which protects a *bona fide* person to whom a document of title has been transferred although the goods had been previously sold by the transferor.

179 See also the description contained in Section 1(4) of the Factors Act 1889. The wording of the act is quite broad, and could even be understood to mean that CMR consignment notes give the right of control to the goods. Obviously, the CMR came later than the Factors Act.

180 *Kum v. Wah Tat Bank Ltd. [1971] 1 Lloyd´s Rep 439*. Todd 1998, p. 115.

181 Articles 8:417, 8:924, 8:482 and 8:50 respectively of the Dutch Civil Code.

182 Zwitser in Transfer of Ownership, p. 253.

principal place of business will govern it.[183] Under English law, the decision as to whether a document is a document of title is determined by the *lex situs* of the goods at the time of the issue of the document.[184] Dutch law considers the law of the state where the issuer of the document has his place of business to be relevant.[185]

The second situation, the law applicable to the transfer of the document of title, may be governed by a law separate from the issue. For instance, according to German law, the transfer of the instrument itself is subject to the *lex carta sitae*.[186] The same applies according to Dutch law.[187] In cases where the transfer occurs using an electronic registry, it would be natural to hold such a registry as the place of the ´document´. Swiss law, on the contrary, seems to the treat the question of rights *in rem* concerning the document of title as subordinate to the rights *in rem* in respect of the goods.[188]

The third situation, the proprietary effects of a document of title, is sometimes governed by the *lex situs* of the goods. This is the case, for instance, in Germany[189]. Under Dutch law, however, the property in the goods is determined by the *lex carta sitae* of the document, wherever the goods themselves may be located.[190]

The above indicates that there is room for uniform conflict of laws rules in respect of documents of title. Such rules should encompass electronic alternatives and should subject the above features to the extent possible under one law, ideally the law of the issue, which in an electronic environment could always be one place, the place of the registry.

VI.3.4.2 Transport documents and conflicting transport laws

The sea transport conventions adopted before the Hamburg Rules provide a uniform and mandatory legal framework for the states that adhere to these conventions and attache legal effects to the use of the bill of lading. For instance, Article X of the Hague-Visby Rules provides that "the provisions of the Rules shall apply to every bill of lading relating to the carriage of goods between ports in two different states if the bill of lading is issued in a contracting State, or the carriage is from a port in a contracting State or the contract contained in or evidenced by the bill of lading provides that the Rules or legislation of any State giving effect to them are to govern the contract, whatever may be the nationality of the ship, the carrier, the shipper, the consignee, or any other interested person".

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183 von Ziegler in *op.cit.*, p. 404.

184 Debattista in *op.cit.*, p. 143. Debattista examines the question of whether the EC Convention on the Law Applicable to Contractual Obligations might be applicable to the question of what constitutes a document of title but comes to a negative conclusion.

185 Zwitser in *op.cit*, p. 254. Zwitser, confusingly, talks about bills of lading only in this context despite the liberal attitude of Dutch law in relation to the constitution of documents of title.

186 Thorn in *op.cit*, p. 190.

187 Zwitser in *op.cit*, p. 254.

188 von Ziegler in *op.cit*, p. 404.

189 Thorn in *op.cit.*, p. 190.

190 Zwitser in *op.cit.* , p. 254.

Generally speaking, parties to a contract of transport are relatively free to select the law applicable to the contract of transport, but because carriers are thought to have more bargaining power than shippers, transport conventions and national laws incorporating them define the scope of the mandatory application of the relevant provisions.

The determinant connecting factors outside a choice of law clause are thus the issue of the bill of lading in a contracting state and the commencement of the transportation from a contracting state. In an electronic environment, the place of issue of a document is not obvious. It would therefore be convenient to stipulate the place of issue of an electronic bill of lading unless an equivalent method of incorporating the Rules is used.

Article X of the Hague-Visby Rules requires two further comments. Firstly, it talks about bills of lading only.[191] Other transport documents, such as sea waybills are not within the mandatory sphere of the provision. There is, however, nothing to prevent contracting states extending the application of their implementing legislation to other transport documents, notably to sea waybills. As noted earlier, many jurisdictions, including France and Nordic countries, have come to that conclusion.

Should a sea waybill, however, refer to the law of a country in which the Hague-Visby rules are not extended to apply mandatorily to cases where no bill of lading is issued, a conflict situation emerges. The court has then to determine, which law should apply. Certain national laws may offer more protection to the shipper or the consignee. As these situations may create great confusion, a suggestion has once been made to amend the the original Brussels Convention by another protocol that would extend its application to carriages performed under a sea waybill.[192] Such a reform will actually constitute a part of the task of the UNCITRAL Working Party on Transport in its efforts to create a new instrument for sea and perhaps partly multimodal transport.[193]

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191 Or, not exactly: if the goods are covered by "a bill of lading or any similar document of title" the Convention applies (article 1(b) of the Hague-Visby Rules). The Carriage of Goods by Sea Act 1971 implemented the Rules in the United Kingdom. In the case RAFAELA S, [2003] 2 Lloyd´s Rep. 113, the question arose whether a non-transferable bill of lading, the presentation of which is anyhow required to claim the goods, is considered to be a document of title within the meaning of the Act and the Rules. On the case, see Debattista, Non-order bills fully in order after the RAFAELA S, at http://www.gard.no/gard/Publications/GardNews/RecentIssues/gn173/art_8.htm, visited on 14.4.2004.

192 Rodière 1991, p. 269. The Hamburg Rules have in fact done this.

193 The draft Instrument on the Carriage of Goods [by Sea] (Doc A/CN.9/WG.III/WP.32, 26.8.2003) has two alternatives for Article 2(1) relating to the scope of the Instrument. Both alternatives have similar lists of connecting factors, including place of receipt by the carrier (or port of loading) in a contracting state and the place of agreed or factual place of delivery (discharge) in a contracting state.

Relevant for electronic commerce, one option is that the contract of carriage is concluded, or the transport document or electronic record (whether negotiable or not) is issued in a contracting state. The transport document is not, however, conclusive, if it was issued under a charterparty covering the relationship between the shipper and the carrier as charterer.

Finally, parties could opt in the Convention even without the above connecting factors.

Even if the bill of lading is not issued in a contracting state, or the transportation does not commence from such state, a bill of lading or a sea waybill may incorporate the Rules as contained in the legislation of a contracting state. Moreover, parties are free to incorporate the Rules directly, i.e. even if this is not mandatory in the country where the bill of lading is issued. This may, however, be wise bearing in mind that many jurisdictions may extend their mandatory transport legislation by using factors connecting the transportation to their jurisdiction in accordance with international conventions.

An example of national legislation treating the issue of its mandatory application is the UK Carriage of Goods by Sea Act 1992. Article 3 of the Act establishes the principle that a contract of carriage shall be governed by the law chosen by the parties. However, the fact that the parties have chosen a foreign law (whether or not accompanied by the choice of a foreign tribunal) shall not, where all the other elements relevant to the situation at the time of the choice are connected with one country only, prejudice the application of rules of the law of that country which cannot be derogated from by contract, i.e. the ´mandatory rules´.[194]

As regards the form of transport documents, transport conventions provide a uniform form for the documents or are merely silent on these matters. The Hamburg Rules provide for how to sign bills of lading, but however subject themselves to the national law of the country of the issuance of the bill of lading should this law provide otherwise.

The applicable transport law, be it the law of the country of issue of the bill of lading or other law connected to the transportation or parties, also prescribes the form requirements as to the transport documents, more notably the bill of lading. Since the parties are generally at some liberty to choose the applicable transport law, they should opt for a regime that is liberal as to form requirements to optimise the possibilities for an efficient trade documentation policy.

The opting in of transport laws may be confronted with limits. Namely, if national law requires bills of lading to be in writing in the traditional sense of the word, parties might not be able to validly agree to use systems where the acts equivalent to possession of documents of title is recorded electronically. *Cova Arria*[195] argues that some civil law countries might not accept a dematerialised bill of lading as evidence without those countries implementing the UNCITRAL Model Law on Electronic Commerce.

Another matter is that some functions relating to bills of lading may need a written form under some jurisdictions. According to the Bolero Feasibility Study 1999, a security assignment requires a written form in some jurisdictions and the

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194 Article 3(3) of the 1992 Carriage of Goods by Sea Act. A relevant case behind this statutory provision is *Vita Food Products Inc. v. Unus Shipping Co. Ltd. (The Hollandia)* [1983] 1 A.C. 565 in which Lord Wright stated that the English courts would always give effect to an express choice of law clause, provided the intention expressed is *bona fide* and legal and provided there is no basis for avoiding the clause on grounds of public policy.

195 Cova Arria, Luis, Legal Obstacles to the Implementation of the Electronic Bill of Lading in Civil Law Countries, ETL, 1997, p. 712.

users of the system are therefore advised to carry out such operations outside the electronic register system.[196]

Sea transport conditions usually refer to a particular national law or to a particular transport convention. The Clause Paramount incorporates the Hague or the Hague-Visby Rules. In multimodal transport, the carriage is subject to several mandatory regimes, which may even be conflicting.[197] Normal network liability provisions in transport documents take this fact into account. Should the transportation be multimodal, parties may use transport conditions that are based on the UNCTAD/ICC Rules for Multimodal Transport Documents.[198]

The liability regime for multimodal transport documents respects the mandatory provisions applicable to the period in each mode of transport, however providing a "lowest common denominator" approach as to damages that occur outside the periods to which mandatory regimes apply. On the contrary, a multimodal transport document is a document of its own kind, which does not need to respect the form requirements that would apply to mode-specific carriages.

VI.4 Developments in the industry

Business and academic communities have been active in creating electronic alternatives to traditional transport documentation, in particular marine bills of lading. As has been already mentioned, the replacement of paper started as early as in the 1970s in connection with sea waybills. This was possible because shippers with established business relationships did not need a bill of lading on Transatlantic routes.

Despite attempts to discourage the use of the bill of lading[199], their role as documents of title serves useful purposes. Moreover, traders are used to the idea of the bill of lading. Therefore, attempts have been made by various private circles to create electronic equivalents for bills of lading. Since these attempts originate from the private sector, they are contractual by nature. These contractual arrangements have to fit into the space that international conventions and national legislation leaves them. As there are particularly many conventions relating to carriage of goods by sea in force, and national law requirements imposed in addition to those of the conventions, the task has not been particularly easy.

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196 See Chapter VIII, 7.1., *post*.

197 For the relationship between Article 2 of the CMR Covention and sea transport, see Scrutton 1996, Article 182. One could mention that a suggested revision of the US COGSA 1936 purports to extend the application of a sea carrier´s liability regime to freight forwarders (´Non-Vessel-Operating Common carriers´, NVOCCs) issuing through bills of lading. The revised act would apply to practically anybody in the transport chain, even though they were under separate liability regimes.

198 ICC Publication No. 481, 1991. FIATA Bill of Lading as well as BIMCO´s Combidoc and Combiconbill are based on the UNCTAD/ICC Rules for Multimodal Transport Documents.

199 See Chapter VIII.2.1.6., *post*.

VI.4.1 Early projects of electronisation

The emergence of EDI led to a number of unsuccessful attempts to implement it in the field of sea transport documents. A project entitled DISH was a joint venture between European shippers and carriers. It was confronted among other things with software problems and was followed by EDISHIP, which was an attempt by ten sea carriers. The first attempt to create an electronic bill of lading[200] system was SEADOCS. It was a joint effort by INTERTANKO[201] and Chase Manhattan Bank and was based on the idea of a central registry through which all parties to the bill of lading would communicate.[202] In this system, Chase Manhattan Bank would have acted as the registry. The bank would have communicated by telex with the other parties of the transaction after having received an original paper bill of lading. SEADOCS was envisaged as a compromise between traditional paper documentation and a fully electronic system and was in fact a demobilisation system. A paper bill of lading was lodged with a central registry from which it did not move. The bank would then notify the parties electronically of the transfer of rights. The system was never used because it proved to be impracticable. As high values of cargoes were at stake, even a minor mistake in the handling or interpretation of documents could have caused extensive liabilities against the parties. Obtaining insurance cover for such liabilities would have been difficult, at least in terms of supportable premiums. The creation and maintenance of a central registry added a new layer of costs which were not offset by savings elsewhere since carriers had to issue ordinary bills of lading anyway. A problem in relation to the use of documentary credits was that the bills of lading were not there to be scrutinised by banks and the registry had to offer itself for that purpose. This idea was not received enthusiastically by traders.[203] Furthermore, trading companies were suspicious of giving information to a central location where they feared it would be available to competitors and intrusive governments. For these reasons, SEADOCS was never operated apart from a pilot project using shadow documents. For a long time, SEADOCS was not finally abandoned by INTERTANKO although Chase Manhattan Bank has withdrawn itself from the project.[204]

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200 Before that, a ´paperless´ system abolishing the use of both bills of lading and non-negotiable transport documents (sea waybills) had been run by the Atlantic Container Line Datafreight Receipt System since 1971, see *supra*.

201 International Association of Independent Tanker Owners.

202 Ziegler, ETL 1997, p. 652

203 Todd 1998, p. 166 quoting an article by Kathy Love, Legal Advisor to Shell International Petroleum, in "Seadocs: The Lessons Learned", [1992] 2 Oil and Gas Law and Taxation Review at 53.

204 Information from 1997, Von Ziegler, ETL 1997, p. 652.

There was another project in the middle of the 1990s entitled GURI, as described in Røsæg, ´Electronic Bills of Lading - sophisticated toys or workable solutions?´, in a Seminar in Maritime Law Autumn 1994, Scandinavian Institute of Maritime Law, University of Oslo, 19.10.1994. GURI was equally based on the use of a central registry together with the use of electronic signatures. Any holder could send electronically signed messages to a central registry for the transfer of the bill or to claim delivery. The commercial history of GURI is not known to the author.

These projects were launched by individual commercial operators with the obvious objective of gaining a competitive advantage. Carriage of goods by sea involves, however, many documentary requirements imposed by other parties (customs officials, insurance companies etc.) than the shipping line issuing the transport document or its electronic equivalent. To deal directly with this wider group of people, the US National Committee of International Trade Procedures (NCITD)[205] came up with the Cargo Data Interchange System (CARDIS). The aim was to bring everyone operating in the port into one electronic system. This would have presupposed the use of standard forms in standard systems in a standard way so that any concerned party could access the system to add or use information. CARDIS therefore tried to create such a set of standards. These were not, however, accepted by the industry because everybody more or less felt that their own solutions were the best for solving their own problems.[206]

VI.4.2 CMI Rules for Electronic Bills of Lading

Comité Maritime International (CMI) incorporated the idea of a bill of lading registry[207] in the Uniform Rules for Electronic Bills of Lading, which were adopted in 1990. These rules were intended to provide a framework for applying EDI to bills of lading. The CMI Rules are a voluntary set of rules and apply when parties so agree. The rules do not aim to replace any part of the substantive law on bills of lading but "merely imitate electronically the paper bill of lading and its characteristic function to vest the holder with a right to control the disposition of the goods and to transfer that right to somebody else."[208]

VI.4.2.1 Proprietary functions not covered

Although the rules are entitled ´rules for electronic bills of lading´ they concern only the aspects of bills of lading relating to the carriage of goods by sea. The proprietary function of bills of lading has not been dealt with at all.[209] This is natural because the rules are not a statutory instrument, and proprietary effects, which are valid even against third parties, require a statutory involvement or custom. To the extent the law allows parties to transfer title through the transfer of a document of title, especially when done electronically, the rules can be helpful in this respect as well. However, as said, they do not classify the mechanism replicating the bill as constituting an equivalent of a document of title.

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205 NCITD could be described as the American equivalent of the UK based ´SITPRO´ (Simpler Trade Procedures Board).

206 Alan Urbach, Electronic Presentation and Transfer of Shipping Documents in Goode (ed.) Electronic Banking – the Legal Implications, pp. 115-116.

207 Which is not necessarily a central registry, see *infra*.

208 Ramberg, ETL, 1997, p. 699.

209 G.J.van der Ziel, ETL, 1997, p. 717. In the view of van der Ziel, the rules should therefore have kept the name used during the drafting stage: ´Rules for the electronic transfer of rights of goods in transit´.

According to the CMI Rules[210], the procedure goes as follows: The Carrier, upon receiving the goods from the Shipper, shall give notice thereof to the shipper by a message at the electronic address specified by the shipper (Rule 4). This Rule further provides the mandatory information to be included in the receipt message. The shipper must then confirm this receipt message to the carrier, upon which confirmation the shipper shall be the Holder. The receipt message shall then be updated with the date and place of shipment once the goods have been loaded onboard. The Holder is the only party who may, as against the Carrier, claim delivery of the goods, nominate the consignee or substitute a nominated consignee for any other party (including himself), transfer the Right of Control and Transfer[211] to another party and instruct the carrier on any other subject concerning the goods, in accordance with the terms and conditions of the contract of carriage.

The transfer has the following phases: 1) The Holder can effect the transfer of the Right of Control and Transfer by first notifying the carrier of his intention to do so. The Carrier shall then confirm this notification. 2) The Carrier shall transmit the relevant information (that mentioned in the receipt message not including the Private Key he has received) to the proposed new Holder. 3) The new Holder shall advise the carrier of his acceptance of the Right of Control and Transfer. 4) The Carrier shall cancel the current Private Key and issue a new Private Key to the new Holder. According to Rule 4(c), the proposed new Holder can effectively refuse to accept the transfer.

VI.4.2.2 Possibilities for a CMI based system – evaluation

As *Grönfors* has noted, The CMI Rules for Electronic Bills of Lading have the special quality of removing possible doubts in the minds of commercial circles as to possibility of using such bills.[212] The rules created the first recognised system of communicating transport data and legal functions without using traditional paper documents.

Another important merit of the Rules is that they make it possible either to use a central registry as an intermediary or simply to work in open systems directly with the parties involved.[213]

The technical approach of the CMI Rules has, however, met some criticism. *Todd* considers that the essential problem with the model is that it assumes transmission of secret codes between the ship and the shore.[214] This transmission is probably a radio communication, which can be intercepted by everybody. Therefore, if the CMI model is to be secure, it is essential according to Todd that the secret code be encrypted. The problem arises in particular in transmissions

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210 I am using capitalisation to denote the parties and acts highlighted in the Rules.

211 Rule 7 deals with the Right of Control and Transfer which is a legal noun specific for these Rules.

212 Grönfors 1991, p. 82.

213 Ibid.

214 Todd 1998, p. 160. Todd prefers to use the expression ´secret code´ instead of ´private key´ since the latter is more frequently used in public/private key cryptography.

from the carrier to the subsequent holders. Todd adds that encryption is problematic because it necessitates decryption. In an open trading system where goods can in principle be sold by everybody to everybody, however, it is very difficult to agree on an encryption algorithm which would be available only to the parties entitled to it and not to fraudsters. The only way would be that such an encryption key is used which is unique to the transaction and is received together with the encrypted message. Transmitting a transaction-specific key to several parties who may be involved creates a risk of interception.

Todd suggests two possible solutions to the problem described above. The first solution is based on the idea of an open system. He first makes a number of assumptions. Each party has a unique public key which is known to everyone and a unique private key which is always kept secret. The encryption algorithm is publicly available. Finally, when a message is sent from A to B, the latter can decrypt the message (by using his private key and A´s public key) but not the other way round.The system suggested by Todd could then work as follows. Each trader knows everybody else´s public key. The carrier gives the shipper the secret code (being the private key within the meaning of the CMI Rules). This communication is not encrypted. The shipper performs a transaction by returning the secret code (and the identity of the transferee) to the carrier, the secret code being encrypted. The secret code is encrypted with the shipper´s private key and the carrier´s public key. Only the carrier can then decrypt this using his private key and the shipper´s public key. The carrier then sends the electronic bill of lading and a new secret code to the transferee (the secret code being encrypted using his private key and the transferee´s public key). The transferee alone can decrypt this using his private key and the carrier´s public key. The transferee, or another ultimate receiver being subject to similar transactions as indicated above, finally obtains the goods from the carrier. In the above system, private keys (in the general meaning of the word) need never be transmitted or disclosed. As the secret codes are encrypted, there are few opportunities for burglars to break in. There is a need for an openly accessible register of public keys. Otherwise this system can operate without a registry.

Another system discussed by Todd[215] is a closed system with a central registry. The *Bolero System* described in Chapter VIII.7., *post*, generally operates through a central registry. In fact, the CMI Rules were one conceptual basis for the *Bolero Rulebook*.[216] In a closed system with a register, it is possible to cut out altogether communication between ship and shore and to confine communications to such transmission channels which are more secure. The carrier needs to know only the ultimate consignee and has no need to know the identity of every trader in a chain.

Todd bases effective system with a central registry on a number of assumptions. All parties are users of a mainframe computer, maintained by a central registry; all transactions are recorded centrally on the mainframe computer. The computer stores all the information that is typically entered onto

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215 Todd 1998, p. 164.

216 Mallon´s interview 24 November 2003.

bills of lading, including the conditions of carriage. Finally, the carrier can access the identity of the ultimate consignee at the port of discharge.

Moreover, when transport documents move through at least two financial intermediaries, the confirming and issuing banks in documentary credit operations, the CMI based system requiring contacts with the ship(s) becomes cumbersome and perhaps risky as well. It would therefore seem that a central registry system operating ashore and also dealing with proprietary issues is a more practical arrangement.[217] An account of various types of registries is provided in Chapter VIII.11.1., *post*.

The private key (or the secret code) represents singularity and uniqueness as compared to a situation where the carrier would simply be given the name of the new consignee. When the party giving instructions or claiming delivery presents the key, this serves as a legitimation in way a piece of paper does. I think that the system could even include one private key ´changing hands´ without necessarily going through the carrier and being replaced by another key every time. This would add a feature comparable to a bearer instrument. How to guarantee safety in such situations is another story.

VI.4.2.3 Can you contract out ´in writing´ requirements in law?

Rule 11 of the CMI Rules provides that "the carrier and the shipper and all subsequent parties utilizing these procedures have agreed that any national or local law, custom or practice requiring the Contract of Carriage to be evidenced in writing and signed, is satisfied by the transmitted and confirmed electronic data residing on computer data storage media displayable in human language on a video screen or as printed out by a computer". Furthermore, it provides that "in agreeing to adopt these Rules, the parties shall be taken to have agreed not to raise the defense that this contract is not in writing". Doubts have been expressed by *Cova Arria*[218] whether this Rule applying the common law doctrine of ´estoppel´ by which a person is precluded from denying a certain state of fact, contrary to previous allegations or conduct, will be admitted in civil law countries as evidence of a contract which is required by law to be ´in writing´.[219] As the applicable local law will determine to what extent such agreement satisfies the legal requirement of evidence ´in writing´, in many countries a dematerialised document would not have any legal value. This situation could, however, be remedied by the relevant civil law countries by adopting the UNCITRAL Model Law on Electronic Commerce, which "adapts the existing statutory requirements so that they would no longer constitute obstacles to the use of EDI".[220]

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217 I have not investigated how far Todd´s concerns reflect today´s commercial and technical realities. One can ask, for instance, how much of the carrier´s information and technical operations need to be connected to the ship in real time, or could they be run from the shore at least as far as sensitive information is concerned.

218 Luis Cova Arria, Legal Obstacles to the Implementation of the Electronic Bill of Lading in Civil Law Countries, ETL, 1997, p. 712.

219 Ibid. Cova Arria argues that ´estoppel´, which in civil law jurisdictions is more or less known as ´tacit consent´, would not be sufficient to evidence the existence of a ´document of credit´.

220 Ibid., p. 714. Report of the Working Group on Electronic Data Interchange (EDI) on the work of its 29th session, UN Doc. A/CN.9/407 para. 23.

VI.4.2.4 Amending the legal relationship based on the CMI Rules

The CMI Rules cover, as has been stated, only part of the functions of a traditional bill of lading. The other functions will have to be considered in the light of the laws applicable to the contract of transport and the contract of sale. For instance, the possibility for the seller to use stoppage in transit is governed by the law applicable to the sales contract.

The CMI Rules do not contain rules similar to the Hague-Visby or Hamburg Rules, but apparently suppose that these come into application through mandatory legislation or Paramount Clauses. So, also under the CMI system, an indorsee of a bill of lading equivalent acting in good faith can claim delivery of the goods stated in the messaging.

VI.4.3 The Bolero System

The Bolero System piloted in 1999 is the principal, if not only, relevant project going on actively at the moment. However, the Bolero System contains many elements that go beyond a simple bill of lading registry system. Namely an entire documentary credit transaction can be carried out through it. Therefore a more comprehensive look into the project is taken in Chapter VIII.7.1., *post*.

However, the legal nature of the instruments created by the Bolero System is interesting. The Bolero Feasibility Study[221] outlines the legal nature of the *Bolero Bill of Lading* (BBL). As the Bolero System is one of the industry initiatives which is not backed by comprehensive facilitating legislation, it is assumed here that many findings of the study extend to other electronic bill of lading projects as well.

The Feasibility Study recalls that the relevant sea transport conventions give the shipper a right to require a bill of lading to be issued by the carrier.[222] The Feasibility Study does not endeavour to align the BBL with such a "documentary bill of lading" due to the fact that these conventions do not expressly require an electronic alternative requirement to be admitted, and national law in many countries may not recognise an electronic bill of lading. On the contrary, the Feasibility Study and the Bolero System build on the assumption that the shipper elects not to ask for a documentary bill of lading and opts for an alternative system designed to achieve the same results.[223]

The Feasibility Study further admits[224] that a bill of lading created under the system "will not be a document of title because it will not be a document, and most national laws will only ascribe the character of ´document of title´ to a

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221 At http://www.boleroassociation.net/downloads/legfeas.pdf, visited on 4.8.2003. See Chapter VIII.7.1., *post*.

222 Bolero Feasibility Study 1999, p. 43, Hague-Visby Rules Art 3(3), Hamburg Rules Art 14(1).

223 Bolero Feasibility Study 1999, p. 44.

224 Bolero Feasibility Study 1999, p. 61.

written physical document". The BBL is transferable, unless the carrier designates a consignee. The operation of the BBL will be examined in Chapter VIII.7.1.4., *post*.

Bearing in mind the local English common law requirement that the status of document of title has to be established by custom, the Feasibility Study further notes that "it is possible that over time an electronic electronic bill of lading may acquire the attribute of negotiability by the custom of merchants in jurisdictions which allow this, but since custom of merchants is something which can only be proved by demonstrating the adherence to the custom of the vast majority of merchants, it is not appropriate for consideration at the introductory stage of the Bolero Bill of Lading".

The Feasibility Study, which was written in 1999, is a practically oriented document and not drafted for legislative or lobbying purposes. It should be noted therefore that an electronic equivalent of a paper bill of lading constituting a document of title can be created more effectively by way of a legislative instrument. The English Carriage of Goods by Sea Act of 1992 especially empowers the Secretary of State to create such an instrument. Such a statute would obviously undermine somewhat the Bolero Rulebook as the legal foundation of the system, but would give the BBL an established status of a bill of lading and a document of title.

Further to the problems relating to the use of a dematerialised bill of lading as a document of title, there is a documentary issue tied to the fact that, formally speaking, the mandatory application of the Hague-Visby Rules presupposes that the shipper requires and the carrier issues a documentary bill of lading.[225] Should the shipper be covered by a dematerialised bill of lading, one could argue that the contract of carriage is beyond the scope of the mandatory application of the Rules. Conversely, it could be argued that contracting-out is prohibited by the Hague-Visby Rules Article III (6) as regards ordinary commercial shipments. This problem is by no means unique to dematerialised bills of lading. The use of the sea waybill needs also to be regarded in the light of its relation to the mandatory application of sea transport conventions.

In some cases, the mandatory application of the Hague-Visby Rules takes place by virtue of law even if no bill of lading is issued. As already stated, national laws in Nordic countries and France have extended the mandatory application of the Convention´s rules to shipments where no bill of lading is issued. In some cases, the Hague Visby Rules could come into application without the issue of a bill of lading or without an express requirement in national law. It would suffice that it is the intention of the parties to follow a custom of the trade covering the carriage in question according to which custom it is usual to issue a bill of lading.[226]

Normally the problem of the applicability of the sea transport convention is avoided by a Clause Paramount in the transport conditions incorporating the

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225 Article 1(b) of the Rules. Cf. Articles 1(6) and 2 of the Hamburg Rules which have eliminated the link between an issue of a bill of lading and the application of the Rules.

226 Honka, p. 30.

relevant convention.[227] This is the practice with the use of sea waybills. The Bolero Rulebook, which is the legal foundation of the Bolero System, contains a sort of a multiple Paramount Clause using a hypothetical issue of a paper bill of lading as a connecting factor.[228] The reference to the issue of a paper (or documentary) bill of lading is made since the mandatory application of the Hague or Hague-Visby Rules is tied to the issue of a paper bill of lading.

The legal regime introduced by the Rulebook is still far from uniform. The Bolero Rulebook is governed by and shall be interpreted in accordance with English law.[229] However, the Bolero Rulebook gives precedence to an international convention or a national law giving effect to the convention. Sea transport conventions, as has been noted earlier, contain rules on their scope of application. These rules, sometimes amended by national law, give significance to the place of issue of the bill of lading.

In the absence of a Paramount Clause envisaged in paragraph (c) of Chapter X of the Hague-Visby Rules, the only clear connecting factor would be the country of the port where the carriage begins.[230] It would be obvious to assume that where a carrier issues a (paper) bill of lading after the goods having been shipped or received, the bill is issued in that country. This is not, however, evident since there is no obligation imposed in the Rules to do so. Another assumption could be made on the basis of the ordinary course of business between regular business partners or on the basis of a custom of the trade. Bearing in mind that there are four sea transport legal frameworks in operation (no convention or any of the three different conventions) and that national law may add something both to the scope and substance, there still remains some work for lawyers to do.

Despite the multiple Clause Paramount, which overrides any provisions in the contract of carriage by virtue of the application of the Bolero Rulebook to which the parties adhere, the actual contract of carriage is created between the

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227 This means, as noted *supra*, either the Brussels Convention of 1924 (the Hague Rules), the said Convention as amended with the 1968 Protocol (the Hague-Visby Rules) or the United Nations Convention on the Carriage of Goods by Sea of 1978 (the Hamburg Rules).

228 The Bolero Rulebook Section 3.2(2) – International Conventions provides:" (*a) contract of carriage in respect of which the Carrier has created a Bolero Bill of Lading shall be subject to any international convention, or national law giving effect to such international convention, which would have been compulsorily applicable if a paper bill of lading in the same terms had been issued in respect of that contract. Such international convention or national law shall be deemed incorporated into the Bill of Lading. In the event of a conflict between the provisions of any international convention or national law giving effect to such international convention and the other provisions of the contract of carriage as contained in the BBL Text, the provisions of that national law or that international convention shall prevail*". For the Bolero Rulebook, see Chapter VIII.7.1.3., *post*.

The Bolero Rulebook pays particular attention to incorporating the US COGSA 1936 into the contracts of carriage, where applicable by providing in respect of US bills that "(w)here the carriage covered by the Bolero Bill of Lading evidences carriage to or from a port or place in the United States, the United States Carriage of Goods by Sea Act 1936 shall be deemed to be incorporated and form part of the contract of carriage contained in or evidenced by the Bolero Bill of Lading."

229 The Bolero Rulebook, section 2.5(2).

230 For Article X of the Hague-Visby Rules, see 3.4.2., *supra*.

carrier and the shipper (or charterer) independently. The carrier can introduce his own conditions of carriage, and the law applicable to the contract of carriage is determined independently of the Rulebook on the basis of a choice-of-law clause or by other operation of mandatory transport laws.

The Rulebook establishes a framework for incorporating standard terms and conditions into the contract of carriage. Section 3.2(1) of the Bolero Rulebook namely provides that "in order to incorporate its standard terms and conditions, otherwise than by setting the said terms and conditions out in full in the BBL Text, a Carrier shall: (a) Express in the BBL Text that external terms and conditions be incorporated into the BBL text; and Indicate where such terms and conditions can be found and read, electronically or otherwise".[231] Section 3.2(2) adds that "(e)ach User agrees that such incorporation shall be effective to make such terms and conditions binding upon the parties to the contract of carriage".

These obligations imposed by the Bolero Rulebook, to which the users adhere, are apparently valid according to English law as being applied to the Bolero Rulebook. The Bolero Feasibility Study 1999 specially addresses the issue of electronic conclusion of transport contracts and the status of exemption clauses in an electronic environment. The Feasibility Study notes "(a)s a further consequence of dematerialising bills of lading, it is possible that exemption clauses are less likely to be effective if they are in electronic form".[232] The Feasibility Study assumes that incorporation of electronic exemption clauses is generally possible, but that national courts might treat the situation differently.[233] The Feasibility Study notes, however, that there are clauses that may require special treatment by virtue of law or the particular nature of the clause. Examples mentioned are jurisdiction clauses, arbitration clauses, lien clauses, guarantees and ´Himalaya´-clauses.[234]

It should be recalled that the issue of the validity of incorporation of contract text is not exactly the same issue as the form of presentation and availability of the contract text or its title. National jurisprudence may impose requirements as to the validity of the incorporation in general or as regards particularly onerous or ´exorbitant´ clauses in particular.[235] These problems have already been encountered in connection with the introduction of ´blank back´ bills of lading.[236]

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231 As already noted, Bolero Operating Rules 35 and 36 of the Operating Procedures facilitate the publication of users´ documents in User Support Resources and determine that a document published in User Support Resources is deemed to be available to all users of the Bolero System as required by the Bolero Rulebook section 3.2(1)(b).

This provision does not require the terms and conditions to be made electronically available in a manner that they can be stored, printed or reproduced but presupposes that they are available in one way or another.

232 The Bolero Feasibility Study 1999, p. 49.

233 Ibid., p. 50.

234 For the Himalaya-clauses, see 1.3.5., *supra*.

235 The pledge (lien) clause of the General Conditions of the Association of Nordic Freight Forwarders represents an example of such onerous clauses, which require special attention.

236 The treatment of blank-back bills of lading in various jurisdictions, and a note on lien clauses, is presented in connection with the issue of streamlining traditional paper documentation in Chapter VIII.2.1.6., *post*.

It is presumed that the validity of the incorporation by reference of transport terms has to be determined jurisdiction by jurisdiction and clause by clause, irrespective of the provisions in the Bolero Rulebook and the liberal attitude of English law[237] to such incorporation, and including the use of ´blank back´ bills of lading. Jurisdictions imposing stringent requirements do not easily allow circumvention. It would be interesting to see, whether there would be willingness among legislators to advance from the general equivalence principle between electronic and traditional incorporation by reference, as contained in Article 5*bis* of the UNCITRAL Model Law of Electronic Commerce, to an attempt to create established legitimacy for using hyperlinks as a way of presenting contract terms in a manner at par with paper presentation. Such legitimacy could be based on the fact that the terms are ´made available´ and there are provisions relating to the onus of proof.[238] I refer to Chapter IV.10., *ante*, where this issue was covered more generally.

A special case of incorporation by reference is contained in section 3.2(3) of the Bolero Rulebook, which relates to incorporation of charterparty terms into the bill of lading and which provides that "words contained in the BBL Text incorporating the provisions of any charterparty shall have the same effect as if such wording had appeared as part of the written terms of a paper bill of lading issued by the Carrier". This wording does not legitimise the incorporation of charterparty terms into bills of lading as such, but equates electronic reference to a reference in paper documentary form. As the parties may select the law applicable to their contract of carriage, such law, or any law being mandatorily applied to the contract of carriage, may determine the validity and significance of the incorporation in the relationship between the carrier and the shipper or charterer on the one hand, and between the carrier and a *bona fide* indorsee of the charterparty bill of lading on the other.

VI.5 Conclusions

UNCITRAL, together with other international organisations and bodies, is conducting surveys and producing new materials for facilitating electronic commerce. It is important that various instruments which result from this work complement each other in a pragmatic way. At the least, a guidebook could be created to give a comprehensive picture of how different instruments should be enacted (or incorporated into contracts).

Bearing in mind the slow process of the ratification of conventions and the implementation of model laws, the possibility of using non-statutory instruments, comparable to the UNCITRAL Arbitration Rules, could be considered. This model has been contemplated with the possible door-to-door component (land leg) of the draft Instrument for the Carriage of Goods [wholly or partly][by Sea]. The problem in transport law is, however, the mandatory nature of many provisions.

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237 *Federal Bulk Carriers v. C. Itoh & Co; The Federal Bulker [1989] 1 Lloyd´s Rep. 103.* Payne & Ivamy 1989, p. 83.

238 The onus would be on the party claiming availability.

Thereby any desired changes in the regime must be made by instruments with equivalent binding effects.

The Working Groups of UNCITRAL should, as suggested by the plenary, join forces to study the new challenges and, in my view, should create a multi-functional negotiable electronic record covering both the transport law and the proprietary roles of negotiable transport documents. Similarly, any model rules of procedure should cover these two aspects. Since no harmonisation of the law of property is easily attainable, national law could be referred to as a supplementary source of law in appropriate situations.[239] It would be very much a unique procedure since sales laws do not usually address the transfer of property rights through the use of documents of title, due to which this aspect rests on custom or the express or implied agreement by the parties.

Contractual arrangements are, however, not appropriate for creating new instruments which extend their effects outside the parties of a contractual relationship. The establishment of electronic documents of title by way of custom is a very slow process. The creation of concepts and recognition for electronic equivalents to documents of title and negotiable instruments is best achieved through legislation. Private contractual systems should be able to tackle the details and to incorporate new technology.

In some jurisdictions, the formation of transport contracts using incorporation by reference is not watertight. The contract instrument repositories of trading platforms such as Bolero User Support Resources are useful in this regard since they are maintained by a third party, the system operator.

Transport liability regimes create points of conflict, and in particular sea transport conventions allow the carrier many defences, the invoking of which creates tension between the carrier and the shipper or the consignee. Therefore streamlining liability provisions, while at the same time trying to eliminate conflicts between legal regimes and instruments, serves the interests of facilitating electronic trading platforms.

Such changes may be opposed by shipping and insurance industries. All parties to a trade transaction should, however, try to compare the reduction of costs of paperwork and claims handling on the one hand to potentially increased liabilities on the other.

The expressions of the functional equivalent approach in respect of transport documents act as a ´first aid kit´. Electronic records recorded in registries do not operate exactly in the same way as paper documents. The ´originality´ of an electronic document does not exist in the same manner as that of paper documents. Therefore precise legislation is needed to define the functions and operation of electronic transport documents. Governments should, however, already consider implementing the provisions of the UNCITRAL Model Law on Electronic Commerce as regards transport documents, since doing so reduces doubts regarding the basic legal framework and facilitates thereby contractual arrangements with further detail.

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[239] E.g. the effect of retention of title clauses on the rights of a holder of a bill of lading is governed by national law.

VII TOWARDS ELECTRONIC LETTERS OF CREDIT AND CONTRACT GUARANTEES

As elaborated in the previous two chapters, the documentation used in international trade plays a part in fulfilling the seller´s delivery obligations under the contract of sale. It has, in some cases, a role in transferring property rights between the seller and the buyer and conferring security rights, or a controlling function that works partly to the same effect. The seller and the buyer, or their agents, are normally parties to a contract of carriage, and transport documents have varying functions in respect of the right of controlling the goods, the right of claiming the goods from the carrier and the transfer of contractual rights and obligations[1] vis-à-vis the carrier. Should the goods be lost or damaged during the sea voyage or other part of the carriage, a document entitling to indemnification from cargo insurance or evidencing a contractual right to claim damages being part of trade documentation protects the buyer.

In the Introduction, documentary credits were described as the ´end product´ of the trade system. In documentary credits, namely, trade documents have a role in fulfilling the seller´s delivery obligation in terms of documents and the buyer´s prime obligation to pay the price, very often in transferring property rights (notably by extinguishing the effect of a retention of title until goods are fully paid for), and in transferring, as between the seller and the buyer, the right of control, the right to claim delivery, and other rights and obligations relating to the contract of carriage. The essential feature of documentary credits, however, is to obtain external security for the buyer´s payment obligations. That security is given by banks, whose own position is regularly secured by the same trade documents which change hands through them. Banks may, alternatively, assist the seller in obtaining the price from the buyer through documentary collections.

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1 With some exceptions, like the US law.

Documentary credits and documentary collections are also payment methods. In documentary credits, the bank usually gives an irrevocable payment undertaking against the presentation of stipulated commercial documents. The same type of irrevocable payment undertaking can be given as a standby facility. In demand guarantees and standby letters of credit, the bank´s liability arises when certain, stipulated documents such as a written statement of default is presented to it. The bank´s duty to examine the documentation and the role of the documentation (albeit somewhat different in nature) in triggering an autonomous payment obligation remains the same. These aspects will be examined in some detail in this chapter.

VII.1 Documentary credits

Documentary credits (or letters of credit) have been used for almost two centuries. Throughout their history, the use of documentary credits has been more common during periods of financial instability. Uncertainty of the buyer´s credit status is a central factor in assessing the need to use letters of credit.[2]

The role of documentary credits in international trade payments has been reduced proportionally during the past decades, but considering the enormous growth of world trade, the volume of sales involving documentary credit operations is still substantial. Using documentary credits could be seen as a logistical problem adding costs and complexities, but this takes always place in exchange for security. It is still very much unknown how an eventual automation of credits might change the picture. There will at least be the chance that automation will ultimately create a cheap and secure (in terms of forgery) means of obtaining transaction- and object- related trade security, at the same time protecting the seller, the buyer and the banker as the middleman. For smaller and medium-sized operators in international trade especially, such facilities could be particularly useful.

VII.1.1 Documentary credits and open account trading

Payment terms under contracts for sale have not been harmonised in the same manner as the terms of delivery in INCOTERMS 2000.[3] For the purposes of this study, it suffices to make a distinction between documentary payment methods (i.e. documentary credits and documentary collections) on the one hand, and open account trading on the other.

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2 Pasanen, pp. 314-315.

3 However, the abbreviations for terms of payment have been harmonised under the title ´PAYTERMS´ and apply to commercial transactions relating to the provision of goods or services (UN/CEFACT Recommendation No. 17). Some national courts, e.g. in Italy, still contest that the Incoterms regulate delivery, and see it as regulating certain obligations between the parties, see Chapter V, *ante*.

Documentary payments are used when the seller wants security in case he has doubts as to the credit-worthiness of the buyer, giving the latter at the same time a means of controlling payment. If the seller does not need this protection, or he is not prepared the bear the costs of using documentary credits, he may stick to open account trading. When the seller decides to use open account trading (or his export credit facility allows him to do so), a guarantee from banks may still be used to cover the country risks.

There is a tendency in industry to move away from the use of documentary credits. This is partly because of reduced country risks in some developing countries.[4] Moreover, the use of the existing paper-based documentary credit is becoming more and more complicated. The checking procedure becomes more expensive. It is difficult to attain the standard which is required of the bankers to apply to the details of the documents. New types of paper documents are called for to be used in documentary credits. Therefore the fees have gone up.[5]

In addition to their payment and guarantee function, documentary credits are also political instruments by protectionist governments to control supply and demand.[6] The use of documentary credits may be a mandatory requirement in either the seller´s or the buyer´s country to comply with export or import regulations, often for foreign exchange control purposes.

Furthermore, in some geographical areas, documentary credits are used as a means of securing pre-shipment finance.

VII.1.2 Documentary credits in their traditional payment function

Documentary credits were, for a very long time, traditional letters of credit where the credit was used to secure payments. A documentary credit within the meaning of the Uniform Customs and Practice for Documentary Credits is defined in Article 2 of those rules. This definition[7] also includes standby letters of credit. In broad terms, however, a traditional or commercial documentary credit provides a promise by a bank of immediate or future payment against the presentation of documents to the bank or its agent.[8] The payment may be made

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4 See Kevin Godier, Trends show a declining reliance on letters of credit, Documentary Credits Insight Vol. 7 No 3, July-September 2001, pages 1 and 23.

5 Note (in 1994) by Ernst Deeg for the Working Party on Electronic Credits, ICC doc No E100-21/3., p. 5. Documentary credit fees may amount to approximately to 1-2% of the invoiced value.

6 See Mark Ford, Governments use L/Cs for economic and political ends, Documentary Credits Insight Vol. 7 No 2 Spring 2001, p. 1 and 23.

7 Article 2 (Meaning of Credit) of UCP 500 provides:

"...the expressions ´Documentary Credit(s)´ and ´Standby Letter(s) of Credit´ mean any arrangement, however named or described , whereby a bank (the ´Issuing Bank´) acting at the request and on the instructions of a customer (the ´Applicant´) or on its own behalf, is to make a payment to or to the order of a third party (the ´Beneficiary´), or is to accept and pay bills of exchange (Draft(s)) drawn by the Beneficiary, authorises another bank to effect such payment, or to accept and pay such bills of exchange (Draft(s)), or authorises another bank to negotiate, against stipulated document(s) provided that the tems and conditions of the credit are complied with."

for goods or, less commonly, for services. A documentary credit is therefore a means of providing payment by substituting a bank for the buyer as the party who will effect payment to the seller. Payment is made against the documents which represent the goods which have been shipped and are in transit.[9]

Instead of using a documentary credit, parties may agree that payment shall made against specified documents presented by the seller to the buyer directly. The seller would then have only the buyer´s undertaking to pay. Should the buyer for some reason fail to respect his commitment, the seller could only resort to the remedies provided for in the contract or legislation. An irrevocable letter of credit gives the parties security. Payment under a documentary credit is a contractual obligation under the contract of sale. A direct claim of payment cannot be made by the seller to the buyer.[10]

VII.1.3 The operation of a commercial letter of credit[11]

A letter of credit transaction can be a three- or four-partite arrangement. In a three-partite arrangement, *the issuing bank* (the bank which is requested by *the applicant* to open the credit) undertakes to make payment to *the beneficiary* provided that the terms and conditions of the credit are met. Normally the documents must comply with the conditions of the credit and they must be presented at a certain time in a certain place.

As the beneficiary is normally in a different country, the issuing bank normally uses a correspondent or *advising bank* to accept the documents and thereafter remit them to the issuing bank. This makes the credit a four-partite arrangement. It will then be the duty of the issuing bank to check the documents to see whether they conform to the conditions of the credit. If not, it sends a notice of refusal to the advising bank.The advising bank may have *confirmed* the credit thus creating a commercial undertaking to respect the conditions of the credit, in addition to the undertaking of the issuing bank. If the beneficiary presents the documents to his bank which acts as an agent, the credit is a ´negotiation credit´ and the bank concerned is *the negotiating bank*.

Thus when the beneficiary, in other words the seller, has shipped the goods, or done anything else that is necessary to bring into being or to obtain the documents needed to operate the credit, he presents them to the bank to which

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8 Jack, p. 2.

9 As a matter of fact no transport document need be designated for the credit. Parties are free to choose the required documentation. It is however within the logic of the credit to require a document indicating shipment.

10 The situation becomes more complicated if one of the parties, especially one of the banks, goes bankrupt whilst having the L/C amount in its account. For insolvency situations in connection with documentary credit, see Lars Gorton, Remburs som betalning, Juridisk Tidskrift vid Stockholms Universitet, Årgang 15, 2003-04, Nr 1, pp. 28-55, this article also analyses a Swedish Supreme Court case (*Nordea/Jula Boats*) reported in Nytt Juridiskt Arkiv 2002, p. 412.

11 The presentation largely follows that of Jack, pp. 1-8.

presentation under the credit is to be made. This bank may be the advising bank or the issuing bank itself. After the banks have checked the documents, they are presented to the applicant buyer, who may accept them, inter alia in order to claim delivery from the carrier, or reject them. While accepting the documents, the buyer pays the price unless other arrangements are made between the issuing bank and the buyer as applicant.

The principal function of the credit is to provide security. A seller can be confident only if there is an undertaking by the bank to pay in given circumstances in which case the credit should be *irrevocable*. A revocable credit is one which may be cancelled or amended by the bank undertaking to pay without the beneficiary´s consent. An irrevocable credit, however, can be cancelled or amended only with the consent of the applicant, the issuing bank and the beneficiary.[12]

Behind the documentary credit, there is an underlying transaction, most commonly a contract of sale, which has earlier been entered into between the applicant and the beneficiary. The contract of sale provides that the credit should be opened in accordance with certain terms. However, the credit is thereafter independent of the terms of the underlying contract (the autonomy of the credit, see *infra*).

VII.1.4 Special types of commercial letters of credit

Commercial practice has created special types of credit. One of them relates to the expiry of the credit. Article 42(a) of the UCP namely provides that all credits must stipulate an expiry date and a place for presentation of documents for payment, acceptance, or with the exception of freely negotiable credits, a place for presentation of documents for negotiation. If a letter of credit contains an evergreen clause it is extended automatically without amendment for another fixed period from the expiry date unless the bank notifies the beneficiary within a certain time-limit that it has elected not to renew the credit.[13]

Where a buyer is a regular customer of the seller, the buyer may arrange a revolving credit in favour of the seller. The buyer gives the bank standing instructions to arrange for a credit in favour of the seller which at no time shall exceed a fixed maximum. A revolving credit does not need renewal.[14]

The documents presented under a letter of credit usually require a transport document evidencing shipment. If the seller wants to have an advance at any

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12 Article 6 of UCP 500 provides: "A credit may be either revocable or irrevocable. The credit, therefore, should clearly indicate whether it is revocable or irrevocable. In the absence of such indication the credit shall be deemed to be irrevocable. There are irrevocable credits with partial responsibility as well."

It may mentioned that the present plans to revise the rules and to create UCP600 seem to discard revocable credits altogether.

13 Schmitthoff, Export Trade, Eighth Edition 1986, p. 188.

14 Schmitthoff in *op. cit*. p. 200-201. A concrete example is said to be the following: A revolving credit of EUR 50,000 open for three months to be operated on by drafts payable within 30 days, and as drafts are drawn they temporarily reduce the amount of the credit below EUR 50,000. As the drafts run off and are presented and paid they are added again to the top of the credit and restore it again to EUR 50.000.

stage before that, the parties may agree on a packing credit or a red clause credit, where the documentary requirements are less stringent.

Where goods are sold and resold by several middlemen before being bought by the ultimate purchaser (´string contracts´), the credit opened by the ultimate purchaser in favour of his immediate seller is used by the latter as security for the credit which he has to open for his own supplier. These credits being identical in terms (except for price) are called back-to-back credits[15] and can be executed with one bank being responsible or between different banks.[16]

The letter of credit is not negotiable[17] in the sense in which a bill of exchange or other negotiable instrument is. The advising bank is not authorised, unless receiving instructions to the contrary, to pay the amount of credit to any person whomever satisfying the conditions of the credit. Credits are namely transferable only if so designated by the issuing bank, which it does on the basis of an agreement by the parties. A'transferable credit requires agreement by the parties and the credit as such is transferred to a new beneficiary with the rights and obligations involved therein. When a commercial letter of credit contains a statement that the credit is transferable, the beneficiary can use the credit to finance the purchase of the goods in a simultaneous purchase-and-sale transaction.[18] A second possibility is that the benefit of the credit is assigned to a new person (assignment of proceeds). An assignment of proceeds is permitted regardless of whether the credit is designated as being transferable.[19]

According to Article 48 of UCP500, the credit may be transferred only once. If a credit is designated as transferable, it may be divided into separate parts without specific authorisation by the bank. Moreover, the fractions of transferable credit can be transferred separately if partial shipments or drawings are not prohibited.

The legal implications of the transfer of the credit are in dispute since legal scholars often see the transfer of the credit as an assignment (which is a case different from the assignment of proceeds).[20] The prevailing view is that the transfer of a credit constitutes a new and separate undertaking of the bank to the new beneficiary.[21] The law governing the assignment determines the legal requirements for it. Certain domestic laws stipulate strict requirements for a valid assignment.[22]

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15 The credit opened by the ultimate purchaser is called the ´overriding credit´.

16 Schmitthoff in *op.cit.*. p. 202.

17 Not to be confused with a ´negotiation credit´, which is mentioned *supra*. Nowadays, ´negotiable´ documentary credits are sometimes used to provide the seller with an advance prior to payment by the opening (issuing) bank (a note in the ICC Doc ECP WG 1/13, 12.10.1998, p. 58).

18 Turner, Transferable standby letters of credit, DCI Vol. 9 No 2, April-June 2003, p. 18. See also Jean Meng Chen, Transferable L/Cs: beware of the unconventional, DCI Vol. 10 No 3, July-September 2004, pp. 13-14.

19 Article 49 of UCP500. Schütze & Fontane, p. 39.

20 Schütze & Fontane, p. 38, Jack, p. 242.

21 Schütze & Fontane, p. 39.

22 Ibid.; French law, for instance, requires that the bank as creditor shall receive a notification of the assignment served by a bailiff.

VII.1.5 The contracts set up by a letter of credit

After a letter of credit has been opened by the applicant, in accordance with the underlying contract of sale, there is a chain of three further potential contracts that are or will be established in the various relationships.

Firstly, when the issuing bank agrees to act on the instructions of the applicant a contract, involving rights and obligations on each side, comes into being between them. Secondly, when a correspondent bank agrees to act on the instructions of the issuing bank and to advise or confirm the credit and to take on whatever further roles the instructions require, a contract comes into being between the two banks with rights and obligations on each side. Thirdly, when an advising bank has confirmed the credit, there is a contract between this confirming bank and the beneficiary. However, this ´contract´ between the confirming bank and the beneficiary must be unilateral, since the benefiary gives no undertaking to the bank.[23]

VII.2 Standby letters of credit and contract guarantees

An irrevocable payment obligation by a bank can be used, not only as secure means of payment, but also as a means to secure the commercial interests of trading partners, should a default occur in a contractual relationship causing delay or financial losses. For these purposes, markets have developed contract guarantees, the relationship of which to the underlying commercial relationship may vary from completely independent (guarantees or bonds payable on first demand) to purely accessory guarantees.

Letters of credit are used to guarantee contractual undertakings as well. This is to a great extent a historical coincidence. During and after the recession of the 1930s in the United States, banks were forbidden to act as sureties.[24] Ingenious bankers started to use the concept of letters of credit for issuing guarantees. This provoked discussion in the United States on whether standby should be treated in law as a guarantee.[25]

The standby letter of credit resembles the traditional documentary credit in that it is issued by a banker and embodies an undertaking to make a money payment to the beneficiary against a document. It differs from the normal

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23 Todd, Documentary Credits Insight, Vol 6 No 2, p. 8. However, if the advising bank does not confirm the credit, no contract is created between the advising bank and the beneficiary.

24 ´Surety´ is a person who binds himself, usually by deed, to satisfy the obligation of another person, if the latter fails to do so. (Osborn´s Concise Law Dictionary, 7th Edition by Roger Bird, London 1983, p. 317) In other words, a surety is a guarantor whose obligation to pay is secondary. It is regularly used within the meaning of conditional accessory guarantee.

25 Goode, Commercial Law, p. 696, and the articles referred therein.

documentary credit in that it is furnished by way of security, not by way of payment. In normal documentary credit operations the undertaking embodied in the issue or confirmation of a credit is a primary obligation. The seller can obtain payment from the issuing or confirming bank (if a confirming bank is involved with the credit) and cannot claim payment from the buyer directly, unless the credit is dishonoured. In a standby letter of credit, however, a payment by the bank is envisaged only if the principal defaults in his obligations.[26]

A standby letter of credit is close to a guarantee payable on first demand. The United Nations Convention on Independent Guarantees and Stand-by Letters of Credit[27] is a legislative instrument to address the practically identical problems relating to these. In the terminology of the Convention the ´principal/applicant´ is the customer of a bank (´principal´ used in guarantees and ´applicant´ used in standbys), the other institution or person is called the ´instructing party/issuer´ (likewise ´instructing party´ for guarantees/´issuer´ for standbys) and the undertaking may be given in favour of the ´beneficiary´ by the ´guarantor´/´confirmer´ at the request of the principal/applicant or on the instruction of the instructing party/issuer who acts at the request of the principal/applicant. The instructing party/issuer may give an undertaking directly, but in many countries the involvement of a local bank is necessary. The standby is regularly used in the United States and in South-East Asia, whereas demand guarantees are more commonly used in Europe and in the Middle East. Standby letters of credit are used for more wide-ranging commercial purposes than independent guarantees, which may not necessarily depend on the characteristics of each, but may reflect commercial tendencies in banking.[28] The use of standbys has expanded and they are now even more commonly used outside the United States than they are inside. The aggregate amount involved in standbys has overtaken the amounts

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26 The difference as described by Goode in *op cit*. p. 696.

27 For the Convention, see *infra*.

28 It is submitted that the use of standbys for a greater variety of commercial purposes may be reflected in how these are reflected in the relevant ICC publications. Typical uses for demand guarantees under URDG 458, and for which uses express model forms are published (ICC publication No 503) are

(a) performance guarantees (or bonds), which support an obligation to perform other than to pay money including for the purpose of covering losses arising from a default of the principal in completion of the underlying transactions,

(b) advance payment guarantees, which support an obligation to account for an advance payment made by the beneficiary to the principal,

(c) bid or tender guarantees, which support the obligation of the principal to execute a contract if the principal is awarded a bid,

(d) warranty (maintenance) guarantees which support an obligation of the principal to provide maintenance in connection with and after goods or services are supplied or works concluded, and

(e) retention money guarantees, which support the obligation of the principal to maintain warranty in connection with the supply of goods or services and enable him to have the sums retained by the beneficiary covering the principal´s warranty obligations released against this guarantee. >>

involved in commercial letters of credit. The main rule is that a standby letter of credit is not transferable, unless it states so.[29]

VII.3 Documentary credits as compared to documentary collections

There is another traditional documentary means of payment, which is less complicated but also less frequently used than letters of credit. The exporter ships the goods and gives his bank the trade documents, which the importer (buyer) needs for delivery and import purposes. If the transport document is a bill of lading, the buyer cannot take delivery without surrendering this document to the carrier.

The standard collection procedure is the reverse to the letter of credit transaction in the sense that the exporter (seller) of the goods is collecting the price of the goods through one or more banks and the payment against documents is made close to the buyer´s location. Thus the importer (buyer) does not thus apply for the arrangement, although its use is normally based on a provision in a sales agreement.

In a collection, the ´principal´ is entrusting the handling of a collection to the ´remitting bank´, which may use another, normally foreign bank as the ´collecting bank´ to participate in the collection as eventually presenting documents as the ´presenting bank´ to the ´drawee´. The principal is frequently a seller who is sending documents evidencing inter alia the shipment of goods to be collected from the drawee, who is the buyer of the goods. A collection may be ´clean´ in which case only financial documents are collected or ´documentary´, which includes commercial documents.

<< ISP98 mentions, in addition to most above situations, other uses for standbys as independent undertakings:

(f) financial standbys support an obligation to pay money, including any instrument evidencing an obligation to repay borrowed money,

(g) direct pay standbys support payment when due of an underlying payment obligation typically in connection with a financial standby without regard to a default,

(h) insurance standbys support an insurance or reinsurance obligation of the applicant (ISP98 uses, like UCP500, the term ´applicant´ to denote the person who applies for the issuance of the credit or for whose account it is issued; it is to be understood here in the same way as the concept ´principal´ in URDG 458)

(i) commercial standbys support the obligations of an applicant to pay for goods or services in the event of non-payment by other methods.

Both publications mention either ´counter-guarantee´ or ´counter-standby´ as a tool to support the issuance of a separate guarantee or standby by the beneficiary of the counter-guarantee or counter-standby.

As the Preface of ISP98 rightly states, these classifications are made, for convenience, descriptively and based on their function in the underlying transaction and without operative significance in the application of the relevant Rules. However, as stated in the Prologue of ISP98 by Dr. Gerold Herrmann, Secretary general of UNCITRAL, some types of actual use, e.g. financial standby and direct-pay standby, have hitherto been extremely rarely found in guarantee practice.

[29] See the article ´Transferable standby letters of credit´ by Paul Turner, DCI Vol. 9 No 2, April-June 2003, pp. 18-19.

Documentary collections first became a popular payment technique for export sales in the 1930s. The system continued to work well until the mid 1960s when goods started to move more quickly than mail.[30]

The ICC published its first Uniform Rules for Collections in 1957, and these rules have been revised in 1978 and 1995.[31] The latest version of the Uniform Rules for Collections, ICC publication No 522, (acronym URC522) came into force in the beginning of 1996.

VII.4 The role of bills of exchange in documentary payment systems

Bills of exchange are used in international trade with or without the use of documentary payment systems. In fact, a payment by accepting a bill of exchange drawn on the buyer is documentary in the sense that a bill of exchange is a negotiable instrument. The regulation of bills of exchange and their form is already one issue in international trade as such. In this context, I limit myself to looking briefly into the role of bills of exchange in documentary credits and documentary collections. It is common to draw a distinction between international and other bills of exchange.

A bill of exchange within the meaning of the United Nations Convention on Bills of Exchange and Promissory Notes from 1988 is "a written instrument which contains an unconditional order whereby the drawer directs the drawee to pay a definite sum of money to the payee or to his order, is payable on demand or at a definite time, is dated and is signed by the drawer".

An international bill of exchange within the meaning of the same Convention is "a bill of exchange which specifies at least two of the following places and indicates that any two so specified places are situated 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, and (e) the place of payment, provided that either the place where the bill is drawn or the place of payment is specified on the bill and that such place is situated in a Contracting State".

Under English law[32], a bill of exchange is defined in Section 3 of the Bills of Exchange Act 1882 as "an unconditional order in writing, addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand or at a fixed or determinable future time a sum certain in money to or to the order of a specified person, or to bearer".

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30 Rowe, p. 159.

31 For the history of the ICC, see the anniversary publication ´Kansainvälinen kauppakamari 75 vuotta´, published by the Finnish Section of the ICC in 1994 and ´World Peace through World Trade´ published by the ICC in 1979.

32 For bills of exchange in English law, see William and Richard Hedley, Bills of Exchange and Bankers´ Documentary Credits, 4th edition, London 2001.

Thus, in a bill of exchange structure, there are three original parties. These are the *drawer*, the *drawee* and the *payee*. The drawer and the payee, or the drawee and the payee may be the same persons, but where the drawer and the drawee are the same persons, the bill is in fact also a promissory note.[33] A bill of exchange is also called a ´draft´, which is the term used by the Uniform Customs and Practice for Documentary Credits UCP500.

Bills of exchange also play a role in documentary collections. If the documents are presented and released for payment, the question is of Documents Against Payment (D/P), and if they are presented or released against acceptance of a bill of exchange, a Documents Against Acceptance (D/A) is concerned.[34]

VII.5 The regulatory framework for documentary credits

The use of documentary credits is governed by a multitude of legal rules, the main part of which is contractual. Still, legislation plays a certain role. Due to this, and since a documentary credit constitutes several contractual relationships, one has to determine the general contract statute for each facet of the documentary credit operation.

VII.5.1 Private rules vs. legislation

Documentary credits are a field where harmonisation of international legal rules has taken place to a great extent under the private sector´s umbrella. This has not been a result of international intergovernmental conventions, but has been materialised through the cooperation of banks[35] under the auspices of the International Chamber of Commerce.

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33 The ´maker´ under Article 3(2) of the United Nations Convention; for English law treatment, see Scmitthoff Export Trade, Eighth edition, pp. 319-320.

34 As bills of exchange are not adapted to electronic commerce (see Chapter VIII.2.2.1. , *post*), Guide to the eUCP, p. 18 mentions with regret a case where a deferred payment undertaking was not the equivalent of a banker´s acceptance in a given situation, see *Banco Santander SA v. Banque Paribas, [2000] 1 All ER (Comm) 766*.

35 It would be tempting for a the bankers to see Uniform Customs and Practice for Documentary Credits as a sheer banking product. Indeed, the ICC Commission of Banking Technique and Practice consists practically exclusively of bankers. However, an advantage of the fact that private rules are created by a business organisation with cross-sectoral membership consisting not only of banks, but also of trading companies, insurance companies and law firms amongst others is that both sellers, buyers and other commercial actors have, at least in principle, a say on the contents of the rules endorsed by the organisation.

It is thought that the various contract guarantee and bond rules, having been initiated in the ICC Commission of Business Law and Practice or in the ICC Commission on Financial Services and Insurance have a wider spectre of drafters than the UCP. It should be added, however, that all ICC rules are commented on by the various national committees of the ICC and are finally adopted by the general decision-making bodies of the organisation.

The first set of the Uniform Customs and Practice for Documentary Credits was adopted by the ICC in 1933.[36] Before that there had been attempts to harmonise rules applicable to documentary credits by national banking associations.[37] This version was acknowledged and used by banks predominantly in Belgium, France, Germany, Italy, Romania, the Netherlands and Switzerland.[38]

After the Second World War, there was a revision of the UCP in 1951.[39] The 1951 version of the UCP gained more ground than its predecessor, and was also accepted in the United States. But it was only the 1962 Revision[40] that secured the approval of banks in the United Kingdom and most Commonwealth countries. This revision made changes that were previously objectionable to British banks. The 1962 revision purported to adjust the UCP to the developments in trade and to create security by a more precise wording of the rules. The 1962 version came close to universal adoption by being acknowledged by banks in 178 countries and territories.

A third revision, the 1974 Revision[41], came into effect in 1975 and was more comprehensive than the earlier versions. Containerisation and the use of combined transport documents were reasons for that revision.

The two latest revisions (1983 producing UCP400 and the 1993 Revision producing UCP500) have largely been motivated by the same developments. Firstly, there have been developments in transport technology by the spreading of multimodal transport and containerisation and, secondly, the trade facilitation activities for the development of new documents and new methods of producing documents. A third factor has been the communications revolution, replacing paper as a means of transmitting information (data) relating to a trade transaction by methods of automated or electronic data processing. Furthermore, the development of new types of documentary credits, such as the deferred payment credits and the standby credit, as well as the increasing interest and influence in international trade of less developed nations have been mentioned as reasons for the revision.[42]

The 1993 revision tried largely to achieve simplification of UCP 400 in order to incorporate international banking practices, facilitate and standardise developing practices, enhance the integrity and reliability of the documentary credit undertaking, and address the problems of non-documentary conditions and

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36 It carried the ICC publication number 69.

37 These include the regulations adopted by the New York Bankers´ Commercial Credit Conference in 1920, the *´Clauses et modalités applicable aux ouvertures de crédit documentaire par l´union syndicale des Banques de Paris et de la Provence´* adopted in 1924, as well as the German *´Regulativ für das Akkkreditivgeschäft der Berliner Stempelvereinigung´* of 1923.

38 Schütze & Fontane, p. 11 referring also to Taylor, The History of the UCP, 2000 Annual Survey 201. The Finnish banks came on board as users of the UCP at the beginning of the 1950s.

39 ICC Publication No 151.

40 ICC Publication No 222.

41 Jack, p. 8.

42 See ICC Publications Nos 459 and 511.

to list in detail the elements of acceptability for each category of transport document.[43]

In addition to UCP500, the ICC has adopted special rules for bank-to-bank reimbursements. There is no possibility for going into the detail of those rules here.[44]

A new revision of the Rules is to be anticipated to enter into force in, say, 2006/2007.[45] A task force has been appointed to develop a strategy for a future UCP revision.[46] The ICC Banking Commission has, however, been able to agree on a preliminary review of seven Articles[47] of UCP500 that had generated the most queries.

Despite some early thoughts, the revision has proceeded on an article-by-article basis. The ICC has carefully involved the other sectoral Commissions in the revision, which should be commended.

VII.5.2 The nature and role of the UCP

According to Article 1 of the 1993 revision (UCP500), the rules shall apply to all documentary credits[48] where they are incorporated into the text of the credit. The application of the rules therefore requires, in principle, incorporation. They might, however, become applicable even without incorporation, for instance, where a court applies it as a banking custom.

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43 The Preface of UCP500 is written by Charles Del Busto, Chairman of the ICC Banking Commission. The means to enhance reliability and integrity were to create a presumption of irrevocability and clarification of the primary liability of both the issuing and confirming bank.

The publication of four Position Papers of the ICC Banking Commission soon after the introduction of UCP500 further clarified the interpretation of the rules.

44 ICC Publication No 525. It can only be mentioned that bank-to-bank reimbursements relate to the situation where an issuing bank arranges that the reimbursement to which a paying, accepting or negotiating bank is entitled, shall be obtained by such bank (the ´claiming bank´) claiming on another bank (the ´reimbursing bank´) by providing such reimbursing bank with the instructions and authorisation to honour such reimbursement claims.

45 An estimate by Mr. Gary Collyer, the chair of the Drafting Group at an ICC Finland seminar in Helsinki on 25 May, 2004.

46 The six person task force had recommended to the ICC Banking Commission that there should be no article-by-article review of UCP500. Instead, the task force recommended that the next update of the Rules should only focus on Opinions and Decisions of the Banking Commission, such as the Decision on Original Documents, on legal cases that have had a direct impact on the understanding and application of the UCP, as well as whether to incorporate in the UCP portions of separate publications such as ISP98, URR525 and the eUCP (Documentary Credits Insight Volume 8 No.2, April-June 2002, p. 28.

47 These were Article 9 (liability of issuing and confirming banks), Article 13 (standard for examination of documents), Article 14 (discrepant documents and notice), Article 21 (unspecified issuers or contents of documents), Article 23 (marine/ocean bill of lading), Article 37 (commercial invoices) and Article 48 (transferable credit).

48 Including to the extent to which they may be applicable, standby letters of credit. If the automated international transfer system SWIFT is used by banks in letter of credit transactions, the UCP apply to the contractual relations between the banks and between them and SWIFT.

The UCP is often regarded as codified commercial customs, customary law or as statutes having a *sui generis* character. In all these cases, the UCP would apply without incorporation, unless the contrary is expressly provided. In many jurisdictions, however, the UCP are treated as a set of standard business conditions which become part of the agreement if the parties explicitly so agree, or their conduct implies that it is the parties´ intention to make the UCP apply.[49] Some jurisdictions subject the application of the UCP to certain conditions imposed by laws, the objective of which is to protect the weaker party.[50] It should be borne in mind, though, that the UCP are, at least in principle, an agreed document, which has been formally adopted by a cross-sectoral business organisation.

Under English law, the UCP do not have the force of law, and neither do they have the status of a trade custom, and the same is found under French law.[51] In the United States, where there are detailed statutory provisions on letters of credit in the Uniform Commercial Code, the UCP prevail if the parties agree on its application.[52] In certain states of the United States, most notably the State of New York, the provisions of the Uniform Commercial Code on letters of credit are replaced by the UCP, not only where the parties have agreed to apply them, but where they are customarily applicable. In Belgium, however, the UCP have been regarded as customary law.[53] In Sweden, the doctrine may have given the UCP the status of customary law.[54] I would think the same applies in Finland, although I doubt that very many such cases would exist where banks offer documentary credit services without resorting to the disclaimers offered by the UCP.

The authors Rolf A. *Schütze* and Gabriele *Fontane* of ICC Publication No 633, *Documentary Credit Law throughout the world,* consider that "the unique character of the UCP as a system of rules that are accepted and acknowledged by all concerned parties, and that [concerns] multiparty interests and their international effect, does not permit comparison of the UCP with any existing scheme of law or contractual provisions". Schütze and Fontane therefore regard the UCP as *´sui generis* rules´, which "at some time in the future, might attain the quality of a *lex mercatoria*".[55] Another way of looking at the matter is to regard the UCP as a

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49 Schütze & Fontane, p. 13.

50 Ibid.

51 Schmitthoff, Export Trade, Eighth Edition 1986, p. 338. For a more recent view with more or less the same effects, see Roger Fayers, Legal inroads on the autonomy of the letter of credit. DCI Vol. 10 No 2, April-June 2004. For France, Schmitthoff refers to *Cour de Cassation, October 14, 1981, in Recueil Sirey-Dalloz, 1982, 301*. See, however, Stoufflet, J., Le crédit documentaire; étude juridique d´un instrument financier du Commerce International, Paris 1957, p. 109 et seq., as referred to by Gorton, p. 43.

52 UCC § 5-116(c), Schütze & Fontane, p. 121.

53 Schmitthoff, Export Trade, Eight Edition 1986, p. 338, referring to *Tribunal de Commerce de Bruxelles, November 16, 1978; Revue de la Banque, 1980*. This approach to ICC rules is reflected in another decision of the Tribunal de Commerce (*S.A.Fabricom and S.A. Laurent Bouillet Ingéniere v. Générale de Banque and ACEC Union Minière, 15 December 1992; Revue de droit commercial belge 1993, p. 1055*), which relates to demand guarantees. Although URDG 458 had been in existence only for a few months, the court decided to apply them without having been incorporated in the guarantee but as a restatement of established trade usage in demand guarantee practice. See also Affaki 2001, pp. 152-153.

54 Gorton, p. 43.

55 Schütze&Fontane, p. 13.

formal customary law, which would mean that there would be no need to refer to the instrument.[56] When the UCP is applied, however, it would become part of the national legal system.[57] Among those favouring a *lex mercatoria* approach is Matti S. *Kurkela*, who considers the UCP as probably the clearest example of the *lex mercatoria* in contemporary international trade.[58] In the historical perspective, contrary to legal dogmatic approaches, the UCP certainly represent *lex mercatoria*, because they emanate from the business community itself which makes them autonomous, because they are universal in character, and because the business community provides instruments for their interpretation.

It is noteworthy that that the ICC itself does not try to elevate its rules into the status of *lex mercatoria*, and Article 1 of UCP500 presupposes incorporation for the application of the rules. The application of UCP500 on a standby letter of credit after the introduction of ISP98 arguably requires an express incorporation. The UCP govern, at the same time, the relationships of multiple parties.

Article 13.a of UCP500 states that "compliance of the stipulated documents on their face with the terms and conditions of the Credit, shall be determined by **international standard banking practice** as reflected in these Articles"(emphasis added). Reference to this standard was a novelty in UCP500. The international standard banking practice shall determine the scope within which reasonable care in examining the documents should be applied.[59] This provision is to be interpreted to presuppose that there are practices beyond the wording of UCP500 which should be observed.[60]

VII.5.2.1 International Standard Banking Practice codified

After the entry into force of UCP500, the experts of the ICC Banking Commission were frequently requested to interpret the Rules so as to give formulations for the international standard banking practice. These formulations were expressed in the form of opinions and decisions of the ICC Banking Commission.

In 2000, the Banking Commission decided to take a step further. It established a task force "to document international standard banking practice for the examination of documents presented under documentary credits" and issued subject to UCP500. The task force sent questionnaires to the ICC national committees, and after two years submitted its deliberations to the Commission, which approved the documented practices at its meeting in October 2002.[61] The acronym ISBP is becoming very familiar to the banking community. The standard

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56 Gorton, p. 44.

57 Ibid. Thus the general contractual principles of national law come into play.

58 Matti S. Kurkela, Pankkitakaukset kansainvälisessä kaupassa, Jyväskylä, 1993, p. 13, and Kurkela, Letters of credit under international trade law: UCC, UCP and law merchant, New York, 1985, pp. 11-21. Kurkela refers, however, to the varying requirements for legal rules to constitute part of the *lex mercatoria*.

59 UCP500&400 Compared, ICC Publication No 511, p. 39.

60 Jack, p. 144.

61 The result was published as ´International Standard Banking Practice (ISBP) for the examination of documents under documentary credits', Approved by the ICC Banking Commission, ICC Publication No 645, Paris 2003.

banking practices are said to be consistent with the UCP and the opinions and decisions of the ICC Banking Commission.[62] However, they do not amend the UCP but "explain how the practices articulated in the UCP are to be applied by documentary practitioners".[63] The parties of a documentary credit transaction are discouraged from incorporating the Practices contractually into the terms of the credit, as the requirement to follow them is implicit in the UCP.[64] Where the parties decide to derogate from the provisions of UCP500, this may have an impact on the applicability of international standard banking practices as well.

It is doubtful whether contractual incorporation of UCP500 automatically incorporates a set of interpretations regarding documentary requirements. The reference to the notion of ´international standard banking practice´ in Article 13a. of UCP500 may be too general to create binding contractual implications.[65] This may not even have been intended. However, where the UCP are considered to constitute a custom, or even part of the *lex mercatoria*, the supplementary status of the ISBP could also be approved. The business community as a group seeking guidance will certainly accept most of the ISBP, which supports the case for eventually accepting it as custom. In any case, the strengthening of this reference could be considered in a possible revision of the UCP, if harmony is sought even at a more elementary level. Some central provisions might even be incorporated in the text of next version of the UCP.

The ISBP could also be seen as a codification of the ICC Banking Commission´s opinions and decisions, which represent suggestions for international uniform application of the UCP. National courts are not bound to apply these suggestions, which are even furnished with a disclaimer, and can base their judgements on national interpretations instead. However, gathering the more relevant interpretations in one document certainly would help to bring uniformity to the application of UCP500.

VII.5.3 The law applicable to documentary credits

The Uniform Customs and Practice for Documentary Credits are nowadays incorporated in virtually all credits irrespective of where they are used. They provide for the necessary uniformity and reduce the differences that might arise when applying conflicting national laws. But, as elaborated later, the question of national law applicable to the credit is not without significance. The applicable law is relevant not only in providing the principles according to which the UCP are interpreted, but also in covering other questions of importance which are not regulated by the UCP. It is also possible that the UCP are not incorporated at all into the contract, and are neither deemed to be applied as customary law or *lex mercatoria*.

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62 The Introduction of ICC Publication No 645, p. 8.

63 Ibid.

64 Ibid., p. 9.

65 See also Paul Turner, ´Standard banking practice´ and the UCP, DCI Vol. 8 No 4, Oct-Dec 2002, pp. 12-13.

The UCP itself contain no provisions relevant to the question of which national law is applied to the credit. If they did, the incorporation of the rules to the credit would constitute an express choice of law by the parties. For comparison, the Uniform Rules for Demand Guarantees URDG 458 contain a governing law clause which covers both the guarantee and counter-guarantee relationships. According to Article 27 of URDG458, the governing law shall be, in the absence of an express provision in the guarantee or counter-guarantee, the law of the place of business of the guarantor or instructing party[66], or, if the guarantor or instructing party has more than one place of business, that of the branch that issued the guarantee or counter-guarantee.

It is ultimately for the court in the jurisdiction hearing the dispute to determine the law which it is going to apply to a dispute concerning documentary credits. The court applies for this purpose its respective conflict of laws rules. These rules may have been defined in statutory law or in jurisprudence, and the legal rules may have their origin in international cooperation.

The EU countries have incorporated into their legal systems the Rome Convention on the Law Applicable to Contractual Obligations. The Convention is partly applicable to documentary credits since it excludes from its scope inter alia "...obligations arising under bills of exchange, cheques and promissory notes and other negotiable instruments to the extent that the obligations under such other negotiable instruments arise out of their negotiable character". Futhermore it excludes the questions as to whether an agent is able to bind a principal ... to a third party.[67] On the other hand, the Convention clearly applies to the contracts set up by a letter of credit, as well as to any contract of carriage.

As said earlier, most jurisdictions recognise the possibility of the parties to choose the law applicable to their contract. Thus if the credit document contains a reference to a law governing the credit, this should, as a rule, be recognised by courts. It has to be noted, however, that the credit document is agreed on between the applicant and the issuing bank.

It is arguable that in determining the law applicable to the credit the decision could depend on the contract in question, i.e. whether the question is of the relationship between the applicant and the issuing bank, between the issuing bank and the advising, confirming or negotiating[68] bank or between the corresponding bank and the beneficiary. A choice of law clause should be effectively taken over by the corresponding bank in its relationship with the issuing bank, but one can ask to what extent does the law agreed upon in connection with the first contract be binding on the beneficiary who has a ´contract´ with the corresponding bank.

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66 The ´guarantor´ and ´instructing party´ are defined in Article 2 in a way similar to the UN Convention of Independent Guarantes and Stand-by Letters of Credit, see *supra*.

67 The questions of agency relate to the role of advising and negotiating banks.

68 All three of which can conveniently be called ´the correspondent bank´, although this term is not used by the UCP.

Since the four contracts under a letter of credit (or under a demand guarantee) are autonomous there is no requirement that the law governing them should be the same.[69] Similarly, it is generally acknowledged that the independence of the documentary credit of the underlying trade transaction makes it clear that a choice of law clause in the actual sales agreement does not extend to a documentary credit as such.[70]

In the absence of a choice of law clause, the secondary provisions of the relevant conflict of laws rules come into play. The applicable law of a documentary credit transaction should be determined considering the place to which the obligations arising under the credit have their closest and most real connection.[71] The EC Convention states that in the absence of a specific choice of law clause, the contract shall be governed by the law of the country to which it is most closely connected. Nevertheless, a severable part of the contract which has a closer connection with another country may by way of exception be governed by the law of that other country. The country of closest connection is determined on the basis of ´characteristic performance´.[72] The characteristic performance approach does not necessarily fit the needs of documentary credits.[73] Moreover, if it appears from circumstances as a whole that the contract is more closely connected with another country, the presumptions of the Convention will not apply.

Schütze and Fontane have analysed the jurisprudence of various countries and have made a number of observations.[74] Firstly, the application of the general rule that the governing law is to be determined by looking at the closest and most real connection of each contract results, in their view, in the internationally acknowledged conclusion that the law governing the relationship between the applicant and the issuing bank is the law of the issuing bank´s domicile[75]. Secondly, it is also internationally acknowledged that the relationship between the issuing bank and the beneficiary is more closely connected with the location of the issuing bank, and that the laws of the issuing bank´s location should therefore be applied.

However, it is highly disputed whether the appointment of a correspondent bank has any impact on the law governing the beneficiary´s claim to honour the credit. In civil law jurisdictions, the prevailing view is that the appointment of an

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69 Todd 1998 p. 294.

70 Schütze & Fontane, p. 26. Todd 1998, pp. 295-296.

71 Schütze & Fontane, p. 26.

72 The Convention further provides: "*It shall be presumed that the contract is most closely connected with the country 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. However, if the contract is entered into in the course of that party´s trade or profession, that country shall be 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.*"

73 Cfr. Todd 1998, p. 293, and *infra*.

74 Schütze & Fontane, pp.26-28.

75 The concept of ´domicile´ is complex in connection with a bank and one should therefore operate with the concept of ´place of business´.

advising bank does not affect the law applying to the relationship between the beneficiary and the issuing bank.[76] The performance of the advising bank is regarded as a purely technical service and does not create a closer connection to its home country than to the home country of the issuing bank.

In common law countries, however, the courts have often expressed the view that the appointment of a correspondent bank subjects the documentary credit to the laws of the place of that correspondent bank.[77] Such a bank can also be a nominated bank under common law jurisprudence. However, courts and authors in civil law countries disagree as to whether the appointment of such an agent creates a closer and more intense connection to the laws of the country of the nominated bank´s location rather than to the country of the issuing bank.[78] Some courts and legal writers see the appointment of a nominated bank as a relocation of the credit´s place of performance to the nominated bank´s domicile, and regard this as the detemining factor pointing out the applicable law. Finally, courts in most jurisdictions support the view that the confirmation of a credit triggers the application of the laws of the confirming bank´s jurisdiction.[79]

In the relationship between the issuing bank and the correspondent bank, the closest and most real connection may be determined by identifying the bank that carries out the main performance. This is normally the correspondent bank, since its performance may be held to characterise the agreement. The role of an advising, confirming or negotiating bank vis-à-vis the benefiary is considered more relevant than the correspondent bank´s entitlement to reimbursement from the issuing bank.[80]

The above presentation relates to traditional letters of credit. In credits where paper documents are replaced by electronic records, the situation should be very much the same if no additional elements are involved. The fact that the documentary credit mechanism is included in an Internet trading platform based on a central registry such as the *Bolero System* may constitute such an additional element.[81] The System is based on the Bolero Rulebook generally governed by English law, which law does not, however, extend to all substantive aspects covered by the system. Still, the existence of a system, in which the parties´ obligations are performed electronically and which operates under a particular legal framework, could be seen as a connecting factor.

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76 Schütze & Fontane, p. 27.

77 *European Asian Bank AG v. Punjab & Sind Bank, (1981) 2 Ll. Rep. 651 (657)* and *Offshore International SA v. Banco Central SA (1976) 3 All ER 749 (751).*

78 Schütze & Fontane, p. 27.

79 Sarna, Letters of Credit – The Law and Current Practice, 3rd edition 1993, pp. 9-16**,** as referred to by Schütze & Fontane, p. 28.

80 Schütze & Fontane, p. 28. Schmitthoff (Export Trade, pp. 191-192) comes to the same conclusion by stating that the weight of the facts will often point to the law of the advising bank because, as that law is likely to apply to the beneficiary, the application of two different laws to two facets of the same commercial transaction would be undesirable.

81 See Chapter VII.1.6., *post*.

VII.5.4 Legislation

Legislation is clearly in a secondary role in the legal framework governing the use of documentary credits. This is because the contractual regime has worked particularly well and because the national laws respect freedom of contract in this domain as well. Some general observations on the role of legislation can still be made.

VII.5.4.1 Questions not covered by the UCP

Despite the fact that the scope of the UCP has extended during the revisions of the past seven decades, there remains a number of issues left uncovered by the UCP. Where national legal rules, whether expressly addressing documentary credits or being general contract law rules, exist, the UCP will normally rank ahead of them, and should the UCP not provide for a conclusive solution for any question, national law will have to be consulted. The same hierarchical principle applies to specific provisions in documentary credits which have priority over any general rules.[82]

The law applicable to the credit (or the relevant contract under the credit) governs a number of aspects relating to the contractual relationship. The formation and validity of the relevant contract is governed by the applicable law. For instance, the question of whether the parties have actually agreed on the application of the UCP shall be determined by the law applying to the agreement to open the credit. That law may, in principle, impose restrictions on the application of the rules, and it determines how the UCP will be interpreted.[83]

Prescription is outside the ambit of the UCP, which do not address the statute of limitations on claims arising from a documentary credit. The expiry date of a documentary credit only stipulates the latest date for the presentation of documents. If the beneficiary presents compliant documents in due time, his claim for honouring the credit comes into effect and remains in existence until the statute of limitations applicable to that claim expires.[84] The applicable substantive law not only determines the statute of limitations of these claims, but also the suspension or interruption of this prescription.

The UCP do not especially regulate, outside the disclaimers in Articles 15 and 16, fraud or its consequences, and the question of how to deal with abusive callings. No mention is made of the effects of forgery of documents either. There are varying standards in each jurisdiction concerning the bank´s right and

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82 Fontane, The law on documentary credits, DCI Vol. 8 No 1. pp. 4-6.

83 Article 17 (force majeure) of UCP500 could be the subject of such interpretation. This Article provides inter alia that *"Banks assume no liability or responsibility for the consequences arising out of the interruption of their business by Acts of God, riots, civil commotions, insurrections, wars or any other causes beyond their control, or by any strikes or lockouts."* The words "or any other causes..." could be interpreted as being a ´catch-all phrase´, or they could be interpreted *ejusdem generis* (where particular words are followed by general words, the general words are limited to the same kind as the particular words). The interpretation appears to be the latter by most commentators. (Shütze & Fontane, p. 41)

84 Shütze & Fontane, p. 42.

obligation to refuse payment in such cases. In any case, the principles of strict compliance and autonomy of the credit require in practice that the right and obligation to refuse payment due to a misuse of the credit can only arise in exceptional cases. In addition to the evaluation of fraud, national law determines the possibilities of court intervention by way of injunctive relief and the scope of the parties entitled to apply for such a relief.

The prevention of fraud could be a matter of public policy in many or most jurisdictions. Although it is possible for the parties to choose the law applicable to the credit, it is doubtful whether any courts would allow a choice-of-law clause eliminating the fraud exception under its national law. The other way round, the question is more interesting. It could be imaginable to make a reference to the UN Convention on Independent Guarantees and Stand-by Letters of Credit, which provides a clear-cut regime for the fraud exception.[85] This Convention also deals with the competence of courts in fraud cases. Where this Convention has not been made part of national law, it is arguable that courts could still accept the competences given by it in the way they accept a choice-of-court agreement.

The UCP do not deal with financial risk allocation in the case of fraud or insolvency. This risk falls easily on the applicant, since a bank has to exercise nothing but reasonable care in examining the documents. The bad faith of the beneficiary generally falls under the buyer´s risk. National law will determine the scope of the damages[86], should the bank be found liable for negligence. Finally, the UCP do not deal with questions of currency or interest rates.

The impact that national law has, when deciding questions relating to contract formation or the validity of the contract, make it also relevant in cases where any of the four independent contracts is entered into electronically. The contract law rules of that jurisdiction come into application. Secondly, national law may impose more stringent requirements as to the presentation of documents than the eUCP do. Thereby a law imposing more affirmative requirements than the eUCP may make an electronic record unenforceable.[87]

Moreover, the approach which the law applicable takes to fraud, forgery and injunctive relief might, in all likelihood, become relevant in an electronic environment as well. It would therefore be desirable that all four contracts be governed by the same law, by necessity based on a uniform choice of law clause, in addition to a comprehensive uniform contractual framework, such as the *Bolero Rulebook,* under which transactions are carried out.

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85 There is an option in the Convention to apply it to commercial letters of credit (Article 1(2)).

86 For instance the extent to which consequential loss will be compensated.

87 The Guide to the eUCP (p. 19) refers to sub-Article 18(d), Disclaimer for Acts of Instructed Party shifting the risk of compliance with laws other than those of the issuer. When the issuer´s law causes problems, this should be tackled by a choice of law clause in the bank´s general conditions.

VII.5.4.2 National law provisions concerning letters of credit

There is a difference in how national laws treat documentary credits. An excellent survey on this has been carried out by Schütze and Fontane in their treatise.[88]

If national laws treat documentary credits in particular, such provisions rank ahead of more general provisions of law.[89] In many parts of the world, legal systems do not have special laws on documentary credits. For instance, except for Greece, all member states of the European Union treat documentary credits under general principles or statutes, and the written laws of many countries do not even spell out the term ´documentary credit´ even though the instrument is recognised by courts and legal doctrine and is widely used in practice.[90]

The most comprehensive set of statutory provisions on letters of credit can be found in the United States. In 1952, a model law on letters of credit was introduced as Article 5 of the Uniform Commercial Code. All US states finally adopted this model law. In 1995, Article 5 of UCC was revised and has been enacted in virtally all states in the US.[91] The revised UCC § 5-116(c) reflects the previous acknowledgement by case law that the UCP prevails if the parties agree on their application. However, the provisions mentioned in the revised UCC § 5-103(c) cannot be modified.

Article 5 of the UCC provides, generally speaking, fallback rules if the parties agree on the application of the UCP, but the UCP does not address a particular question. In covering practicalities and techniques, the UCC comes very close to the UCP. It does not contain a detailed list of requirements for transport documents. Its wording is slightly more stringent than the UCP in stating, in § 5-108(a), that an issuer shall honour a presentation that "appears on the face strictly to comply with the terms and conditions of the credit". A major difference to the UCP is that UCC § 5-9 regulates the effects of fraud.

According to Fontane[92], typical documentary credit statutes contain a definition of the documentary credit, distinguish between revocable and irrevocable credits, deal with the liability of the banks involved, refer to the

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88 Their work ´Documentary Credit Law throughout the world; annotated legislation from more than 35 countries´ (ICC Publication No 633) contains provisions of national legislation from 35 countries. These are in alphabetical order: Austria, Bahrain, Bolivia, Bulgaria, Canada, Colombia, the Czech Republic, Egypt, El Salvador, Germany, Greece, Guatemala, Honduras, Hungary, Iraq, Israel, Kuwait, Libya, Malaysia, Mexico, Oman, Qatar, Russia, Singapore, Slovakia, Sudan, Switzerland, Syria, Tunisia, Turkey, the United Arab Emirates, the United Kingdom, the United States of America, Yemen and Yugoslavia.

At the end of their book, Schütze and Fontane list 84 countries which are not known to have specific rules on documentary credits. One of these countries is Ukraine. Your author, however, recalls from his period as the Secretary General of the Finnish Section of the ICC that in the middle of 1990s Ukraine was reported to have implemented UCP400 in its legislation although UCP500 was already in force. This matter was verified by the International Secretariat of the ICC. It is not known to the author what happened to Ukrainian law thereafter.

89 *Lex specialis derogat lex generalis,* as the well-known legal maxim goes.

90 Fontane, The law on documentary credit, DCI Vol. 8 No 1, January-March 2002, pp. 4-5.

91 Schütze & Fontane, pp. 120-132.

92 Fontane, The law on documentary credit, DCI Vol. 8 No 1, January-March 2002, pp. 4-5.

principles of autonomy and strict compliance, and contain rules on the transfer of the credit. However, the focus in each law is different. Some laws focus on the liability of the parties, especially the liability of banks, as well as their duties under the credit and on their entitlement to reimbursement and fees or on collateral for the benefit of the bank.[93]

Article 14.5 of Hungarian Decree No. 6/97 deserves mentioning since it makes the UCP binding for all documentary credit transactions, regardless whether or not the parties have agreed on their application.[94]

VII.5.5 The UN Convention on Independent Guarantees and Stand-by Letters of Credit

On 11 December 1995, after five years of preparatory work, the United Nations General Assembly adopted a single set of legal standards for two related instruments in the form of the UN Convention on Independent Guarantees and Stand-by Letters of Credit.

The Convention covers guarantees and counter-guarantees shown to be international and independent of the underlying transaction. Suretyship or accessory undertakings are exluded as well as insurance, commercial papers and bilateral contracts. Whereas standby letters of credit are directly covered, an option is provided to issue commercial letters of credit subject to the Convention (Article 1(2)).

One of the most important aspects of the Convention is that it provides standard rules for determining as to whether extraordinary relief is appropriate in cases of alleged fraudulent drawings or fraudulent drawings. Unfair calling of guarantees and letters of credit has been a major object of litigation and the relevant jurisprudence has tried to define grounds on which a payment obligation could be enjoined by courts on the initiative by the applicant contractor to prevent abuses not legitimised by the underlying contract.

The Convention has not yet come into force in the absence of sufficient ratifications, but I think that its contents deserve a detailed presentation. The ICC Commission on Banking Technique and Practice endorsed the Convention on 21 June 1999. In its view "the Convention sets forth the basic principles of law for independent undertakings in a manner which fully assures their independent

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93 Ibid., p. 5.

94 Thus a product of a private organisation becomes applicable by way of being incorporated directly, or by reference, to national law. Another example of this is India, which has incorporated the UNCTAD/ICC Rules for Multimodal Transport Documents, ICC Publication No 481, into its legislation.

For comparison, during the preparation of Council Regulation 2002/1606/EC concerning the application of international accounting standards, it became evident that EC law does not recognise the possibility to refer to a private set of rules without those being formally adopted by the Community and published in the Official Journal of the European Communities. The relevant Regulation gave the Commission powers to adopt any IAS standards created by the private International Accounting Standards Board in accordance with a comitology procedure.

nature, which guarantees the widest possible party autonomy and which establishes a uniform international legal standard for limits to the exception for fraudulent or abusive drawings".[95]

Article 3 of the Convention defines the ´independence´ of an undertaking in a way which is said to promote international understanding of the non-documentary character of undertakings.[96] An undertaking is independent where the guarantor´s or issuer´s obligation to the beneficiary is not dependent upon the existence or validity of any underlying transaction, or upon any other undertaking (including standby letters of credit or independent guarantees to which confirmations or counter-guarantees relate). Likewise, an undertaking is independent where it is not subject to any term or condition not appearing in the undertaking or if it is not subject to any future, uncertain act or event except the presentation of documents or another such act or event within a guarantor´s or issuer´s sphere of conditions.

The Convention contains a definite rule on the moment an undertaking becomes legally effective. It happens when it leaves the sphere of control of the guarantor or issuer (Article 7). An undertaking may be issued in any form which preserves a complete record of the text of the undertaking and provides authentication of its source by generally accepted means or by a procedure agreed upon by the guarantor/issuer and the beneficiary. This provision facilitates an electronic issuance of the undertaking.

Article 13 of the Convention links the critical determination of conformity of a demand for payment, in accordance with the stated terms of the undertaking, to generally accepted sound international commercial usages.[97] The terms and conditions can especially refer to any rules, general conditions or usages, but even in the absence of an express reference, such rules, general conditions or usages can become applicable. A court might find, for instance, that the relevant rules such as the Uniform Rules for Demand Guarantees (URDG 458), the International Standby Practices (ISP98) or even UCP500 might be applicable as generally accepted international usages.

The Convention applies to an international guarantee or stand-by letter of credit undertaking if the place of business of the guarantor or issuer at which the undertaking is issued is in a contracting state, or if the rules of private international law lead to the application of the law of the contracting state.

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95 ICC Endorsement of the UNCITRAL Convention on Independent Guarantees and Stand-by Letters of Credit, published i.a. in ICC publication No 500/2.

96 United Nations Convention on Independent Guarantees and Stand-by Letters of Credit, Introductory Note by James E.Byrne and Harold Burman, 35 I.L.M. 735 (1996). The Convention uses the term ´undertaking´ to describe the subject matter of the Convention, which is (according to Article 2) "*an independent commitment, known in international practice as an independent guarantee or as a stand-by letter of credit, given by a bank or other institution or person (´guarantor/issuer´) to pay to the beneficiary a certain or determinable amount upon simple demand or upon demand accompanied by other documents, in conformity with the terms and any document conditions of the undertaking, indicating, or from which it is to be inferred, that payment is due because of a default in the performance of an obligation, or because of another contingency, or for money borrowed or advanced, or on account of any mature indebtedness undertaken by the principal/applicant or another person.*"

97 "Regard shall be had to generally accepted international rules and usages of independent guarantee or stand-by letter of credit practice".

Interestingly, the Convention contains a conflict of laws rule (Article 1(3)) to be applied even if the Convention does not prove to be applicable law. This is in effect a ´mini-convention´ (an expression of Byrne and Burman) within the general treaty text consisting of Articles 21 and 22 on choice of law and applicable law. These provisions apply in a contracting state, even if in a given case the particular instruments do not fall under the Convention´s substantive provisions.

Article 21 subjects the undertaking to the law which is stipulated in the undertaking or demonstrated by the terms and condition of the undertaking, or agreed elsewhere by the guarantor or issuer and the beneficiary. However, failing a choice of law in accordance with Article 21, the undertaking is governed by the law of the state where the guarantor or issuer has that place of business at which the undertaking was issued.

Article 1(2) of the Convention giving parties rights to subject commercial letters of credit to the Convention can also be interpreted as giving the parties rights to subject their contracts to the regime of the Convention even in the absence of other connecting factors than the choice of law. This means that the contracting states will recognise the incorporation of the Convention, whether or not forming part of the law applicable to the undertaking, and have to give effect to its provisions.

The Convention contains, in Article 20, a requirement for courts to issue provisional measures in certain cases. It is likely that such measures are sought in jurisdictions with additional connecting factors, such as the issue of the guarantee, since otherwise the court seized usually declines jurisdiction. The Convention namely has no provisions on jurisdiction. Contracting states obviously abide by the Convention, but it is doubtful whether the parties could, by way of incorporating the Convention´s provisions, produce procedural implications concerning interim measures and evidence in a jurisdiction which is not party to the Convention. One can only say that this depends on the *lex fori*. By using arbitration, parties can more freely define the legal framework applicable to their relationship. But arbitration is much less helpful since no interim measures can, as a rule, be ordered. Moreover, subjecting the validity of a claim to arbitration renders the guarantee accessory.

VII.6 The regulation of standby letters of credit and contract guarantees

Although Uniform Customs and Practice for Documentary Credits UCP500 is intended to apply to standbys as well, the International Chamber of Commerce has created its own rules for them, namely International Standby Practices ISP 98.

ISP98 states “as standbys came into their own under the UCP, it nevertheless became clear that issues of practice had emerged which required different solutions than those provided by the UCP. ISP98, in a sense, is an evolutionary product of the application of the UCP to standbys, as can be seen in the similarities between the two sets of rules. It is important to note that standbys

can still be issued subject to the UCP, if the parties determine it is their wish to do so".[98]

Already before ISP98, the ICC had approved rules for demand guarantees (Uniform Rules for Demand Guarantees, ICC Publication No 458, the acronym of which is URDG458) in 1992.

URDG458 was not, however, the first set of guarantee rules adopted by the ICC. The Uniform Rules for Contract Guarantees (ICC Publication No 325, acronym URCG325) were adopted in 1978 but had not gained wide acceptance, because the markets in the1980s predominantly used demand guarantees.

Although URDG458 was drafted to remedy the failure of URCG325 to achieve market acceptance, the ICC decided that both sets of rules would co-exist, at least for the time being. URCG325 is said to govern guarantees of a hybrid nature combining characteristics of independent undertakings and accessory undertakings. On the one hand, they affirm the independence of the guarantees subject to their rules (Article 3) but do condition, on the other hand, the payment of the guarantee on the proof of the principal´s default (Articles 2 and 9).[99] The Rules provide that where the guarantee does not specify the documentation to be produced in support of a claim or specifies as the relevant document only a statement of claim by the beneficiary the beneficiary must (in the case of a performance guarantee) submit either a court decision or an arbitral award justifying the claim by the beneficiary or the written approval of the principal to the claim and its amount.[100] In this way, guarantees issued under URCG325 could perhaps still be described as ´documentary´ in the sense that the guarantor bank has no duty or right to investigate the facts or use its discretion.

URDG458 applies to independent guarantees and bonds which are payable on first demand. Demand guarantees differ from documentary credits in that they are properly invoked only if the principal is in default. However, the guarantor, like the issuer of a documentary credit, is not concerned with the fact of default, but with documents only. URDG458 does not apply to suretyships or conditional

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98 This statement is part of the Foreword of ICC Publication 590 by Maria Livanos Cattaui, Secretary General of the ICC. During the latest revision of the UCP, it was agreed unanimously that the standby credit is not to be merged with the bank guarantee rules regulated by the ICC Uniform Rules for Demand Guarantees, URDG458. Whilst the standby credit was seen legally as a twin of the demand guarantee, there are important differences between the two: the standby credit has developed into an all-purpose financial support instrument embracing a much wider range of uses than the normal demand guarantee (see *supra*). Therefore the link between the UCP and standbys was maintained in the 1993 Revision of the UCP. However, it was felt impossible to indicate the articles normally applicable to standbys.

99 Georges Affaki, ICC Uniform Rules for Demand Guarantees, A User´s Handbook to the URDG, ICC publication 631, pages 21 and 136-137.

100 Article 9.

bonds, guarantees or other accessory undertakings under which the guarantor´s duty to pay arises only on actual default by the principal.[101]

Probably the most relevant (and disputed) provision in URDG458 is Article 20[102], which stipulates the requirements for demands under the guarantee. The beneficiary has to state that the principal is in breach and to what extent he is in breach. Unless otherwise stipulated in the terms of the guarantee, he does not have to prove the existence of the default, but has to assert that a default has taken place. This provision can be seen as a compromise facilitating an immediate possibility of obtaining the sum of the guarantee on the one hand, which enhances its use as a security, and the aim of avoiding unjustified demands under the guarantee on the other.

The ICC soon approved rules also for purely conditional or accessory guarantees, which require that a breach has been established. The Foreword of ICC publication 524 states that "due to a need in the insurance industry for a uniform set of rules applicable internationally to contract bonds creating obligations of an accessory nature, the ICC Commission on Insurance undertook to elaborate the ICC Uniform Rules for Contract Bonds". Following these Rules, which bear the acronym URCB524 and which came into effect on 1 January 1994, the bank or insurance company is obliged to pay after having received a claim in writing.[103]

A claim shall not be honoured unless a default has occurred, and the claim has been made and served in accordance with the provisions of paragraphs (a) to (f) of Article 7 before the expiry date. A default shall be deemed to be established for the purposes of URCB524 upon issue of a Certificate of Default by a third party (who may be without limitation an independent architect or engineer or a Pre-Arbitral Referee[104] of the ICC) or, if the bond in question does not provide for the issue of a certificate by a third party, the guarantor himself may issue a certificate of default[105], or by a final judgement, order or award by a court or

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101 As stated in the Introduction of URDG 458.

The basic distinction is between demand guarantees, which are independent of the underlying transaction, and accessory guarantees (suretyships), which require an established breach. All guarantees do not fit easily into this dichotomy, and various stages (up to ten) between these two extremes have been distinguished in literature. German domestic practice knows a ´suretyship on first demand´, where the demand obliges the bank to pay, but the bank can claim the amount back if the demand can not be legitimised. See Affaki, Breisig and Carouge, German court decisions hit suretyships on first demand, DCI Vol. 10 no 2, April-June 2004, pp. 13-14.

102 Article 20 stipulates that "*Any demand for payment under the guarantee shall be in writing and shall (in addition to such other documents as may be specified in the Guarantee) be supported by a written statement (whether in the demand itself or in a separate document or documents accompanying the demand and referred to in it) stating: that the principal is in breach of his obligation(s) under the underlying contract(s) or, in the case of a tender guarantee, the tender conditions; and the respect in which the principal is in breach*".

This provision applies to the extent it is not expressly excluded from the guarantee.

103 Article 7 of URCB 524 contains detailed rules of the claim procedure.

104 See the Rules for the Pre-Arbitral Referee Procedure under the auspices of the ICC International Court of Arbitration.

105 This resembles in my view the way a non-life (casualty) insurer verifies the existence of indemnifiable damage.

(arbitral) tribunal of competent jurisdiction. The issue of a certificate of default by a third party or by the guarantor does not, however, restrict the rights of the parties to bring any disputes relating to the bond or the alleged default before a court or tribunal of competent jurisdiction. It is submitted that the ´parties´ envisaged in the above provision are the principal and the beneficiary.

VII.7 The key principles applicable to documentary credits

There are certain principles which have laid down the foundation for the use of documentary credits and for the use of demand guarantees as standby letters of credit during their commercial history. These principles concern the link between the credit and the underlying relationship, and how the documents presented shall be examined.

VII.7.1 The autonomy of the credit

The autonomy of documentary credits means that banks are not concerned with the contract of sale or other underlying contract. Following civil law terminology, the autonomy of the promise of a bank to pay under a letter of credit is characterised as an abstract transaction.[106] The principle of the autonomy of the credit is laid down in UCP500 Article 3 (Credits v. Contracts), which provides that

> *"Credits, by their nature, are separate transactions from the sales or other contract(s) on which they may be based and banks are in no way concerned with or bound by such contract(s), even if any reference whatsoever to such contract(s) is included in the Credit. Consequently, the undertaking of a bank to pay, accept and pay Draft(s) or negotiate and/or fulfil any other obligation under the Credit, is not subject to claims or defences by the Applicant resulting from his relationships with the Issuing Bank or the Beneficiary."*

Like commercial letters of credit, demand guarantees and standby letters of credit are also undertakings independent of the underlying contracts meaning that the obligation to pay arises independently of the situation e.g. in an underlying construction contract. This is provided in Article 2(b) of URDG 458 and Rule 1.06 (c) of ISP98.

The principle of the autonomy of the credit applies separately to each of the four contracts making up the confirmed letter of credit.[107] Another principle

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106 See Jean Stoufflet, Payment and Transfer in Documentary Letters of Credit: Interaction between the French General Law of Obligations and the Uniform Customs and Practice, Arizona Law Review, Vol 24, 1982, p. 267.

107 Todd, Documentary Credits Insight Vol. 6 No 2, p. 7. Or, in other words, three contracts or contractual relationships are independent of the fouth, the underlying contract.

going hand in hand with the autonomy of the credit is that banks deal in documents and not goods.[108] This is stated in Article 4 (Documents v. Goods/ Services/Performances) of UCP500:

> *"In Credit operations all parties concerned deal with documents, and not with goods, services and/ or other performances to which the documents may relate."*

Therefore, if the documents are in conformity, the bank must honour its payment obligation under the credit. It is irrelevant that it may be alleged that the goods are not of the standard required by the contract. Banks assume responsibility of nothing else than the documents, which is provided in Article 15 (Disclaimer on Effectiveness of Documents) of UCP500:

> "Banks assume no liability or responsibility for the form, sufficiency, accuracy, genuineness, falsification or legal effect of any document(s), or for the general and/or particular conditions stipulated in the documents(s) or superimposed thereon; nor do they assume any liability or responsibility for the description, quantity, weight, quality, condition, packing, delivery, value or existence of the goods represented by any documents(s), or for the good faith or acts and/or omissions, solvency, performance or standing of the consignors, the carriers, the forwarders, the consignees or the insurers of the goods, or any other person whomsoever."

The above rule relates to the liability of the bank. The applicant of the credit is, in any case, the bank´s customer and banks may feel compelled to consider their interest to some extent despite the general principle.[109]

The only (or principal[110]) exception to the rule of the autonomy of the credit is the so called ´fraud exception´, where there is fraud on the side of the beneficiary. UCP500 does not especially mention the fraud exception, but its

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108 *Todd* refers to this principle in the first part of his article that handles strict compliance, whereas *Jack* considers this principle to be so interrelated with the principle of the autonomy of the credit that it should be presented separately, see Jack, pp. 17-18.

109 Schmitthoff´s Export Trade mentions (on page 281) the practice with ´stale bills of lading´. Article 43(a) of UCP500 stipulates that transport documents must be presented within a specified time after issuance and, if no time is specified, banks may refuse documents if presented to them later than 21 days after issuance of the bill of lading or other transport document. Sometimes transport documents are, however, presented so late that the buyer as consignee might become involved in legal or practical complications, or might have to pay additional costs, e.g. for the warehousing of the goods. Although banks are in principle not concerned with the underlying transactions, they may feel compelled to reject such transport documents, notably bills of lading, as ´stale´.

110 *Goode* has mentioned (during his lectures at Queen Mary College in 1986-87, which your author attended) some other possibilities for the bank's refusal of payment:

- the issue of the guarantee was induced by fraud or misrepresentation;
- the issuing bank has a right of set-off against the beneficiary; and
- the payment pursuant to the demand would be illegal under the law governing the guarantee.

Under letters of credit, in addition, the payment could be refused on the ground of forgery and unenforceability on the ground of the International Monetary Fund Rule VIII 2b. One should also note the situations mentioned in the UN Convention on Independent Guarantees and Stand-by Letters of Credit, see *infra*.

existence was recognised by the ICC Banking Commission in response to a query made to it.[111] There is a volume of jurisprudence on this issue, which is also explicitly dealt with in the UN Convention on Independent Guarantees and Stand-by Letters of Credit, as well as by some national laws including the Uniform Commercial Code. Generally speaking, the extent of admitting a fraud exception to the principle of the autonomy of credit is a matter for the national law governing the transaction (i.e. presentation of documents). To what extent one could tolerate fraud in a transaction is a matter where state courts may wish to exert the public policy of their jurisdiction.

VII.7.2 How to treat abusive callings

The courts which have had to decide on whether to interfere with the bank´s obligation to pay, have stood between two legitimate objectives. The autonomy of letters of credit and independent guarantees, including standby letters of credit, plays an important role in the commercial world. As one English judge has put it, letters of credit are the "life blood of international commerce".[112] On the other hand, it has been said that "fraud unravels all"[113] and should not be tolerated by courts.

For the banks themselves, it is important for their commercial reputation to be able to honour their obligations in respect of independent undertakings.[114] It is therefore understandable that banks sometimes do not want to take the decision of not honouring their obligations. The bank may inform the applicant of the call, and the applicant has to decide on whether to seek an injunction from the competent court to enjoin the bank´s payment.

Another reason for banks to honour their obligations is that the standards of evidence required in different jurisdictions concerning fraud, although varying from country to country, are very high. Therefore, in practice, banks will not refuse to honour a credit unless an alleged fraud is confirmed by a court order prohibiting the bank to pay.[115]

I shall first pay attention to certain court cases which are mainly Anglo-Saxon and thus linguistically accessible to me and which illustrate the problems

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111 Opinions (1980-81) of the ICC Banking Commission, ICC Publication No 399 at R 76.

112 Kerr L.J. in *R.D. Harbottle (Mercantile) Ltd. v. National Westminster Bank Ltd.* (1978) Q.B. 146. Ackner L.J. adds in *Intraco Ltd. v. Notis Shipping Corporation of Liberia (The Bhoja Trader),* (1981) 2 Lloyd´s Rep. 256, 257 that "thrombosis will occur if, unless fraud is involved, the Courts intervene and thereby disturb the mercantile practice of treating rights thereunder as being the equivalent of cash".

113 Lord Diplock in *the United City Merchants* case (United City Merchants v. Royal Bank of Canada, (1983) 1 AC 168) translating and applying the Latin maxim *ex turpi causa non oritur actio.*

114 This was expressly referred to in the English case case *Bolivinter Oil SA v. Chase Manhattan Bank* (1984) 1 All ER 351n.

115 Schütze & Fontane, pp. 33-34. Schütze & Fontane state, on the basis of their survey of national law, including jurispudence, that the bank is entitled and obliged to refuse payment, if there is ´*prima facie* evidence´ of fraud. (emphasis added)

and the answers provided for in the jurisprudence. English case law could have significance in an electronic documentary credit environment on the basis of a choice-of-law clause, which is the case under the *Bolero System*. The case material more or less equates independent guarantees and commercial letters of credit in respect of the fraud exception. Secondly, attention is paid to the attempts to regulate the matter of fraud exception in the UN Convention on Independent Guarantees and Stand-by Letters of Credit.

In the American case *Sztejn*[116], courts enjoined the payment under a letter of credit in circumstances where the seller had virtually shipped rubbish instead of the bristles contracted for. The judge held that "where the seller´s fraud has been called to the bank´s attention before the drafts and documents have been presented for payment, the principle of the independence of the bank´s obligation under the letter of credit should not be extended to protect the unscrupulous seller". This case is an authority for English courts as well.[117]

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116 *Sztein v. Henry Schroder Banking Corporation, 177 Misc. 719, 31 N.Y.S. 2d 631 (1941)* The conclusions of the Sztein case were later codified into the Uniform Commercial Code, (Dolan, pp. 4-14).

117 Jack, p. 209. The Uniform Commercial Code § 5-109 contains the following provisions as to fraud and forgery in a letter of credit transaction.

" a) If a presentation is made that appears on its face strictly to comply with the terms and conditions of the letter of credit, but a required document is forged or materially fraudulent, or honor of the presentation would facilitate a material fraud by the beneficiary on the issuer or applicant:

1. the issuer shall honor the presentation, if honor is demanded by (i) a nominated person who has given value in good faith and without notice of forgery or material fraud, (ii) a confirmer who has honored its confirmation in good faith, (iii) a holder in due course of a draft drawn under the letter of credit which was taken after an acceptance by the issuer or nominated person, or (iv) an assignee of the issuer´s or nominated person´s deferred obligation that was taken for value and without notice of forgery or material fraud after the obligation was incurred by the issuer or nominated person; and

2. the issuer, acting in good faith, may honor or dishonor the presentation in any other case.

b) If an applicant claims that a required document is forged or materially fraudulent or that honor of the presentation would facilitate a material fraud by the beneficiary on the issuer or applicant, a court of competent jurisdiction may temporarily or permanently enjoin the issuer from honoring a presentation or grant similar relief against the issuer or other persons only if the court finds that:

1. the relief is not prohibited under the law applicable to an accepted draft or deferred obligation incurred by the issuer;

2. a beneficiary, issuer, or nominated person, who may be adversely affected is adequately protected against loss that it may suffer because the relief is granted;

3. all of the conditions to entitle a person to the relief under the law of this state have been met; and

4. on the basis of the information submitted to the court, the applicant is more likely than not to succeed under its claim of forgery or material fraud and the person demanding honor does not qualify for protection under subsection (a)(1)."

The provisions of the Code are not mandatory, and can be replaced by referring to UCP500. However, as UCP500 does not deal with the fraud exception, it is complemented by UCC. § 5-109 in cases where it is the law applicable to the credit.

The leading English precedent on fraud and on illegality is *United City Merchants*.[118] In that case, a bill of lading presented under a credit showed that shipment had been made on 15 December 1976 when it had in practice been made the day after, and the credit called for a bill signed on the 15th at the latest. The date was inserted by an employee of the loading brokers to the carriers, who knew that the date inserted was a false one.

The House of Lords decided, in general terms, that the fraud exception relates to the conduct of the seller as beneficiary, and rejected the argument that the bank should not pay in a situation where the documents, although these appear on their face to be in conformity with the terms of the credit, contain some statement of material fact that is not accurate. The judgement established the main principle, according to which a bank, when considering whether to pay, may take account of something external to the presented documents, which appear on their face to conform to the terms of the credit. This external matter is a fraud which is known to the presenting party. Moreover, there were arguments, on the basis of which one can conclude that in certain cases banks may require a document, which is a ´nullity´.[119]

There are a number of other English cases regularly quoted in the literature, and I would like to mention some rules established by them. In *Edward Owen*[120], a demand guarantee stood on the same footing as an irrevocable letter of credit and had to be honoured in the absence of clear fraud of which the bank had a notice. According to the judgement in *Esal*[121], it was held that the bank does not have a duty to inform its client, the applicant of a demand guarantee, of the call. If the bank acquires knowledge of clear fraud before payment, it must, pursuant to *United Trading*[122], decline payment.

As regards the possibility to obtain a court injunction to block the payment under a letter of credit or demand guarantee, only a clear notice of fraud is sufficient (*Bolivinter* case, as referenced *supra*). The customer (applicant) has a duty not to interfere with the bank´s duty to pay in the absence of clear fraud. Thus, if such interference results in the bank´s liability, the applicant would be liable to the bank for this (*Harbottle*). The evidence as to the fraud and the bank´s knowledge thereof has to be clear (*Edward Owen*). The court requires "strong corroborative evidence" of the allegation so that the only realistic inference to draw from the material presented to the court is fraud. This evidence must be composed of "contemporary documents emanating from the buyer" (the beneficiary under the guarantee). The buyer/benefiary must get an opportunity to answer and no adequate answer has been given by him (*United Trading*).

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118 *United City Merchants v. Royal Bank of Canada, (1983) 1 AC 168*

119 Jack, pp. 216-218. Forgery and nullity are different things. According to *Jack*, a document may be fraudulent without being forged, and a document may contain a forgery without being a nullity.

120 *Owen (Edward) Engineering Ltd v Barclays Bank International Ltd (1978) QB 159*.

121 *Esal (Commodities) Ltd and Reltor Ltd v Oriental Credit Ltd and Wells Fargo Bank NA (1985) 2 Lloyd´s Rep 546*.

122 *United Trading Corporation SA v Allied Arab Bank Ltd (1985) 2 Lloyd´s Rep 554*.

Generally speaking, English courts have been reluctant to grant injunctions, although these cases have formulated precisely the situation where an injunction can be granted. In *Tukan Timber*[123], which involved a commercial letter of credit, fraud in the form of forgery of signatures was established, but no injunction was granted when the bank had already refused to pay. Moreover, it was noted that it had not been shown that the third presentation of the documents had been fraudulent.

In other European jurisdictions, however, there are cases where the possibility of not honouring an abusive call is admitted. German jurisprudence of the 1980s contains examples of this.[124] The same goes for French jurisprudence.[125] This kind of decision was also taken by the Finnish Supreme Court of Justice in the *Bank Tejarat* case.[126] The peculiar circumstances of this case had emerged in the aftermath of the Islamic Revolution in Iran which had rendered it virtually impossible for the Finnish constructor to complete the project ordered by an Iranian Ministry. The Finnish court held that the Iranian corresponding bank Tejarat was in such close a relationship with the Iranian state that the same grounds for refusal could be raised against it as could be made against the Ministry as the beneficiary. At the same time, the court held that the guarantor under a demand guarantee could refuse to pay if the demand represents an abuse of the right created by the guarantee. No reference was made to the general clause[127] of Finnish contract law.

It is obvious that the volume of the case law relating to the fraud exception has highlighted the need to settle the matter through an international convention, the UN Convention on Independent Guarantees and Stand-by Letters of Credit. After all, the matter has not been alien to national legislation either, since it has been regulated by statute in the United States through UCC § 5 –9.

Article 19 paragraph 1 of the Convention lays down the general principle of not honouring an abusive call by stating that

> *"if it is manifest and clear that any document is not genuine or has been falsified, no payment is due on the basis asserted in the demand and the supporting documents or, judging by the type and purpose of the undertaking, the demand has no conceivable basis, the guarantor/issuer acting in good faith, has a right, as against the beneficiary, to withhold payment."* (emphasis added)

Paragraph 2 of the same article gives types (evidently on a non-exclusive basis) of situations in which a demand has no conceivable basis. One situation is when "the contingency or risk against which the undertaking was designed to

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123 *Tukan Timber Ltd v Barclays Bank plc (1987) 1 Lloyd´s Rep. 171.*

124 *Landesgericht Frankfurt am Main, 11.12.1979; Landesgericht Dortmund, 9.7.1980.* German jurisprudence frequently refers to the ´Treu und Glauben´ provision contained in BGB § 242. See Timo *Esko,* "On first demand"-ehtoiseen pankkitakaus- tai pankkitakuusitoumukseen perustuvan vilpillisen maksuvaatimuksen torjumisesta, Defensor Legis 1985, pp. 482-488.

125 Ibid., pp. 492-497.

126 *KKO: 1992: 145 (Bank Tejarat v. Kansallis-Osake-Pankki).*

127 Oikeustoimilaki (Contracts Act) 1929 Section 36 (as amended in 1982). This general clause is one which entitles the courts to adjust or disregard unconscionable contract terms.

secure the beneficiary has undoubtedly not materialised". Secondly (and similarly), where the underlying obligation has undoubtedly been fulfilled to the satisfaction of the beneficiary there is no conceivable basis for the demand.

Thirdly, if the underlying obligation of the principal or applicant has been declared invalid by a court or arbitral tribunal, the demand has no conceivable basis, unless the undertaking indicates that such contingency falls within the risk to be covered by the undertaking.

In these three above mentioned situations, the Convention gives the principal or applicant a possibility to resort to provisional court measures to interfere with the bank´s undertaking to pay. Pursuant to Article 20, the court may issue a provisional order to the effect that the beneficiary does not receive payment, or that the proceeds of the undertaking paid to the beneficiary are blocked, taking into account whether, in the absence of such an order, the principal or applicant would be likely to suffer serious harm.

It is noteworthy that the Convention gives objective criteria for circumstances where payment may be withheld. If subjective criteria relating to the knowledge of the beneficiary were used, a fraudulent beneficiary would be able to transfer the credit to a second beneficiary acting in good faith.[128] Secondly, it should be observed that the bank has a right, not an obligation, to withhold payment even if the demand (in commercial letters of credit presentation) has no conceivable basis. Should the bank refuse to cooperate, the principal has to resort to provisional court measures.

The application for such an order can be made by the principal or applicant or by the instructing party. The person applying for the measure has to submit to the court "immediately available strong evidence" to justify the measure.[129]

There are two further other situations which justify an exception to payment obligation, although no court injunction is possible. Firstly, when the fulfilment of the underlying obligation has clearly been prevented by the wilful misconduct of the beneficiary, the demand has no conceivable basis. Secondly, in the case of a demand under a counter-guarantee, the beneficiary of the counter-guarantee

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128 It should be recalled that a transferable credit requires the consent of the parties whereas the assignment of proceeds does not. In the case of assignment of proceeds, the presentation has to be made by the original beneficiary. In the Austrian *Creditanstalt*-case (*Singer&Friedlander v. Kreditanstalt-Bankvererein, 17 Cg 72/80, Handelsgericht Wien 1980*), a fraudulent beneficiary had assigned the proceeds to a *bona fide* second beneficiary, who was not allowed to make the presentation because the assignment of proceeds did not give him such a right. The right remained with the assignor, against whom the bank was able to make the fraud defence.

It is here submitted, that the approach of national law to assignment determines largely what the positions of a *bona fide* beneficiary who is the transferee of a transferable credit. The same must go for the assignment of the whole benefit of the credit.

129 As noted *supra*, parties can make the Convention applicable even if there are no other connecting factors. The Convention must, however, form part of the *lex fori* to bind the court seized. If not, it depends on the *lex fori* and its conflict of laws rules and public policy how far the provisions of the Convention should be respected. It is possible that courts would not give effect to the procedural rules of Article 20 as such, but would give weight to the ´substantive´ provisions of the Convention.

has made payment in bad faith as the guarantor or issuer of the undertaking to which the counter-guarantee relates.

As stated earlier, the UN Convention is not yet in force. In practice, therefore, the only possibility seems to be court intervention. An applicant of a letter of credit might apply for an injunction prohibiting the beneficiary from receiving payment of the credit. In a four-partite relationship, the payment to the beneficiary is effected in his country. Some laws require an injunctive order to be served on the beneficiary prior to the order becoming effective, and so, if the law of the beneficiary´s domicile requires this, practical problems may arise.[130]

Another method of preventing payment is to attach the payment of the claim if the *lex fori* provides that an attachment order becomes effective at the time of the service on the bank, which is the case in Switzerland and Germany.[131] Service on the beneficiary need then only be effected after a certain period of time counted from the court order, and the payment is blocked in the meantime.[132]

VII.7.3 The doctrine of strict compliance

The doctrine of strict compliance is a legal principle meaning that the bank is entitled to reject documents which do not strictly conform to the terms of the credit. The reason underlying this rule is that the advising bank is a ´special agent´ of the issuing bank, and the latter is a special agent of the buyer.[133] If such an agent goes beyond his strict authority or mandate, he has to bear the commercial risk of the transaction since the principal (issuing bank or buyer) is entitled to disown the act of the agent. If the principal ratifies the unauthorised payment against defective documents, he forfeits his right to refuse reimbursement. In English case law[134] at least, even silence or inaction relating to the irregularity of documents may amount to an implied ratification of the documents.

VII.7.4 The standard of examination of documents

The principle of strict compliance causes particular problems in the practice of documentary credits since discrepancies exist in a substantial part of all credits.[135] Thus, there are pressures for relaxing the doctrine of strict compliance. *Todd* refers

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130 Schütze & Fontane, p. 35.

131 *Esko* refers, however, in his article to materials from the early 1980s, according to which attachment was regarded not to be available for these purposes, see Esko, p. 483.

132 Ibid.

133 Schmitthoff, Export Trade, p. 342.

134 *Bank Melli Iran v Barclays Bank (Dominion, Colonial and Overseas) (1951) 2 Lloyd´s Rep. 367.*

135 According to a reference in Todd´s article in Documentary Credits Insight Vol 6 No 2, p. 7 this figure is one half, see also *infra*.

in his article[136] to various English court cases introducing slight relaxation to the doctrine. A bank involved in a documentary credit transaction examines the documents presented to see whether they meet the requirements of the credit. The standard for examination of documents is laid down in Article 13.a. of UCP500:

> *"Banks must examine all documents stipulated in the Credit with reasonable care, to ascertain whether or not they appear, on their face, to be in compliance with the terms and conditions of the Credit. Compliance of the stipulated documents on their face with the terms and conditions of the Credit shall be determined by international standard banking practice as reflected in these Articles. Documents which appear on their face to be inconsistent[137] with one another will be considered as not appearing on their face to be in compliance with the terms and conditions of the Credit."* (emphasis added)[138]

The standard of ´reasonable care´ is "the care that would be exercised in the particular circumstances by a bank to handle documentary credit transactions".[139] It is important to note that the bank need not examine the small print clauses usually on the reverse side of the bill of lading and transport document, since according to Article 23.a.v of UCP500 "banks will not examine the contents of such terms and conditions".[140]

For clarity and consistency, a phrase was added to UCP500 stating that banks must examine documents

> *"...to ascertain whether or not they appear, on their face, to be in compliance with the terms and conditions of the Credit".*

The determination as to whether there is compliance or not shall be made on the basis of documents alone (Article 14.b of UCP500). The words "appear on their face" mean that the decision whether the documents do or do not comply with the terms and conditions of the credit and are consistent with one another, is based exclusively upon the banker´s examination of the document and not upon somebody else´s understanding. In other words, there is a method for the examination of documents under the documentary credit which is peculiar to bankers. This method attempts to find whether certain statements, terms or

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136 Ibid. p. 8, to be continued in Documentary Credits Insight Vol 6 No 3, p. 20. *Todd* is opposed to the idea of relaxing the doctrine, and calls for sellers to address the problem by stipulating in the contract of sale provisions restricting the freedom of the buyer to exercise his right of rejection.

137 ISBP para. 24 adds that "(t)he requirement is not that the data content be identical, merely that the documents not be inconsistent".

138 The Article adds that "Documents not stipulated in the Credit will not be examined by banks. If they receive such documents, they shall return them to the presenter or pass them on without responsibility".

139 As stated by *Jack* on p. 144. This definition is circular in my view.

140 UCP500 provides now expressly, unlike its predecessor UCP400, that it is prudent to present documents with full terms of contract of carriage. UCP500&400 Compared, ICC Publication No 511, p. 67. If a bill of lading consists of more than one page, such as addenda or attachments, each of such pages must include reference to being an attachment to and/or an intergral part of the bill. A signature on the first page suffices. ICC Banking Commission Opinion R.279 of the 1997 Queries.

conditions appear on the document. It should be added that the phrase ´on their face´ is not to be interpreted as meaning either the ´face´ (*recto*) or the reverse (*verso*) of the document.[141]

Consequently, the assumption is, according to *Jack*[142], that the exercise of reasonable care will detect all discrepancies in the documents which "appear on their face" to conform. So the expressions ´reasonable care´ and ´appear on their face´ would go hand in hand. Jack considers though that even if the assumption would not be appropriate, there could be an exceptional case where a failure to accord with the credit appears on the face of documents but is not discovered despite the exercise of reasonable care. Such scenario, it is argued by Jack, would entitle the bank to be reimbursed.

What if the bank finds in its examination statements that are not correct or are not possible? An ICC Banking Commission Opinion[143] suggests that the bank cannot in this kind of a situation turn ´a blind eye´ to the problem, although the bank is still obliged to pay for documents which appear on their face to comply with the credit. The burden of proof is on the bank´s customer to establish first that there is a discrepancy between the documents and the terms of the credit, and second that there has been a lack of reasonable care in examining the documents.[144]

If the documents appear on their face not to be in compliance with the terms and conditions of the credit, banks may refuse to take up the documents. Should the bank (issuing, confirming or negotiating bank) decide to take up the documents in any case, it bears a risk that the party next in the chain, ultimately the buyer, will not accept the discrepancy. The issuing bank has, pursuant to Article 14d. of UCP500, the possibility in its sole judgement to approach the applicant (buyer) of the credit for obtaining a waiver of the discrepancies. This possibility does not allow going beyond the seven day limit stipulated as a reasonable time to examine the documents.[145]

According to Article 13b. of UCP500, the issuing bank, the confirming bank or a nominated bank acting on their behalf have each a reasonable time, not to exceed seven banking days following the day of the receipt of the documents, to examine the documents and determine whether to take up or refuse the documents and to inform the party from which it received the documents

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141 Ibid. p.39. The term "appears on its face" was first used in UCP151 of 1951 (Guide to the eUCP, p. 46).

A Swedish court (*Svea Court of Appeal T 9371-99*) found that a document referring, on the front page, to general conditions on the reverse, which was blank, was a conforming document. However, the document was also a forgery. 'For the judgement, see Lars Gorton, Remburs, dokumentgranskning och doktrinen om strikt uppfyllelse in 9 svensk Juristtidning 2003, pp. 957-969.

142 Jack, pp. 142-143.

143 R.261 of the 1997 Queries.

144 Jack, pp. 145-146.

145 See also *Cour d´appel de Lyon, 3e chambre, 22 October 1999, SA Lyonnaise de Banque v. SARL CERATHERM, Journal du Droit International 3, 2000, p. 741*.

accordingly. This Article does not always allow seven banking days. A reasonable time is in many cases less than that. It is ultimately for the national law in question to provide guidelines as to what is reasonable.[146]

Further to a disclaimer on the effectiveness of documents in Article 15 of UCP500, there is a disclaimer in Article 16 on the transmission of messages. Article 16 provides that banks assume no liability or responsibility for the consequences arising out of delay or loss in transit of any messages, letters or documents, or for delay, mutilation or other errors arising in the transmission of any telecommunication. Furthermore, banks assume no liability or responsibility for errors in translation or interpretation of technical terms, and reserve the right to transmit credit terms without translating them.

The significance of the strict compliance doctrine in everyday life can be illustrated by the fact that during recent years, the rejected rate for the first presentation of documents under letters of credit is said to be between 70% and 85%, depending on the source of information.[147]

VII.7.5 Demand guarantees and strict compliance

Both demand guarantees and standby letters of credit are subject to the principle of strict compliance. The liability regimes of banks are therefore similar to UCP500. However, Article 15 of URDG458 provides expressly that "Guarantors and Instructing Parties shall not be excluded from liability or responsibility... for their failure to act in good faith and with reasonable care".

URDG458 provides in Article 2(b) that "the duty of a Guarantor under a Guarantee is to pay the sum or sums therein stated on the presentation of a written demand for payment and other documents specified in the Guarantee which appear on their face to be in accordance with the terms of the Guarantee.

Furthermore, Article 9 reads "(a)ll documents specified and presented under a Guarantee, including the demand, shall be examined by the Guarantor with reasonable care to ascertain whether or not they appear on their face to conform to the terms of the Guarantee. Where such documents do not appear so to conform or appear on their face to be inconsistent with one another, they shall be refused".

ISP98 Rule 1.06d. notes that "because a standby is documentary, an issuer´s obligations depend on the presentation of documents and an examination of required documents on their face". Rule 4.01.b. provides that "whether a

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146 ICC Banking Commission Opinion R264 of the 1997 Queries. This is a deviation from a *lex mercatoria* approach.

147 Gary Collyer, Documentary Credit Dispute Resolution under the DOCDEX Rules – Three years On, Arbitration, Finance and Insurance – Special Supplement 2000, ICC International Court of Arbitration Bulletin, p 67.

DC-PRO LC Market Intelligence Survey 2003 indicates that there are wide variations between the discrepancy rates between different letter of credit departments: the highest rate was 95% and the lowest 10%!

presentation appears to comply is determined by examining the presentation on its face against the terms and conditions stated in the standby as interpreted and supplemented by these Rules which are to be read in the context of standard standby practice".[148]

It is the guarantor´s duty to accept the demand only when it conforms strictly with the requirements of the guarantee. Although not expressly stated in the rules, the standard of strict compliance is inherent to the URDG458 and was implicitly relied upon by the ICC Banking Commission in an opinion.[149] Strict compliance is the natural corollary of the guarantor´s duty to limit his examination to the appearance of conformity of the demand.[150]

Rule 4 of ISP98 contains detailed requirements for documents to be presented under standby letters of credit. Moreover, demands for honour of a standby must comply with the terms and conditions of the standby.

In contrast, as conditional guarantees such as those envisaged in URCB524 are not purely documentary and compliance requirements for documents do not play a similar role since it does not suffice that documents ´appear on their face´ to comply.

The documents to be presented under a guarantee are a demand together with certain other documents such as an expert´s opinion, whereas in a commercial letter of credit the documents are commercial documents. This very nature of documents makes the examination of documents envisaged in the terms of guarantees somewhat different in practice.

VII.8 L/C´s going electronic – the main developments

The idea of electronic letters of credit is not new. It has been mentioned in the literature since the 1980s. Since then many projects that build on the idea either accurately or loosely have seen daylight. Electronic letters of credit have remained very much at the level of theory. There are many reasons for that. The main one is, however, that the legal and technical infrastructure has remained far from adequate. It is possible to replicate the legal functions by contractual arrangements to some extent. Such arrangements require sophistication among trading partners and trust between them, whereas the reason for using

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148 ´Standard standby practice´ is a term equivalent to ´standard banking practice´ added into Article 13.a of UCP500.

149 ICC Doc 470/TA.361rev(2). In the case behind this opinion, the guarantee required a written statement stating that "(t)he principal is in breach of his payment obligation(s) under the contract for the deliveries under the contract during the period from 1st April until 20th August of year 1998" without specific mention of the contract number or date. Whilst this information was included within the introduction to the guarantee it was not requested as part of the requirements for the statement under the guarantee. The opinion stated that the bank should honour the claims as submitted.

150 Affaki 2001, p. 85.

documentary credits is often the lack of trust. Moreover, documentary credits are used in trading with countries where legal and technical sophistication has perhaps not yet reached its peak.

VII.8.1 The role of automation for letters of credit

Information technology can come into the picture in automating documentary credit procedures in four different areas. Firstly, banks organise their back-office to process credits in-house. There has, for a long time, existed software products to facilitate this development. A question that emerges in the automation is to what extent it can be applied to odd cases. Traditional wisdom would answer that these should be handled manually.[151] It depends of course on the complexity and variability of the documentation and the rules. A simplified trade credit product could be handled more easily by computers than a traditional letter of credit e.g. with complicated charterparty bills of lading.

Another question is whether the operation should be integrated with the bank´s central computer system or function on a decentralised basis. Even today´s information technology systems may have difficulties in coping with the volume of information that is generated in this way (see GUIDEC II).

The second area, an area where automation has been the rule for a long time, is the interbank intercourse. As already stated, SWIFT has produced standard messages for the applicable version of Uniform Customs and Practice for Documentary Credit.

The third front where automation should come into play is the relationship between the bank and its customer. Major banks have since the 1980s been able to receive documentary credit applications in electronic form. The systems enable customers to send credit opening instructions electronically from their offices and to use the same computer hook-ups to check progress on operations. At an early stage in the 1980s, few banks succeeded in directly interfacing incoming customer messages with the bank´s back-office processing system.

The fourth, and by far the most difficult front where electronic solutions could be applied, is the document handling which is normally used to verify the data showing that goods have been shipped and other requirements such as insuring the goods have been complied with.

The examination of documents presented electronically will eventually be carried out using centralised utilities, removing any of the subjectivity inherent in today´s checking processes. This will apparently reduce the range and number of disputes and the concomitant delays in payment.[152]

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151 Rowe p. 134.

152 Neil Chantry, The future of the eUCP, Documentary Credits Insight, Vol 8 No.2, April-June 2002, p. 1 and 27.

However, electronic documentation creates new problems. The documents come from many different sources and have many functions, the most problematic one being the document of title function of the bill of lading. As noted already, discrepancies between the instructions and the actual documents exist, depending on the source (cf. *supra*), but in any case in more than 50% of the credits. This causes vital difficulties for an automated scrutiny. Going electronic would still require manual examination of the problem cases and in cases of system malfunction. Moreover, since many or most ´electronic credits´ would be mixed credits, manual scrutiny would be equally needed.

The parallel system of electronic and manual examinations would not immediately reduce transaction costs, which is normally the key motive for automation, and could discourage banks stepping into the electronic world. At the same time, complexities encountered by trading companies would be detrimental for the use of documentary credits.

Open account finance works during good times, but when a purchaser´s creditworthiness becomes questionable, suppliers start to look at ways of mitigating payment risk. In this way, there is a role for documentary credits. It is also conceivable that a simplified version of documentary credit (e.g. one where only standardised electronic documentation is used, and in which little manual scrutiny is needed) could become, if used with increased rapidity[153], a more widely used trade financing instrument than a present day documentary credit is.[154]

One way for the banks to go into the electronic documentary credit business is to link themselves to commercial schemes for electronic contracting. In the Bolero System, banks may become members by signing the Rulebook. The ICC ´Paction´ application[155] or its equivalents might facilitate links to banks in such a way that when the customer selects ´documentary credit´ as the payment method, the buyer could be asked whether he would like to create an application for a documentary credit with a named bank.[156]

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153 It should be noted that the eUCP has retained the time of seven days for banks to examine the documents.

154 See the presentation of the SWIFTNet Trade Services Utility in Chapter VIII.7.5., *post*.

155 The electronic version of the ICC Model International Sale Contract (Manufactured Goods Intended for Resale), ICC Publication No 556; for ´Paction´, see Chapter IV.8.4.2., *ante*.

156 As presented by Åke Nilsson in his article ´Model sale contract goes live´, Documentary Credit Insight, April-June 2002, on page 23. Nothing would apparently prevent the system from adding hyperlinks to a number of banks to choose from, where these banks had declared to be able to receive documentary credit applications electronically through this kind of application. At the same time, banks could announce to be able to receive actual L/C documents electronically.

Nothing should prevent financial institutions from creating their own applications for electronic contracting. As Nilsson explains, the very application could be developed into a branded and tailored version for financial institutions to integrate into their own customer offerings.

VII.8.2 Developments within the ICC

The emergence of EDI led the ICC to consider an ´electronic data credit´ already at the end of the 1980s. At its meeting on 24 October 1989, the ICC Commission on Banking Technique and Practice appointed a ´think tank´ to consider the matter. In one contribution to those discussions, Mr. Bernard W*heble*[157] noted the state-of-play that had set the discussions on their course. EDI was already applied to the issuance and amendment of traditional documentary credits and to the inter-bank transfer of funds in respect of payments thereunder. The big step still to be taken to create a paperless credit was to replace the traditional paper documents by standard electronic messages as payment triggers.

The think-tank also considered the question of to what extent electronic data transfers should be taken into account in the revision of the Uniform Customs and Practice for Documentary Credits (UCP400). Such revision did take place, as already stated, at the beginning of the 1990s. However, during the ICC´s June 1990 Hamburg Congress, the ICC Commission on Banking Technique and Practice decided not to formulate an independent set of rules applicable to EDI credits. The Commission contemplated however whether it should insert articles in UCP500 for the possible new paperless documentary credit technology inspired by EDI.

The conclusion was that UCP500 should, at the time, only deal with contemporary practices of the time and not with future or anticipated practices, even if they included an electronic documentary credit transaction. Moreover, the Group also concluded that UCP should retain primacy over any other set of rules related to documentary credits.[158]

In the drafting of UCP500 the use of electronic documents was largely omitted, even though a set of rules for electronic bills of lading had already been created in 1990 by the CMI. As compared to the UCP, the other landmark product of the ICC, INCOTERMS1990 had included provisions on the use of electronic documents.[159] As stated earlier, point A.8 of each term mentioned electronic transport documents making the obligations in respect of them equivalent to the paper documents referred to therein. Likewise, points A.10 and B.10 of each term referred to "documents or electronic messages (other than those mentioned in A.8) issued or transmitted in the country of shipment and/or of origin which the buyer may require for the importation of the goods and, where necessary, for their transit through another country". These wordings were reiterated in INCOTERMS 2000.

On 31 October 1994, the work in the ICC to create new instruments in the field of electronic commerce re-started after having been discontinued in 1990.

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157 Wheble was at the time a Honorary Chairman of the ICC Banking Commission as well as Joint Legal Co-Rapporteur of ECE Working Party 4. The document referred to is part of a set of letters and reports distributed to the relevant ICC Working Party in 1995.

158 UCP500&400 compared, Article 1, p.3.

159 See Chapter V.1., *ante*.

The intercommissionary project was first named *Project E-100*.[160] After the members of the ICC Commission on Maritime and Surface Transport had raised the need for multi-disciplinary discussions within the ICC on a possible review of the ICC´s activities in the field of international trade transactions, the group decided to start a review in response to developments in electronic commerce technology, major projects in the field of electronic trade, transport and financial data transfer, the increased risk and incidence of document forgery, the accelerated speed of modern goods transport and the evolution of EDI in local trade.

The Terms of Reference describe the initial meeting on 31 October 1994 as follows:

> "The participants agreed that the Committee´s initial objective should be to explore ways of developing a viable electronic alternative to existing international trade payment methods, in order better to meet the requirements of modern trading and transport practice. There was general agreement that this objective required a fundamental unbiased rethinking of the entire system. Any electronic alternative should learn from, though not necessarily be based on, existing practice."

It was decided under the Terms of Reference that the project should consider among other things the commercial viability of any proposed recommendation, legal and liability issues, security issues and links to related electronic services. To reach these ends, a number of working parties were established.

In April 1997, the E-100 Project reached its second phase and was renamed the ´Electronic Commerce Project´(ECP). The second phase had a clearer focus and concentrated on projects and ´deliverables´[161]. All policy issues were excluded from the Project to be dealt with by each relevant policy Commission of the ICC. An important aspect of the ECP was to develop partnerships with significant electronic commerce initiatives elsewhere. Under an ECP Steering Committee operated three working groups, namely those for E-terms, Information Security and Electronic Trade Practices.

In late 2001, the ICC decided to reorganise its working structure again, leading to the Commission on Telecommunications and Information Technology being renamed ´the Commission on e-Business, IT and Telecommunications´, and the Electronic Commerce Project (ECP) being thereby dissolved.

The outcome of the Electronic Commerce Project was good and bad. The ICC eventually created a number of new instruments, for instance the GUIDEC (now GUIDEC II), the eUCP, the ´Paction´ electronic sale contract, as well as a pilot project for E-Terms. The ICC has continued its activity by recently releasing the

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160 The very first name was actually ´Joint Committee of Electronic Trade Payment Systems´. See The Terms of Reference of the E-100, endorsed by the ICC Council at its 169th session on 14 June 1995, ICC doc no 321-35-3/10 REV.2.

The author of this study was present at that meeting representing the Finnish Section of the ICC.

161 This means rules and guidelines based on self-regulation, which are tangible ´products´.

E-Terms 2004. However, the most far-reaching ideas did not gain ground. Still, one should not underestimate the learning process which is involved in these kinds of efforts. That is a reason to give coverage to these issues in this study as well.[162]

Generally speaking, however, it should be noted that in the ICC´s project old trade instruments were given new impetus in electronic form, but no real ´new animals´ for international trade were created. It appears to be very difficult to create everyday commercial instruments in a laboratory, since there is no obligation for companies to adhere to new trading patterns. Business organisations do not have the same possibilities of investing in product development and marketing as companies do. Only if the benefits derived from new instruments are manifest is adherence guaranteed. On the other hand, most corporate solutions are limited to a restricted geographical area, and may involve restricted ´proprietary´ technology, whereas a global business organisation can create more neutral and comprehensive instruments, such as the ´eUCP´, deployed e.g. by the'*Bolero System*.[163] The problem of creating general rules is, however, their very abstract nature. Generally speaking, private incentive is the engine of new developments in electronic commerce and international trade payment and security systems. It is the task of legislators to see that there is an adequate legal infrastructure and still enough autonomy for electronic commerce to facilitate private incentive.

VII.8.3 Models of electronic credit

The development of an electronic alternative for documentary credits inspired organisations involved in the development of trade procedures to analyse what an electronic letter of credit should look like. This work resulted in conceptual models, which may have enhanced understanding of traditional trade procedures and paved the way for new solutions such as the *Bolero System* in its present shape.

The United Kingdom based The Simpler Trade Procedures Board (SITPRO) produced in the middle of the 1990s a conceptual model ´Towards replacing the paper based letter of credit´.[164] The SITPRO model was intended to provide a framework for discussing the development of a paperless credit that will meet the business requirements of paper-based documentary credit transactions. It described the business processes required and indicated the points at which electronic messages could fulfil those processes. It was developed to illustrate the maximum potential for using EDI, in particular the UN/EDIFACT messages, throughout a documentary credit´s operation and contained a detailed analysis of the required messages in each commercial phase.

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162 It seems also that some of the ideas have resurrected very recently, see Chapter VIII.7.5., *post*, for the *SWIFTNet Trade Services Utility*.

163 For the eUCP, see *infra*, and for documentary credits under the *Bolero System*, see VIII.7.1.6, *post*.

164 SITPRO (Simpler Trade Procedures Board), Electronic commerce, Towards replacing the paper based letter of credit, A conceptual model, version 1.0, 29/12/94 in ICC Doc No 321-35-3/8.

After the ICC had launched its E-100 Project, another model was created by a drafting group.[165] The objective was to explore ways of developing a viable electronic alternative to the payment systems used in international trade in order to meet more effectively the requirements of modern trading and transportation methods. The model for an electronic equivalent of the documentary letter of credit was referred to as an ´Electronic Trade Credit´.[166]

An Electronic Trade Credit (ETC) would have been more than a letter of credit set up and advised by electronic means. It was designed to constitute a method for banks to commit to pay on receipt of specified electronic messages from the shipper and third parties to a trade transaction, such as carriers or insurers. It proposed the use of digital signatures to prevent fraud. An ´Agreed Data Record´ relating to the commercial details of a shipment would have been used for contacting the relevant parties to the transaction in question.[167] The Agreed Data Record would have been based on the contract of sale. The difference between the ETC and an ´electronic letter of credit´ would have been that carriers and insurers would not have issued independent documents with contents which would have to comply with the terms of the credit, as is the case with tradional documentary credits, but that they would have issued confirmations in respect of the details required in the Agreed Data Record. For instance, a carrier would have confirmed that the goods described in the Record have been loaded on board "in apparent good order and condition" as the standard expression says. Moreover, an insurer could have certified that the consignment is covered by a marine policy against loss or damage in transit.

However, the ETC contained some original characteristics as compared to other comprehensive electronic trading schemes described in this study. For instance, there would have been a direct physical inspection of the goods in a case of dispute.This might have been undertaken by the companies who carry out the present pre-shipment inspections.[168]

Before that, a ´Cyber-Notary´, a neutral body employed by banks and other interested parties, would have been used to verify, in addition to the authenticity of messages (unless this was done by banks themselves), the correctness of data submitted. An example of such verification would have been, for instance, electronically contacting the Lloyd´s Register of Shipping to check that a vessel named in the transport messages actually has called the port specified at the specified time, and that the vessel is of an appropriate type and tonnage.

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165 Report to the Joint Committee on Electronic Trade Payment Systems (ETPS), submitted by the Strategic Drafting Working Party, ICC Doc No 321-35-3/8, 20/1/1995.

As already noted, the Electronic Commerce Project started on 31 October 1994 as the Joint Committee on Electronic Trade Payment Systems (soon to establish the E-100, later ECP). The Joint Committee had appointed a ´Strategic Drafting Working Party´ to report to it.

166 The name and idea of an ´Electronic Trade Credit´was advocated by the banking sector of the UK and was also favoured by Mr Bernard Wheble at the turn of the 1990s.

167 An Agreed Data Record was to be used so that the information contained therein could have been checked by all the recipients.

168 Verification services are offered by chambers of commerce in some countries in cases of dispute. Moreover, reference is made to the services of the ICC Centre for Technical Expertise.

The ETC was ambitious and interesting, but it is unclear under what institutional framework it would have been operating under. The banks are traditionally only interested in checking the documents which have to appear to comply on their face to the terms of the credit. Who would then have instituted a Cyber-Notary to check the whereabouts and the condition of the goods, and other commercial details, when even the traditional manual examination of documents is too expensive for bank customers? An ETC would not necessarily have respected the principle of the autonomy of the credit either, since the system linked the confirmations to the actual contract of sale and, moreover, presupposed some verification of facts by the system. Today´s letter of credit works with documents which evidence the facts stated therein only "on their face".

Another matter is that the documents used in the letter of credit contain legal information and can be subject to legal requirements as to their content (such as the Hague-Visby Rules requirements concerning bills of the lading), and a mere electronic confirmation of contractual details expressed in the Agreed Data Record might not suffice to satisfy the legal requirements. Many jurisdictions do not have a positive attitude towards the use of blank back bills of lading[169] or incorporating limitation of liability clauses by reference, and the ETC model would have gone even beyond that. Shipowners and other carriers certainly wish to see that that their smallprint, including particular or local clauses, is valid.[170]

As mentioner earlier[171], the Electronic Commerce Project of the ICC has later discussed a document called ´the Uniform Rules and Guidelines[172] for Electronic Trade and Settlement´ (URGETS) which was originally presented in conjunction with scenarios representing the idea of bringing the various parties connected to a sale of goods transaction under the same umbrella arrangement with a view to conducting the transactions electronically. The first draft[173] for the Rules established theoretical models for transaction-oriented trade finance, which could replace documentary credits. Although these models have not survived any better than the actual URGETS, it is important to note them, since they represent elaborated illustrations of the possibilities for electronic trading platforms.

The Electronic Trade and Settlement Process (ETSP) described in the first draft provided an overview of the four levels of ETSP functionality and described the ability of each level to provide risk mitigation. These levels were not copied from existing practice. [174] ETSP seems to have been based on an early model of

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169 For blank back bills, see Chapter VIII.2.1.6., *post*.

170 A confirmation of a list of goods can amount to a receipt, but if there are needs to clause a confirmation, the record produced draws closer to an equivalent of a document, but may not be acceptable by courts unless there is a specific legal framework allowing that. Reference is made to the presentation of the replication of the functions of paper documents in electronic form, see Chapter VI.2. to 4., *ante*.

171 See Chapter IV, *ante*.

172 The word ´guidelines´ was added at a later stage of the preparation.

173 Document ECP WG 1/13 of 12 October 1998.

174 The four levels were:
- Dematerialised Trade Transaction,
- Basic Functionality,
- Enhanced Functionality, and
- Financial Functionality. >>

the ETC in that the various third party service providers would not issue documents, only confirmations based on the requirements established by the contract of sale (Electronic Agreement, Agreed Data Record etc.), which are communicated to them for confirmation. However, whilst the examination of the

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<< In a *Dematerialised Trade Transaction,* the Buyer and Seller enter into an electronic sales contract with details such as the terms of delivery and the terms of payment, as well as service requirements by Third Party Service Providers (banks, insurance companies etc.). Extracts of contract are then used to form ETSP instructions to the Third Party

Service Contracts. Thir parties will perform their services and provide proof of performance in electronic form to the buyer.

After receiving these messages as well as the goods, the buyer will authorise payment in accordance with payment terms. This level does not provide protection against risks inherent in trade transactions.

In *Basic Functionality* the services of ´Trusted Service Supplier´ (a central registry) are used to process data and liaise with all parties to the trade. At this level of functionality, all messages are routed through the TSS, which will authenticate each message and forward it to the buyer. After receiving the messages and goods, the buyer will authorise payment in accordance with payment terms. This level also does not provide protection against risks inherent in trade transactions.

The *Enhanced Functionality* has four variations and introduces the concept of the ´automatic trigger of payment´ that will assist in mitigating seller´s risk as payment is no longer subject to buyer´s approval. The payment would be triggered through the buyer´s irrevocable ´Conditional Payment Order´ to his Financial Intermediary. The Trusted Service Supplier provides additional services by checking messages, providing confirmations and monitoring payments. The four variations cover situations where payment is triggered automatically or not, and the goods are or are not under the control of the TSS. In all these variations, the ability of the buyer´s Financial Intermediary to effect payment is solely based on the availability of funds in the buyer´s account.

Finally, the *Financial Functionality* has a process and message flow similar to the Enhanced Functionality except that in the Financial Functionality payment is guaranteed by the buyer´s Financial Intermediary, and additional guarantee may be given by a second Financial Intermediary (usually that of the seller´s). This functionality also includes automatic trigger of payment, and the goods are under the control of the TSS during the process. The buyer gives in advance an irrevocable Conditional Payment Order to his Financial Intermediary to pay upon the receipt of TSS´s Release of Payment Message. The TSS will check all the messages received to ensure they meet the ETSP requirements. Once the payment requirements are met, it will notify the buyer´s Financial Intermediary for payment. Message details enabling clearance of goods and authorisation to release goods to the buyer are not sent until payment is made.

The Financial Functionality model is close to the concept of an electronic equivalent of a paper-based letter of credit. However, the examination of documents is replaced by the checking of messages by the Trusted Service Supplier. (Some commercial models such as the late *Seadocs* and *@Global Trade* vest the task to examine documents to a third party; see also Chapter VIII.7.1.6., *post*, on *BoleroSURF*).

In those ETSP functionalities where the goods are under the control of the TSS, the TSS is acting as the ´trustee holder´ of the title of the goods. This would mean, in traditional terms, that the TSS is the holder of the electronic version of the document of title. In the paper world, when a bill of lading is consigned "to order" and indorsed in blank, the buyer´s Financial Intermediary (bank) has control and indirect possession of the goods by being the holder of a document of title. However, the bank can transfer the indirect possession and control by indorsing and/or delivering the document of title, or may choose to take delivery and ownership of the goods. In the ETSP, however, it is not anticipated that the Trusted Service Supplier would take delivery and title and become the physical owner or holder of the goods.

In the *Bolero System*, a Financial Intermediary holding the document of title is a ´pledgee holder´. However, the TSS is not a bank and does not need security. It is unclear whether a third party service supplier should use the construction of ´trustee holdership´ to run the services of a title registry. The concept of trust in Anglo-Saxon law follows from equity, which is unknown as a system to other legal cultures.

confirmations would have been done by banks in the ETC, the ´Cyber-Notaries´ taking care of the authentication of messages (and in some cases verification of certain data), the ETSP gave the ´Trusted Service Supplier´ the task to determine, in connection with levels using an automatic trigger of payment, that the conditions of payment have been met. Thus, it would no longer have been the ´Financial Intermediary´ (the bank) examining whether the preconditions for payment have been met.

For this type of system to work, the requirements established in the Electronic Agreement would have to be elaborate and indisputable for the carriers, freight forwarders, insurers etc. to issue their confirmations. In order to obtain an advanced level of clarity, highly standardised terms of delivery, insurance and shipment would have to be available. Otherwise, third party service providers would find it very difficult to confirm the service provided. In any case, the level of detail in contracts of sale would increase. This would have to be managed, in practice, by incorporating various sets of rules by reference. There would be a need for enhanced sophistication of standard terms in order to make them serve the anticipated system properly.[175]

A ´Trusted Service Supplier´ acting almost automatically could not react to ´conditional´ confirmations, but would have to refer these to the seller for negotiations. Banks could perhaps exonerate themselves from liability for unauthorised payment relating to confirmations in the way the UCP has enabled that possibility during the years, but how would the material liability for the malfunction of a Trusted Service Supplier be established? The *Bolero System* has relatively high compensation limits, and the liability is apparently covered by liability insurance.[176]

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175 I will illustrate the difficulties of the reference and confirmation system by an example:

Let´s imagine that the contract of sale is made using the trade term CIF INCOTERMS 2000 Calcutta. The contents of this Incoterm, which are laid down in ICC Publication No 560, presuppose that the seller has to contract for carriage *"on usual terms...to the named port of destination by the usual route in a seagoing vessel...of the type normally used for the transport of goods of the contract description"*. The carrier could confirm that the goods have been loaded on board vessel X and refer to its standard conditions incorporating the Hague-Visby Rules (which incorporation could be relevant in the absence of a bill of lading).

It is unclear whether these standard terms would become binding if they were communicated by a reference only to the´Trusted Service Supplier´, which would not be a party to a contract of transport. Perhaps a TSS could be regarded as an agent of all parties concerned (like Bolero International in the Bolero System). If, however, a TSS were to be regarded as a party to the contract of carriage by virtue of being a ´trustee holder´ of a document of title, it would then become liable for freight against the carrier.

The ´usual terms´ may differ from port to port as to the division of costs and tasks as regards loading and discharge. At the buyer´s end, the costs may be levied on the buyer as the consignee. Therefore, detailed provisions as to the division of costs and tasks may be useful in the contract of sale. But will the carriers accept ´ solutions tailor made´ by others?

Moreover, the term CIF INCOTERMS 2000 requires the seller to obtain insurance only in accordance with the minimum cover of the Institute Cargo Clauses. Normally, however, the buyer needs a better cover, and this has to be elaborated in detail in the contract of sale, so that no surprises happen.

176 See Chapter VIII.7.1.8., *post*.

VII.8.4 The application of UCP500 to electronic credits – the ´eUCP´

In the spring of 2000, the ICC Banking Commission appointed a working group with the task to create an addendum to UCP500 to clarify the position with regard to electronic presentation of documents under documentary credits. The ICC adopted the eUCP in November 2001, and they came into force on 1 April 2002.[177]

The ICC calls normally for expressions of support from the banking industry and publishes lists of banks or their organisations committing themselves to adhere to them. One of the first adherents to the eUCP was Bolero.net, which promised that its messaging would be eUCP compliant right from the start, 1 April 2002. The service concept of the Bolero network will certainly benefit from the new rules and the network will certainly be one of the main utilisers of the new rules.[178]

VII.8.4.1 The scope of the eUCP

The eUCP is an optional supplement to the eUCP rules, which is stated in Article e1: "the UCP Supplement for Electronic Presentation (´eUCP´) is intended to supplement the Uniform Customs and Practice for Documentary Credits (1993 Revision ICC Publication No. 500, ´UCP´) to accommodate presentation of electronic records alone or in combination with paper documents."[179] The rules thus attach themselves to UCP 500, and address the sole issue of electronic presentation. The Working Group did not see the need to address any issues relating to the issuance or advice of credits electronically, since current market practice and the UCP have long allowed for credits to be issued and advised electronically.[180]

Like the GUIDEC and other ICC documents, the eUCP has been specifically drafted to be independent of specific technologies and developing electronic commerce systems. Therefore it does not address specific technologies or systems necessary to facilitate electronic presentation.[181] The parties can choose these according to their own preferences.

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177 As the eUCP is to be applied in conjunction with UCP 500 (in the first place at least), the Articles contained in eUCP are marked with the letter ´e´ to distinguish them from the articles of UCP500.

178 The Bolero website quotes a representative from a bank having signed up to the system saying "(t)he core requirement of the eUCP for document authentication would require each trading party around the world to manage and access potentially all the worlds´s certification authorities. This would be impractical. The only way to proceed is via a trust broker´s central hub."

179 The eUCP is specific to UCP500, and, if necessary, may need to be revised as technologies develop, perhaps already prior to the next revision of the UCP. For that purpose the eUCP is issued in version numbers that will allow for a revision and subsequent version if the need arises. Excerpts from the final Working Party draft, DCI Vol 7 No 4, October-December 2001, p. 2.

180 Ibid.

181 The Introduction of the eUCP.

The eUCP has been written to allow for presentation completely electronically or to allow for a mixture of paper documents and electronic presentation. It is therefore possible that some documents, such as the invoice, packing list and insurance certificate are presented electronically, whilst, for example, a bill of lading and export/import clearance certificates are paper documents. The Working Party believed that providing exclusively for electronic presentation would not be entirely realistic and would not promote the development of the transition to total electronic presentation.

The application of eUCP requires, like UCP500, that it is incorporated into the text of the credit.[182] The Working Group did not want the supplement to be added to UCP500 without specific incorporation by the parties. According to one member of the Working Group, it was felt that "this would open the door for unanticipated electronic presentations when the parties and financial institutions may not be in a position to handle them and that this would result in the exclusion of eUCP articles in a majority of credits".[183] This wording also ensures that where an electronic presentation is anticipated, the parties will know that they are covered by the supplementary articles included in the eUCP. However, as is the case with the UCP, it is conceivable that it could come into application through the use of SWIFT or through customary law without an express reference.

A credit must indicate the applicable version of the eUCP. If it does not do that, it is subject to the version in effect on the date the credit is issued, or, if made subject to eUCP by an amendment to the credit, to the version in effect on the date of that amendment (Article e1(c)).

According to Article e2, a credit subject to eUCP is also subject, without express incorporation, to the UCP. Therefore, a single reference to the eUCP might suffice to incorporate both sets of rules in the credit. A standard reference will undoubtedly cover both texts.[184]

If there is discrepancy between the two sets of rules, the provision in the eUCP prevails to the extent it would produce a result different from that produced by the UCP.

VII.8.4.2 Electronic records as documents

Article e3 contains the definitions used in the rules. Where specific words or phrases used in the UCP are defined in the eUCP, these definitions, unless otherwise stated, apply wherever the terms appear in the UCP.[185]

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182 The incorpration of the eUCP suffices to incorporate UCP500 as well.

183 Bill Cameron on what remains to be done before the new eUCP takes final form, Documentary Credits Insight Vol. 7 No 3 July-September 2001 p. 2.

184 For instance, the Bolero reference contained in the eUCP XML Guide: "This Bolero document shall be subject to the Uniform Customs and Practice for Documentary Credits, 1993 Revision, ICC Publication No. 500 and the Supplement to the Uniform Customs and Practice for Documentary Credits for Electronic Presentation ('eUCP') unless the terms of the credit state otherwise."

185 The Working Group is said to have reviewed, in drafting the eUCP, various definitions used in other ICC documents as well as rules and regulations promulgated by governmental and international bodies.

An ´electronic record´ is defined by requiring authenticity and integrity for the message. It is "data created, generated, sent, communicated, received or stored by electronic means that is capable of being authenticated as to the apparent identity of a sender and the apparent source of the data contained in it, and as to whether it has remained complete and unaltered, and is capable of being examined for compliance with the terms and conditions of the eUCP Credit". A telefax message in its traditional sense would not be an electronic message, but under today´s technology the answer is more complex.[186]

The use of electronic records in lieu of paper documents renders it impossible to refer to originals or copies as such. Reference can be made, however, to Article 8 of the UNCITRAL Model Law on Electronic Commerce, which contains requirements for a data message to constitute a functional equivalent of an original document required by law. The eUCP tackles the problem by equating originals and copies. Article e8 makes it clear that "any requirement of an UCP or eUCP Credit for presentation of one or more originals or copies of an electronic record is satisfied by the presentation of one electronic record". The requirements for an ´original´ within the meaning of the Model Law could be met by the definition of an ´electronic record´ in the eUCP.[187]

Unless an electronic record contains a specific date of issuance, the date on which it appears to have been sent by the issuer is deemed to be the date of issuance. (Article e9) If an electronic record evidencing transport does not indicate a date of shipment or dispatch, the date of issuance of the electronic record will be deemed to be the date of shipment or dispatch.[188]

The date of receipt will be deemed to be the date it was sent if no other date is apparent. However, an electronic record is 'received', according to the Article e3 definitions, when it enters the information system of the recipient designated in the credit in a format capable of being accepted by that system. It is added that any acknowledgement of receipt does not imply acceptance or refusal of the electronic record.

The ´place for presentation´ in the case of electronic records means an electronic address.

The eUCP contains its own definition for electronic signature, which here means "a data process attached to or logically associated with an electronic record

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186 Guide to the eUCP, p. 81.

187 The eUCP definition and the requirements in Article 8 of the Model Law are very similar. The Model Law states "there exists a reliable (cf. ´apparent´) assurance as to the integrity of the information from the time it was first generated in its final form, as a data message or otherwise". The Guide to Enactment of the Model Law stresses (on pages 35 and 36) that the requirements (here: reliability) should be seen as a minimum.

Reference is made to the ICC Banking Commission´s policy statement "The determination of an 'original' document in the context of UCP500 sub-article 20(b)". This statement represents the standards of authenticity prevailing at present in the banking world. See Chapter VIII.6.2.1., *post*.

188 Article e10. If an electronic record bears a notation that evidences the date of shipment or dispatch, the date of the notation will be deemed to be the date of shipment or dispatch. A notation showing additional data content need not be separately signed or otherwise authenticated.

and executed or adopted by a person in order to identify that person and to indicate that person´s authentication of the electronic record".[189]

VII.8.4.3 Presentation under the eUCP

The presentation of a record is format-linked so that a bank must be technically able to receive a presentation of a credit. Should it not be able to do that, it may be forced to turn down an invitation to be the nominated bank for a given credit. Article e4 provides that an eUCP Credit must specify the formats in which electronic records are to be presented. If the format of an electronic record is not so specified, it may be presented in any format.[190]

An eUCP Credit allowing presentation of electronic records must state a place for presentation of the electronic records. Should an eUCP Credit allow for presentation of both electronic records and paper documents, it shall also state a place for presentation of the paper documents.[191]

Each presentation of an electronic record and the presentation of paper documents under an eUCP Credit must identify the eUCP Credit under which it is presented. A presentation not so identified may be treated as not received. An electronic record that cannot be authenticated is deemed not to have been presented.

VII.8.4.4 Notice of completeness needed

Electronic records may be presented separately and need not be presented at the same time. The beneficiary is responsible for providing a notice to the bank to which presentation is made informing that the presentation is complete. The notice of completeness may be given as a paper document or electronic record and must identify the eUCP to which it relates. Presentation is deemed not to have been made if the beneficiary´s notice is not received. This is a difference as compared to paper documents under UCP500. The requirements for a presentation are that the message has entered the bank´s system and it is authenticated by the bank´s systems.

VII.8.4.5 Examination of electronic records

Article 6 contains some provisions relating to the examination of electronic records. These include a provision on hyperlinks to an external system, the role of a Nominated Bank and the inability of a bank to examine the credit in a special format.

If an electronic record contains a hyperlink to an external system or a presentation indicates that the electronic record may be examined by reference to

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189 For the role of electronic signatures in documentary credit process, see Chapter VIII.6.2.2., *post*.

190 That means that a presentor could have fulfilled his obligations by presenting the document in any format and the bank´s liability to pay would arise irrespective of whether it has been able to receive it. Compare the situation under ISP98.

191 Article e5 point a.

an external system, the electronic record at the hyperlink or the referenced system shall be deemed to be the electronic record to be examined. The failure of the indicated system to provide access to the required electronic record at the time of examination shall constitute a discrepancy.

When a nominated bank forwards, pursuant to its nomination, electronic records, this is deemed to signify that it has checked the apparent authenticity of the electronic records. The inability of the issuing or confirming bank to examine an electronic record in a format required by the eUCP credit is not a basis for refusal of the documents. If no format is required by the credit, the issuing or confirming bank cannot refuse it at all by referring to the format.

Article e3(a)(i) of the eUCP provides that the expression "appears on its face" contained in UCP500 shall apply to the examination of the data content of an electronic record. This means that an electronic record is examined only for the data received and not the reality that it represents. Even where there is an express reference to external systems that may provide added assurance of the validity of the data, the examination under the eUCP is limited to the data provided at that site or system and not of the underlying reality represented.[192] This does not mean the examination only of the data that appears on the screen of the examiner. Examination of data is namely related to the content required to ascertain compliance with the terms of the credit.[193]

VII.8.4.6 Time for examining the documents not shortened

If the bank to which presentation is to be made is open but its system is unable to receive a transmitted electronic record on the stipulated expiry date and/or the last day of the period of time after the date of shipment for presentation, as the case may be, the bank will be deemed to be closed and the date for presentation and or the expiry date shall be extended to the first following banking day on which such bank is able to receive an electronic record. If the only electronic record remaining to be presented is the notice of completeness, it may be given by telecommunications or by paper document, and will be deemed timely, provided that it is sent before the bank is able to receive an electronic record (Article e5 e).

According to Article 13(b) of UCP500, the issuing bank, the confirming bank, or a nominated bank acting on their behalf shall each have a reasonable time, not to exceed seven banking days following the day of receipt of the documents, to examine the documents and determine whether to take up or refuse the documents and to inform the party from which it received the documents accordingly. However, as noted earlier, seven days is the maximum and does not represent reasonability in all cases.

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192 Guide to the eUCP, p. 47.

193 Ibid. The Guide adds that the format of a computerised program used to view the electronic record may hide certain data and only show the data it is programmed to reveal. Some of this suppressed data may necessitate examination for some purposes and not others. Certain header or footer tags will be reviewed in authenticating the transmission or ascertaining the data sent or received. It is not expected, however, that any prior correction to the document that may be embedded in the message transmitted will be taken into account.

The working group having drafted eUCP tried to create a special eUCP provision for all-electronic presentation of documents by shortening the seven-day period contained in Article 13(b) of UCP500. There was "strong sentiment in the Working Group to shorten this period in the case of all-electronic presentations – because technology should allow for a quicker turnaround – the suggestion was rejected by ICC national committees, who apparently believed that setting up different time frames would result in unnecessary confusion".[194] Therefore a provision to this effect was dropped from the final version.

The time period for the examination of documents commences on the banking day following the banking day on which the bank receives the the notice of completeness by the beneficiary. If the time for presentation of documents or the notice of completeness is extended, the time for the examination of documents commences on the first following banking day on which the bank to which presentation is to be made is able to receive the notice of completeness (Article e7 a).

VII.8.4.7 Rules on rejection

Pursuant to Article 14(d) of UCP500 the issuing, confirming or nominated bank - as the case may be - deciding to refuse the documents must give notice to that effect by telecommunication, or, if that is not possible, by other expeditious means, without delay but no later than the close of the seventh banking day following the day of receipt of the documents. Such notice shall be given to the bank from which it received the documents, or to the beneficiary if it received the documents directly from him, and must state all discrepancies in respect of which the bank refuses the documents.

The eUCP contains a provision (Article e7 b) stating that if an issuing or confirming bank, or a nominated bank acting on their behalf, provides a notice of refusal of a presentation which includes electronic records and does not receive instructions from the party to which notice of refusal is given within 30 calendar days from the date the notice of refusal is given for the disposition of the electronic records, the bank shall return any paper documents not previously returned to the presenter but may dispose of the electronic records in any manner deemed appropriate without any responsibility.

VII.8.4.8 Corruption of records

A provision akin to Article e7 b is to be found in Article e11 concerning the corruption of an electronic record after presentation. Electronic records (which are actually documents presented in electronic form) may contain viruses or be in a corrupted form and cannot therefore be processed. This problem may make it inadvisable or difficult to open the messages which contain the records. The message that enters a system has to be "in a format capable of being accepted by (the) system". If a message containing a record does not meet these requirements, a record should consequently be deemed not to have been

[194] eUCP Final vesion approved, DCI Vol 8 No 1, January-March 2002 p. 2.

presented. But, as has been pointed out, the case of a virus in the system may be different, because the record may be capable of entering the information system of the designated recipient, but the recipient may be forced to reject it because of the danger it presents to other data contained in his system.[195]

Article e11 addresses this problem by stating that if an electronic record that has been received by the issuing bank confirming bank or another nominated bank, appears to have been corrupted, the bank may inform the presenter and may request that the electronic record may be represented. Should the bank request this, the time for re-examination is suspended and resumes when the presenter represents the electronic record. If the same electronic record is not re-presented within thirty calendar days, the bank may treat the document as not presented.[196] No deadlines are extended.

The inclusion of Article e11 was one of the most disputed items in the discussion within the ICC. Those opposing its inclusion considered this to be left to national law. According to them, it would have been a mistake for an organisation like the ICC to create rules dealing with dispute situations, in which the parties are arguing who has made a mistake. Furthermore it was argued that it is unclear what ´corruption´ means in this context. Finally, the 30-day maximum period was considered to be too long a time for a re-presentation to be made. In the end, however, the Article was accepted, largely because the process introduced by it is optional for the bank. In other words, the bank has has a choice to reject the record or to request a re-presentation. If the bank chooses to apply Article e11, it will have to deal with the beneficiary directly.

VII.8.4.9 Additional disclaimer

As already noted, UCP500 contains two disclaimer provisions exonerating the banks involved in a documentary credit transaction from liabilities arising in connection with it.

According to Article 15, banks assume no liability or responsibility for the form, sufficiency, accuracy, genuineness, falsification or legal effect of any documents. Neither do banks assume responsibility for the goods represented by the documents, or for the acts or omissions of persons involved, like carriers, forwarders or insurers.

In addition, pursuant to Article 16, banks assume no responsibility arising out of delay or loss in transit of messages or documents. Neither do banks assume liability for delay, mutilation or other errors arising in the transmission of any telecommunication. There is a further disclaimer for translation errors and errors in the interpretation of technical terms.

The drafters of the eUCP found it appropriate to add an additional disclaimer of liability for presentation of electronic records under the eUCP in Article e12 of

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195 Cameron in Documentary Credits Insight Vol. 7 No 3 July-September 2001 p. 2.

196 If the Nominated Bank is not the Confirming Bank, it must provide the Issuing Bank and any Confirming Bank with notice of the request for representation and inform it of the suspension.

the Rules. This Article states that "by checking the apparent authenticity of an electronic record, Banks assume no liability for the identity of the sender, source of the information, or its complete and unaltered character other than that which is apparent in the electronic record received by the use of a commercially acceptable data process for the receipt, authentication and identification of electronic records".

The bank can thus rely on what is ´apparent´ in the record. Furthermore, the bank need use only ´commercially acceptable´ data processes. It is submitted that this allows the bank to use standard processes, which are within reasonable costs, for the identification and need not invest in particularly expensive or sophisticated processes. There is thus no absolute duty to use Public Key Infrastructure. This provision may help to make more banks operative in electronic systems. The standard that the eUCP imposes for banks is lower than that envisaged for an "addressee" under Article 13 (attribution of data messages) of the UNCITRAL Model Law on Electronic Commerce which requires the use of reasonable care (paragraphs (4)(b) and (5)).

The disclaimers of the eUCP and UCP500 have to undergo the litmus test of national law. Modern commercial law namely allows parties to allocate the risk of negligence up to but not including gross negligence or wilful misconduct. However, as it is stated in the ICC Guide to the eUCP[197] "most systems of local law require more specific and detailed provisions than those contained in UCP500 to achieve this result". The Guide states that the liabilities disclaimed in the eUCP and UCP500 are the result of external systemic or third party actions, inactions or risk.

VII.9 Electronic presentation under the ´sister rules´

By the beginning of 2002, only UCP500 had been amended by a supplement applicable to electronic presentations.

As for documentary collections, URC522, which came into effect at the beginning of 1996, does not mention either electronic documents or presentation. A commentary on URC522[198] states, regarding ´EDI collections´, that "there is considerable uncertainty on a number of matters in connection with Electronic Data Interchange, and as those include legal issues, it was not considered feasible to attempt to write rules to cover such items this time".

In a documentary collection arrangement, documents are presented by the presenting bank to the drawee in order to obtain payment or acceptance of draft. Generally, documents are divided into ´financial documents´ meaning bills of exchange, promissory notes, cheques, or other similar instruments used for

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197 On page 146.

198 ICC Publication No. 550, p. 10.

obtaining the payment of money, and ´commercial documents´ meaning invoices, transport documents including bills of lading being documents of title and any other documents not being financial documents. However, it should be noted that a collection instrument is not governed by pre-set guidelines such as those in a letter of credit. Therefore an importer and exporter can agree on any documentation to see the collection reach fruition. The banks in a collection chain are merely acting as intermediaries based upon the initial paperwork provided by the principal.[199]

In documentary collection arrangements, the drawee (the buyer receiving the documents in exchange for cash or the acceptance of a bill of exchange) is not a bank but could be any commercial undertaking. Therefore electronic presentations are less practical than they are in documentary credits. There is no obstacle of making also collections electronic, if the documents could be presented to the drawee in an electronic form, and the drawee can make use of those documents with the carrier and import formalities. The ´documents´ or messages can be transmitted directly to their ultimate recipients.

As early as the 1980s, *Skandinaviska Enskilda Banken* of Stockholm concluded agreements with several European banks to carry out paperless collections. The scheme used is interesting but it contained limitations.[200] The ICC Electronic

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199 ICC Banking Commission Opinion R439 from the 2000-01 Queries.

200 In that scheme only the transport documents were sent electronically through banks. Other documents were sent to the buyer by post. The scheme operated in the following manner:

1. When the seller ships the goods, he instructs the carrier that they are to be consigned to the collecting bank, which is noted in the transport document.

2. The seller gives his collection instructions and the transport document to the remitting bank, whilst mailing all other documents.

3. The remitting bank teletransmits its collection order to the buyer´s country.

4. The collecting bank notifies the importer that the goods will be released against payment. Alternatively, the buyer can sign a promissory note to make payment on deferred terms.

5. The collecting bank advises the remitting bank by telecommunication when payment has been made and goods released.

6. The remitting bank credits the customer´s account after deducting any charges.

An essential feature of this system is that the consignee is the collecting bank. The earlier version of the ICC Uniform Rules for Collections (URC322 from 1978) did not allow this, due to which an express agreement by the parties involved to the contrary was necessary. The present Rules, URC522, make this possible, if the collecting bank gives its consent thereto. The system did not work if a bill of lading was issued, because in that case an original document had to be surrendered when the goods were released. (Rowe, pp. 159-162)

It is arguable that an electronic bill of lading based on a central registry such as that in the *Bolero System* could make it possible for the collecting bank to be designated to act as a ´Pledgee Holder´ or equivalent until it has received payment, at least when the bank has advanced finance. On the other hand, a non-negotiable document, such as a road, rail or air transport document, as well as a combined transport document issued by a freight forwarder, would not be relevant in the hands of the buyer, should he have been named as the consignee, after the goods had reached their destination. However, if the seller retains the duplicate of a railwaybill, he can dispose of the goods until these reach their destination.

Commerce Project sketched, at its initial stages, an ´Electronic Collection´, which would have had some similar characteristics as the ´Electronic Trade Credit´.[201]

As regards contract guarantees or bonds, whether ancillary, documentary or simple demand guarantees, as well as standby letters of credit, the practice is, as stated in the Preface[202] of ISP 98, "more conducive to electronic presentations", which is because "standbys infrequently require presentation of negotiable documents". This applies to all guarantee undertakings.

The possibility to use electronic documents in a guarantee or standby raises at least three issues. The first is, whether the guarantee (or counter-guarantee) can be issued electronically. The second and perhaps more relevant is, whether documents stipulated in the terms of the guarantee to trigger payment can be presented electronically. The third is whether electronic communications are permitted to make the communications and notices envisaged in the guarantee.

The newer ICC guarantee and bond rules do take into account the existence of electronic documents, and this would seem to facilitate both the issuance of an electronic letter of guarantee as well as the presentation of electronic documents in accordance with the terms of the guarantee. Furthermore, various communications such as the rejection of documents or release from liability could take place electronically, subject to the conditions explained later in connection with each set of rules.

The earliest set of the ICC guarantee rules, the Uniform Rules for Contract Guarantees (URCG325), is from 1978 and, due to this, the technical development of markets had not made electronic documents or presentations an issue yet. There would be nothing, however, to prevent the principal, the instructing party and the ultimate guarantor from adding a clause to this effect. The documents may be specified in the guarantee. These could include court decisions or arbitral awards, but could also be less stringent, should the guarantee so provide.

The ICC Uniform Rules for Demand Guarantees (URDG458) are comparable to letters of credit in the sense that documents play a determinant role for the bank in ascertaining whether it is obliged to pay in accordance with the terms of the guarantee. Therefore the form and contents of the documents, as well as the

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201 Report to Joint Committee on Electronic Trade Payment Systems (ETPS), submitted by the Strategic Drafting Working Party, ICC Doc No 321-35-3/8, 20/1/1995, pp. 45-46. For the Electronic Trade Credit, see *supra*.

In the ´Electronic Collection´ (EC), the seller would have specified the Agreed Data Record. Both the seller and third parties (carrier, insurance company etc.) nominated by the seller would have issued confirmations on the accuracy of the data. The confirmations would have been authenticated by digital signatures. The seller´s bank would have sent the EC electronically to the bank in the buyer´s place for collection. Both the ETC and EC models would have facilitated, at least it is stated so, the use of the bill of lading as a negotiable instrument. The drafts do not specify how this would have been done. Obviously, a Private Key as envisaged in the CMI Rules for Electronic Bills of Lading could pass on to the importer in exchange for a draft.

However, if the buyer or seller would have liked to use the bill of exchange´s character as a negotiable instrument commercially in connection with the Electronic Collection, this would not have been possible under the envisaged system.

202 ISP98, ICC Publication No 590, p. 7.

examination of them to see whether they appear on their face to conform to the terms of the guarantee, are essential.

URDG458 applies, in addition to traditional paper-supported guarantees, to guarantees issued electronically. The issue of guarantee may be preceded by the instructions of the principal and the instructing party in electronic form.[203]

URDG458 contains an express provision in Definitions (Article 2 (d)) stating that the expressions ´writing´ and ´written´ shall include an authenticated teletransmission or tested electronic data interchange message (´EDI´) message equivalent thereto. According to *Affaki,* tele-transmission and EDI cover a wide range of communications, including cable (wire), telex, facsimile, SWIFT, electronic files sent through the Internet and even telephone messages if they can be converted into an electronic or paper format.[204]

Affaki adds that the above-mentioned means of communication are valid, if the messages "can be authenticated or tested in a way that allows for (i) the identification of both the sender and the recipient, and (ii) the integrity of the message to be ensured by confirming its authenticity and its non-repudiation (including, if need be, the use of the services of a certifying third party)...". According to this, the expression "tested electronic data interchange message" has a meaning which conforms to the standard requirements for binding electronic messages, namely that messages can be authenticated (verified to have been sent by the right person), have integrity (they must have come through in their entirety and in an unaltered form) and cannot be repudiated.[205] A claim made by a telefax message can be refused since although the telefax is a form of teletransmission it is not authenticated. The normal and proper practice in such cases is to require the telefax to be confirmed by an authenticated instruction.[206]

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203 The working group which drafted the eUCP anticipated that letters going electronic would eliminate the role of the advising banks and thereby gradually make the four-partite relationship a three-partite relationship. According to the same commercial logic, the need for the instructing party to transfer the instructions to the ultimate guarantor would disappear, and instructing parties would issue guarantees themselves more often. This kind of situation might take place in standby letters of credit as well. In the demand guarantee and standby L/C practice a four-partite model would however be needed for commercial reasons.

204 Affaki, p. 55.

205 Cf. the definition of ´electronic record´ in the eUCP states among other things that (the record) "is capable of being authenticated as to the apparent identity of a sender and the apparent source of the data contained in it, and as to whether it has remained complete and unaltered...". This definition adds to the concept of authentication (in addition to verifying the sender) the need to verify the apparent source of data. It would be useful to add this definition to the guarantee rules, since the data replacing documentation required to trigger payment may come from a third party, for instance, a certificate from a designated expert.

The eUCP definition does not, however, mention that the recipient of the message should be mentioned expressly. Neither does it state the need for non-repudiation of the message. It is submitted that these obvious characteristics have been left out as unnecessary bearing in mind the development of interchange techniques. Affaki mentions, however, the authentication requirement in the context of the issue of an electronic guarantee, in which case the beneficiary has to be mentioned (and the guarantee letter sent to him).

206 Goode, Guide to the ICC Uniform Rules for Demand Guarantees, ICC Publication No 510, p. 48.

The same provision, Article 2(d), also permits the presentation of a demand, including a statement of breach[207], in electronic form. As already explained before, Article 20 of these Rules provides that "any demand for payment under the guarantee shall be in writing and shall be supported by a written statement stating that the principal is in breach of his obligations under the underlying contracts and the respect in which the principal is in breach". The possibility of using electronic presentations does not require that the demand guarantee in question has been issued in electronic form. It is also possible to combine paper documents and electronic documents in the presentation. The demand is validly presented if all the documents, whether electronic records or paper documents or both are presented within the validity period of the undertaking (i.e. before the Expiry Date or the Expiry Event whichever occurs first).

The ICC Uniform Rules for Contract Bonds (URCB524) from 1993 mention consistently EDI among the means of conducting messaging. Article 7 of the Rules (Submission of claims and claims procedure) point (b) provides that a claim submitted by authenticated tele-transmission, EDI, telex or other means of telefax, facsimile or electronic transmission shall be deemed to be received on the arrival of such transmission. There is no rule here for when the message is considered to have arrived. Recourse could be had to other rules specifying when a message is deemed to be received. Article 15 of the UNCITRAL Model Law on Electronic Commerce provides an answer to this question, just like the UNCID rules and the interchange agreements based thereon.

URCB524 does not, however, give electronic messages full legal significance. Point (e) of Article 7 states namely that the beneficiary shall, when giving notice of any claim by telefax, other teletransmission or EDI, also send a copy of such claim by post. Correspondingly, point (l) of Article 7 provides that the guarantor, after having considered any claim expeditiously, in the case he wishes to reject the claim, shall immediately give notice thereof to the beneficiary by authenticated tele-transmission or other telefax, facsimile transmission, telex, cable or EDI, confirming the same by a letter, setting out the grounds for the refusal.

Further to the exchange of communications, it is worthwhile to study whether the Rules allow presentation of electronic documents. It should be highly stressed, however, that the presentation of documents under an accesory guarantee is not a trigger mechanism of payment as it is in demand guarantees or letters of credit. The documents required to establish a default under URCB524 are, as has been stated earlier, a certificate of default by a third party (an expert) or by the guarantor himself, or a final judgement or arbitral award. A guarantee (surety) under URCB524 can thus be made largely ´documentary´.

The Rules do not expressly state that these mentioned documents could be in electronic form. However, the Definitions (Article 2) state, like URDG458, that ´writing and written´ shall include any authenticated tele-transmissions or tested electronic data interchange (EDI) message equivalent thereto. This would in my view enable the issue of relevant certificates in electronic form. However, Article 7 point (j)(i) requires that the certificate of default (or a certified copy thereof) issued by a third party be served on the guarantor. As stated above, the service requirements do not facilitate pure electronic communications, since copies of

[207] This statement can be included in the demand itself.

documents have to be mailed as well. The requirement to send a mail copy seems very much a precautionary measure, and therefore an electronic record should be sufficient to meet the expiry date stipulated in the guarantee.

It is imaginable that in the future, court judgements and arbitral awards could be retrieved and presented in electronic form under accessory guarantees to the extent allowed by the relevant legislation. So electronic documents are an issue with the URCB524 as well. Procedural documents will be examined in greater detail in Chapter IX, *post*.

The International Standby Practices (ISP98) apply, like UCP500 and URDG458, to independent undertakings, where payment obligation is triggered by the presentation of stipulated documents. ISP98 goes into more detail by proposing requirements to meet where the standby permits or requires presentation by electronic means. The general rule is namely that the standby must expressly permit electronic presentation, save one exception (see the details of ISP98 Rule 3.06 *infra*).

The Definitions of ISP98 (under Terminology, Rule 1.09(a)) state that a ´document´ means "a draft, demand, document of title, investment security, invoice, certificate of default, or any other representation of fact, law, right, or opinion, that upon presentation (whether in a paper or electronic medium) is capable of being examined for compliance with the terms and conditions of a standby". ´Signature´ is defined to include "any symbol executed or adopted by a person with a present intent to authenticate a document". This definition covers both handwritten and electronic signatures as is in line with the content of the various definitions of electronic signature.

Rule 1.09(c) of ISP98 deals explicitly with electronic presentations giving meaning to terms in a standby providing for or permitting electronic presentation unless the context otherwise requires.

These definitions correspond to other similar definitions, but are (probably due to the requirements set by American legal practice) more elaborate than their counterparts in the sister-rules of ISP98.[208]

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[208] An ´electronic record´ is defined in ISP98 to mean "a record (that is inscribed on a tangible medium or that is stored in an electronic or other medium and is retrievable in perceivable form, is communicated by electronic means to a system for receiving, storing, re-transmitting, or otherwise processing information (data, text, images, sounds, codes, computer, programs, software, databases, and the like) and is capable of being authenticated and then examined for compliance with the terms and conditions of the standby".

An electronic record is ´authenticated´ when it is verified by generally accepted procedure or methodology in commercial practice to check: i. the identity of a sender or source, and ii) the integrity of or errors in the transmission of information content. The criteria for assessing the integrity of information in an electronic record is whether the information has remained complete and unaltered, apart from the addition of any indorsement and any change which arises in the normal course of communication, storage and display.

An ´electronic signature´ is said to mean letters, characters, numbers, or other symbols in electronic form, attached to or logically associated with an electronic record that are executed or adopted by a party with present intent to authenticate an electronic record.

Finally, a ´receipt´ (of a record) is said to occur when an electronic record is entered in a form being capable of being processed by the information system designated in the standby, or an issuer retrieves an electronic record sent to an information system other than that designated by the issuer. >>

Rule 3.02 lays down the requirement for the bank to check individual documents, even if a full set of documents is not furnished. The receipt of a document required by and presented under a standby constitutes a presentation requiring examination for compliance with the terms and conditions of the standby even if not all the required documents have been presented.

Rule 3.06 deals with the medium of presentation. To comply, a document must be presented in the medium indicated in the standby. Where no medium is indicated, to comply, a document must be presented as a paper document, unless only a (written) demand is required, in which case a demand that is presented via SWIFT, via tested telex or via similar authenticated means by a beneficiary that is a SWIFT participant or a bank complies with the credit as to its medium. In other situations, a demand that is not presented as a paper document does not comply unless the issuer permits, in its sole discretion, the use of that medium.

A document is not presented as a paper document if it is communicated by electronic means even if the issuer or nominated person receiving it generates a paper document from it. Where presentation of an electronic medium is indicated, to comply a document must be presented as an electronic record capable of being authenticated by the issuer or nominated person to whom it is presented.

The text does not explicitly deal with the format of electronic presentation. However, the requirement that the record must be capable of being authenticated by the issuer or nominated person means that the message must have been received ín a format which makes it possible to verify the sender as well as the integrity of the message.

ISP98 deals with electronic presentations with a specificity comparable to the eUCP. There appears to be no discrepancy between the practical handling of electronic presentations. The eUCP is said to apply where the credit indicates that it is subject to the eUCP. Thus, it has to be incorporated explicitly. For situations where no incorporation has taken place, but electronic presentation is made, the electronic records are thought to comply generally if the possibility to present them electronically is otherwise in accordance with the terms of the credit. ISP98, however, lays down a rule that in certain cases (in inter-bank relations where a simple demand is transmitted) an electronic presentation will always comply, and in other cases the issuing bank may accept electronic presentation.

It is interesting to note that the different sets of rules published by the ICC differ to some extent in their technical construction, but not perhaps as regards the substance of electronic presentations. It could be useful to seek to harmonise the wordings in the next revision round making the rules correspond more

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<< There is no explicit rule on the place of electronic presentation. It is apparent that an electronic mail address should be specified in the credit for this purpose. Should this not happen, Rule 3.04 provides rules that can be followed even in the case of electronic presentations. If no place of presentation to the issuer is indicated in the standby, presentation to the issuer must be made at the place of business from which the standby was issued. Furthermore, if no location at the place of presentation is indicated, the presentation may be made (*ex analogia*) to the general e-mail address.

exactly in their wording. Another alternative could be to extend the eUCP to apply as supplement to the UCP, the URDG and the ISP, which all contain the criterion that documents "must appear on their face to conform... (with the terms)".

VII.10 Electronic documentary credits in practice

Attempts to cut trade paper administration costs by the digitalisation of documentary credit procedures have been launched in various projects. These attempts have so far been foundered on the need for a genuinely independent, secure service to which users could entrust their confidential documents and negotiable instruments in particular such as bills of lading the possession of which is regarded as proof of title in the goods during their transit.

The *Bolero System* is designed to solve the problems relating to the use of documents of title through its Title Registry. It has adopted the eUCP rules created by the ICC and published an explanatory user-guide[209] on the impact on eUCP on bolero.net standards.

The Bolero$_{xml}$ designed, from the outset, the relevant document models to meet the compliance requirements of UCP500. The compliance is achieved through validation aspects of the Core Messaging Platform and the business rules that Bolero$_{xml}$ specifies.

Fully electronic documentary credit mechanisms covering both payment and shipment procedures are still generally lacking in practice, although impressive attempts have been made to that effect. A realistic expectation is that there will be a period of credits with mixed electronic and paper presentations, which has also been anticipated in the drafting of applicable rules. One expert´s estimate[210] is that during 2004-2009 there will be an exponential growth of electronic presentations, as most OECD and Southeast Asian trade will be in an electronic format, with little or no paper documents involved. After 10 years there will be virtually no paper-based trade documentation.

So far, however, the penetration of electronic commerce to letter of credit practice has been slow. A relatively recent survey[211] found that 67% of letter of credit departments do not offer their customers an online method for letter of credit applications. Some 85% of letter of credit departments do not have an online business-to-business facility offering trade finance services and information to their customers. Finally, and most importantly, none of the departments surveyed indicate that they have already processed an eUCP credit.

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209 These are available at http://www.bolero.net/boleroxml/introduction, visited on 10.4.2002.

210 Neil Chantry, Future of the eUCP, Documentary Credits Insight Vol. 8 No 2, April-June 2002 pages 1 and 27.

211 DC-PRO LC Market Intelligence Survey 2003.

VII.11 Documentary credit principles in an electronic environment

There is apparently no case law or opinions of the ICC Banking Commission relating to electronic presentations, outside perhaps their general availability. Therefore, attempting to make some observations is merely guesswork.

Electronics should not, in any case, change the fact that the credit is independent of the underlying transaction and the autonomy of the credit should thus remain preserved. If electronic records do comply with the terms of the credit, the bank is obliged to reimburse the presenting party and take up the records, which means changing their status in the information system. A letter of credit will be recognisable as a promise to pay against representative data rather than against the realities that underlie that data.[212]

The doctrine of strict compliance may gain a special meaning in an electronic environment as the wording "appears on its face" contained in Article 13.a of UCP500 has to be interpreted in a particular way. Article e3 a.i. of the eUCP provides that "appears on its face" and the like shall apply to the data content of an electronic record. It is unclear what this means in practice, since there is no ´face´ to look at. It could be imagined that standards (´layouts´ in paper terms) for presenting the data content would become commonplace, and that a major part of the examination could be automated.[213] As anticipated by a banker "(t)he mundane tasks will disappear and the focus will be on fewer but more professional document examiners whose task is to make decisions of substance, having consigned the trivia to machine processing".[214]

Electronic presentations are expected to reduce the role of correspondent (i.e. negotiating or collecting) banks, since presentation can easily be made to the issuing bank directly through electronic media. On the other hand, there are many reasons to maintain a confirming bank in a credit transaction, including political, country and bank risks. The traditional role of a confirming bank may change, since documents can still be presented directly to the issuing bank. The

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212 Gary Collyer in the Preface of the ICC Guide to the eUCP, p. 8.

213 DCI Vol. 9. No 1 January-March 2003 mentions a couple of examples of letter of credit processing online:

- FleetBoston Financial Corporation, which is the seventh largest financial holding company in the United States has launched an online imaging application ´Trade Key Online Images´ (TKOims). Fleet´s trade services customers will be able to use TKOims to view documents related to commercial letters of credit, documentary collections and electronic trade payment transactions over the Internet.

- Bank of America has developed with its partner the ´S1 Trade Finance Purchase Order Processing System' (S1 POPS). This system performs automated examination of shipping documents against the original purchase orders from the buyer for letter of credits and open account transactions. The S1 POPS compliance engine also performs automated discrepancy and variance checking by comparing the purchase order data supplied by the bank´s customer with the shipment data entered by the bank´s staff; then reports payment and shipment information, as well as any discrepancies, back to the bank´s customer.

214 Gary Collyer in the Preface of the ICC Guide to the eUCP, p. 7.

confirming bank comes up only in the case of default. This is the current practice with standby letters of credit.[215] This obviously has an impact on the law applicable to the first presentation.

There should not be much relaxation of the principle of strict compliance, which is vital for the subsequent buyers in the chain of goods in transit. Those parts of messages which do not comply with the terms of the credit in an electronic examination could be separated for manual examination as a printout, where possible.[216] Electronics will in any case facilitate speedier communications. Communications may also become easier due to the fact that, as noted, the role of the advising bank may be reduced. It may be technically easier to obtain waivers from the buyer within the short time-limits.

It is also unclear to what extent the transition to an electronic medium would solve the problem of discrepant documents. According to the eUCP, the bank will only check the "apparent authenticity" of an electronic record and could rely on presentation of documents using standard technical devices. One of the key reasons for using electronic documentation is the need to avoid the re-keying of information. The same data elements are used over and over again. By doing this, the requirement of consistency between the documents, as called for by Article 21 of UCP500 and as interpreted by ISBP para.24, would not pose as many problems as in the paper environment.

The liability of a bank using compliance engines is determined by the UCP and the eUCP. As mentioned, UCP500 lays down the general framework for liability, and Article 12 of the eUCP adds a disclaimer on the authenticity of electronic documents. A compliance engine is, on the other hand, an ´electronic agent´ for which its programmer, the bank, is responsible.[217] Liability may arise, first, out of the selection of mechanical tools. The eUCP Article 12 requires banks to use only commercially reasonable methods for authentication. It is unclear whether this applies to other aspects of the examination of compliance. As soon as the electronic records and their data contents are standardised, the task for the machinery becomes easier.

The second liability aspect relates to the programming of compliance engines. The bank should program them to check the requirements expressed in the credit. If the programming is stringent, unwanted irregularities leading to manual checks or communications with the client may occur. If, on the other hand, the programming is "tolerant", discrepancies may pass through the system, leading to losses for the beneficiary. General contract law qualifying the use of electronic agents might impose more stringent diligence requirements on the use of machines as is the case with human involvement. Therefore it is not certain how far the disclaimers of the documentary credit rules apply.

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215 Guide to the eUCP, p. 15.

216 In a manual examination, the information contents should be decisive. One may recall the nightmare that was created by the use of mechanical (non-computerised) voting machines of Florida in a close presidential race of the United States in 2000.

217 See Chapter IV, ante, as regards the UNCITRAL draft convention on electronic contracting, and the provisions in the US UETA addressing the use of electronic agents.

Today´s electronic documentation is, in the absence of a general legal regime to transfer title to tangible goods through electronic records, less relevant than paper documentation. Once the banks´ examination bears relevance to the various property and security rights held by the various parties involved, which may possibly be protected by good faith exceptions, the liability regime will really be tested.

Encryption and authentication methods should complicate forgery of documents. Full-fledged authentication procedures, i.e. the use of digital signatures, involve both the verification of the sender and the integrity of the message.[218] The document remains intact after it leaves its originator, who can be verified by using electronic signatures. What cannot be verified is whether the originator was authorised to send the message or not, or whether he was compelled to send it. The use of the signature may be unauthorised or induced by coercion or misrepresentation, which has an effect on the validity of a contractual undertaking determined pursuant to the applicable law.

It is therefore more difficult to present forged electronic records than records that are ´nullities´ *ab initio*, which means e.g. situations where the documents are produced by a non-existent carrier or insurance company. Although banks may be reluctant to accept any more liabilities, the procedure of authentication could include, in connection with the verification of the origin of the message and data, some sort of verification as regards the nature of sender. It would not be out of question to connect the holdership of certain types of public keys of commercial enterprises with entries in commercial registers.

For instance, a shipowner could be registered in a register connected with e.g. Lloyd´s Register of Shipping. For fields of business requiring authorisation, such as insurance, the nature of the sender as an authorised insurance company could be somehow indicated in its public key. The possibility to obtain such a key could be conditioned on an approval of (e.g. insurance) supervisory authorities or, in businesses not under licence or supervisory requirement, commercial registers.

Fraud cases would therefore relate to the factual background and the information contained in the authentic documentation. At the same time, the increased speed in the examination (should the seven day limit for the reasonable time to examine documents[219] be eroded) and reimbursement will in practice make it more difficult to introduce court injunctions to enjoin payments. As the banks will only examine what ´appears on the face´ of the documents, their role could be easier and their responsibility even lighter. This would help to reduce the costs of these trade finance instruments.

Paper documents which are rejected and returned to the bank in an amended form do not leave a trace on the bank´s records. The presenting party is informally notified that the documents do not conform, after which it is for him to take measures to correct them. Therefore they are, in a way, presented fresh when finally approved. An electronic record, on the other hand, leaves a trace on

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218 See Chapter VIII.6.8., *post*.

219 Article 13.b of UCP500 not altered by the eUCP.

the data log which the bank inevitably must have for risk management. This log may be used for evidence in fraud cases.

The maintenance of the documentary credit system would not easily tolerate further disclaimers in respect of mechanical examination with utility compliance systems. The liability of the bank for the operation and malfunctions of a mechanical system should be in line with the ´reasonable care´ standard applied to manual examination. Utility compliance systems are a tool used by the bank which should be responsible for the operation of the tool. Reference can be made here to the discussions in the UNCITRAL Working Party on Electronic Commerce.[220]

Making electronic documentary credits transferable may pose problems where the law applicable to the credit treats the transfer of the credit as an assignment and imposes form requirements for an effective assignment.

As already said, there are apparently no opinions of the Banking Commission relating to the substantive aspects of the use of the eUCP. The large volume of opinions of the ICC Banking Commission relates to the current revision of the UCP and in particular documentary requirements thereunder. Contemporary transport documentation does not yet have many electronic equivalents in use. Therefore, it is unclear to what extent the interpretations relating to the use of traditional transport documents have a bearing on the electronic equivalents. Should the use of traditional transport documents decrease and be replaced by exact electronic functional equivalents, the opinions and case law could still have some significance.

VII.12 Documentary credits and other secured payment arrangements

In Chapter V.6., *ante*, various trade security systems were analysed from the point of view of what role trade documentation plays in them, and in particular securing the bank involved in the transaction. In the next few paragraphs, a general overview is made of the methods other than documentary credits, collections, or trade guarantees, to mitigate the payment risk in international sale of goods transactions. The banking industry is namely observing with some anxiety the rise of new and old secured trade finance arrangements, many of which are provided by operators other than banks. This may eventually force the banks to accelerate their product development vis-à-vis electronic presentations.[221]

In factoring, the right to obtain the price of the goods is effectively sold to the bank. Today, companies can raise up to 80 per cent of the value of their invoices on exported goods or services as soon as goods are shipped or made available with the balance, charges deducted, being paid when the customer pays.

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220 See Report of the thirty-ninth session, Doc A/CN.9/WG.IV/WP.95, paras. 78-79.

221 See the objectives of SWIFTNet Trade Services Utility, Chapter VIII.7.5., *post*.

The factor will also undertake to collect the payment from the customers and provide a 100 per cent protection against bad debts if required.[222] Recently, trade receivables financing has included new actors such as parcel carriers.[223]

Credit risks can also be insured. Traditionally, official state supported export credit agencies have insured credit risks involved in international trade transactions. During the recent years, however, private credit insurers have moved from the domestic market to the international arena.[224] Risk management not relating to individual transactions but based on portfolios, like credit insurance, can be offered online.[225]

The idea of documentary credits is to make the payment conditional on the presentation of conforming documents which usually give *prima facie* proof that the seller has complied with his delivery obligations in respect of the goods. In ´conditional payments systems´, systems handling clean payments can be programmed to monitor the observance of certain electronic requirements that have to be fulfilled before payment is effected. These requirements are checked electronically, and banks can undertake (guarantee) to pay, if the agreed requirements are fulfilled by the seller.[226] The checking of requirements may be done by special ´compliance engines´.[227] Conditional payment systems as described above resemble the ETC and ETPS models discussed by the ICC in the 1990s, see *supra*, and may find shape in the applications of the *SWIFTNet Trade Services Utility* to be launched, see Chapter VIII.7.5., *post*.

While documentary credits are based on guarantee, the traditional alternative (the concept known probably known to almost every tenant in the world) is an escrow account. Electronic escrow accounts are based on a contract stipulating the terms and requirements needed to effect payment. The seller transfers the payment to a closed account with a bank and receives the payment once he provides the required online documentation.[228] Banks can use the Web to market credit lines in respect of certain countries in electronic marketplaces, in which buyers and sellers can opt for the cheapest alternative. This represents the ´reverse auction´ model.[229]

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222 Mark Ford, Alternatives to L/Cs on the rise, DCI Vol. 9 No 2, April-June 2003, pages 1 and 22-23.

223 Ibid., referring to ´UPS´. Christensen (p. 4) refers to an article published in 1999 in the International Transport Journal concerning ´Cash Forwarding´ which has been introduced by ´Danzas´ and covers the insurance of the goods, security of payment and monitoring and supervision.

224 Ibid.

225 Christensen, pp. 3-4. An example that is up and running is ´eCredible´.

226 Ibid., p.3. According to Christensen, there were no conditional payment systems running live at the beginning of 2003, but he mentions the *E-Payment Plus* of SWIFT as an example of clean payment systems, on which conditional payment systems could be built.

227 Ibid. An example of compliance checking is TradeCard, see Chapter VIII.7.2., *post*. The checking of compliance with 'requirements' should be distinguished from automated compliance checking of documents such the *BoleroSURF* (see Chapter VIII.7.1.6., *post*) or the banking examples mentioned *supra*. The distinction is whether the relevant information is presented in documents or electronic records or whether it can be obtained from a source on request. Transport law and invoicing relevant for international trade both build on the notion of a document as a carrier of required information.

228 Ibid., p. 4. An example is ´escrow.com´.

229 Ibid. An example mentioned is ´LCconnect´. See Chapter II.3.1., *ante*.

VII.13 Conclusions

Electronic documentary credits are still very much theory when it comes to making the presentations in electronic form. This is mostly because the documents themselves are really not yet electronic. There are reasons to believe that this instrument will exist one day in practice, as it is able to facilitate trade finance tied to the transaction in a way that protects the interests of the parties involved, including the banks. As stated earlier, documentary credits are used in trade with countries in which the commercial infrastructure is less developed. Perhaps international organisations could make the development of the electronic commerce infrastructure in these countries one of their priorities, following international and national models. This would not only enhance the possibilities of obtaining trade finance more cheaply, but improve the prospects of SMEs in general.

The contractual structure applying to documentary credits is becoming slightly patchy due to the introduction of the eUCP and the International Standard Banking Practices. As the eUCP should follow technological developments, it could be revised in the course of these developments and could be made a document to cover electronic presentations of documents common to the sister-instruments, the UCP, the International Standby Practices and the Uniform Rules for Demand Guarantees. The stable parts of the eUCP not subject to technology changes could be taken into the UCP itself. This would make the regulatory framework for documentary credits more coherent. If parts of the International Standard Practices were to be included in the future UCP600, this would elevate the rules contained in the ISBP to a higher contractual status if harmony is desired in more detail, which may not be the case. Once electronic presentations start spreading, similar practices may evolve in the electronic field as well.

Perhaps one could amend the next version of the UCP by a provision regarding the interpretation of the UCP which would be somewhat similar to Article 7(2) of the CISG stating that the rules should be interpreted in the light of their international origin and nature. This would add normative legitimacy to the Banking Commission´s opinions and interpretations vis-à-vis interpretations made by national courts.

As regards documentary requirements imposed under letter of credit transactions, see the comments on the matter in Chapter VIII.6.8., *post*.

VIII A HOLISTIC APPROACH EMERGES WITH A NEW INFRASTRUCTURE

This study has, in the preceding chapters, summarised the developments in electronic contracting in general, introduced the present and possible future transport documentation systems and the basics of documentary credit law, including standby letters of credit as well as demand guarantees amongs other topics.

In this chapter, my intention is to give an outline of contemporary trade facilitation initiatives, some of which have already been shortly visited.[1] These initiatives aim at streamlining trade procedures e.g. by improving trade instruments by making them electronic, harmonising document layouts and creating uniform lists of abbreviations. Replacing paper documents with electronic records is one of the principal measures suggested by trade facilitation schemes. Therefore these are often two sides of the same coin.

The replacement of paper documents with electronic records requires, in addition to their general legal admissibility, a good basic infrastructure for electronic commerce in transport, banking, insurance and administration, and customs organisations in particular. Intercourse with customs authorities takes place serving fiscal or reporting purposes. Some countries maintain exchange control systems, which may impose documentary requirements. It is widely understood that general interconnection between the parties should be the aim to further effective supply chain management. Interconnection has a technical, commercial and legal dimension.

Trade facilitation aims, among other things, at streamlining trade documentation. The role of documents, as was noted in Chapter III.1., *ante*, either in traditional paper form or as an electronic record, is to contain a set of

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[1] See Chapters II.2.2. and IV.1., *ante*.

data or information recorded as such. Therefore it is useful to have a look into the present documentary credit requirements for the data content for various trade documents used in documentary credits in the light of UCP500 along with the International Standard Banking Practice (ISBP), as well as the contemporary form requirements imposed on them. Such requirements will inevitably become the subject of scrutiny during the next revision of the Uniform Customs and Practice for Documentary Credits of the ICC. A preliminary look at such issues is taken in this study.

VIII.1 Towards a new conception of international trade

Trade facilitation and supply chain management pave the way for a ´holistic´ view of the system of international trade. Trade facilitation aims at cutting costs by simplifying procedures. Supply chain management invites a horizontal look at the system. In this way, the idea of a comprehensive Internet trading platform gains ground. To achieve this, one must tackle both the technical and legal problems involved. As put forward by a Dutch model code of conduct "(a) good trans-border legal infrastructure assures legal and technical interoperability, thereby enabling the creation of above all legal security".[2] The need for a holistic approach was recognised by the CMI in 1999 when it identified a number of interfaces between the different types of contracts involved in international trade and transport of goods and wanted to collect and analyse the rules governing them.[3]

In Chapter VII.8.3., *ante*, a look was taken into some ideas expressed within the ICC for the design of a comprehensive international trading system based partly on models created by national trade facilitation boards. These are fine examples of a holistic approach. I decided to present them in connection with documentary credits since they build largely on the idea of the documentary credit, although other conceptions were also present that precede the publication of the eUCP, which is largely a functional equivalent of traditional paper-based credits. As expressed at the beginning, documentary credits are, in a way, the ´end products´ of the traditional trading systems that have a multiplicity of contractual relationships.

As an example of the holistic approach to international trade law and practice, a closer look will be taken into the *Bolero System* and some other similar systems or projects. One must stress that similar ideas were contemplated in various *fora* in the middle or late 1990s. Sometimes even gentle rivalry could be sensed among those privy to the projects.

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2 Electronic Commerce Platform Netherlands model code of conduct as endorsed by UN/CEFACT Recommendation 32, p. 8. This phrase relates apparently to a narrower context, but the idea obviously remains the same.

3 See Chapter VI.3.2.1., *ante*.

VIII.2 Trade facilitation efforts

Trade facilitation is generally understood to mean the efforts conducted by international organisations to improve and harmonise trade procedures including customs procedures and the use of electronic communications.[4] At the highest level, trade facilitation is one of the objectives of the World Trade Organisation (WTO), especially following the Doha Ministerial Declaration. It has many useful effects on the economies of industrialised and developing countries.[5] For the purposes of this study, it suffices to mention the objective of lowering the costs of trade transactions. Numerous estimates have been made that trade facilitation measures could lower costs on export transactions by 6 to 10%. UNCTAD has suggested that transaction costs can account for 2-3% of the arrived costs of goods.[6] Trade facilitation is closely linked to logistics, in particular the information processes connected therewith, by developing and enhancing procedures that augment the logistical processes in companies.

One of the key bodies in charge of trade facilitation is the Centre for Trade Facilitation and Electronic Business (CEFACT; formerly the Centre for the Facilitation of Procedures and Practices for Administration, Commerce and Transport) of the Economic Commission for Europe (UNECE). As has been already mentioned, UNECE Working Party 4 (Trade Facilitation) created the EDIFACT message standards in the 1980s. There are, as already noted, corresponding organisations at the national level in many countries, e.g. SITPRO in the United Kingdom, DEUPRO in Germany, and NORDIPRO in the Nordic countries.

VIII.2.1 CEFACT model of the international supply chain

CEFACT has adopted over 30 recommendations relating to trade facilitation. Some of them were adopted by the UNECE before the establishment of CEFACT in its present form in 1999, but are now anyway presented under its name.

One of the more recent CEFACT recommendations is ´Facilitation Measures Related to International Trade Procedures´[7], which is also important from the

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4 See the Terms of Reference of the Facilitation of International Trade Procedures of UNECE WP.4, http://www.unece.org/trade/facil/wp4_tor.htm, visited on 12.2.2000.

5 See Trade facilitation, Contributions to the WTO: Trade Facilitation and Development, Communication from the European Community, 10 March 1999.

6 Ibid. p. 2.

7 Recommendation No. 18, third revised edition, adopted by the the United Nations Centre for Trade Facilitation and Electronic Business, Doc. ECE/TRADE/271, New York and Geneva, 2001. The International Trade Procedures Working Group, which developed the Recommendation, considers it to be a ´living document´, subject to a constant review process in order to keep it up to date with the rapid developments in trade facilitation and electronic business. The first version of Recommendation No. 18 was adopted by UN/ECE WP.4 in 1981 and the first revised version of the Recommendation was adopted just a short time after, in 1982.

perspective of this work. It provides a comprehensive set of recommendations regarding international best practices and standards for trade facilitation and harmonisation of trade transactions, from initial commercial documents to payment measures, official controls and transportation of goods. The document reflects ongoing changes brought about by the adoption of e-business tools and related business models.[8]

In addition to the UN/CEFACT Recommendation No 18, the efforts to streamline trade documentation are worth noting. One such effort was made at the national level on the initiative[9] of the Finnish Ministry of Transport and Communications in 1998, the results of which are presented hereafter together with the UN/CEFACT Recommendation.

In order to understand the complexity of international trade, including the key elements of a trade transaction, CEFACT developed a model of the international supply chain. Based on this model, specific measures were developed to cover the key elements of the trade transaction process.These are presented under four main categories: commercial measures, international payment measures, official control measures and transport related measures.[10]

VIII.2.1.1 Buy–>Ship–>Pay

The CEFACT model has been set out using an internationally accepted modelling technique – The UN/CEFACT Modelling Methology – UMM. The ultimate aim is to provide a reference model which gives a view of the international supply chain in its entirety. The aim is to create a simplified model of the international supply chain based on the assumption that an international trade transaction always includes commercial, shipping and payment processes. The recommended measures, which are grouped into four categories, relate to these three processes. The ´Buy´ process covers all commercial activities related to the ordering of goods. The ´Ship´ process covers all activities involved in the physical transfer of the goods, including official controls. The ´Pay´ process covers all activities involved in the payment of goods.

In the report published on the basis of the Finnish project, including three categories[11] of trade, the routine trade transaction includes the following communications, in chronological order:

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8 CEFACT Recommendation No 18, Foreword by Paolo Garonna.

9 Logistics Chain EDI Project, see also Chapter II.3., *ante*.

10 Ibid.

11 In the report, trade transactions were divided into three categories: inland trade, intra-Community trade and ´foreign´ trade outside the European Community. It is not possible to go into details about the differences, but generally customs clearance is replaced by Intrastat reporting.

1. The buyer invites the seller to tender (invitation to treat); 2. the seller makes an offer to the buyer; 3. the buyer makes an order based on the offer; 4. either the seller or the buyer arranges for transportation[12]; 5. the seller delivers the goods to the buyer; 6. the seller invoices the the buyer; and 7. the buyer finally pays for the goods.

The report concluded that there are typically 24 parties to a transaction and listed 36 categories of trade documents involved.[13] All of these have their equivalents as UN/EDIFACT messages, which nowadays exist in XML form[14], which makes the transition to electronic communications easier.

VIII.2.1.2 Simplification of trade procedures

The CEFACT Recommendation on trade facilitation outlines some general principles. Trade procedures should be kept to a minimum, and they should be commercially oriented and relate more closely to trade and transport requirements. Moreover, procedures should be simplified, harmonised and should comply with international standards.

Similarly, data requirements should be kept to a minimum and should be simplified, harmonised and standardised in order to ease the information flow. To illustrate the data requirements, reference is made to the Finnish report[15] which lists six categories of data content in the documents used in a trade transaction:

1. the content linked to the entire document, e.g. the invoice number and the maturity date;. 2. the content linked to the parties, such as contact persons for the trading partners and the party responsible for the carriage as well as client numbers; 3. the information relating to the delivery and transportation, such as the mode and date of delivery, the route used and the estimated time of arrival (eta); 4. information relating to the goods, such as their weight and unit price; 5. information relating to taxation, such as the turnover; and 6. conclusive information such as the total price.

UN/CEFACT Recommendation No. 18 goes on to state that laws, regulations and other information regarding procedures and data requirements should be readily accessible to all parties concerned. This is in line with the attempts of some organisations to create international repositories of trade-related information.

VIII.2.1.3 Recommendations for trade documents

According to UN/CEFACT Recommendation No. 18, documentary requirements should be kept to a minimum. Documents should be in line with UN

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12 This is regularly agreed upon by referring to one of the INCOTERMS 2000 in the contract of sale, see Chapter V.1., *ante*.

13 *Logistics Chain EDI Project*, pp. 15-16.

14 see http://www.xml-edifact.org/LIB/xml-edifact.03, visited on 15.2.2003.

15 *Logistics Chain EDI Project*, p. 26.

Recommendation No 1, UN Layout Key for Trade Documents[16]. The use of plain paper documents produced or appearing to be produced by reprographic, automated or computerised systems should be acceptable. The presentation of supporting documents should not be required. Finally, hand-written signatures and their (physical) equivalents should be avoided.

VIII.2.1.4 Transition to electronic documents

UN/CEFACT Recommendation No. 18 encourages the use of information and communication technology and the resulting electronic solutions. In particular, the requirement for authentication should be able to be fulfilled by means of technological solutions and should not require an accompanying paper document signed or otherwise authenticated.

There are a number of benefits deriving from the eventual replacement of paper documents with electronic records. Electronic records, especially authenticated with digital signatures, are more reliable ways to convey information than paper documents since their forgery is very difficult.

Secondly, the use of electronic records reduces the need to re-key information into information systems.[17] This naturally reduces errors, which can cause confusion and costs and can eventually lead to the rejection of documents presented under a commercial letter of credit. The data content common to several commercial documents can be used again electronically. If the common data content is stored centrally with a third party service provider such as the *Bolero System*, there is further assurance as to the integrity of the data content.

Thirdly, electronic transfers of information naturally make information flows faster and automatic. The sender of a message receives an acknowledgement of receipt instantly, and automatisation makes it much easier to monitor message flows and find relevant documents in the system.

Outside the legal impediments to the use of electronic records in lieu of paper documents in trade transactions, their use is also hampered by the fact that there are several message standards in use. It may be recalled that, in view of the facilitation of electronic commerce, a substantial number of XML-based EDIFACT messages exist for various types of commercial documents and messages used in international trade. XML languages used in proprietary systems, however, are in need of convergence.

It should be stressed that many projects are underway on in this respect. Global, cross-industry organisations like *W3C*[18], the International Standardisation

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16 UN/CEFACT Recommendation 1, United Nations Layout Key for Trade Documents, at http://www.unece.org/cefact, visited on 12.3.2003.

17 *Logistics Chain EDI Project*, pp. 30-31. For instance, in the ´Portnet´-system (see http://www.tt-tietopalvelut.fi/luotain/portnet/portnet.htm, visited on 15.1.2003), the shipowner keys the ship´s manifest constituting the list of cargo into his information system, after which it is readable by all interested parties. Keying cargo information into electronic information systems also facilitates shipment tracking. See also US Customs Regulations: Advance electronic presentation of cargo information, http://www.gard.no/portal/page?_pageid=53,33696&_dad=gard&_schema=PORTAL&p_d., visited on 14.4.2004.

18 W3C stands for ´World-Wide Web Consortium´ which is an organisation created to develop common protocols for the Internet, and is defining, among other things, public standards for the use of XML.

Organisation and the UN/CEFACT are currently endorsing a process which may make convergence a reality, as one can see it from the support these initiatives have received.[19] The EU has noted the need for interoperability and standardisation. The Commission has called for support from Member States to address interoperability issues.[20]

Other non-legal impediments to the use of electronic trade documentation are non-integrated or lacking information systems, the absence of partners willing to communicate electronically, bearing in mind the large number of parties involved in a transaction, as well as problems felt in the field of information security.

VIII.2.1.5 The role and future of the invoice

The report[21] based on the Finnish survey paid particular attention to the invoice and the transport document, more particularly the waybill as distinct from a negotiable bill of lading.

The role of the invoice is to collect within it certain of the most essential information relating to a trade transaction is collected in it. After receiving the invoice, the payer commences the payment procedure to the recipient. In documentary credits, the invoice is presented to the (confirming, negotiating etc.) bank among other documents. Payment of the price, tax and customs duties are connected with the goods sold using the invoice. The report suggests that a commercial invoice could be dispensed with altogether.[22] Some companies in a well-established commercial relationship are doing this already.

This logistic ideal has been, however, confronted with legal requirements. For instance, in France the law requires that an invoice is issued, and also prescribes details of its contents.[23] Similarly, a CIF seller under English common law must tender a commercial invoice.[24] The requirement for an invoice also

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19 Paul Miserez, Converging message standards for e-trade, DCI Vol. 8 No 1, pp. 6-7. The initiatives include the ISO 15022 XML initiative and the UN/CEFACT ebXML initiative.

20 For the Community policy on interoperability, see eEurope 2005 Mid-term Review, COM (2004) 108 final, p. 6. See also Chapter IV.2., *ante*.

See also the website of the European Committee for Standardization http://www.cenorm.be, visited on 3.9.2004. For one of the latest developments in the field of interoperability, see the press release ´Europe and Asia collaborate to test interoperability of ebXML standards´ at http://www.cenorm.be/cenorm/index.htm, visited on 3.9.2004.

21 *Logistics Chain EDI Project*, pp. 33-40.

22 The idea of the suggested model is that the dispatch and reception of the goods are notified electronically, linking the buyer´s notification of the receipt (with a POD= Proof of Delivery) to his payment system in a manner which identifies the goods to be paid. Some international companies such as Nokia Corporation use self-billing which means that they run the invoicing themselves when collecting items from supplier; e.g. the proprietary RosettaNet is used to run self-billing schemes.

23 Loi no 2001-420, 15 mai 2001, art 53, Journal officiel 16 mai 2001, p. 7776, Code de Commerce, article L. 441-3, Ordonnance no 86-1423/1.12.1986). This obligation has been contested, but has been found not to be in contradiction with EC law by creating impediments to the free movement of goods (Cass. Crim., 18.6.1998, no 97-81.510, Lamyline), see Lamy Transport 2002, 333 on page 221.

24 Todd, p. 141.

exists in international commercial law. Point A1 of CIF INCOTERMS 2000 requires namely that the seller must provide the goods and the commercial invoice, or its equivalent electronic message, in conformity with the contract of sale and any other evidence of conformity which may be required by the contract. Invoices may be useful for other purposes connected with the sale of goods transaction. Under English law, for instance, transfer of debt effected in legal factoring arrangements requires notice to the debtor, i.e. the buyer. Invoices serve this formality as well.

If the use of invoices is maintained, an important step is to transform invoicing into an electronic system. In fact, the invoice as a commercial document used in documentary credits is the one most amenable to a breakthrough in electronic communication methods. When electronic invoices are used in business-to-business relations, the data content is transferred from the seller´s invoicing system to the buyer´s finance management´s computer system. This facilitates the computerisation of accounting. The need for rekeying information manually will be eliminated, which diminishes risks of typing errors. The costs of invoice handling will be reduced drastically.[25]

The use of electronic invoices in commercial transactions is rising steadily. In Finland, the proportion of electronic invoices is already quite high since almost one half of corporate invoicing is already in electronic form.[26] In the other Nordic

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[25] According to some estimates, the sender (seller) saves up to one half of his expenses by using electronic invoicing. This is because no printing and mailing is needed. The savings accrued to the receiver (buyer) are even more substantial. They amount to 60-90% of the receiver´s costs. This is because the sender can add details regarding automatic cost attribution and accounts to the invoice.

The costs involved in connection with an invoice in Finland including both the sender´s and the receiver´s costs are estimated to be 30-100 euros, some 80% of them being borne by the receiver. (Timo Ronkainen, Verkkolasku osana Nordea Rahoituksen rahoituspalvelua, 24.6.2003) One figure relating to the invoice handling costs at the buyer´s end is EUR 16.66 whereas electronic invoice handling costs between EUR 1.66-3.33 (Heli Salmi at an Elma Oy seminar on 7 November 2002, Cash Manager Client Magazine 3/2001, Analyste; studies on aspects relating to electronic invoicing have been conducted at the University of Jyväskylä in Finland). At the EU level, the proportion of electronic invoicing in 2002 was, outside the Nordic countries, some 15% (http://digitoday.fi/digi98fi.nsf/print/finanssi20020530091354_kni_62934309, visited on 30.5.2002).

See also the cost save figures for international trade operators quoted by by Mallon 2002, pp. 2-3, http://www.imf.org/external/np/leg/sem/2002/cdmfl/eng/index.htm, visited on 30.11.2003.

[26] According to one service provider interviewed (Verkkolaskutus lisääntyy nopeasti, Helsingin Sanomat 26.4.2003) there are, at the corporate level, some 100 million electronic invoices sent in Finland every year, as compared to some 120 million paper invoices. These figures apparently take into account both Internet-based billing and invoicing carried out through the EDI networks used by large companies. Further at the consumer level, electronic invoicing is taking its first steps. It is estimated that electronic invoices would amount to 25% of total consumer invoicing in 2005 (IDC: Nordic Electronic Billing and Payment Market, 2000-2005).

If one multiplies the savings achieved for an individual invoice by the total amount of invoices, the aggregate benefit for the national economy could rise to billions of euros.

It should be said that the amount of electronic invoicing would benefit from interconnection agreements between operators as well as from a uniform standard for an electronic invoice. In the worst cases, the scanning of paper invoices is necessary. In Finland, a project has been launched by the main commercial banks, the main operators and a service organisation (Elma Oy) to establish a system in which electronic bills would cross the borders between different operators. The Finnish Finnvoice standard for e-invoicing has been taken into use by Swedish banks as well.

countries, the role of electronic invoices is also increasing rapidly and is estimated to rise to around 20-30 per cent by 2005.[27] However, the reasons for the transition may differ. In Finland, the transition is mostly motivated by its economic efficiency. In Sweden, on the contrary, the main motivation is said to be the environmental friendliness of a system that cuts paper consumption.

To replace paper documents altogether presupposes, however, that electronic documents are approved for accounting by corporate tax systems. As already noted, invoices have a role in the collection of value added tax as well as in customs procedures, which requires the approval of the relevant legislator for a move towards electronic invoicing in international trade transactions.

Changing the system to allow electronic invoicing was the objective of Council Directive[28] 2001/115/EC which primarily related to the collection of value added tax. Article 2 of the Directive amends an earlier directive[29] by restating the principle that every person taxable for VAT shall ensure that an invoice is issued for the goods or services supplied. Such invoices may be sent either on paper or, subject to acceptance by the customer, by electronic means. The Directive also provides for the requirements of the storage of invoices.[30]

Of interest to the objectives of this study are the form provisions relating the transmission of electronic invoices. It is namely provided that invoices sent by electronic means are accepted provided that the authenticity of the origin and the integrity of the contents are guaranteed by means of an advanced electronic signature within the meaning of Article 2(2) of Directive 1999/93/EC on electronic signatures. Member States may even ask for the advanced electronic signature to be based on a qualified certificate and created by a secure-signature-creation device, within the meaning of Article 2(6) and (10) of that Directive.

Alternatively, the authenticity and integrity of the invoice may be guaranteed by means of EDI as defined in Article 2 of Commission Recommendation 1994/820/EC relating to the legal aspects of electronic data

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27 Source: IDC Nordic Electronic Billing and Payment Market.

28 Council Directive 2001/115/EC of 20 December 2001 amending Directive 77/388/EEC with a view to simplifying, modernising and harmonising the conditions laid down for invoicing in respect of value added tax, OJ L 015, 17.1.2002, p. 24.

Recital 4 of the Directive states that "it is (...) necessary, in order to ensure that the internal market functions properly, to draw up a list, harmonised at Community level, of the particulars that must appear on invoices for purposes of value-added tax and to establish a number of common arrangements governing the use of electronic invoicing and the electronic storage of invoices, as well as for self-billing and the outsourcing of invoicing operations". Member States shall bring their legislation in line with the Directive with effect from 1 January 2004 (article 5).

29 Before codification of the present and former directives takes place, exact referencing is not even attempted.

30 The transmission and storage of invoices ´by electronic means´ is said to mean the "transmission or making available to the recipient and storage using electronic equipment for processing (including digital compression) and storage of data, and employing wires, radio transmission, optical technologies or other electromagnetic means".

interchange, when the agreement relating to the exchange provides for the use of procedures guaranteeing the authenticity and intergrity of the message.[31]

The two means mentioned of sending invoices electronically may, however, be waived by the Member State concerned. As the technology of electronic invoicing may evolve, the Commission will undertake to present, at the latest by the end of 2008, a report, possibly suggesting further legislative measures, amending the conditions on electronic invoicing in order to take account of possible future technological developments in this field. In its present form, the Directive gives Member States several options as to the technique and level of verifying the authenticity and integrity of the invoice.

The Directive further gives a number of particulars that must appear on the invoice, whether paper or electronic. It is not feasible to reproduce the exhaustive list in detail in this study. Such items will form part of the terms of letters of credit, including where electronic presentation is made possible. Another matter is that EU-based companies use letters of credit more with exports, which are exempt from VAT. The legislation of the (often underdeveloped) target country may not approve of electronic invoices.[32] An international agreement on electronic invoicing, possibly under the framework of the World Customs Organisation, the OECD, the WTO or a UN organisation, would be useful.

When electronic transport documents are replaced by functional equivalents, the functions of the paper document are replaced, as stated earlier, by entries in registries. When electronic invoices are used, however, the invoice is visualised for electronic approval, circulation and filing purposes. Such visualisation may also be instrumental when electronic invoices are presented under electronic letters of credit. The notion "documents appear on their face to comply..." could get a visual rather than a mechanical interpretation.

VIII.2.1.6 Transport documents in the spotlight

It is useful to look at the the logistical developments in the use of transport documents, since transport documents could be regarded as the nucleus of commercial documentary credit operations, with the delivery of documents constituting a ´constructive delivery´.

The Finnish report cited *supra* suggests further that a waybill could be dispensed with for logistical purposes, its importance being greatest for the carrier and not actually relevant either to the consignor or the consignee.[33] As in the

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31 The recommendation referred to, as noted in Chapter III, *ante,* contains a model interchange agreement, which apparently is sufficient for the purposes of the Directive in question. As standard interchange agreements are very similar in these respects, many of them may suffice for the Member States. In addition, however, the Directive entitles Member States to require "an additional summary document on paper".

32 Directive 2001/115/EC provides, however, that Member States are able to take into account certain invoices concerning goods emanating from third countries.

33 In fact, Finnish practice has often dispensed with the issue of sea transport documents in respect of individual consignments, a practice that has been made possible by close commercial or ownership links between carriers and their customers.

case of the invoice, the data content of the waybill can logistically be scattered throughout other messages.[34] Legally speaking, as has been mentioned, a physical copy of a waybill serves few purposes unless documentary payment systems are used.

The use of the bill of lading is frequently discouraged in favour of sea waybills,which could more easily be replaced by electronic records or dispensed with altogether, as the Finnish report suggests. The need to use a negotiable bill of lading is evident only when goods are resold during their transportation. UN/CEFACT Recommendation No. 12 ´Measures to facilitate maritime transport documents procedures´[35] had already suggested, in its original version in 1979, that unnecessary use of negotiable bills of lading should be discouraged. Since then, maritime legislation has been extended to cover sea waybills e.g. in the United Kingdom in 1992 and in the Nordic countries in 1994. Outside statutory regimes, the adoption by Comité Maritime International of the CMI Uniform Rules for Sea Waybills creates a model for transport conditions that are used in conjunction with sea waybills. The Uniform Customs and Practice for Documentary Credits also expressly provides for sea waybills (see *infra*).

UN/CEFACT Recommendation No 12 further calls for the restriction of the number of originals and copies issued.[36] Moreover, the development and use of a standard documentary format should be encouraged. The UN/CEFACT layout key for bills of lading, for instance, serves as a model for a standard format for bills of lading.

The use of ´short form´ or ´blank back´ documents should also be encouraged. This means, as noted in Chapter VI 1.3.2., *ante*, incorporation of the ´small print´ which would otherwise appear on the reverse side of the transport document, simply by referring to it on the front page. The production of bills of lading can more easily be computerised if short forms are used. This logistical

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34 The consignor sends a dispatch list with the goods, which the carrier then confirms. During the transportation, a deviation notice may be used. When the goods arrive at the destination, the consignee confirms reception. For regular customers, a special customer card can be used, which corresponds to the information in the carrier´s delivery list. The carrier then confirms delivery with a POD (proof of delivery). *Logistics Chain EDI Project*, pp. 36-37.

35 UN/CEFACT Recommendation No. 12 second edition, Geneva October 2001, ECE/TRADE/240. The first edition of Recommendation No 12 was adopted in 1979 (Document TRADE/WP.4/INF.61). Recommendation No 18 is addressed to:

- "participants in international trade, including ship owners, consignees, banks and insurers and other parties interested in the maritime transport of goods to accept and implement the facilitation measures described hereafter";

- "To Governments, international organizations concerned and national trade facilitation organs to accept and encourage the implementation of these measures, and to report on action taken to give effect to the present Recommendation".

36 The Hague and Hague-Visby Rules are silent about the number of bills issued, whereas the Hamburg Rules only mention (in Article 15) that the bill of lading must mention the number of originals issued. In France, the legal requirement (Article 37 of Decree No 66-1078 of 31 December 1966) is two originals, but the practice is four originals (Lamy Transport 2002, tome 2, 444 (c), p. 305). In Belgium, Article 86 of the Maritime Code requires that each bill of lading must be issued in four originals at least, but the practice has reduced the number into two (Putzeys-Rosseels, no 512, p. 289).

ideal is, however, confronted with requirements imposed by contract law. The consignee, who becomes part of the contractual relationship, is in some jurisdictions required to be duly aware of the full terms and conditions to which the short form makes reference. Moreover, the use of the short form for a series of shipments may need explicit acceptance on the part of the consignee.[37]

Blank backs are accepted, for instance, in the United Kingdom, where a clause stating that a carriage covered by a short form document is governed by the conditions which would be applicable as if a (ordinary long form) bill of lading were issued. In the United States, a reference to the general clauses of the carrier is valid as regards the usual terms, but not as regards unusual or ´exorbitant´ clauses.[38]

The maritime laws of the Nordic countries[39] are not against the use of blank back bills of lading. The legislative proposal[40] for the Finnish Maritime Code of 1994, which is practically identical with the codes in the other Nordic Countries, expressly refers to the possibility of using blank back bills of lading provided that an adequate reference is made to the conditions of carriage. This does not mean that such conditions shall be deemed to be accepted as such. Unusual or exorbitant terms might still not be enforceable. Many national laws contain general clauses to this effect.[41] If parties are business partners, even onerous clauses can be enforceable if they have expressly been agreed by the parties.

An example frequently referred to in this context in the Nordic countries is the set of standard terms entitled ´The General Conditions of the Association Nordic Freight Forwarders´ which grants the freight forwarder a lien or pledge[42] on the goods in his possession as security for all costs incidental to the goods and even for previous claims. To be valid in Denmark, such conditions must be separately accepted by the owners of the goods, or the pledge clause must be emphasised so that the person in question must be deemed to have impliedly accepted the conditions.[43] The other Nordic countries may follow similar incorporation requirements.

In France and Belgium, however, the clauses and conditions generally have to be placed in the document in a clear and readable manner in order to be enforceable against the shipper or the consignee. The jurispudence is very strict on this manner in these countries. Even if the clauses are on the bill of lading, but are printed with characters too small, they cannot be enforced. The same applies to conditions which are found on a totally separate document unknown

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37 Recommendation No. 12, point 28., p. 6.

38 Lamy Transport 2002, tome 2, 477, p. 325, Payne & Ivamy 1989, p. 83.

39 ´Nordic countries´ usually refers to Finland, Sweden, Norway, Denmark and Iceland, but here reference is made to Finland, Sweden, Norway and Denmark, which have revised their Maritime Codes in the 1990s.

40 Hallituksen esitys eduskunnalle uudeksi merilaiksi (HE 62 -1994 vp), p. 53.

41 The general clause of the Finnish Contracts Act (oikeustoimilaki § 36) could at least conceivably be applied in business-to-business relationships in the field of transport law.

42 For the difference, see Chapter V.4.1., *ante.*

43 Ronøe in Transfer of Ownership, p. 124.

to the party entitled to the goods.[44] In contrast, the use of blank back sea waybills appears to be somewhat more admissible than the use of blank back bills of lading in France, which constitutes an argument for their use in that country.[45] The mandatory provisions of French maritime law apply, in any case, irrespective of whether a bill of lading is issued or not.

Article 5bis of the UNCITRAL Model Law on Electronic Commerce gives incorporation by reference made by electronic means the same status as incorporation on a paper document has. An electronic record does not have a front (*recto*) or reverse (*verso*) side, which makes this traditional criterion useless in the electronic environment. However, the admitted possibility of using incorporation by reference technique in connection with blank back documents should have significance if the approach suggested by the UNCITRAL Model Law were followed. If all documents of general interest can be displayed on the company´s website, the shipper and especially the consignee are much better placed to examine the conditions than when the conditions of carriage have to be inspected at the carrier´s office.

One of the most important form requirements as to transport documents is the requirement of signatures or other authentication. These are also of major importance to documentary credit operations, as signatures and other authentication methods are those which are regularly examined by banks. It is thought that signature and authentication requirements for documents or electronic records could be central to the next revision of the Uniform Customs and Practice for Documentary Credits. Advanced authenticity requirements help to tackle fraud, but may be cumbersome in commercial and banking practice

The requirements for the carrier´s signature are fairly liberal in sea transport conventions. This relates to the form and eventual validity of the bill of lading or other transport documents. Despite the absence of convention-based form requirements as to the carrier´s signature, national law may impose such requirements.[46] French jurisprudence requires even the signature of the shipper on the bill of lading in order to make sure that the shipper knows the transport conditions.[47]

In documentary credits however, signature requirements are imposed by the UCP500 as elaborated by the ISBP. The articles relating to transport documents all carry a requirement for the "signing or otherwise authenticating" the document by the carrier, whereas the UCP500 provisions relating to insurance documents, on the contrary, contain a requirement that insurance documents have to be

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44 Court of Appeal of Antwerp, 8 November 1978, ETL, 1979, p. 624.

45 See Rodière 1991, 349-2, pp. 268-269; cfr. Lamy Transport 2002, tome 2, 477, p. 325.

46 For French law see Decree no 87-992, 12 Nov. 1987, OJ 18 Nov., p. 13432; see section 46 of the Finnish Maritime Code, which adds that the signature shall be made by mechanical or electronic means.

47 French Decree no 87-992, 12.11.1987 has abolished statutory requirements as to the shipper´s signature. However, the jurisprudence considers the shipper´s signature to be indispensable to make the shipper bound to transport conditions; see e.g. *CA Aix-en-Provence, 10.1.1991, SNTM-CNAN c/Réunion européenne, Lamyline*. Similar requirements have been laid down for Belgium as well, see *CA Anvers (Antwerp), 19.12.1990, Jurispudence Anvers 1992, p. 39*).

signed. I shall revert to the current requirements contained in the UCP500 and in the ISBP, *infra*.

The elimination of traditional trade documents such as the invoice and the waybill based on a logistical analysis serve best in established trading relationships. International trade law , however, establishes some documentary requirements. Such requirements are imposed partly by national law and partly by the Incoterms, which reflects the existing logistical patterns. Documentary requirements are also imposed by documentary credit law, in particular the Uniform Customs and Practice for Documentary Credits. Outside the requirements of customs and other authorities, however, the documentary requirements imposed by legal rules can be waived by the parties.

In documentary payment systems, trade documents have a representative or a symbolic function added through the legal effects associated with the documents, which effects afford security to the buyer and the intermediary banks. The representative or symbolic function may go beyond the precise legal effects and the data content of the document. Therefore logistical and legal approaches do not always go hand in hand. Legislative reforms should make logistical improvements possible while keeping the sophistication and functions of legal instruments in place.

VIII.2.2 Survey on legal impediments created by international trade law instruments

A survey has been conducted regarding the legal barriers to the development of electronic commerce in international instruments relating to international trade.[48] At its thirty-second session, in 1999, UNCITRAL considered a recommendation that had been adopted the same year by UN/CEFACT. It was suggested that UNCITRAL consider actions necessary to ensure that references to ´writing´, ´signature´ and ´document´ in conventions and agreements relating to international trade allowed for electronic equivalents.

The Working Group on Electronic Commerce agreed to recommend to UNCITRAL´s Commission to undertake work towards the preparation of an appropriate international instrument or instruments to remove those legal barriers to the use of electronic commerce which might result from international trade law instruments. This would be preceded by a comprehensive survey of possible legal barriers to the development of electronic commerce in international instruments.[49] At its thirty-fourth session, the Commission endorsed that

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48 See the Note by the Secretariat of 14 February 2002, A/CN.9/WG.IV/WP.94,

49 UN/CEFACT had prepared a similar survey in 1999, see Review of definitions of ´Writing´, ´Signature´ and ´Document´ employed in multinational conventions and agreements relating to international trade, submitted by the Legal Working Group (LWG), Revision of Document Trade/WP.4/R.1096 dated 22 July 1994; TRADE/CEFACT/1999/CRP.2, 25 February 1999.

UNCITRAL considered going beyond the UN/ CEFACT survey but limited itself to the instruments deposited with the Secretary-General of UNCITRAL.

recommendation.[50] The notion of ´international instrument´ refers more closely to conventions and agreements between governments. Most of these conventions relate to the transportation of goods, but I have thought that the results would be most categorically presented in this chapter.

An initial analysis conducted by the UNCITRAL Secretariat covered 33 international conventions and are presented as an annex to the Note by the Secretariat. Some main results of the analysis are presented here.

VIII.2.2.1 Bills of Exchange

Bills of exchange are negotiable instruments used in trade payments. At best, bills of exchange are supposed to move freely like currency.[51] UNCITRAL has created the United Nations Convention on International Bills of Exchange and International Promissory Notes which was approved in 1988. This Convention, which has not entered into force due to insufficient adherence, aims to reconcile two legal families. One is based on the Geneva system, founded on three Geneva Conventions of 7 June 1930 on the Unification of the Law relating to Bills of Exchange, and accepted by countries in continental Europe as well as Brazil and Japan. The Anglo-American system applies in the United Kingdom, most parts of the Commonwealth, the United States and other countries which found their systems on common law.[52]

Despite the fact that the UNCITRAL Convention was drafted relatively lately, a new legal framework for bills of exchange, particularly in view of their status as negotiable instruments, has to be developed. The UNCITRAL Secretariat has suggested that such a comprehensive study might be undertaken in the course of the Working Group on Electronic Commerce´s consideration of legal issues related to the transfer of rights in tangible goods by electronic means.[53]

VIII.2.2.2 CMR Convention

The questions concerning this road transport convention relate to replacing the paper-based ´consignment note´ and various notices. As regards the transport document, recalling that individual copies of the document have legal

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50 Ibid.

51 Under English law, the only difference between a bank-note and a bill of exchange is that only the former is a legal tender and cannot be refused in payment of a debt. Bolero Feasibility Study 1999, p. 75. One reason that negotiable instruments are required by commercial purposes is that the legal restrictions on assignments of debts make the simple assignment of a debt a complex process, and by embodying the debt in a piece of paper which is passed by delivery these difficulties can be overcome.

52 Schmitthoff, Export Trade, p. 152.

53 A/CN.9/WG.IV/WP.94, paras. 28 to 34. The Bolero Feasibility Study 1999 contemplates (on page 75) that it would perhaps be possible to develop a system for the transfer of payments with the same functionality as the bill of exchange mechanism through the creation of irrevocable payment undertakings by banks transferable within the Bolero System, similar to those used in institutions like the CREST or the Euroclear systems for equity settlement. The US Uniform Electronic Transactions Act deals in Section 12(e) with the retention of checks. The UETA specifically provides that when a law requires the retention of a check, that requirement is met when the front and back of a check are recorded electronically and saved for future retention.

significance for the control of goods in transit, the Secretariat found that "an appropriate legal framework would seem to require more than simply recognizing the validity of data messages as substitutes for traditional consignment notes". Furthermore, authentication methods and conditions for the functional equivalence of data messages to ´original´ consignment notes would also need to be considered.[54]

VIII.2.2.3 The bill of lading and sea carriage

As regards the Hamburg Rules, the survey found that questions relating to transport documents, whether a negotiable bill of lading or other transport documents, need to be resolved. The bill of lading is a document of title. Rights in goods represented by documents of title are typically conditioned by the physical possession of an original bill, a paper document. The replacement of the bill of lading by electronic records would require replacing the system based on an instrument in tangible documentary form that is capable of being transferred by endorsement.

Reference is made to the attempts undertaken in the UNCITRAL´s Working Group on Transport to create legal rules for negotiable electronic records, as described in Chapter VI.3.2.3., *ante*. However, in addition to those rules, attention should be paid to the question of how to replace the functions of a tangible document with the use of public records, whether they are central registries or not.

As regards non-negotiable transport documents covered by the Hamburg Rules, the survey came to similar conclusions as it did with the CMR consignment note. The Hamburg Rules also envisage a number of ´written´ communications that have to be tackled.

It is obvious that the findings relating to bills of lading and notices could apply to the preceding sea transport regimes, the Hague and Hague-Visby Rules.[55]

VIII.2.2.4 Conclusions

UNCITRAL Working Group IV (Electronic Commerce) has had a chance to discuss the results of the survey. It would seem to be useful for the results to be discussed in other working groups, at least the one related to Transport Law (WG III). Some barriers contained in the instruments are such that an equation made in basic electronic commerce legislation, such as the UNCITRAL Model Law on Electronic Commerce, or statutes derived therefrom nationally (such the US UETA) can eliminate. In some cases, however, the functional equivalence approach is not enough. The rights and obligations of various parties involved are not understandable, if the law is not sufficiently precise about them.

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54 Ibid. p. 19. It is anticipated that CMR will be revised in the not so distant future (Mallon 24 November 2003).

55 In many Spanish-speaking civil law countries, maritime law considers a bill of lading, which is not a written instrument, to be non-existent (Luis Cova Arria, Legal Obstacles to the Implementation of the Electronic Bill of Lading in Civil Law Countries, ETL 1997, p. 710).

VIII.3 Electronic payment systems

This study focuses on documentary trade payment and guarantee arrangements, and not on payment obligations in general, or electronic payment systems between banks or other institutions. It suffices to mention that UNCITRAL has adopted a Model Law on International Credit Transfers in 1992. The Model Law deals with operations beginning with an instruction by an originator to a bank to place at the disposal of a beneficiary a specified amount of money. It covers such matters as the obligations of a sender of the instruction and of a receiving bank, the time of payment for a receiving bank and the liability of a bank to its sender or to the originator when the transfer is delayed or another error occurs. This model law inspired a legislative process within the European Union that resulted in the adoption of Directive 97/5/EC of the European Parliament and of the Council of 27 January 1997 on cross-border credit transfers[56]. The EU legislatures were particularly interested in the consumer dimension.[57] In the United States, funds transfers are partly regulated by the Uniform Commercial Code, Article 4A of which prescribes, among other things, a set of risk allocation rules applicable to covering situations of mistake, fraud, and negligence in transmitting funds electronically. These instruments and the legal questions of funds transfer are not examined in detail here. It should be noted, however, that the automation of payment systems is already at an advanced stage as compared to documentary payments.[58] Questions relating to netting and settlement finality in payment and securities settlement systems could be of interest in analysing registries serving the sale of tangible goods, but will have to be omitted.[59]

No attempt will either be made to deal with payments by consumers or enterprises using the Internet, e.g. by providing a credit card number through e-mail, or by using the portals provided by banks for effecting banking transactions (see, however, Chapter III.2.6, *ante*).[60] Equally, issues relating to ´e-money´ would be worth a separate study, and are not dealt with here.[61]

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56 OJ L 43,14.2.1997, p. 25.

57 Juusela, pp. 40-41.

58 For questions relating to payment systems, see for instance Goode, Payment Obligations in Commercial and Financial Transactions, London 1983; UNCITRAL Legal Guide on Electronic Funds Transfers, New York, 1987; Rowe, Electronic Trade Payments, London 1987; Funds Transfer in International Banking, A compendium on Capital Adequacy, SWIFT, EDI, Bank´s Liability and Payment Systems in the 1990´s, ICC Publication No. 497; Baker, Donald I. and Brandel, Ronald E., The Law of of Electronic Fund Transfer Systems, Revised Edition, Boston 1996; ICC World Payment Systems Handbook, ICC Publication No 566, Paris 1997; William and Richard Hedley, Bills of Exchange and Bankers´ Documentary Credits 4th edition, London 2001 (especially Part Four); and Juusela, Kansainvälinen tilisiirtomaksu oikeudellisesti tarkasteltuna, Helsinki 1995.

59 See Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement finality in payment and securities settlement systems, OJ L 166, 11.6.1998, p. 45.

60 See Commission Recommendation of 30 July 1997 concerning operations involving electronic payment means, OJ L 208, 2.8.1997 and Communication from the Commission to the Council and the European Parliament ´Retail payments in the Internal Market, Brussels 31.1.2000, COM (2000)36 final. See also Salaün, Les paiements électroniques au regard de la vente à distance, 1999/2 Droit de l´informatique & des télécoms, pp. 19-31; and Poullet &Vandeberghe (Eds.), Telebanking, Teleshopping and the Law, The Hague 1988.

61 For the legal infrastructure for ´e-money´ at the European level, see Directive 2000/46/EC of the European Parliament and of the Council of 18 September on the taking up, pursuit of and prudential supervision of the business of electronic money institutions; OJ L 275, 27.10.2000, p. 39.

VIII.4 SWIFT

Electronic contracting has become commonplace in banking, both as regards the relationship between the bank and its customer but even more so in the relationship between the financial institutions. The latter to a great extent is taken care of by a cooperative named the Society for Worldwide Interbank Financial Telecommunications (SWIFT).

As early as the 1980s, banks had become interested in automating documentary credit transactions. There were many reasons for this development. Banks wanted to reduce costs and labour-intensive areas often come under scrutiny in this respect. Institutions that have developed international electronic networks for treasury management systems have been keen to find new uses for them and to reduce unit cost. Trade finance could be seen as less risky than pure lending in situations of international lending crises[62].SWIFT was founded in 1973 supported by 239 banks in 15 countries to create a shared worldwide data processing and communications link and a common language for international financial transactions. By the year 2000, the number of user institutions had extended to 7125 in 192 countries. SWIFT provides messaging services to banks, broker-dealers and investment managers, as well as market infrastructures for payments, treasury, derivatives, securities and trade services. SWIFT standards are the accepted norm for financial messaging worldwide. SWIFT is also the messaging hub for a growing number of high-value payment systems, securities infrastructures and foreign exchange settlement systems. As such it acts as a trusted third party which provides services to its various users.

Most banks have their own networks. These networks allow them to telecommunicate messages between branches and subsidiaries in different countries, but not directly to other banks. For that, local public data networks can be used or banks may resort to third party service providers.

SWIFT had already created by 1983 standard messages for the Uniform Customs and Practice for Documentary Credits UCP 500 to be exchanged between banks. The early experiences were not always encouraging. In 1987, SWIFT documentary credit messages accounted for only 6% of total documentary credit traffic.[63] One reason was that SWIFT formats go only part of the way towards providing the necessary standardisation. Some institutions used SWIFT standards as building blocks to construct tighter frameworks in-house.[64] After the revision of UCP 400 into a new set of rules, UCP 500, SWIFT created new

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62 Rowe, p 122.

63 Ibid., p. 136

64 Ibid., an example is Bank of America´s ´Greybook´ standard. It should be added that the formats used between the banks and their customers e.g. as regards letter of credit instructions have not been harmonised internationally.

messages on the basis of the new set.[65] One recent service offered by SWIFT for e-commerce is the ´E-Payment Plus´ method for clean payments. Very recently, SWIFT has made public plans to launch a new service, SWIFTNet Trade Services Utility (TSU), which is devoted a separate treatment in connection with similar initiatives, see 7.5. *infra*.

VIII.5 Customs and ´e-government´

The development of e-commerce requires that communications between government and trading companies relating to required documentation and certificates should also be possible by electronic means. Attention is paid below to the development of electronic customs clearance. Taxation and regulatory procedures could be mentioned as other fields where e-government could serve trade purposes.[66] As regards the settlement of disputes[67], governments can facilitate procedures by allowing electronic documents to be used in *ex parte* debt collection, in addition to allowing electronic documents to be used in court proceedings.

VIII.5.1 Customs authorities turn to EDI

One of the main elements of trade facilitation is the improvement of customs procedures. Efforts have been made by the Customs Cooperation Council (CCC) and its successor the World Customs Organisation (WCO) to encourage automatic data processing among its members.[68] This international customs organisation, and the national authorities who are its members, have done pioneering work in promoting electronic communications between authorities and the public.

Three major legal issues in have been encountered the adoption of EDI by customs authorities. These are the authentication of electronic data transfers, the

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65 There was a contradiction between Article 1 of of the UCP and SWIFT´s Handbook (Chapter 4, MT 700 and MT 701) in the sense that Article 1 of the UCP requires an express incorporation of the UCP into the credit, which is contrary to the SWIFT guidelines that presume such an incorporation when issuing and transmitting a credit through the SWIFT network.

According to one commentary, SWIFT-communicated credits are subject to the UCP because of what can be described as a generic incorporation. This type of incorporation automatically subjects each credit issued and communicated through the SWIFT network to the UCP. Those parties who do not wish to incorporate the UCP into their SWIFT-communicated credit must override this automatic incorporation of the UCP. See *UCP 400 & 500 compared,* p. 3.

66 In some countries, a ship registry can be consulted and a mortgage filed electronically (Gauthier, ETL 1997, p. 695).

67 See Chapter IX, *post*.

68 The advantages of electronic customs clearance are obvious. *Gauthier* (ETL 1997, p. 695) mentions that the North American railways, using the R-EDI, have made customs clearance a very quick procedure. A long train can take no more than 15 minutes to clear customs. The manifest and other pertinent documentation are sent to the American customs authorities electronically ahead of the train and clearance is effected so quickly that the train rarely even stops at the border. The process may today be even faster.

evidence of such data as evidence in legal proceedings and the need for traders to retain records of all relevant trade for a certain period of time in order to make it possible for the authorities to carry out audits.

CCC was a representative body, which could only issue recommendations to national customs authorities.[69] The recommendations of the CCC during the 1980s concerned a) urging the elimination of manually signed invoices as supporting documentation for goods declarations, b) urging the acceptance of goods declarations transmitted electronically which may be authenticated by means other than handwritten signatures and c) recommending the necessary changes in evidentiary rules to admit electronically transmitted and authenticated data.[70] The adoption of the UN/EDIFACT standard made it easier to make progress in electronic customs clearance. The CCC recommended in 1990 the use of EDIFACT to its members and all Member States of the United Nations.[71] The Customs Declaration Message ´CUSDEC´ is used to transfer data from the declarant to a customs administration in respect of a declaration of goods for import, export or transit. It incorporates the necessary transport, statistical or customs information and facilitates the inclusion of appropriate commercial information which may be accepted by customs authorities in lieu of supporting documentation.[72]

At a national level, a survey conducted by the WCO indicates that the automatisation of at least some customs procedures has been one of the main components of most national initiatives towards modernisation.[73]

Finnish Customs adopted modern information technology early. Since the early 1980s, the Finnish Customs accepted customs declarations for imports completed by magnetic tape instead of a paper declaration form. In the autumn of 1991, the Finnish Customs introduced an EDI pilot project involving five importing and forwarding companies.[74] In the middle of the 1990s electronic customs clearance was made possible for all import and export transactions. The relevant importer or exporter, or usually their freight forwarder, had an agreement with customs. This was maintained through a bilateral interchange agreement. In 1990, the CCC had already issued a guideline concerning the use

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69 Savage & Walden in Walden, p. 68.

70 The Legal Facilitation of International Electronic Commerce, UNCTAD, 6.10.1992, by Jeffrey M. Ritter, p.66.

71 Recommendation of the Customs Cooperation Council concerning the use of the UN/EDIFACT rules for electronic data interchange, 26 June 1990.

72 Blomfelt 17.11.1993, p.4.

73 UNCITRAL doc A/CN.9/WG.IV/WP.94, p. 12 referring to the survey text to be found at the website http://www.wcoomd.org/hrds/surve_e.htm#INTRODUCTION, visited on 29.6.2002.

74 EDI in Finnish Customs, Telecom Finland document, 8 September 1992. However, it was only in early 2003 that electronic customs clearance entered a pilot project stage at the customs border between Finland (i.e. the EU area) and Russia. The pilot project concerns a few Finnish companies exporting to Russia which submit their clearance information to the Finnish authorities. The Finnish authorities transmit the information to their Russian counterpart in St. Petersburg. The information then finds its way to the border station where it is compared to the documentation that travels with the goods themselves and goes finally to the customs point at the destination where the final clearance takes place. Electronic clearance makes it more difficult to forge or manipulate invoices in order to avoid duties (Helsingin Sanomat 9 March 2003, p. A12).

of interchange agreements and user manuals among Customs authorities and traders.[75] This was to be done in situations where governmental regulations were absent. Finnish Customs has implemented the Community NCTS customs transit scheme and the first electronic transit procedures took place in November 2003.[76]

At a regional level, in 2000 the European Union has moved into electronic customs transit procedures. Customs transit makes it possible to clear the goods in customs at the country and place of the final destination instead of at the place where the goods reach the territory of the Union for the first time.

In 2003, the Commission issued a Communication which covers amongs other things "a simple and paperless environment for Customs and Trade".[77] This Communication notes that the Commission should act as a ´catalyst´ to ensure that the legal and operational framework is appropriate to the creation of a simplified and paperless environment for customs and traders and that interoperability between existing IT systems is achieved. Electronic communications between customs authorities is hampered by the lack of common standards outside the new computerised transit system NCTS.[78]

According to the Communication, "supply chain management and collaboration has reduced delivery times enormously with the support of IT applications linking all actors involved. If the customs process stays out of this circuit, it is a stumbling block to just-in-time delivery.[79] The Council of Ministers has studied the Communication and has issued a resolution[80] on the basis of it. The Council emphasises coordination between authorities to create a ´single window´ policy in customs administration. Furthermore, it is necessary to establish a regulatory framework in support of reformed customs procedures in a computerised context which will guarantee, *inter alia*, the security of the system and respect for personal data.

At an international level, the use of IT for customs and trade facilitation are part of the political agenda of the World Customs Organisation (WCO) and of the WTO. The WCO Customs Data Model provides a common understanding on customs information requirements. In line with the revised Kyoto Convention[81] concerning international customs procedures, a global standard exists for the implementation of customs provisions dealing with initial reduced electronic data requirements and subsequent submission of periodic declarations and supporting documents.[82]

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75 The Guideline Concerning Customs-Trader Interchange Agreements and EDI User Manuals.

76 See ´NCTS – new Computerised Transit System, uusi tietokoneavusteinen passitusjärjestelmä´, at http://www.tulli.fi/fi/02_Yritykset/10_NCTS/index.jsp, visited on 15.3.2004.

77 COM (2003) 452 final, Brussels 24.07.2003.

78 Ibid., p. 6.

79 Ibid., p. 9.

80 Council Resolution of 5 December 2003 on creating a simple and paperless environment for customs and trade, OJ C 305, 16.12.2003, p. 1.

81 Official Journal of the European Communities L 86, 2.4.2003, p. 3.

82 COM (2003) 452 final, pp. 7-8.

VIII.5.2 ASYCUDA

One significant practical international initiative is the Automated System for Customs Data (ASYCUDA), a computerised customs management system developed by UNCTAD which covers most foreign trade procedures. ASYCUDA has been or is being installed in some 60 countries and it is expected that the number of user countries will grow to 100, making it the *de facto* world standard for Customs, although the EU makes more progress regionally.

ASYCUDA handles manifests and customs declarations, accounting procedures, transit and suspense procedures, and generates trade data that can be used for statistical economic analysis. This data takes account of the international codes and standards developed by the International Organization for Standardization (ISO), the WCO and the United Nations. It can be configured to suit the national characteristics of individual customs regimes, national tariffs and customs legislation. Furthermore, ASYCUDA provides for electronic data interchange between traders and customs authorities using the EDIFACT standard.

VIII.5.3 G7 harmonises messages for customs purposes

A working group of the G7-countries (the United States, the United Kingdom, France, Canada, Italy, Germany and Japan) has created harmonised data sets for import and export documents between their customs authorities. Part of the process consisted of reducing the maximum of data elements to 126. Edifact standard messages will continue to be supported while XML-based messages will also be developed.[83] This development shows that trade facilitation measures can be taken from time to time on an *ad hoc* basis.

VIII.6 The existing commercial requirements for trade documentation

The above parts of this chapter were dedicated to trade facilitation recommendations and statutory requirements regarding various documents used in international trade. Next, attention is paid to the requirements imposed by documentary credit practice, which has very recently been ´codified´. The aim is to portray the logistical requirements of the paper-based world in the light of the possibilities offered by electronic commerce.

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[83] Anne Queree, Digital Documents: The burdensome paperwork of trade could be alleviated with e-transport standards, Financial Times 20.6.2001.

VIII.6.1 Requirements of UCP500 as elaborated by the ISBP

Uniform Customs and Practice for documentary credits UCP500 does not lay down any requirement that a particular document should be presented under the credit. It is completely up to the parties to determine in the terms of the credit which documents satisfy its commercial purposes.

UCP500 does, however, lay down express requirements for various documents used in trade, from transport documents to invoices. These requirements are relatively general, and banks have interpreted them in a variety of ways. The approval of the International Standard Banking Practice by the ICC Banking Commission in October 2002 aims therefore at setting more precise standards for the examination of documents under documentary credits.

These requirements, as we can see next, can be divided into those concerning the form and authenticity of the documents on the one hand and to those as to their data content on the other. The ISBP seeks to harmonise existing practices. The next step, particularly in view of enhancing electronic commerce, is to develop practices in accordance with trade facilitation objectives. One has to form a picture of the practices in the paper-based world in order to see what levels of certainty one seeks when electronic messages are used in lieu of paper documents. A choice can be made e.g. to enhance safety particularly in an electronic environment to boost trust in electronic methods. However, by doing so, the practice of international trade will be modified. I shall come back to this question *infra*.

VIII.6.2 Form requirements under the present documentary credit rules

As form requirements within the meaning of this chapter one can mention the originality of documents and how they are constituted (titles, page numbering, attachments etc.), proof of the issuer of the document including signature requirements, and the treatment of typing errors. In an electronic environment, one uses terms such as authenticity, attribution and the integrity of the messages, most of which have their equivalents in the paper-based world.

VIII.6.2.1 UCP500 and the ISBP

In commercial practice, an original document plays a particular commercial role. For instance, an original bill of lading or an original insurance policy authorises the holder to the goods or to indemnification. Technically, it is sometimes difficult to distinguish between originals and copies, particularly if no hand-written signature is used. UN/CEFACT Recommendation No. 12 ´Measures to facilitate maritime transport documents procedures´ defines an ´original bill of lading´ to be a "Bill of Lading designated as original Bill of Lading".

Electronic records and messages in their more stringent meaning have so far been infrequently used under documentary credits, but mechanical means other

than computer-based means of conveying text have been in wider use. As noted in the Guide of Enactment to the UNCITRAL Model Law on Electronic Commerce, ´electronic commerce´ within the wider sense of the word might include such means as telex and facsimile. The International Standard Banking Practice reiterates the ICC Banking Commission´s policy statement The Determination of an ´original´ document in the context of UCP500 sub-article 20(b) defining which documents are to be regarded as an ´original´ document under UCP500. The statement is included in ICC publication No 500/2, and has therefore an ´elevated status´ among the norms produced by the ICC, and the statement is also referred to in para. 35 of the ISBP.[84]

Sub-article 20(b) states that (unless otherwise stipulated in the credit) banks will also accept as an original, document produced or appearing to have been produced: (1) by reprographic, automated or computerised systems, or (2) as carbon copies, provided that it is marked as original and, where necessary, appears to be signed. According to the above policy statement, banks treat as non-original any document that is produced at the bank´s telefax machine. Therefore telefax presentation is not possible, unless the credit permits presentation by telefax.

A document is not an original, if it (1) appears to be produced by a telefax machine, (2) appears to be a photocopy of another document which has not been completed by hand or copied to original stationery, or (3) states that it is a true copy of another document and that another copy is the sole original.

There are a number of ICC Banking Commission Opinions relating to the questions of original documents. In one case, where the credit required the presentation of 3 commercial invoices and 3 packing lists, the Banking Commission concluded that this requirement is satisfied by the presentation of one of each of the documents being marked ´original´ and two copies either marked ´copy´ or not marked as original. This would not be required if the documents appeared on their face to be originals.[85]

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84 Under English jurisprudence, a central case is Glencore International AG v. Bank of China [1996] 1 Lloyd´s Rep p. 135. In that case, the credit required the presentation of a beneficiary´s certificate certifying that a full set of non-negotiable documents had been sent to the buyer. A certificate was produced on an ordinary word processor and printer. That document was then photocopied onto the same paper as that used by the printer. The case proceeded so that one of the photocopies was signed and presented. The court held that signature of a copy document does not make it an original, but such a photocopy must also be marked as original.

85 R338 from the Opinions of the ICC Banking Commission (2000-01), see also R204 from the 1995-96 Queries R274 from the 1997 Queries, R437 of the 2000-01 Queries and R431 from the 2000-01 Queries.

The last-mentioned Query is the most interesting one. A shipping company sends its bills of lading to selected shippers via the Internet and the signature of the carrier is imaged onto the document. The company asked whether this practice is acceptable in the light of UCP500.

The response was that the imaged signature is considered valid as being a facsimile signature envisaged in Article 20(b) and the related ICC Decision on Original Documents. Moreover, a bill of lading or multimodal transport document which specify on their face that they are original or carry wording indicating this are regarded as originals. As this was the case with the documents referred to in the query, the Banking Commission regarded the documents as acceptable.

There are express requirements in UCP500 for the signing of transport and insurance documents.[86] Furthermore, even if not stated in the credit, drafts, certificates, and declarations by their nature require a signature.[87] The signature need not be handwritten. A document may be signed by handwriting, by facsimile signature, by perforated signature, by stamp, by symbol (e.g. a chop), or by any other mechanical or electronic method of authentication.[88] These options are identical to Article 14(3) of the Hamburg Rules, which represents an example of good interaction between international legal instruments affecting an international sale of goods transaction.[89] A signature need not be placed in a box reserved for it. A photocopy of a signed document does not qualify as a signed original document, nor does a signed document transmitted through a fax-machine which is absent an original signature.[90] A signature on a company´s letterhead paper will be taken to be the signature of that company, unless otherwise stated.[91]

When a bill of lading is indorsed (thus it is not a ´bearer´ bill), the only requirement under documentary credits is that the indorsement be completed by the party shown on the face of the bill of lading to be the ´order´ party or the ´order´ party by virtue of a previous indorsement. The manner in which the indorsement is completed is not governed by UCP500. In practice, an indorsement may be completed by typewriter and signed by stamp incorporating the name of the indorsing party and a signature or signed entirely in handwriting.[92]

The same generality which applies to signature requirements, may be also seen in the requirements for verifying the issuer in general. ISBP para. 25 provides namely that "(i)f a credit indicates that a document is to be issued by a named person or entity, this condition is satisfied if the document appears to be issued by the named person or entity. It may appear to be issued by a named person or entity by use of its letterhead, or, if there is no letterhead, the document appears to have been completed and/or signed by, or on behalf of, the named person or entity."

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86 Transport documents, unless ´blank-backs´, usually contain several pages. According to ISBP para. 30, a signature is normally placed on the first or last page of the document, but unless the credit itself indicates where a signature or indorsement is to appear, the signature or indorsement may appear anywhere on the document. As an example of particular signature requirements for transport documents, including the shipper´s signature, see the presentation on French law, *supra*.

87 ISBP para. 39.

88 UCP500 sub-Article 20 (b) second paragraph..

For the legal argument at the time the Hamburg Rules were drafted, see UN/CEFACT Recommendation 14, ´Authentication of trade documents by means other than signature´ from 1979,at http://www.unece.org/Trade Facilitation, visited on 30.11.2003.

89 Article 35(a) of the draft Instrument for Carriage of Goods [wholly or partly] [by Sea] (doc. A/CN.9/WG.III/WP.32, p. 37) states that "(a) transport document shall be signed by the carrier or a person having authority from the carrier". The Secretariat invites the Working Group to consider whether ´signature´ should be defined as, for example, it was in Article 14(3) of the Hamburg Rules, particularly in light of modern practices.

90 ISBP para. 41.

91 ISBP para. 42.

92 Late unpublished Banking Commission Opinions, DCI Vol 9 No 2, April-June 2003, pp. 7-8.

There is no need to entitle documents. It suffices that the content of a document appears to fulfil the function of the required document.[93] This may not, however, be quite true in respect of all transport or insurance documents. A document consisting of several pages physically bound together, sequentially numbered, or containing internal cross-references is to be examined as one document, even if some of the pages are regarded as an attachment.[94] Misspellings and typing errors that do not affect the meaning of a word or the sentence in which it occurs do not make a document discrepant.[95]

VIII.6.2.2 The eUCP

The Supplement to UCP500 for electronic presentations (the eUCP) has been quite thoroughly introduced in Chapter VII, *ante*, but it is necessary to point out some key features for comparison. An electronic record has to be such that the apparent identity of the sender and the apparent source of data can be verified and that it has remained complete and unaltered. These requirements of authenticity and integrity are not verified beyond ´apparent´, and banks are exonerated from liability beyond that point. Banks do not undertake to verify that the data message (electronic record) is attributable to the person who is supposed to have sent it within the meaning of Article 13 of the UNCITRAL Model Law on Electronic Commerce. Article e12 refers "to the use of a commercially acceptable data process for the receipt, authentication, and identification of electronic records". This means that there is no requirement for a level of authentication, which is extraordinary even if it were technically feasible. Nor is a bank expected to utilise the most current system containing the most sophisticated features.[96]

The introduction of the eUCP did not change the regime for signatures. UCP500 had already made it possible to use electronic signatures. In eUCP Article e3 b. ii., there is, however, a new definition of ´electronic signature´.[97] Those

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93 ISBP para 43.

94 ISBP para 29.

95 ISBP para 28.

96 ICC Guide to the eUCP, p. 150.

97 An electronic signature within the meaning of the eUCP (and documentary credits in general) is, as stated already in Chapter VII.8.4.2, *ante*, "a data process attached to or logically associated with an electronic record and executed or adopted by a person in order to identify that person and to indicate that person´s authentication of the electronic record".

The eUCP definition is a slightly more elaborate definition than the general definition contained in Directive 1999/93/EC of the European Parliament and of the Council of 13 December 1999 on a Community framework for electronic signatures. The general EU law definition is, however, amended by the concept of ´advanced electronic signature´ which describes such functions of the signature that functionally resemble a physical signature. An advanced electronic signature is uniquely linked to the signatory and is capable of identifying the signatory. Furthermore, it is created using means that the signatory can maintain under his sole control and it is linked to the data in such a manner that any subsequent change of the data is detectable.

To add one more definition, to relieve the reader from having to check cross references, one can cite Article 2(a) of the UNCITRAL Model Law on Electronic Signatures, according to which an ´electronic signature´ means data in electronic form in, affixed to or logically associated with a data message, which may be used to identify the signatory in relation to the data message and to indicate the signatory´s approval of the information contained in the data message. There is an equivalent of an ´advanced electronic signature´ in the UNCITRAL regime as well (see Chapter IV.5.5., *ante*).

documents that are required to be signed under UCP500, the credit practice as reflected by ISBP para. 39, or the terms of the credit may follow that definition. An exception may follow from general legal requirements for commercial documents or their electronic equivalents. For instance, the European Union regulates electronic invoicing, which may or may not be compatible with the general principles of documentary credits. Such regulations obviously become part of the terms of the credit, at least where mandatory.

The requirements for an electronic signature in the eUCP are technology neutral in the sense that they do not endorse any specific technology. According to the definition, the name of the signer at the end of the data message would constitute an electronic signature if it appeared to be used to identify the signer and to authenticate the electronic record and its content.[98] In most cases an electronic signature is enclosed in the envelope of the message or embedded within the electronic record itself, which meets the requirement that the message is "attached to or logically associated" with the record. It must be associated with the message in such a manner so as to indicate the identity of the signer. As to the authenticity and identication, the examiner of an electronic record is only concerned with the appearance of correctness that can be implied from examining the face of the electronic record and not the actual intention of the signer.[99]

What is essential in the letter of credit practice is that neither in the paper world nor in an electronic milieu exist requirements for signatures equivalent to traditional hand-written signatures. In terms of electronic signatures this means that the system does not presuppose Public Key Infrastructure (PKI) or the use of any form of ´advanced electronic signatures´.[100] A reference can be made to Article 6(1) of the UNCITRAL Model Law on Electronic Signatures, which states that "(w)here the law requires a signature of a person, that requirement is met in relation to a data message if an electronic signature is used that is as reliable as was appropriate for the purpose for which the data message was generated or communicated, in the light of all the circumstances, including any relevant agreement". The incorporation of the eUCP certainly is an agreement envisaged in the provision.

As one can observe, the signature requirements of UCP500 come from the maritime world corresponding to the Hamburg Rules (or *vice versa*). Obviously, there must be correspondence between the form requirements of commercial documents outside and inside documentary credit operations. One should therefore closely observe what the drafters of the UNCITRAL draft Instrument for Carriage of Goods [wholly or partly][by Sea] have in mind as to signing transport documents electronically. Furthermore, as noted in 2.1.5., *supra*, the drafters of Council Directive 2001/115/EC decided to set a general rule according to which

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98 Guide to the eUCP, p. 68.

99 Ibid.

100 Very often the term ´digital signature´ is used for an electronic signature using the PKI. In other words, the eUCP does not presuppose digital signatures (Guide to the eUCP, p. 69). However, should that term be used in the credit, it would imply that the credit actually requires the use of the PKI.

an ´advanced electronic signature´ is to be required. In comparison, the UCP do not even require a signature for an invoice. It may happen that the EU Directive becomes a ´benchmark´ statute outside its mandatory territorial scope and leads to increased formalisation of trade processes.

The more advanced the electronic signature is, the less potential for fraud, especially forgery, there will be. In the paper-based world, as already mentioned in Chapter IV, *ante*, a hand-written signature is considered to identify the signer as the author of the document, as it identifies himself with the sending of the exact data content of the message rather than approving it generally (´authenticate´ the message). Moreover, it verifies the integrity of the document as complete and unchanged. The completeness indicates finality and calls for caution, if the text signed appears to have been changed. Electronic signatures imitate these functions. In fact, the ends of authentication and integrity are considered to be reached in a secure manner comparable to hand-written signatures at this time only with the use of digital signatures based on public key cryptography.[101] One can also note that the *Bolero System* uses, as a rule, digital signatures, and the same goes for another platform with similar functions, TEDI. The *Bolero System*, which is closely examined *infra*, is the prime example of electronic documentary credit practice.[102] Thus, two standards prevail at the moment, the general one being more liberal, and the practical applications being more stringent. The reason must lie in the fact that the *Bolero System* is concerned with the transfer of rights between the seller and the buyer e.g. vis-à-vis the carrier, which calls for more certainty. In the paper-based world, the requirements for an indorsement presuppose a hand-written signature (see *supra*), although the shipowner may ´sign´ the transport document issued, in the maritime world at least, in accordance with the procedure described in Article 14(3) of the Hamburg Rules, whether these apply as such or not.

As to the other form requirements listed above in connection with UCP500 and paper documents, there are no originals or copies as such under the eUCP. It suffices that an electronic record is sent once. The requirement for an original has effects which the eUCP does not fully imitate. It should be recalled that the requirements for originals (bills of lading, insurance policies or certificates etc.) are included in UCP500 and its predecessors because such originals give the holders entitlements. In the electronic milieu, there are useful provisions in the UNCITRAL Model Law on Electronic Commerce relating to originality[103] as well as to singularity and uniqueness[104]. The holdership of an original document of title is the equivalent of control (including direct or indirect possession) of the

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101 Digital Signatures, p. 7, Jos Dumortier in Lodder & Kaspersen, Chapter 3, p. 42.

102 There is no clear indication in the published materials that Bolero´s adherence to the eUCP would have led to a reduction of electronic signature standards accordingly.

103 Article 8 states that the requirement of originality is met if there exists a reliable assurance as to the integrity of the information from the time when it was first created in its final form, whether a data message or otherwise, and, where it is required that information be presented, that the information is capable of being displayed to the person to whom it is to be presented.

104 Part II Chapter I Article 17(3) provides that "if a right is to be granted to, or an obligation is to be acquired by, one person and no other person, and if the law requires that, in order to effect this, the right or obligation must be conveyed by using one or more data messages, provided that a reliable method is used to render such data message or messages unique".

goods.[105] So far, the rules do not require the bank to verify any such circumstances, which are still very much abstractions. I will come back to this in the concluding remarks of this sub-chapter, *infra*.

Documents which contain general conditions or other documents presented often as attachments may be incorporated by way of hyperlinks. It may be irrelevant to consider whether a record with hyperlinks is one record or more. This may, however, follow from the circumstances. As transport documents mostly contain general conditions on the reverse, a hyperlink to the carrier´s general conditions is naturally part of the same record, to follow an analogy.

There should be no difference as to the treatment of misspellings or calculation errors between electronic and paper media. Another matter is that automatic document compliance checking programs may easily misunderstand such matters and bring the records back to the domain of manual scrutiny.

VIII.6.3 Transport documents

The requirements for transport documents are stated in the relevant credit. The latest version (1993) of the Uniform Customs and Practice for Documentary Credits (UCP500) lays down standard requirements for some common transport documents to be presented under a credit, which requirements shall apply unless otherwise provided by the terms of the credit. To some extent, however, UCP500 lays down tolerance even if the credit contains express provisions.

The credit does not have to require the presentation of any transport document. However, as any transport document proves that the goods have been shipped or received for shipment, and since the handing over of the transport document by the seller makes it practically impossible for him to exercise control over the goods during transit, with the notable exception of stoppage in transit, the document may be of paramount importance to the buyer. Should the transport document be a document of title, its possession and surrender is a precondition for obtaining the goods from the carrier as well as exercising some contractual rights against him. The normal requirement under documentary credits is the full set of clean on board bills of lading, issued ´to order´ and indorsed in blank.[106]

VIII.6.3.1 Marine transport documents

Article 23 of UCP500 deals with the *marine/ocean bill of lading,* and Article 24 concerns the *non-negotiable sea waybill*. For both types of documents is a provision that banks will accept a document, however named, which appears on its face to indicate the name of the carrier and to have been signed or otherwise

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105 Sections 16(b) and (c) of the US UETA have set prerequisites for the exercise of control through transferable electronic records (see Chapter VI.3.3., *ante*).

106 Hemmi, Teollisuuden Vientikuljetukset, TKL–Palvelu Oy, 1986, p. 199.

authenticated[107] by the carrier, his agent, the master or agent on behalf of the master. Any signature or authentication of the carrier or master must be identified as carrier or master, as the case may be. An agent signing or authenticating for the carrier or master must also indicate the name and the capacity of the party, i.e. the carrier or master, on whose behalf that agent is acting.

For both an ocean bill of lading and a sea waybill is provided that these documents shall indicate that goods have been loaded on board or shipped on a named vessel. The documents have to show the date of shipment. If loading on board or shipment is indicated by pre-printed wording, then the date of issuance is deemed to be the date of shipment.[108] The documents must furthermore indicate the port of loading and the port of discharge stipulated in the credit. The bank must receive all originals of the bill or waybill.

The ocean bill of lading or the sea waybill must appear to contain all the terms and conditions of carriage or some of such terms and conditions by reference to a source or document other than the bill of lading (short form or blank back bill of lading).[109] Moreover, the document must contain no indication that it is subject to a charterparty. Finally, the document must in all other respects meet the stipulations of the credit.[110]

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107 This provision is wide enough to make it possible to use electronic signatures or other methods of electronic authentication.

108 Unless the credit states otherwise, there is no requirement for the ´on board´ notation to be authenticated or signed. The notation must, however, be dated if the bill of lading is a pre-printed ´received for shipment´ bill of lading. (ICC Banking Commission Opinion R34).

109 DCI Vol 8 No 4 Oct-Dec 2002 contains, on p.11, a query concerning the situation where bills of lading are printed through the Internet, and the terms and conditions are on the front page of a blank back bill. In France, for instance, the materials examined indicate that this is the case, and especially draws the shipper´s attention to the conditions. The terms and conditions are numbered as page 1 and the normal front as 2.

The response given by the Banking Commission sees a problem when terms and conditions appear on the ´face´ of the document since the bank must examine the face. Moreover, any document which is produced using Internet services must conform to the requirements of Article 23 in respect of the B/L issuance and content plus the content of sub-Article 20(b) with regard to the originality and signing thereof.

110 The ICC Banking Commission has been recently confronted with a problem relating to ´bills of lading´ that contain various clauses authorising the carrier to release the goods without surrendering an original bill of lading. For instance, a P&O bill states: "*If the carrier so requires*, before he arranges delivery of the Goods, one original Bill of Lading, duly endorsed, must be surrendered by the Merchant to the carrier..." (emphasis added). One bill belonging to the Maersk group states: "Where the bill of Lading is non-negotiable, the Carrier may give delivery of the Goods to the named consignee upon reasonable proof of identity *and without requiring surrender of an original bill of lading...*".

One approach is to regard these clauses as terms and conditions of contract of carriage and disregard them by virtue of UCP500 sub-Article 23(a)(v) which states that banks do not pay attention to such conditions.

Another way of looking into the matter is to require that a document entitled bill of lading is in fact an effective document of title. If the carrier is entitled to release the goods without the production of an original bill of lading, the document would no longer be a bill of lading as understood by the international commercial community. For this controversy, see Laurence A.J. Bacon, The Intrinsic value of a bill of lading, DCI Vol 10 No 2, April-June 2004, pp. 11-12.

A *charterparty bill of lading* (UCP500 Article 25) has to indicate that that it is subject to a charterparty. It does not, however, have to indicate the name of the carrier. It has to appear to be signed by the master or owner (and not the carrier) or a named agent on their behalf. Even if the credit requires the presentation of the charterparty in connection with a charterparty bill of lading, banks will not examine such charterparty, but will pass it on without responsibility on their part.

VIII.6.3.2 Multimodal transport document

A *multimodal transport document* (UCP500 Article 26) is subject to very similar requirements as an ocean bill of lading and sea waybill. However, it has to indicate on its face either the carrier or the multimodal transport operator, and the latter may also have signed or authenticated the document. A multimodal transport document must indicate that the goods have been dispatched, taken charge of or loaded on board. This provision is therefore less stringent than the equivalent provisions in respect of the ocean bill of lading, the charterparty bill of lading or the sea waybill.

The possibility of transhipment under the transport documents covered by the UCP500 varies. Transhipment within the meaning of Articles 23 and 24 means unloading and reloading from one vessel to another vessel during the course of ocean carriage from the port of loading to the port of discharge stipulated in the credit. Under the ocean bill of lading and sea waybill, banks will accept these transport documents, which indicate that the goods will be transshipped, provided that the entire ocean carriage is covered by one and the same document. This applies unless the credit prohibits the transhipment. However, should the relevant cargo be be shipped in containers, trailers or ´LASH´ barges, and the entire carriage is covered by one and the same transport document, or if the transport document incorporates clauses stating that the carrier reserves the right to transship, the banks would accept a transport document indicating that the goods will be transshipped, even if the credit prohibits transshipment.

For the multimodal transport document, the UCP500 is even more permissive. Even if the credit prohibits transshipment, banks will accept a multimodal transport document which indicates that transshipment will or may take place, provided that the entire carriage is covered by one and the same multimodal transport document.

VIII.6.3.3 Air, road, rail and inland waterway transport documents

An *air transport document* has to indicate, in addition to the carrier, that the goods have been accepted for carriage. It must also indicate the actual date of dispatch, if the credit requires this, and the date indicated accordingly in the document will be deemed to be the date of shipment. In all other cases, the date of issuance of the air transport document will be deemed to be the date of shipment. Moreover, an air transport document has to indicate the airport of departure and the airport of destination.[111]

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[111] UCP500 Article 27. See also ICC Banking Commission Opinion R 231 from the 1995-96 Queries.

The actual air transport document must appear to be the original for the consignor or shipper and will be accepted by the bank even if the credit stipulates a full set of originals.[112]

Even if the credit prohibits transhipment, banks will accept an air transport document which indicates that transshipment will or may take place, provided that the entire carriage is covered by one and the same air transport document.

A road, rail, or inland waterway transport document must indicate, again in addition to the name of the carrier, that the goods have been received for shipment, dispatch or carriage. In the absence of any indication on the transport document as to the numbers issued, banks will accept the transport documents presented as constituting a full set. Banks will accept as original the transport document whether marked as original or not.[113]

Even if the credit prohibits transshipment, banks will accept a road, rail, or inland waterway transport document which indicates that transhipment will or may take place, provided that the entire carriage is covered by one and the same transport document and within the same mode of transport.

VIII.6.3.4 Documents issued by freight forwarders

As regards *transport documents issued by freight forwarders*, banks will accept them only if they appear on their face to indicate the name of the freight forwarder as a carrier or multimodal transport operator (MTO) and to have been signed or otherwise authenticated by him as carrier or MTO. Alternatively, a transport document issued by a freight forwarder may be issued as a named agent for the carrier or MTO, and the document must identify these parties.[114]

VIII.6.4 Insurance documents

Insurance documents must appear on their face to be issued and signed by insurance companies or underwriters or their agents. If an insurance document indicates that it has been issued in more than one original, all the originals must be presented unless otherwise authorised in the credit. Cover notes issued by brokers will not be accepted, unless specifically authorised in the credit.[115]

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112 Ibid.

113 UCP500 Article 28.

114 UCP500 Article 30.

115 Article 34 of the UCP500. Such notes could be useful if they entitle the assured to obtain a formal policy, or the insurer gives them the same value as a document issued by the insurer himself. The question is also whether a broker as agent can effectively bind the insurer. If not, the cover note is only evidence which can be adduced when taking action against a negligent agent having failed to effect insurance. The new Directive 2002/92/EC on Insurance Mediation divides insurance intermediaries into independent intermediaries (brokers) and tied agents, but is silent on issues relating to the binding force. In the electronic world, the right of an intermediary to bind an underwriter could be achieved by granting the intermediary a limited right to use the insurer´s electronic signature and the communications made by the agent could be attributable to the insurance company unless contrary is proved.

The signature requirement is relieved by the provision, according to which banks will accept an insurance certificate or a declaration under an open cover pre-signed by insurance companies or underwriters or their agents. A formal insurance policy will always be accepted even if the credit would call for a certificate.

An insurance document must be in the form as required by the credit and, where necessary, be indorsed by the party to whose order claims are payable. A document issued to bearer is acceptable where the credit requires an insurance document endorsed in blank or vice versa.[116]

If the credit is silent as to the insured party, an insurance document evidencing that claims are payable to the order of the shipper or beneficiary would not be acceptable unless endorsed. An insurance document should be issued or endorsed so that that the right to receive payment under it passes upon, or prior to, the release of the documents.[117]

The insurance document must be expressed in the same currency as the Credit. The insurance document must indicate, unless otherwise provided in the Credit, the insurance cover to have been effected for the CIF or CIP value of the goods, as the case may be, plus 10% when the CIF or CIP value can be determined from the face of the documents. The insurance cover should be effective at the latest from the date of loading on board or dispatch or taking charge of the goods. If this is the case, banks could accept a document which bears a later date of issuance.

In UCP500 is an instruction to add into the credit a stipulation regarding the type of insurance required and the additional risks to be covered. This is because failing specific stipulations in the credit, banks will accept insurance documents as presented without responsibility for any risks not being covered.

VIII.6.5 The Invoice

UCP500 does not require any particular documents to be presented under a letter of credit. Consequently, the seller does not have to provide a commercial invoice. However, there are, as noted before, commercial and administrative requirements according to which an invoice should be provided. Therefore, an invoice invariably forms part of the letter of credit documentation.

A credit requiring an ´invoice´ without further definition will be satisfied by any type of invoice presented. A commercial, customs or tax invoice will therefore do. However, invoices identified as ´provisional´ or ´pro-forma´ are not acceptable unless specifically authorised by the credit.

UCP500 provides[118] that commercial invoices must appear on their face to be issued by the beneficiary named in the credit and must be made out in the name

116 ISBP 194. at p. 53.

117 ISBP 195. at p. 53.

118 Article 37.

of the applicant of the credit. A commercial invoice need not be signed. The required number of originals and copies must be presented.The main function of an invoice is to evidence the value of the goods shipped. If a trade term such as ´CIF INCOTERMS2000 Calcutta´ is part of the goods description in the credit or stated in connection with the amount, the invoice must state the trade terms specified mentioning the source of the term as well.

The description of the goods in the commercial invoice must correspond with the description in the credit. In all other documents, the goods may be described in general terms not inconsistent with the description of the goods in the credit.

VIII.6.6 Other documents specially mentioned in UCP500

Article 38 of UCP500 stipulates that if a credit calls for an attestation or certification of weight in the case of transport other than by sea, banks will accept a weight stamp or declaration of weight which appears to have been superimposed on the transport document by the carrier or his agent unless the c Credit specifically stipulates that the attestation or certification of weight must be by means of a separate document.

VIII.6.7 Other documents used in international trade

There are many commercial documents that are not especially mentioned in UCP500. Some of them are pure commercial documents, as is the packing list for which no formal requirements exist. Some documents serve administrative purposes, and form requirements may exist in administrative regulations. As there are tens of regularly used commercial documents, it is not feasible to try to list them all but a few of of them may be mentioned.

UCP500 provides, however, in Article 21 a general rule which states that "(w)hen documents other than transport documents, insurance documents and commercial invoices are called for, the Credit should stipulate, by whom such documents are to be issued and their wording or data content. If the Credit does not so stipulate, banks will accept such documents as presented, provided that their data content is not inconsistent with any other stipulated document presented."

In some cases the importer asks the seller to provide a certificate of origin in order to be exempted from tariffs or to receive reduced tariff rates. There are special forms for certificates of origin, and the customs authorities of the exporter´s country certify this form. Under certain conditions, however, the origin of the goods is confirmed in the invoice, in which case the exporter himself can do the verification.

In some countries, the authorities may require a pre-shipment inspection (PSI) certificate among the commercial documents. Such a certificate constitutes a

part of the documentation presented under the letter of credit, the use of which may also be a required by the authorities.

For over a century, private sector buyers and sellers have resorted to the practice of inspecting goods before their shipment in order to ensure that the quantity and quality of the goods to be traded conform to the specifications of the sales contract. The buyer might not rely on the seller or on the description in the transport document, which declares the apparent condition of the goods. This kind of commercial inspection may result in a certificate by an inspection agency, the issue of which diminishes the role of the goods description in the transport document as ´proof´ of the conformity of the goods. There are little general form requirements for such a certificate, but the parties may agree to such in their contract of sale or otherwise.

During the last thirty years, however, this purely commercial practice in some importing countries, has been made an official requirement, particularly in countries where it was felt that the customs organisations and other official agencies were inefficient thereby prejudicing revenue collection and enabling corrupt practices and fraud.[119] This practice was reported to the UN/ECE Working Party on Facilitation of Trade Procedures in 1976, which a few years later decided to discourage the use of this procedure as one of its suggested trade facilitation measures.

In 1999, UN/CEFACT agreed to adopt a separate recommendation[120] on the subject, reaffirming its previous position and taking into account recent developments such as the Agreement on Preshipment Inspection adopted by the World Trade Organisation, the Arusha Declaration concerning integrity in customs adopted by the WCO and the development of 19 trade facilitation recommendations regarding customs practices. In the recommendation of 1999, UN/CEFACT reiterated its position that preshipment inspection should not be made a regulatory requirement. If this recommendation could not be complied with by states, PSI should be considered to be a short-term measure. A deadline, which should not exceed five years, should be established for removing regulatory PSI procedures.

The issue of regulatory PSI certificates is, in commercial practice, very centralised, and the form requirements for certificates apparently follow the practices of those undertakings. Chambers of commerce might also play a role in this respect.

As noted in Chapter V.10., *ante*, it is normal in some trades, notably bulk trades, to organise commercial surveys of the goods before they are shipped or, in any case, before the risk passes to the buyer. Documentary credits therefore sometimes call for the presentation of an ´original, full survey report issued by an independent surveyor´. The purpose of the survey and the corresponding

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119 UN/CEFACT Recommendation on preshipment inspection, Recommendation No. 27, first edition, adopted by the United Nations Centre for the Facilitation of Procedures and Practices for Administration, Commerce and Transport, Geneva, June 1999, ECE/TRADE/237, p. 3.

120 Recommendation 27 mentioned in the previous note.

certificate is to verify that the goods meet the specifications of the contract of sale. The contract and the credit specify the requirements for the certificate. Usually the contents and order of the data elements required are carefully specified. Sectoral trade organisations contribute to the elaboration of models for this activity.[121]

VIII.6.8 Do the documentary requirements of the UCP need adaptation?

As noted earlier, the ICC has launched a revision procedure of UCP500. Some of the earlier revisions have taken into account developments observed in international trade and transport practices, in particular the containerisation of transports. Similarly, the current revision should note what is happening in the commercial environment. In addition, it is suggested, the drafters should examine developments in the regulatory environment. I would not like to express anything concerning traditional paper documents in this context, but a couple of issues on the electronic side deserve attention.

One of the benefits of electronic documentation is that it is easier to avoid fraud. Digital signatures using the Public Key Infrastructure can effectively curb forgery. Safety is one of the main advantages in the transition to electronic commerce. It should be borne in mind that contemporary documentary credit law and practice is not very stringent in terms of authenticating messages as to their sender and contents. The practice in electronic transactions might become safer. Safety is needed when other functions of trade documents are contemplated. Safety involves the authenticity, integrity and confidentiality of the message. The Title Registry of the *Bolero System* that is recording rights to goods in transit functions by using digital signatures (i.e. the PKI). When a negotiable electronic transport document is transferred, the act of transfer may require a sophisticated electronic signature in order to be conclusive. One must choose between an approach stressing safety or one building on case-specific relativity as reflected in Article 6(1) of the UNCITRAL Model Law on Electronic Signatures.[122] The case-specific relativity seems to apply e.g. in US case law, but is not necessarily shared by other jurisdictions.[123] All in all, there does not seem to be a single clear direction towards which authentication policy is heading at the moment.

One should wait and see what happens regarding the UNCITRAL draft Instrument on Carriage of Goods [wholly or partly] [by Sea]. This instrument purports to regulate for the first time negotiable electronic transport documents.

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121 Mr. Heikki Vaara´s interview on 25 February 2004.

122 The English Law Commission has not taken a stand as to what kind of an electronic signature would be required for the issue (and indorsement) of a maritime policy. It is submitted that for the issue of an insurance document the signature requirement could be more liberal, whereas the indorsement of a policy (and contract) could be aligned with the treatment of electronic bills of lading. (Law Commission 2001, p. 34)

123 See the note of the UNCITRAL Secretariat, Doc. A/CN.9/WG.IV/WP.104/Add.3, paras.18 to 24.

Although the present versions of the draft Instrument focus on transport law relations, aspects of property law may be have to be considered later in accordance with the instructions of UNCITRAL. Just as banks are today verifying the originality of documents as they appear on their face for the reason of protecting their customers in their quest to gain control and title, tomorrow´s banks should be vested the tasks to verify (in addition to authenticity and integrity) the uniqueness and singularity of records, very possibly under the relevant rules of procedure envisaged in the draft Instrument. It is not the idea of a document that is relevant, but the legal effects of the document.

Banks may, furthermore, be asked to do more than to verify the record as it appears "on its face". As Åke *Nilsson* observes[124] "a quick search of the Web can unearth many facts to support or overrule the evidence ´on the face´ of the document". Imposing obligations to banks could be seen to be an act of opening a Pandora´s Box and undermining the independent and abstract nature of the banks´ undertakings.

However, the possibilities afforded by the Internet and the fact that even electronic signatures could, at least theoretically, be associated with certain information (e.g. a shipowner´s or master´s public key could perhaps reveal the place where the ship is registered, or an insurance company´s key its place of establishment) and would make it possible for intermediaries to go deeper than the ´face´ of the record.[125]

Both the UCP and the INCOTERMS should generally recognise that all documents may exist in electronic form. For instance, INCOTERMS 2000, despite all its merits, does not envisage the possibility of an insurance document being electronic.[126] Furthermore, a traditional commercial document such as the bill of lading is not necessarily replaced by one message, but a series of messages (see the Bolero Bill of Lading, *infra*). A scrutiny of an individual document may have to be replaced by a verification of compliance of a particular procedure set out in designated rules of procedure.

The requirements concerning data content follow from the terms of any particular credit or, especially in the case of invoices and transport documents, from law. The details of the data content are not particularly interesting from a trade facilitation point of view, although the possibility of not having to re-key that information is perhaps the main benefit of electronic commerce together with its speed. Since the data content is not re-keyed, inconsistencies between the documents presented will not often appear, unless the inconsistency is intended, which may result from inconsistent legal or contractual requirements, see *infra*.

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124 Åke Nilsson, The new Guide to the eUCP, in Electronic trade news, DCI Vol. 9 No 1, Jan-March 2003, p. 22.

125 The ETC model as presented in Chapter VII. 8.3., *ante*, gave tasks to the banks and the ETSP model to a trusted third party. The problem is that the customers are hardly prepared to pay the costs of such fact finding. Making as many features as possible automatic serves both ends to some extent.

126 See the conclusion of the Law Commission in Chapter V.3.2., *ante*.

VIII.7 Going the commercial way

Light has already been shed on some early projects of the electronisation of transport documents.[127] In this sub-chapter, I focus on comprehensive systems or platforms which purport to include the multitude of contracts and diverse functions protecting the parties involved in the transaction. By far, the most developed of such attempts is the *Bolero System*, which will be examined first.

The list of objectives of moving to electronic systems for international trade documentation is impressive. Its benefits cover corporate activities comprehensively.[128]

The Bolero System, like its predecessors, is an endeavour of the private sector. The Bolero Feasibility Study, studied more closely *infra*, refers to the role of commercial practice in the creation of solutions before legislation:

> "Commerce often advances ahead of the law. Historically the law has adapted to serve commercial and financial demands and to facilitate trade. Bills of lading and negotiable instruments are examples of pragmatic devices fostered by commerce and the law in partnership to meet trade requirements even though contrary to the strict legal doctrine of the time. The electronic revolution is another step where adaptation of the law will be required in many jurisdictions. The transition period is likely to require some hybrid transactions involving a mix of paper and electronics. Nevertheless it appears to us that there already is, particularly in the more flexible legal systems, a legal platform for the Bolero System."

The evolution of commercial instruments through commercial practice took a long time. Today, the rise of electronic commerce is facilitated by governments and international organisations, which can largely build on the dynamism of the private sector. The establishment of a balance between private and public is one of the biggest challenges ahead.

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127 see Chapter VIII.3.1.1 *ante*.

128 The Bolero Feasibility Study 1999 lists (on page 3) the following objectives of using electronic trading systems

- greater speed (for example bills of lading often arrive after the goods themselves, leading to port congestion, hold-ups and costs);
- cheaper administration;
- reduction of errors which presently result from re-keying data;
- reduction of transfer costs for paper documents;
- reduction of fraud and security risks;
- the benefits of a single infrastructure instead of multiple systems;
- improvement of customer service, inventory control and processes;
- improved retrievability, analysis of information, audit and reconciliation;
- better sharing of information with others and a greater ability to provide documents for scrutiny by approved interested parties;
- integration with the internal applications of entities involved in trade;
- reduction of transaction risks;
- improvement payment mechanisms;
- more efficient customs clearances; and
- the opportunity to add other useful services.

VIII.7.1 The *Bolero System*

Private sector initiatives pave the way for electronic trading in international trade. One of the most ambitious initiatives is the *Bolero System*, which has a long background. This study will analyse Bolero in great detail, since the amount of study of the issues and experiments within its framework is paramount. As private sector initiatives are needed to obtain sufficient interest and funding to create new instruments and patterns for trade, a situation is created where a legal framework for conducting business is created, to a great extent, on commercial grounds. Thus the legal framework, like the technical software solutions, is commercially exclusive and may be protected by copyright itself.

After the CMI Rules for electronic bills of lading had been completed in 1990, BIMCO[129] undertook a project to develop an electronic bill of lading system based on the CMI Rules. This project was found to be too costly. However, the results of this examination were utilised in the Bolero Project, which has had several starts, since at times there were difficulties in obtaining funding for the project.[130] The initial Bill of Lading for Europe (Bolero) pilot project was funded in part by the European Union in the context of its Infosec Program (at the time, Directorate General XIII held responsibility).[131]

Chandler describes the scope of Bolero in its earlier forms as very ambitious. The concept was to provide EDI service to all the parties concerned with the carriage of goods such as the shipper, the carrier, the bank and the consignee, notwithstanding the inevitable conflicts that arise in the normal course of events between these parties. Moreover, like SEADOCS, it was based on the idea of a central registry, which created problems of liability and confidentiality. These issues were not resolved in the first attempts to create Bolero.[132]

The latest effort behind Bolero is a joint venture by SWIFT and the Through Transport Club (TT Club). The project at this stage was relaunched in 1997 by first doing studies and marketing. In 1999, 120 participants in Bolero trials carried out a series of pilot tests, doing away with paper documents such as bills of lading, customs forms, insurance certificates and even letters of credit. It was reported that the initiative typically reduced document management and processing cycles from almost two weeks down to half a day.[133]

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129 Baltic and International Maritime Commission, seated in Copenhagen

130 George F.Chandler, III, Maritime Electronic Commerce for the Twenty-First Century, Presented at the Centenary Conference of the Comité Maritime International in Antwerp, Belgium 10.6.1997. ETL 1997, p. 668.

131 Transfer of rights in tangible goods and other rights, Note by the UNCITRAL Secretariat, A/CN.9/WG.IV/WP.90, para 76.

132 Chandler, III, ETL 1997, p. 668.

133 Kevin Godier, Electronic Trading: new systems emerge, Documentary Credits Insight, Vol 6 No 2, Spring 2000

Bolero has the following mission statement:

> "Bolero´s mission is to provide guaranteed and secured delivery, in electronic form, of trade documentation globally, based on a binding legal environment and common procedures. Bolero will provide a platform for provision of neutral cross-industry services."

The participants of the project commit themselves by adhering to a special *Bolero Rulebook*[134], which, as amended from time to time, governs the relationship between users and their rights and obligations arising from the *Bolero System,* which is a concept loosely referred to throughout this study meaning the service in general, without going into the detail of Bolero´s two-company structure supported by membership and various contractual arrangements.[135]

The Rulebook is therefore a multilateral contract which covers various contractual relationships normally found in an international trade transaction, as well as the "service provider" facilitating the transaction. The Rulebook fills the *lacunae* existing in the legal framework for electronic trading. It should be noted, however, that the background legislation for the Rulebook is English law and is based on its concepts and ideas, which need therefore be studied in some detail later.

Bolero may use the techniques of EDI and digital signatures for messaging between the parties. However, a technique based on a separate XML standard is promoted. The users of *bolero.net* have access to some 65 different XML-based

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134 The *Bolero Rulebook* is made available at http://www.boleroassociation.org/downloads/rulebook1.pdf, visited on 4.8.2003.

In fact, the users join *Bolero Association Limited* by signing a *BAL Service Contract* at (http://www.boleroassociation.org/downloads/bal_sc.pdf, visited on 3.8.2003), which gives, in Clause 3(1), the association the status of agent in signing the Rulebook on behalf of the member. This is practical, since it is impossible for each member to sign every time a new member joins the system. See the factsheet ´Welcome to Enrolment into the Bolero System´ at http://www.boleroassociation.org/downloads/enrolment.htm, visited on 4.8.2003.

In addition to acting as an agent for the signing of the Rulebook, the Bolero Association maintains registers of its membership, convenes user groups, acts as an information channel between its members and *Bolero International Limited*, which runs the operative system. Furthermore, the Bolero Association administers disciplinary procedures and has a special committee created for that purpose, and administers the Rulebook Committee in accordance with its stipulated amendment procedure.

One function of the non-profit association structure is to safeguard that access is available to the system and that service is not denied, provided that users act in accordance with the rules of the system. This serves an important aspect as regards competition law since the practically unique system might otherwise be seen as potentially restraining trade.

135 The *Bolero System* signifies the business processes and methods, together with the digital information system, which are provided by *Bolero International Limited* for communicating messages and documents and facilitating business transactions, as well as the *Bolero Rulebook* and its appendix, the *Operating Procedures* (http://www.boleroaaociation.org/downloads/op_procs.pdf, visited on 3.8.2003).

The relationship between the users of the Bolero System and Bolero International Limited is governed by the *Operational Service Contract*, which incorporates *Standard Terms* (http://www.boleroassociation.org/downloads/op_sc.pdf, visited on 3.8.2003).

document messages.[136] An essential feature of Bolero.net is the Title Registry (Bill of Lading Archives), which is designed to make it possible to transfer rights during the application of the system, most typically while goods are in transit. The registry is a passive store of electronic data and only the holder of the rights is able to transfer those rights to another user. The Registry authenticates the identity of the originator of the data and the holder of the rights and will provide a sophisticated security structure to prohibit interference with the data. The Title Registry is an example of the dematerialisation of property rights like the securities settlement systems such as the Euroclear.

The Title Registry records Bolero Bills of Lading (abbreviated ´BBL´), which are stated to be "a BBL Text together with its related Title Registry Record". [137] Bolero Bills of Lading replicates the function of a physical bill of lading by means of an electronic acknowledgement by the carrier to the BBL holder that the carrier holds the goods to the order of the BBL holder.

In March 2002, a new online mechanism, BoleroSURF (Settlement Utility for Risk and Finance) for trade settlement, was launched. Once a buyer and seller agree on the contractual terms, the necessary documentation will then be lodged with the SURF mechanism. Every stage of the transaction is then verified and validated. BoleroSURF accommodates all methods of payment from open account to documentary credits, and, running parallel to other elements in Bolero´s infrastructure, users will be able to use electronic documents with automated compliance checking.[138] BoleroSURF will be examined more closely later.

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136 The objective of a separate *Bolero*$_{xml}$ is said to be "to enable users of bolero.net to take full advantage of electronic commerce by providing a set of standard electronic documents that will facilitate interoperability amongst the members of the community". The aim is to eliminate the need for bilateral interchange agreements that describe the structure and contents of electronic data being exchanged between the parties by providing a set of common standards that can be applied multilaterally.

Boleroxml incorporates a number of components. The Document Definitions are a set of specifications which each describe a standard structure and contents of the electronic version of a common trade document and include such documents as Commercial Invoice, the Bill of Lading and Packing List. The Analyzer is a software application, which provides a non-technical presentation of the Document Definitions in an MS-Windows environment. The Validator checks that business documents, which are exchanged via the bolero.net service, comply with the rules defined in the Document Definitions.

In May 2001, UN/CEFACT which developed and maintains the EDIFACT standard messages, approved ebXML, a suite of specifications for the exchange of data over the Internet, which was developed in cooperation with a consortium of primarily made up of software developers and consultants which was called Oasis (Anne Queree, Digital Documents: The burdensome paperwork of trade could be alleviated with e-transport standards, Financial Times 20.6.2001).

As an example of other recent developments mentioned by Queree, a body funded by the Department of Trade and Industry of the United Kingdom, SITPRO (meaning The Simpler Trade Procedures Board), now controls ´Topform´, including such items as exports cargo shipping instructions, which UK exporters must complete. In a partnership with an individual software developer, SITPRO has developed ´WebElectra´, a service which allows exporters to access the Topform via the net, complete the forms and deliver them online. According to Queree, there has been discussion at the United Nations Economic Commission for Europe (UN/ECE) to accept the system underlying WebElectra for adoption as an international standard. One reason for this is that Topform is the outcome of earlier UN based standards work such as the Edifact format standard messages.

137 Bolero Rulebook, definition 11, page 4

138 Introductory note in Documentary Credits Insight Vol 8 No 1 January-March 2002 p.28.

VIII.7.1.1 Bolero Feasibility Study - background

Before launching the project, those responsible for it conducted a legal feasibility study.[139] Two major international law firms, *Allen&Overy* and *Richards Butler*, were invited to carry out the work. The study selected eighteen jurisdictions[140] worldwide chosen either on the basis of their economic significance or because they were representative of a particular type of legal system. The work was originally undertaken in 1997 but was substantially updated in 1999 to take account of the changes in the legal framework that had taken place in the meantime.

The task of the study was to "establish the general legal feasibility of the Bolero system, which is intended to replace paper transport documentation by electronic messaging and, in the case of Bolero Bills of Lading, entries in the Title Registry".[141]

VIII.7.1.2 The primary findings of the study

The feasibility study concentrated on issues featuring the functions of a bill of lading and on certain other general issues which have to be taken into account when implementing this kind of a system. Many observations have already been mentioned in the earlier parts of this study, but a summary of findings is given here. The Feasibility Study relates to the situation in 1999 before legislation based on functional equivalence approaches was generally in place.

The first issue studied was writing requirements in contracting. Writing requirements may emerge in connection with contracts of carriage. There appears to be a reasonable degree of acceptance of electronic contracts of sea carriage. However, the European CMR Convention applied to road carriage requires contracts of carriage to be in writing.[142] The contracts of sale of goods and insurance policies are sometimes subject to writing requirements. Bills of exchange and promissory notes invariably have to be in writing.

The second general item was electronic evidence. The study noted a general tendency towards allowing electronic records as evidence, although problems over this still existed in some jurisdictions. The implementation of EC Directive 2000/31/EC and similar legislation adopted in other parts of the world may have already changed the picture essentially since 1999, for which a detailed presentation does not seem be necessary here.

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139 The Report written on the basis of the study is published on the Bolero.net website http://www.boleroassociation.org/downloads/legfeas.pdf, visited on 4.8.2003..

140 These were New York State and US Federal Law in the United States; Belgium, England, France, Germany, Ireland and Netherlands in Europe; Abu Dhabi in the Middle East; and China, Hong Kong, Indonesia, Japan, Malaysia, Philippines, Singapore, South-Korea, Taiwan and Thailand in Asia.

141 The Preface of the Report, p.9.

142 Mallon mentioned on 24 November 2003 that the CMR requirements posed one obstacle to the inclusion of road transport, another was the limited use of portable devices in haulage. He adds that since 1997, the price of portable devices has dropped considerably whilst their functionality has increased dramatically. Mallon anticipated that a revision of the CMR Convention in respect of allowing electronic transport documents is looming.

The third question of general importance was how to effect the transfer of goods, the transfer of contract of carriage and the transfer of insurance cover by electronic means. The transfer of goods was regarded not merely from the point of view of transferring possession but also from the point of view of transferring the title to or property in the goods. In the case of some commodities, such as grain or oil, the cargo is frequently traded during transit and thus the title to it or its parts changes but in container traffic trading in transit is not very common.

Bankruptcy situations pose particular problems in connection with transfers of title. Title is to be distinguished from possession and in most jurisdictions studied these did not go hand in hand. However, the vesting of constructive possession[143] in the holder is necessary in some jurisdictions to protect the owner from unauthorised dispositions which might defeat the owner´s property in the goods.

The contract of carriage allows the buyer as the consignee to receive the benefit of the contract of sea carriage so that the buyer can claim against the carrier for non-performance or defective performance of the contract of carriage. According to the study, a significant number of commercial jurisdictions require that an assignment of the benefit of the contract is in writing. Even more jurisdictions claim that a formal notice of assignment is given to the carrier in order to be effective on the insolvency of the shipper as assignor.[144]

The Bolero Rulebook has construed a structure whereby a properly entitled holder of the Bolero Bill of Lading receives a direct commitment that the carrier is responsible under the relevant contract of carriage, by virtue of a novation[145]. The Rulebook is governed by English law. The Feasibility Study submits that Anglo-Saxon jurisdictions would recognise the Rulebook provision, whereas a question is raised of whether civil law jurisdictions might treat this as a transfer and require a formal notification to the carrier or a written form.

Insurance policies must almost invariably be in writing, and very frequently assignments of insurance policies must be in writing as well. The appropriate course according to the study[146] is that insurance policies be taken out for the benefit of both sellers and buyers, or for sellers to give the benefit of the policy to buyers by entering into the policy as agents on behalf of buyers as well as sellers in their own right.

An important question that is addressed in the study is the taking of security. In particular, it is questioned whether security interests in respect of specific consignments by way of electronic messages can be completed in the same way as security interests over cargoes and contracts of carriage by delivery of a physical bill of lading.

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143 For the concepts of bailment, attornment and constructive possession under English law, see Chapter V.4.1., *ante*.

144 P. 12 of the Study, see also chart 1, column 9.

145 Under English law, a *novation* replaces the contract entirely with a new contract. The term novation denotes a change of parties, as where in a contract between A and B is agreed that B shall be released and C shall take his place as the other party to the contract (Goode p. 109). Novation has its roots in Roman law and is known in civil law countries as well. For the role of novation in Finnish securities netting systems, see Rudanko, p. 126 ff.

146 On page 13.

According to the study, it would seem that it would be possible in the surveyed states to complete a pledge of particular goods with an electronic acknowledgement by the carrier to a user bank as holder of the electronic bill of lading stating that the carrier holds the goods to the order of the bank. The study also submits that this would not be registrable in a public register as a security interest under either the US or English-based charge registration or filing systems.[147] A few jurisdictions might impose writing requirements for the acknowledgement by the carrier to the bank.

According to the study, a physical bill of lading is useful for avoiding these requirements, especially as far as security over contracts of carriage are concerned, since using the bill of lading replaces in many jurisdictions the requirement of serving a written notice of assignment on the debtor (which is the carrier in the case of an assignment of the contract of carriage). In addition, some other formalities may be imposed. Some jurisdictions require the security assignment to be in writing, and the identification of a particular contract as being subject to the security might itself have to be in writing.

The Rulebook directly provides in favour of banks who are also users of Bolero that carriers will be committed to banks to the extent of their interest as long as they are Pledgee Holders. In some jurisdictions, this might not be enough to evade the rules of security assignments, and thus perfecting security would have to take place outside Bolero. However, in most jurisdictions electronic security can be effected without formalities.

The Bolero Feasibility Study is useful for indicating where problems might lie. Therefore, it suggests in case of doubt that contractual solutions be created outside the system to make sure that the desired outcome is attained.

The problem of security over insurance contracts could be solved by simple commercial arrangements stating that they are to avail the interest of pledgees as well. Security over the contract of sale and price in addition to the use of bills of exchange to support trade finance will be outside Bolero as well.

The study notes that stamp duties, data protection legislation and cryptography do not pose major obstacles in implementing the System. Data protection laws are generally designed to protect individuals, and so clear business-to-business transactions should not pose major problems to implementing a system like Bolero. As regards encryption, some states, like France and the United States, have controls on the use or export of encryption techniques.

Simultaneously with the Feasibility Study, a factsheet entitled ´Welcome to the Bolero Bills of Lading under U.S. Trade and Commercial Law´ was issued. It finds in particular that the documentary requirements of the relevant statutes, the Harter Act, the Pomerane Act, and the Uniform Commercial Code (Article 7) may not be applicable when a party has become bound by the *Bolero Rulebook*. Moreover, the requirements imposed by Article 9 of the UCC relating to the perfection of security as a prerequisite for priority in banktruptcy should be met by the Bolero legal framework, since both operate with the concept of attornment. I am not going into further detail into U.S. law issues.

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147 For the creation, enforcement and transfer of security rights under English law, see Goode, Commercial Law, pp. 735-756.

VIII.7.1.3 The role of the Bolero Rulebook

The Bolero System involves several contracts to which the user is tied. There are actually two companies maintaining the structure. The system is mainly based on the *Bolero Rulebook*. The *Operating Procedures* are appended to the Rulebook and provide a technical description of the transactions stipulated in the Rulebook itself.[148] The contractual structure includes also an *Operational Service Contract* with *Standard Terms*[149], which defines the relationship between the operator of the system (*Bolero International Limited*) and the user, including liability provisions. The contractual package also includes also the *BAL Service Contract*, which authorises *Bolero Association Limited* to act as the user´s agent in signing the *Rulebook*. As every user grants the Association that status, it may create new contractual relationships between a new user and former users. The Bolero Association also maintains a committee for possible revisions of the Rulebook and a disciplinary committee. It is thereto in charge of accepting users to the system.

The Rulebook could be considered to play the role of a ´multilateral interchange agreement´, which provides, together with the Operational Rules, for the normal legal principles of electronic commerce such as the evidential admissibility of electronic data and messages and establishes that a sender cannot repudiate a Bolero message. Although both the legal and messaging components are present, the comparison to interchange agreements is not appropriate, since technically the *Boleroxml* initiative purports to do away with interchange agreements by providing an Internet-based technique to exchange documents openly without resorting to exclusive ´proprietary´ systems. Neither are there rules on contract formation.

More appropriately, however, the Rulebook is an instrument which has to contain all necessary contractual mechanisms to bind its users to all other users. This makes it necessary not to accept parties not having committed to the Rulebook, since no binding effect could be established for them. The system is a closed one in that only subscribers will be permitted to use it. It makes it impossible for a casual buyer to make use of the electronic bills of lading held by the system. Furthermore, the Rulebook has to provide for the parties´ rights and obligations in the Bolero System. In doing so, it reflects, so far as possible, the functions of the equivalent paper contracts.[150] A Bolero Bill of Lading replicates the functions of a physical bill of lading as a contract of carriage, a receipt for the goods, a document representing the entitlement to possession of the goods and a means of transferring the contract of carriage. In this way, it provides for the holdership, transfer and pledges of entitlements to the goods and the contract of carriage and will ensure through security procedures that the entitlements were originated, authenticated and transferable only by the authorised holder. In other words, the guarantee of singularity has to be maintained. Finally, the Rulebook

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148 Portions of the Operating Procedures are labelled ´Operational Rules´. These are binding obligations according to their terms, the same as any other obligation under the Rulebook. The remaining descriptive portions of the Operating Procedures are of the nature of non-mandatory recitals (Rulebook Rule 2.1.2.(3)).

149 At http://www.boleroassociation.org/downloads/op_sc.pdf, visited on 3.8.2003.

150 On the functional equivalence approach, see the UNCITRAL Model Law on Electronic Commerce in Chapter IV.4.3., *ante*.

has to incorporate, directly or by reference, the provisions of underlying contracts, such as contracts relating to the carriage and documentary credits.[151]

The Rulebook is a major innovation in that the legal framework for continuous and divergent transactions and legal relations is covered by a multilateral contractual arrangement. A contractual structure has been used and encouraged in the case of interchange agreements between two or more parties applying EDI. These agreements, at least their European versions, do not regulate substantive aspects of the transaction. Bolero is a very ambitious attempt to regulate not only aspects of technical interchange but entire legal relationships, although it refers ultimately to English law. It does not attempt to be a ´self-regulatory contract´[152]. The fact that the Bolero System deals with proprietary rights in connection with documents of title, and the fact that transport law applies to a great extent on a mandatory basis, would make it very risky to detach the system from its closest national law.

The binding nature of the multipartite contract in English law is founded on case law. In *Satanita*[153], the British House of Lords decided that an owner whose yacht sank following a collision in a yacht race could recover the full value of his yacht, although the defense of the defendant was based on the well-known principles of the limitation of liability applying to marine collisions. The defendant was a sponsor of the race and had signed a letter to the Yacht Club agreeing to be responsible for all damages caused by his yacht without the right to limit liability.The defendant had thereby validly waived the right of limitation by virtue of joining the multipartite contract.[154]

Finally, like any contract, the Rulebook provides for the applicable law, this being English law and for the jurisdiction of English courts. Thus, the Rulebook and the legal relationships governed thereby are subject to English law. In general, as it is stated, all jurisdictions which affect Bolero recognise the choice-of-law clause contained in the Rulebook since party autonomy is almost universally recognized. This principle is embedded in Article 3 of the Rome Convention on the Law Applicable to Contractual Obligations, which now also forms part of English law.[155] However, where the Convention does not apply, but English conflict of laws rules are applied, the English common law doctrine of

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151 Bolero Feasibility Study 1999, p. 25.

152 Self-regulatory contracts are an expression of party autonomy to the extent that parties regulate their legal relationship by a contract in an exhaustive manner and no national law lies behind it. This possibility should exist in jurisdictions that admit party autonomy. For arguments for this view, see Schmitthoff (Ed.) The Sources of Law of International Trade, pp. 29-32. For later discussions on the scope of party autonomy, see Chapter X, *post*.

153 *Clarke v. Dunraven, ´The Satanita´ [1897] AC 59*.

154 Under English law, a contract involving more than two parties may be concluded either through the intermediary of a third, independent entity or directly between the parties (including their representatives or agents). For multipartite contracts under English law, see Owzia, pp. 323-327.

155 For English conflict of laws, see Dicey & Morris, The Conflict of Laws, Thirteenth Edition by Lawrence Collins with Specialist Editords, London 2000, Part Seven, Law of Obligations. See also cases *Mount Albert Borough Council v. Australasian etc. Assurance Society Ltd*. [1938] A.C. 224, 240 and *Vita Food Products Inc. v. Unus Shipping Co* [1939] A.C. 277, 289-290.

´proper law´ enters the picture.[156] The proper law of the contract is primarily the law chosen by the parties. Sometimes the legislature or courts intervene to limit the effect of an express choice of law where the chosen law is foreign and where, but for the choice, English law would have governed the contract. In such cases the choice of foreign law is valid but nevertheless the mandatory provisions of English law apply.

Moreover, where the sole matter at issue between the parties is a claim for non-compliance with or breach of the Rulebook, all proceedings in respect of such claim shall be subject to the exclusive jurisdiction of English courts. On other issues, such as the rights and obligations of the various parties involved, even including the intepretation of the Rulebook, the parties´ rights to institute proceedings in other courts are not limited. Even in such cases, a non-exclusive English jurisdiction clause creates a possibility to start proceedings in another court. In maritime law, the jurisdiction of courts is normally preset by legislation.

Despite the fact that the users of Bolero undertake to subject the Rulebook to English law and primarily to the jurisdiction of English courts, the Feasibility Study advises that certain arrangements be effected, for instance, security assignments requiring writing according to a particular national law, outside Bolero to avoid problems. The conclusion of the Feasibility Study in respect of the applicable law is that English law, as a choice of law and England as having a non-exclusive jurisdiction over the Rulebook will enhance the position of Bolero users.

In addition, users are recommended to select for underlying substantive contracts (like the contract of sale) a jurisdiction which itself has tolerant rules concerning electronic contracts and which ignores foreign procedural formalities requiring writing.[157] As already noted earlier, the application of English law is by no means exclusive to the *Bolero System*. The contracts of sale, transport, and, to the extent applicable, insurance are each governed by their own laws, which may of course coincide. Since the Rulebook contains obligations relating to many of these contracts, otherwise governed by separate law, a mixture of laws will govern the transaction.

It also has to be borne in mind however that Bolero leaves outside its scope certain questions, such as bills of exchange, for which exists a legal system determined ultimately by the choice of law rules applied by a competent court.

As noted earlier, the *Bolero System* is based on incorporation by reference so that the parties can incorporate their standard terms into their contract of carriage by reference. English law is tolerant of this possibility stipulated in the Rulebook. All other laws involved may not necessarily be.

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156 The scope of the Rome Convention is discussed in Chapter VII.5.3, *ante*.

157 See p. 39 of the Bolero Feasibility Study 1999.

VIII.7.1.4 What is a Bolero Bill of Lading?

The Bolero Bill of Lading (BBL)[158] is "a shorthand to describe the rights of the registered holder in respect of the contract of carriage and the goods".[159] This is because the system does not create a single electronic document to fulfil the same functions as a paper bill of lading. The paper bill of lading is replaced by a series of electronic messages, instructions and data records in the Title Registry, which combine to fulfil the functions.

The BBL is therefore a receipt for the goods from the carrier, freight forwarder or combined transport operator. This receipt carries the date of shipment (like *shipped* B/Ls) or the the date of receipt for shipment and any reservations as to the condition of the goods. In addition, there are details of the consignment and packing lists where appropriate. The BBL incorporates the contract of carriage by reference to the standard terms of the carrier or the forwarder.

Like a normal bill of lading, the BBL gives its holder rights to give instructions to the carrier, e.g. as to the re-routing and unloading when this is permitted by the contract. Moreover, the BBL entitles its holder to designate the person entitled to possession and delivery. This is usually achieved by a transfer in the registry to a new holder. The BBL facilitates novation of the contract of carriage to a new holder. A new holder can pledge or transfer rights in the goods. Finally, a prospective new holder can inspect the entries in the registry before becoming a holder.[160]

The BBL imitates the operation of a paper bill. The Rulebook defines a number of roles[161] that a user can occupy in relation to the BBL as well as a number of functions[162] which users in these roles can perform.

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158 I have used capital letters exceptionally to mark the concepts in a ´proprietary´ system (proprietary in the sense that its concepts are unique; the Bolero System expressly distinguishes itself from proprietary systems in technical terms)

159 Ibid., p. 41.

160 Ibid., p. 42.

161 These roles are (the Bolero term first then the counterpart in the paper-using world):
Carrier is the carrier in the paper world;
Surrender Party is the carrier´s agent (if any) at the port of discharge;
Shipper is shipper;
Consignee is a consignee of a non-negotiable (straight) bill;
To Order Party is an indorsee of a negotiable bill of lading;
Holder is the party having physical possession of the operative paper bill of lading;
Bearer Holder is the party having physical possession of the operative paper bill, which is negotiable simply by transfer of physical possession; and
Pledgee Holder is a party having a financing or checking interest in the bill.
(Factsheet ´Welcome to the Legal Aspects of a Bolero Bill of Lading, p.1)

162 These functions are (the Bolero term first then the counterpart in the paper-using world):
Create is the issuance of the bill of lading by the carrier.
Designate Holder-to-order is an endorsement of the bill of lading by its legitimate holder;
Blank Endorse is an indorsement of a bill of lading so as to make it negotiable by bearer;
Designate Pledgee Holder means delivery of the paper bill to a bank or similar institution;
Designate Holder means the transfer of physical possession of the operative paper bill of lading;
Amend means change by the carrier of the bill of lading; and
Surrender means surrender of the bill of lading by its holder at the discharge port.
(Factsheet ´Welcome to the Legal Aspects of a Bolero Bill of Lading´, p.1)

It should be noted that the Bolero System, like other electronic bill of lading registry systems have to operate with the concept of ´holder´. This is because an electronic system cannot fully reproduce the function of a ´bearer´ instrument which has been indorsed *in blanco*. A traditional bill of lading, on the other hand, can be indorsed to´bearer´, which makes it easier to transfer the bill further, e.g. by a pledgee or an agent, which also prevents trading patterns from being revealed through a chain of indorsements.[163] In traditional documentary credits, bearer instruments are useful because they facilitate a chain of pledges without indorsements ´to order or assigns´ in each case.

Electronic bill of lading systems have to safeguard the guarantee of singularity. The main interface where this problem is felt is the relationship between electronic and paper documents.[164]

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163 There is, however, a possibility for a user of the system to be a *Bearer Holder* by becoming designated a *Holder* of a *Blank Endorsed Bolero Bill of Lading*. To *Blank Endorse* means to render, by the process described in the Operating Procedures, a BBL capable of transfer simply by designation of a new *Bearer Holder*. Another possibility is that a

Holder is also *To Order Party,* in which case he is a *Holder-to-order*. The functional equivalence is created by labelling the status differently. Both types of designations are recorded in the central Title Registry, which of course contains the entire chain of transfers in either direction. There is no way for the holdership to change hands without the system knowing. On the other hand, trading patterns of preceding right holders can be kept secret by confidentiality obligations in cases of bearer holdership (see the Bolero Operating Procedures 4.5.2.2., p. 94).

164 Rule 3.7 contains provisions in respect of a switch to paper, which is an essential interface between an electronic world and the normal paper-based ´incomplete´ transport world. It may become relevant in respect of electronic documentary credits as well, where a credit may allow the beneficiary to choose between presentation of paper documents or electronic records. (For electronic credits, see the the presentation on the eUCP in Chapter VII.8. et seq., *ante)*.

Rule 3.7 provides the following:

Persons Entitled to Switch to Paper. At any time before the goods to which the Bolero Bill of Lading relates have been delivered by the carrier, a current Holder, Holder-to-order, Pledgee Holder or Bearer Holder shall be entitled to demand that the Carrier issue a paper bill of lading in accordance with the Operational Rules (set of rules appended to the Rulebook).

Form of Paper Bill of Lading. The Carrier shall, immediately upon receipt of such a demand, issue a paper bill of lading which sets out all the data contained in and all of the terms and conditions contained in or evidenced by the original BBL text: a statement to the effect that it originated as a Bolero Bill of Lading, the date upon which it was issued in paper form, and a record issued by Bolero International of the chain of Users which have been parties to contracts of carriage with the Carrier, from the date of the creation of the Bolero Bill of Lading until the date on which its switch to paper demand was sent by Bolero International.

Discrepancies. In the event of any discrepancy between the paper bill of lading so issued and the electronic record of the Bolero Bill of Lading, the electronic record shall prevail.

Delivery of paper bill of lading. The Carrier shall deliver the paper bill of lading in accordance with the instructions of the person currently entitled to hold it, being:

- the current Pledgee Holder; or if none
- the current Holder-to-order or Bearer Holder; or if none
- the current Holder.

End of Bolero Bill of Lading. A User that has knowledge or notice that the switch to paper has been demanded shall give no further Title Registry Instructions in relation to the Bolero Bill of Lading. The Bolero Bill of Lading shall cease to be effective as from the moment of the issue of the paper bill of lading.

Where the carrier creates (i.e. issues) a BBL, he can make it non-transferable by naming a consignee. The system appears to have had traditional sea carriage as its model. The contractual structure need not, however, be limited to sea carriage alone. The BBL could be used for multimodal or pure land transports, in which the use of transferable or negotiable documents has not been common, and where English law has generally not recognised documents of title to exist. The materials are silent about situations in which the carrier is a contracting carrier only and there is a chain of contracts of affreightment between him and sub-carriers. This is because the system is only concerned with the contracting carrier. As against the Shipper or the Bearer, the contracting carrier is solely responsible.[165]

VIII.7.1.5 A comprehensive trading system envisaged

As the *Feasibility Study 1999* lists[166], initially the main contracts which will be initially formed or transmitted are the contracts of carriage, letters of credit and various ancillary documents, such as commercial invoices and insurance certificates. Contracts of sale and contracts of insurance are not included in the system entirely, since in some jurisdictions legislative changes will be required to permit these contracts to be concluded electronically. Therefore today´s Bolero System could be characterised as a ´semi-integrated trading platform´.

However, the Rulebook already contains some provisions on contracts of sale. Rule 3.10. namely provides the messages used in concluding the legal value of the contract. Furthermore, where a contract of sale between users requires that shipping documents are to be tendered to the buyer or to another party nominated by the buyer, such documents may be in the form of electronic records provided that they contain all of the information required by the contract of sale. The Rulebook also validates the transfer of property by using Bolero Bills of Lading in cases where this would happen otherwise based on the intention of the parties or law.

The Bolero System can transmit and store various documents (i.e. equivalent messages) relating to the contract of sale: the contract itself, the commercial invoice, certificates of quantity or quality and certificates of origin, and consignment data such as the packing list. The system includes messages to the effect that the carrier, on the seller´s request, acknowledges holding the goods to the order of the buyer, which in the above mentioned circumstances amounts to transfer of property.

For insurance documents, insurance policies may be stored in the system for information only, whereas insurance certificates may be transmitted through the system.

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165 Mallon does not, in his written interview 24 November 2003, anticipate that the chain of affreightment contracts would become electronic.

166 On p. 26.

As regards documents relating to the carriage of goods, the system is most comprehensive. The conclusion and recording of a contract of carriage by sea, road and rail is possible whilst air transport contracts are not. The system does not store any electronic transport documents that could be printed as such, but replicates their functions with electronic messages. The Bolero Bill of Lading can be made non-transferable by designating a consignee. Other documents in this field are the receipt of goods, instructions for delivery and advice to consignee, freight invoice and freight payment receipt. Finally, there is a message for the novation of contract of carriage from shipper to consignee or to the pledgee bank.

The system knows also an acknowledgement by carrier[167] to bank that, at the direction of the owner of the goods, the carrier holds the goods to the order of the bank so that they are under the control of the bank. This acknowledgement effects the pledge of the goods. On the other hand, specific security agreements over the goods, the contracts of carriage, the contracts of sale and insurance in respect of the goods cannot be made using the system. This is because national laws impose too many formalities on these arrangements. The *Bolero System* also excludes governmental documents such as cstoms declarations, clearances or responses as well as certificates concerning dangerous or controlled goods and foodstuffs.

The possibility to conduct documentary credit operations through the *Bolero System* will be covered separately see *infra*. It should be mentioned that the *Bolero Feasibility Study 1999* opens the door for enlarging the system to other services. These could include the management of bills of exchange, freight derivatives and futures, leasing interchanges, e.g. for the hire of containers, plants and vehicles, transport information and booking services, vessel and aircraft chartering, the securitisation of goods in transit as well as international quota control by regulatory authorities, e.g. compliance with tariff agreements. This list illustrates that although the developments are still at their initial stages, the international trade of tomorrow may look very much different from what it is today. The development towards comprehensive integration platforms built following a ´holistic approach´ is underway.[168]

Mallon has mentioned that an important decision was made early on in the development of Bolero and that was that the Bolero solution would, as far as possible, seek to replicate the legal relationships and results that would apply if traditional documentation was used. This commercial decision was based on the widely held view amongst the constituency of putative Bolero users that to modify those relationships and results would cause considerable difficulty in adoption and, to the extent that one or more parties would have been disadvantaged, would even create an immediate barrier to adoption. According to

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167 Bolero International acts as the carrier´s agent in carrying out the notifications prescribed in the Rulebook.

168 Mallon indicates (Mallon 2002, p. 13) that a fully comprehensive system was avoided for commercial reasons.

Mallon, the cooperation of a variety of parties performing a variety of functions is required for an international sale of goods to proceed smoothly.[169]

VIII.7.1.6 Documentary credits in the Bolero System

A provision in the Rulebook especially permits electronic presentation of documents under a letter of credit. Until the entry into force of the ICC Supplement to UCP 500 for electronic presentations - eUCP, the Rulebook constituted the set of rules to follow. The Bolero System subscribed to the eUCP right from the beginning thereby incorporating UCP500 as well.[170] Operationally, the eUCP must apparently be complemented by some provisions of the Bolero contractual structure such as the Operational Rules. The Bolero Association Limited should revise the relevant provisions of the 1999 Rulebook so that the exact regulatory framework applying to documentary credits under the Bolero System would be more concrete. Moreover, as compliance checking takes place through the BoleroSURF facility, which is also subject to its own Rulebook, clarity could be added.[171]

Before 1 April 2002, however, the Rulebook provisions applied to electronic presentations and the presentation of any documents by electronic transmission through the Bolero System were accepted as if they were equivalent to paper documents, where a User issued, advised or confirmed a Documentary Credit on the instructions of an Applicant User[172]. Under such a Documentary Credit, a Beneficiary User was required to present stipulated documents in order to

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169 Mallon 2002, pp. 6-7. In his written interview on 24 November 2003, Mallon gives his "long term vision" of a "fully integrated trading platform", complex in its overall construction, but focussed in its use according to the function that the participant is performing.

This would be a system which would not use documents moving between parties, but rather a common user database where data elements were populated by only those entitled to do so, those being the primary sources of that data. For instance, only the actual carrier could populate the data field ´actual shipment date´. Certain elements of the data would be open and others would be confidential, including, for example, the key or code required to obtain release of the goods or give instructions to the carrier. Furthermore, the right of access to such confidential data elements could be made conditional on the population of other fields. For example, a bank could populate the data elements confirming that payment would be made contingent on other data fields being populated correctly by the appropriate parties. These other fields could indicate that shipment was on time, export licence was granted or an inspection company confirmed the quality and quantity of the goods.

Mallon´s vision resembles, in my view, the Electronic Trade Credit model discussed by the ICC in the middle of the 1990s (see Chapter VII.8.3., *ante*) and seems to have similarities to the anticipated SWIFTNet Trade Services Utility, see *infra*. In both models documents and equivalent message flows would be replaced by new functions.

170 ICC Publication No 500/2 has entered into force on 1 April 2002. There exists the ´eUCP XML Guide´ published by the Bolero Association.

171 Mallon noted (on 24 November 2003) that the eUCP left many questions open for future determination.

172 Applicant User is a user who instructs a bank to issue a documentary credit. A Beneficiary User is a user who is designated under a documentary credit as the party to whom, or to whose order, payment is to be made or whose bills of exchange are to be accepted and paid. Even before the entry into force of the eUCP, a Documentary Credit in the Bolero system followed the definition of the Uniform Customs and Practice for Documentary Credits or the International Standby Practices 1998 (see the Rulebook Definitions pp. 3-5).

operate the Credit, provided that the Credit expressly indicated that presentation under the Bolero System was acceptable, and the data contained in such transmissions was presented in Documents whose description matched that of the documents required to be presented by the terms of the Credit. Furthermore, where the Credit required that a particular document be issued, authenticated or signed by a particular person, the data transmission had to be signed by that person or by a user who was authorised to act and take responsibility on his behalf.[173] No change is assumed to have taken place in the transition to the eUCP in this case.

Rule 3.11(2) provided that a requirement that an ´original´ document be presented is satisfied by the presentation of a document from a message bearing the signature of the person said to have issued or created the document or that of a user who is authorised to act and to take responsibility on his behalf. Moreover, where the terms of the Credit required that a number of copies of a document be presented by a Beneficiary User to another User (´the Recipient User´), such a requirement was satisfied by a single transmission of the equivalent document to that Recipient User. The latter was entitled or empowered to make the number of onward transmissions, or, if necessary, to create the number of copies of that document as would have been necessary to complete the transaction in a paper environment. However, no Bolero Bill of Lading shall have more than one holder.[174] The provisions probably repealed were more elaborate than the eUCP provisions.

Rule 3.11(4) contained a provision regarding the role of banks as holders of Bolero Bills of Lading. According to this provision, where a User acting as an issuing or confirming bank is designated as a Pledgee Holder or Bearer Holder of a BBL for the purpose of the performance of a documentary credit, that User shall only acquire such property in and responsibility for the goods as the parties to the credit transaction intend.

The Bolero Feasibility Study 1999 finds back-to-back documentary credits possible within the Bolero System. So the benefiary of a letter of credit can procure from his bank a new letter of credit backed by the receipts due under the original letter of credit.

A complex framework needs illustrations to be understood. I therefore borrow the Association´s own example[175] on how the system works:

(1) A seller agrees to sell to an importer a quantity of sprockets at a specified price under the term CIF Calcutta Incoterms 2000, the payment taking place through a documentary credit.

(2) The seller takes the sprockets to a carrier, which loads them. The carrier then creates

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173 Rule 3.11(1).

174 Rule 3.11(3).

175 Welcome to: Legal Aspects of a Bolero Bill of Lading http://www.bolero.net/downloads/bbls.pdf, visited on 3.8.2004.

(3) a Bolero Bill of Lading and designates the seller as the Shipper and Holder of the Bolero Bill of Lading and the importer as the To Order Party.

(4) Bank A examines the Bolero Bill of Lading, finds it in order, credits the seller´s account, and designates Bank B the new Pledgee Holder. Bank B originally issued the letter of credit, which Bank A confirmed.

(5) Bank B performs any additional checking of the electronic records that it requires and charges the importer´s account. Bank B then relinquishes its pledge and designates the importer as the Holder of the Bolero Bill of Lading. The importer is already To Order Party for the bill, and now, being the Holder also, the importer can transfer the Bill. On behalf of the carrier, Bolero International notifies the importer that the carrier holds the goods to its order.

(6) The importer sells the sprockets while underway to a buyer. Accordingly, the importer designates the buyer as the Holder-to-order (Holder + To Order Party) of the Bolero Bill of Lading. On behalf of the carrier, Bolero International notifies the new Holder-to-order that the carrier holds the goods to its order.

(7) The goods arrive at the port of destination and the buyer surrenders the Bolero Bill of Lading. No further Bolero-based transactions are now possible for the bill. Bolero International gives notice of surrender to the carrier and confirms surrender to the buyer.

(8) The buyer´s representative turns up at the port with the proof of identification required by the carrier and/or port. The carrier delivers the goods to the buyer´s representative.

The transition to the eUCP has not been implemented in the Rulebook yet, although technical specifications have been made. Both the UCP500 and the eUCP are brought in by incorporation by reference. Documentary credits, in which presentation takes place through the Bolero System, involve a connecting factor in favour of English law, since that is the law applicable to Rulebook obligations. Yet, it is not obvious that English law would apply to all contractual relationships of a credit operated under the system since the place of the closest and most real connection could be regarded as following a tradional framework. It has not been the policy of the Bolero System to subject all contracts covered by the system to English law, because mandatory maritime laws would take precedence in any case.

One might still consider amending the Rulebook´s choice of law clause to the effect that it applies to the parties´ obligations under documentary credit operations in which presentation takes place through the Bolero System. This would apply to questions not covered by the UCP or the eUCP, of course. Such background law would mainly address general contract law issues and the scope of the fraud exception. Injunctions enjoining payments would, I believe, have to be sought before English courts. It would be ideal if the UN Convention on Independent Guarantees and Stand-By Letters of Credit 1995 could be applied to the criteria of the fraud exception. I presume that English courts would not grant any relief based on a contractually incorporated piece of ´anational´ law.

Documentary collections can be replicated in the Bolero System in a way similar to letters of credit. An essential feature is that the seller´s bank and the buyer´s bank may gain security over the documents.

Documentary credits are managed through SURF, a fully automated documentary settlement system. SURF exploits the services provided by the Bolero Core Messaging Platform to provide document compliance services with optional bank guarantees. The SURF system can automatically check all commonly used trade documents like commercial invoices, bills of lading[176] and certificates of weight. It supports documentary credits by managing the request for payment assurance via a bank and it performs compliance checking of trade documents and ensures that payment is made before title to the goods is transferred through the Bill of Lading via the Bolero Title Registry.[177] In addition to serving documentary credit operations; SURF is useful in document verifications relating to open account trading and documentary collections as well. The legal aspects of SURF are contained in the SURF Rulebook, which is part of the Bolero Rulebook. SURF enables compliance with UCP500.

VIII.7.1.7 How about other rights affecting the goods?

The Title Registry does not include all rights affecting the goods, even if all relevant participants were its Users. For instance, retention of title clauses are not recorded in it. The Bolero System may store, or ultimately include, contracts of sale, but due to confidentiality principles, its terms remain undisclosed to other users. Moreover, the seller has the right of stoppage in transit, and the carrier may exercise his lien rights.

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176 Although this is not expressly stated in the materials available on the Web, other bills than Bolero Bills of Lading can be checked.

177 Introduction to SURF at http://www.bolero.net/decision/service/surf/index.php3?printable=1, visited on 3.8.2003.

The stages of the SURF Agreement are (according to the SURF Product Overview to be downloaded from the same website)

1. Establishment of the SURF Agreement

After the commercial agreement has been established the SURF agreement is established between the buyer and the seller. The SURF agreement describes the terms of the underlying agreement as it relates to settlement.

2. Fulfillment of pre-conditions

Both parties (buyer and seller) may optionally require their counterparty to provide a payment undertaking as a condition of the SURF Agreement. A conditional payment undertaking from the buyer´s bank, confirming that the bank will pay the seller if compliant documents are presented, is an example. SURF uses the SWIFT e-Payments Plus protocols when exchanging payment information with a bank.

3. Document presentation and checking

To evidence compliance with the terms of the agreement, the seller must present a set of trade documents to SURF.

Normally the presentation is to take place immediately after the shipment of the goods. The SURF Agreement will stipulate the terms of the presentation. The trade documents must be in *Boleroxml* format. SURF will validate the trade documents based on the requirements stated in the SURF agreement.

4. Payment

Before documents are released by SURF evidence of payment may be required in the form of a debit or credit confirmation from a bank.

5. Release of the documents

Once the process reaches this stage the trade documents will be released to the buyer (or nominated party) and the SURF settlement transaction will be concluded.

The Bolero Rulebook is subject to English law as a selected law. The obligations under the Rulebook are subjected to the jurisdiction of English courts. It is therefore opportune to consider that English conflict of laws rules also apply to determine other rights in the goods than those defined in the Bolero Rulebook.

English law will treat questions of stoppage in transit likely according to the law of the contract of sale.[178] On the other hand one view seems to be that the retention of title (´Romalpa´) clause is ´an incident of property´ and that it should therefore broadly follow the *lex situs* of the goods at the time of their despatch to the buyer.[179]

Under English law itself, the right of an innocent bill of lading holder prevails against an unpaid seller exercising his right of stoppage.[180] The fact that even contracts of sale are recorded in the same system as the contract of carriage could afford the possibility to record an unpaid vendor´s reservation for a right to use stoppage in transit. Such a recording could effectively eliminate the possibility for the Holder of a BBL to claim to be in good faith.

As explained in Chapter V.4.1., *ante*, the goods in transit are frequently subject to rights that can be categorised here as the carrier´s lien rights. English courts characterise liens as procedural matters and have therefore broadly applied the *lex fori*.[181] As noted equally, at English common law, the carrier has a right to retain possession of the goods in three cases. Through liens he can recover general average contributions, expenses incurred in protecting the cargo and freight. The lien is restricted to possession and does not represent property or the right of re-sale. In addition to common law and other non-contractual liens, lien rights are established in transport contracts. Contracts extend the carrier´s possessory lien for the non-payment of freight or of other charges.[182] Such lien clauses, contained in the general conditions of the carrier, are part of the contractual framework established by the Bolero Rulebook. There may be a conflict between a lien clause incorporated by reference, among other transport conditions, on the one hand, and the Rulebook Holder provision. It is submitted that such a retention right, based either on common law or contract, would prevail over the Rulebook Title Registry provisions.

Ideally, all rights that affect the carrier´s delivery obligations, could be recorded in the Title Registry or its equivalents in other possible systems and make it thereby more informative. The availability of information on conflicting rights could be taken into account when a new Holder´s good faith is to be assessed.

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178 Debattista in Transfer of Ownership, p. 146, citing Benjamin, Sale of Goods, 5th Edition, London 1997, paras 25-154.

179 Ibid., paras 25-118.

180 Section 47 of the Sale of Goods Act 1979, Debattista in Transfer of Ownership, p. 147.

181 Debattista in Transfer of Ownership, p. 148, Jackson, Enforcement of Maritime Claims, p. 344.

182 Debattista in Transfer of Ownership, p. 150.

VIII.7.1.8 Liability and confidentiality issues in the *Bolero System*

It was noted, *supra,* that liability and confidentiality issues were among the biggest stumbling blocks during the early unsuccessful launches of Bolero. Therefore these matters certainly deserve some coverage although they are somewhat out of the centre of gravity of this study based on choices of focus rather than underestimating the importance of the matter. It is impossible to cover the liability regime of the Bolero System in great detail, although it is certainly of interest to those considering enrolment to the system. Some general observations should therefore suffice.

The liability regime of the Bolero System is complex. In the case of the Bolero Association, it is the BAL Service Contract, and in the case of Bolero International, the Operational Service Contract, which determine the liability principles. The Bolero Rulebook refers to these instruments in Rule 2.1(3) in its relations with the defined Users of the System. Moreover, liability arising from obligations owed by one User to another is excluded in Rule 2.1(2). For liability issues in practical operations, it is the Operational Service Contract (referred to hereafter as the OSC) that is more relevant.

The general liability provision in the OSC is section 2.14, which contains exonerations concerning the acts of others (including users and third party networks), an exclusion of liability in force majeure situations and exclusions of "external matters" and all indirect and consequential losses, unless these result from fraud on the part of Bolero International. The liability may be based on contract, tort, negligence, misrepresentation or other cause.

Part 4 of the OSC then specifies the causes and limits of liability for various acts or omissions on the part of the operator. Generally, liability for an individual act or omission is covered up to USD 100 000 per user and per loss. It is a slightly boring exercise to go through all the situations listed for using this ceiling. Still, such a list will give an impression of what services the system is renders, and what could in principle go wrong, necessitating the involvement of lawyers.

Firstly, liability arising from message sending including a misdirection or loss of a message or a delay in its sending will be covered. The same goes for message accuracy violated by the acts of the operator, including situations where the message is altered, the message sender incorrectly identified, the message falsely created, and for diverse problems that may emerge in message validation.

Secondly, the operator may fail to maintain an accurate log or audit trail of transactions through the system, due to which a User may not be able to prove his case in a dispute settlement with another user. Moreover, the system may violate its confidentiality obligations.

Thirdly, liability may arise in the context of certification. The operator may issue certificates improperly, or it may fail to issue a requested certificate. A user may rely on erroneous information contained in a certificate issued by Bolero International, or the latter may fail to revoke a certificate according to its obligations set out in the OSC. Conversely, the operator may revoke a certificate unilaterally without being permitted to do so.

The OSC anticipates the rare situation[183] that all certificates issued by Bolero International could become unreliable or unsuitable for use as stated in their documentary forms, which would lead to a number of users suffering direct losses. In such a case, the aggregate compensation to all claimant users paid by Bolero International shall be USD 1 million.

Furthermore, there is a USD 100.000 limit for breach of information confidentiality (as distinct from message confidentiality). Likewise, liability may arise out of failures in record retention. It may be the result of a failed creation or erroneous deletion of an RID[184] or a failure to change a sub-account.

Again, if several users are entitled to claim USD 100.000 for any of the acts specified *supra*, the maximum aggregate liability of the operator is USD 1 million, irrespective of the number of users entitled to a claim. Moreover, the operator´s aggregate liability for all claims arising during one calendar year shall be limited to USD 10 million.

The OSC anticipates some degree of claims, or it is designed to be customer friendly as it spells out the procedure for claims. The user shall provide proof in support of the claim for the loss, its extent, the causal linkage between the breach and the loss claimed, and that the user has satisfied all requirements spelled out for the presentation of the claim. The claim shall be made four months after the incident at the latest. Although the user has the burden of proof, the operator has a contractual obligation to cooperate in the process to a reasonable degree.

The result is that the system compensates damages for actual, direct loss suffered by the enrolling user, including out-of-pocket expenses, resulting solely from Bolero International´s act or omission in providing the service which results in one or more of the causes listed *supra*, but always excluding any indirect or consequential loss, or loss of profits, opportunity, goodwill, reputation, trading or contracts, or exchange rate losses.[185]

The system is required to treat commercial information as confidential. The confidential status of a message may be based on the provision in the Operating Procedures. Alternatively, information may be marked as ´confidential´ by a user or may result from other provisions of the Operational Service Contract.

To regulate the accessibility of information about the users of the system, Bolero International operates according to a single, uniform privacy policy that is incorporated into all Operational Service Contracts. That privacy policy is implemented for the most part as technological restrictions on information access and to a lesser degree as practices employed by the personnel of Bolero International. On the other hand, information is not kept confidential and may be disclosed to anyone requesting it, unless the provisions of the Operating Procedures make it confidential.[186]

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183 The author was writing this text while listening to news about the New York blackout in August 2003.

184 An RID is used in user identification together with a digital signature. An RID consists of a Root Identifier and one or more optional special identifiers, which may indicate e.g. the department of a company (Operating Procedures, p. 17).

185 Part 4.1.(1) of the OSC.

186 Operating Procedures 7.1., p. 141. The relevant privacy provisions are in sections 4.5.2.2. (indorsement chain records), 5.2.2. (enrolment) and 7.1. (general list).

Finally, as already observed *supra*, the Bolero System requires the use of digital signatures. As rights are transferred between parties, the use of digital signatures adds safety.

VIII.7.2 TradeCard[187]

Competitors or parallels to Bolero have emerged in the last few years. The New York based *TradeCard* service, supported by a group of banks, had its marketing launch in early 2000.[188] It provides electronic automation of all the documentary data required in an international trade transaction newly positioned on an Internet trading platform. It incorporates fresh components such as payment guarantees, cargo insurance and inspection agency partners.

TradeCard works by establishing a transaction in electronic form with the seller and the buyer, after which digital signatures are put in place. Each purchase order is then attached to a payment guarantee (to make sure that the buyer will make the payment automatically after receiving the goods) and is then stored electronically in TradeCard´s patented and proprietary database. Electronic shipping documents may then be created by the seller together with his freight forwarder in accordance with the details agreed.

There is a patented compliance checking system, which checks the purchase order against shipping documents. When the central processor is satisfied that the exporter has complied exactly with the terms and conditions of the purchase order, a message is sent to the importer´s bank to credit the exporter´s account with the payment for the transaction.

Both TradeCard and Bolero aim to incorporate and to go beyond such trading platforms or electronic marketplaces which facilitate trade between unknown buyers and sellers but lack the ability to oversee financial settlement in a secure manner.

Bolero is, however, a legally more ambitious project through its Rulebook but TradeCard also has a similar concept, although it is not presented as being as ambitious. The difference lies in that Bolero uses encryption technology and offers liability insurance to protect users against any loss attributed to forgery, security breaches or the failure of the system to relay and handle messages and documents.

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187 This presentation follows an article by Kevin Godier in Documentary Credits Insight Vol 6 No 2, Spring 2000, p. 1, 22 and 23. See also the website http://www.tradecard.com, visited on 18.7.2004.

188 It is principally designed for finished goods with a shipment value between 10 000 and 100 000 US dollars to be traded between Asia and North America.

Trade Card has established partnerships with international money mover Thomas Cook and credit insurer Coface (Mark Ford, Alternatives to L/Cs on the rise, DCI Vol. 9 No 2, April-June 2003, p. 23).

VIII.7.3 @Global Trade

Another commercial product in the field of electronic trade credit systems is "@GlobalTrade", which aims to take documentary credit transactions online.[189] This trading system is said to be "a fully open interactive secure payment and trade management system capable of serving multiple financial institutions anywhere in the world".

The procedure operates in the following manner: The exporter first receives a message from the system saying that the importer is opening a credit in his favour. The exporter and importer then log into the @Global Trade system to examine the credit, this being a sort of pre-verification of the credit allowing the parties to negotiate the details before the credit is processed and advised to the exporter.

When the exporter then receives the actual credit he moves it downstream to service providers like ocean carriers and insurance companies.

@GlobalTrade is said to be compatible with UCP 500 and does not, in its marketing, challenge the need for a documentary credit, but is said to facilitate it. It is based on a separate User Agreement as well. The introduction of the new eUCP rules is said to reduce the scope of the User Agreement since it covers to a great extent the same issues but is not intended to compete with it.

The functions of individual banks in checking documents manually for compliance are replaced by the same task carried out by a Documentary Clearance Center. A negotiable bill of lading is replaced with non-negotiable waybills, as well as three clauses that are believed to make a waybill as functional as a negotiated bill of lading, and reduce the use of negotiated bills of lading.[190]

@Global Trade, however, claims to introduce commercial trade credit innovations. The ´eLC Card´ stands for electronic letter of credit card which is designed for small purchases from USD 5000 upwards depending on the credit limit. The financial security of an irrevocable letter of credit is provided satisfying the need for a secure payment instrument between unknown parties.

Another innovative element is a ´FastTrack documentary credit´. It is intended to be a simple irrevocable conditional payment instrument subject to UCP 500 that offers some new features. Firstly, it allows the credit to be advised directly to the seller via e-mail. Secondly, the buyer has the convenience of a pre-defined FastTrack application form.

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189 This summary is based on an interview with Arthur O.Thomas, Senior Vice President Business Development for CCEWeb Corporation published in ICC´s Documentary Credits Insight Vol 7 No1 Winter 2001.

190 The clauses are not disclosed in the interview in DCI, but apparently these relate at least to the incorporation of a liability system (Hague Rules etc.) as well as a clause granting the consignee (which could be the bank) the right to dispose of the goods whilst in transit.

VIII.7.4 TEDI

Yet another system for replacing paper documents with electronic equivalents is the *Trade and Settlement EDI (TEDI) System*, which is led by a project consortium composed of industrial, financial and commercial transnational corporations from Japan that are active in international trade transactions. The system is web-based and allows participants to communicate and exchange data messages relevant to trade transactions over the Internet. Like the *Bolero System*, TEDI builds on the existence of third party service providers that maintain records of data messages transmitted through the system and maintains records of data messages of the status of cargo shipments to which those messages pertain. Similarly, a set of data messages are intended to replicate the functions of paper bills of lading. In order to ensure the security and reliability of the system, data messages are attributed to participants through public key certificates issued by recognised certification authorities.[191]

A multi-party contractual framework consists of three types of contracts among the relevant players, namely the *TEDI Interchange Agreement*[192], *TEDI Repository Service Terms and Conditions*[193] and the *TEDI Electronic Signature Agreement*[194]. These are not studied here in detail since these largely reflect the same functions and solutions as the contractual framework of the *Bolero System*.

One basic difference to be mentioned is that where the Bolero System is based on membership or a scheme through which each member is in contractual privity with each other member irrespective of the actual flow of goods, TEDI presupposes contract formation at each level in the trade chain, through a series of bilateral agreements independently entered into, by reference to and employing certain common, standard and required mandatory terms used throughout each link in the trade chain.[195]

VIII.7.5 SWIFTNet Trade Services Utility

At the time of the finalisation of this study in July 2004, SWIFT publicised its plans to launch a new payment-related trade service which could eventually, given the wide coverage of the banking sector by SWIFT, represent the widest application of electronic trade instruments providing risk coverage and finance. I have therefore endeavoured to collect information on the project at its early stages.[196] The plan is to establish the SWIFTNet Trade Services Utility (TSU), the

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191 Information based on the UNCITRAL Note Doc A/CN.9/WG.IV/WP.90, para 86. See also the organisational website http://www.tediclub.com, visited on 18.7.2004.

192 For the agreement with annotation, see http://www.tediclub.com/english/pdf/IA-English_Ano.pdf, visited on 18.7.2004.

193 For these terms and conditions with annotation, see see http://www.tediclub.com/english/pdf/RSP-English_Anno.pdf, visited on 18.7.2004.

194 For this agreement with annotation, see http://www.tediclub.com/english/pdf/CA-English_Ano.pdf, visited on 18.7.2004.

195 TEDI Interchange Agreement (with Annotation), p. 1. According to the document, the adoption of a membership model is being considered.

196 I would like to thank Ms Béatrice Goethals, Senior Product Manager at SWIFT for providing the relevant information.

development of which is largely based on a staircase model from less complicated payment transactions up to electronic equivalents of commercial letters of credit. Subject to decisions to be taken later on, a commercial product would be developed with a view to undertaking commercial piloting during the later part of 2005.[197]

The TSU is the banking sector´s response to the needs of growing international trade. The banking community has traditionally provided risk and finance instruments, but their use has remained relatively static whilst trading companies are increasingly using payments on open account. This is because the companies are either willing to accept greater risks or are using other than banking products such as credit insurance to mitigate them.[198]

Information technology advancements and an improved economic climate have given impetus to companies´ plans to automate their supply chains. The results are the growth in outsourcing and corporate networks as well as the convergence of cash and trade. Banks are looking forward to becoming intermediaries in the corporate supply chains with the provision of the insourcing of accounts payables and receivable services, enhanced financing and broader information services.[199]

The development of the TSU, if finally adopted by SWIFT, would be undertaken in intermediate steps to support banks in the provision of services from open account payments to complex letters of credit. The TSU will be a "collaborative[200], centralised utility for use by the banking community for interbank messaging and data matching.[201] It will provide minimum common functionality, which enables banks to differentiate their service offering. The standards will be based on the concept of data elements, and the data will be extracted from trade documentation and input into the TSU by the banks. The data is said to represent only the information that banks need to carry out their obligations and to enable a range of trade services to be offered to their corporate clients.[202]

Ideally, the bank would be involved at an early stage of the supply chain, the purchase order stage. The central utility would receive data elements from a client´s document. The centralised TSU will initially compare messages and data elements from documents by matching a subset of information from the buyer and seller. Extracts from at least a ´purchase order´, ´invoice´ and ´transport document´ are used in this process. The TSU will then use messages to accept

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197 SWIFTNet Trade Services Utility Information Paper, p. 3.

198 Ibid., p. 1.

199 Ibid.

200 SWIFT differentiates between collaborative and competititive spaces. The collaborative space consists of bank-to-bank communication where common messaging services, standards and infrastructure could help to control costs. The competitive space comprises bank-to-corporate offerings where banks compete with each other.

201 The TSU will be a SWIFT owned, developed and operated service using newly developed XML messages, a central data matching and work flow engine, and SWIFTNet messaging services.

202 SWIFTNet Trade Services Utility Information Paper, p. 2.

associated document data elements related to the transaction, link them to the first document provided and match the defined fields within and between messages.[203]

By using the TSU, banks could offer trade data checking services to trading companies. The TSU would be able to compare data within and between associated information on a structured basis and provide an early identification of discrepancies. More importantly, at least in the light of the objectives of this study, banks may be able to offer finance against an authenticated purchase order or a portfolio of orders similar to invoice factoring and, especially by using data elements specific to transport documents, fully automated documentary credits.[204] The availability of more timely information regarding trade transaction details could help to reduce risks and would possibly lead to more advantageous pricing for companies.

An elementary staircase model exists of the functionalities that would eventually be covered by the service. The staircase starts from a Short Form Purchase Order (SFPO) matching and adds, at each stage, new services such as payment initiation, corporate trade data matching and document checking. An equivalent of documentary collections would be reached at halfway up the staircase, and a fully electronic letter of credit based on the SFPO and governed by the eUCP would constitute the ´end stage´. The system would recognise, in its intermediate stages, the possibility of using both electronic messages and paper documents in documentary collections and letters of credits.[205]

The system would, as I have understood, not build on electronic documents similar to paper documents but on data content that would not be repeated or re-keyed. Each participant such as the carrier would fill in (´populate´) only data essential for his contribution and the system will remember the rest. The information produced in traditional trade documentation is divided between ´key data´ and other information. A traditional trade document is a ´set of data content recorded as such´ on paper, and its electronic equivalent replicates the same in electronic form. The idea of the TSU would go beyond a straight equivalent of a paper document and would relate more closely to the information (data content) than its expression on a paper or in a message.

As SWIFT is a banks´ organisation, and the relevant players in the supply chain are mostly other than banks, there needs to be a framework under which users are connected to the functionality. The aim is to establish ´user groups´ most probably through participating banks.[206] The contractual framework has not been made available yet, but would probably constitute ´rules of procedure´ similar to the Bolero Rulebook, as envisaged in Article 59 of the ´draft Instrument for Carriage of Goods [wholly or partly] [by Sea]´, since replicating fully the functions of a traditional letter of credit electronically would have to include the use of electronic transport documents and documents of title.

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203 Ibid.

204 Banks might also use different data from trade documents to increase finance along the trade transaction cycle as perceived risk is reduced.

205 Collyer in Helsinki, 25.5.2004.

206 Ibid.

VIII.8 Characteristics of a central registry system such as the *Bolero System*

Central registries are used in electronic trading platforms that contain settlement and logistic functionalities. Being a user of a platform requires, in addition to legal constructions, a commercial relationship with the party maintaining the registry. Trading platforms, very few in number still, are not interoperable in the technical, commercial or legal sense. Being a member of many potential platforms becomes a cost factor for companies.

A question may be asked of whether a registry is needed to effect transactions with electronic documents. Between two commercial partners, this does not seem to be necessary, since parties to, for instance, an interchange agreement are contractually required to keep data logs and store documents. The integrity of stored documents can be verified.

When third parties enter the picture, the question becomes more complicated. Transfer of rights by virtue of a transfer of an electronic document would require an indorsee becoming part of a contractual arrangement or a legislative framework for facilitating such transfers. If the document is simply evidence, such as a sea waybill subject to legislation that has detached the right of control from the possession of a copy of the document, the problem may not be pertinent. However, when documents of title or negotiable instruments are used, it is difficult to see how effects equivalent to those in the paper-based world could be achieved in a system where transmissions take place only between traders.

As noted earlier in Chapter VIII.3.3., *Todd*[207] thinks that section 1(5) of the English 1992 Carriage of Goods by Sea Act giving the right to the Secretary of State to implement appropriate regulations for the creation of electronic transport documents assumes the direct transmission of transport documents between traders. However, as the said Act does not elaborate on the type and operation of transport documents to be created, it is difficult to draw any conclusions from it. Todd[208] thinks it might be possible to transfer a single electronic document from trader to trader, with the appropriate use of encryption techniques. However, he adds quite rightly that signature authentication would be required for the entire chain. Therefore, the system would not be cost-efficient as compared to communicating with the carrier.

The creation of electronic equivalents of negotiable instruments is still in its infancy. It is beyond my competence to assess whether mathematical and technical means could be created in a feasible manner to verify the transfer, possession and singularity of an electronic negotiable instrument, which would exist outside any organised registry. In any case, such an instrument should be the "to order of a named person" type and should not be a bearer instrument, given the pitfalls of computer-based crime. Any such regime would inevitably require legislative intervention if the large scale use of such instruments were desired.

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207 Todd, pp. 247-248.

208 Ibid.

The possibility of recording information in a central registry to which all or most relevant parties are connected would facilitate real time information regarding the goods, which would help the management of the supply chain. These ideas may not be commercially feasible for a number of years, but I think they should still be mentioned, because they change the infrastructure in which maritime transport business is conducted.

One very imaginable use for central registries could be to register rights and claims relating to the goods which are beyond the regular transfers of an electronic bill of lading. This would be mostly for informative purposes. Such information could turn out to be legally relevant. A good faith transferee of a bill of lading can namely claim delivery of the goods in most cases irrespective of conflicting claims e.g. based on stoppage in transit. Where such claims are to be recorded in a central registry, the indorsee can be made able to verify them through electronic means, which would normally deprive him of the possibility to refer to his good faith. Similarly, loss of or damage to the cargo could be recorded in real time, which could have a bearing on the transferee´s ability to claim delivery of the goods as originally recorded, see 9.1., *infra*.

VIII.9 Interaction between the contract of sale and the contract of transport

The contract of sale and the contract of transport are separate contracts. This basic principle has to be remembered and has found expression in the guidelines entitled the Golden Rules of Incoterms. The parties and the subject matters of these contracts are different. However, a contract of carriage is a contract ancillary[209] to the contract of sale, and the latter contains provisions as to the former. Where the goods are to be delivered by an independent carrier, either the seller or the buyer is expected to contract for the carriage, usually in accordance with a chosen trade term.

There has been a grey area between these two contracts, but this area has been subject to legal studies in the Nordic countries.[210] My intention in this study is not to try to explore this complicated interrelationship in its entirety, for one reason because it would require too much space. In any case, at least in principle it would sound attractive that full interaction could work between the different contracts in the supply chain. Since the number of parties involved in a trade transaction is great, the fewer conflict points that exist between the legal regimes applying to each facet of the transaction, the more possible it is in my view for the parties to a transaction to agree to electronic trading and documentation methods.

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209 Ramberg calls, the contract of transport ´anslutande avtal´ in Swedish in his 1993 treatise, which has a similar meaning.

210 See Selvig, Grenseland (1974), Ramberg 1993 as well as Hoppu, Kauppa- ja kuljetussopimusten keskinäisestä suhteesta (1968/69) and Kuljetuskauppa (1992).

The legal rules relating to the international sale and carriage of goods are under constant development by international organisations, and it would be useful to consider measures of avoiding conflicts between these two contracts and clarifying to the legal regimes. If some contracts are ´ancillary´, they should support the main purpose of the transaction, the sale. But this is not so evident. Independent or abstract undertakings are sometimes more useful for promoting commerce. However, these raise the problem of good faith. For instance, documentary credits are autonomous of the main contract with the exception of clear fraud in the transaction.

This suggested approach of linking two contracts has well-known pitfalls. In the 1855 Bill of Lading Act of England, the right to sue the carrier under the contract of transport was connected to the passage of property in the goods under the contract of sale. That linkage caused substantial problems but over a century was needed to repeal the Act.

Attention will be first paid to the role of the carrier in the contract of sale. The next point is the stoppage in transit, which is a strange animal in relation to the contract of transport. The issue of to whom to deliver in case of conflicting claims, one of them being a call of stoppage in transit, could equally be dealt with as a conflict between retention of title clauses and obligations based on the contract of transport. Finally, loading and discharge obligations are often seen as points of conflict between the two contractual relationships. Nordic discussions and contract practice are used mainly as good examples and illustrations of the problematics, especially as regards stoppage in transit.

VIII.9.1 The carrier and the contract of sale

A starting point for the presentation of the relationship between the two contracts is to illustrate how the carrier becomes indirectly involved in the sales contract. I limit this short presentation to sea transport, in which bills of lading are used and add particular aspects, and use the Nordic Maritime Codes partly as a basis since these are very recent pieces of legislation and take into account aspects of both the Hague-Visby and Hamburg Rules.

Indeed, the carrier gets involved in the contract of sale and becomes significantly liable to the buyer for the sellers´s breaches of the contract of sale.[211] When the risk under the contract of sale passes at the buyer´s end, a delivery to a person not entitled to claim delivery from the carrier often leads to the failure of the seller´s delivery obligation. The carrier becomes liable under general principles of law, and it is a general conception (at least in the Nordic countries) that there is liability is and it may not be limited.[212]

Another point of liability for the carrier as against the buyer may arise out of the particulars relating especially to goods specification in the transport

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211 As expressed by Selvig, Grenseland, on p. 163.

212 Selvig, Grenseland, p. 79, Honka, p. 139.

document. The information contained in the transport document has to be reliable, especially as regards safeguarding the merchantability of transferable documents of title.[213] The verification of the apparent condition and packing of the goods when received by the carrier may have some bearing, not only as to the carrier´s own liability, but also in applying the rules relating to the passing of risk under the INCOTERMS. If it can be verified that goods were damaged when being loaded, the loss or damage may have to be borne by the seller, depending on the term applied. Such verification is, however, usually impossible, especially in container traffic.

The carrier shall to a reasonable extent check the accuracy of the particulars included in the bill of lading. These particulars include the apparent condition of the goods and their packing.[214] However, the carrier does not verify contract specifications in the contract of sale. If the carrier has reasonable grounds to suspect the accuracy of such particulars, or if he had no reasonable means of checking their accuracy, he must insert in the bill of lading a proper reservation to this effect.[215]

According to Article 3.4 of the Hague-Visby Rules, bill of lading representations are made conclusive evidence by ´estoppel´[216] as far as the transferee bill of lading holder is concerned, provided that the transferee acted in good faith.[217] In the relationship between the shipper and the carrier (as well as between the carrier and the consignee where a sea waybill is used) the representations in the bill of lading are only *prima facie* evidence. However, a limitation of liability normally comes into play.

In the light of the preparations of the draft Instrument on the Carriage of Goods [wholly or partly][by Sea], it seems that the carrier´s obligations are generally not extended from what they are now according to the Hamburg Rules. The rules drafted are more elaborate, distinguishing between containerised and non-containerised goods. There are new provisions defining what ´reasonable means of checking´ are and when the carrier is considered to be acting in good faith in issuing a transport document or electronic record.[218] All in all, the

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213 The Nordic Codes have expanded the scope of representations the carrier is liable for under the Hague-Visby Rules and created a two-tier system for the carrier´s liability for misrepresentations: one treating the situation as if the goods had been lost or damaged during the carrier´s liability period, the other being an independent system based on misrepresentations only and covering also other aspects than those relating to the goods; see Honka, pp. 117 ff.

214 This is the rule of Finnish Maritime Code chapter 13 sections 46 and 48. The Hamburg Rules 15.1(a) and (b) are more elaborate as to what the carrier has to record than Article 3.3 of the Hague-Visby Rules. In any case, the shipper may require the insertion of certain particulars.

215 Finnish Maritime Code chapter 13 section 48. Such reservation is usually valid, but as against a third party it is not if the carrier realised or ought to have realised that a particular relating to the goods was inaccurate (Ch. 13 s.49).

216 Estoppel is a rule of evidence of the doctrine of law which generally precludes a person from denying the truth of some statement formerly made by him.

217 Generally, the Hague-Visby Rules do not require that the third party has relied on the information, whereas the Hamburg Rules place such a requirement. According to Honka (p. 122), the Nordic Codes should be interpreted as following the Hague-Visby interpretation. Once there is a good faith transfer, the subsequent transferee can be in bad faith.

218 See Article 38 of doc A/CN.9/WG.III/WP32.

relevance of the information contained in the transport documents for evidence, conclusive or not, is also upheld as regards electronic documents.

Electronic communications can, however, add information contained in the delivery chain, which may, in individual cases, have legal effects. Shipment tracking could be used, in addition to verifying the location of the shipment, to record any events that could possibly affect the condition of the cargo, should the carriers be willing to accept it.

Such information could constitute evidence challenging the *prima facie* information contained in the document or the good faith of the parties in the chain. Where a central registry is used, for instance, damages happening at any time during the chain could be recorded in it, in addition to or replacing the existence of an electronic record used in lieu of a transport document. A transferee of a transferable electronic record could be empowered to verify the recordings regarding the goods, and thereby effectively deprive him of the possibility to use good faith as an excuse in some cases.[219]

VIII.9.2 Stoppage in transit

As was explained in Chapter V.5., *ante*, Article 71(3) of the CISG makes the right of stoppage in transit greatly subordinate to the rights created under transport law. The carrier could safely deliver the goods to a party surrendering a bill of lading. The problem is that the goods may become an object of parallel rights based on two different contracts and the legislations behind them.[220] I have noticed that many commercial and transport law writers treat the right of stoppage in transit with certain embarrasment: the right exists, but its scope is limited or uncertain in relation to transport law. The right seems to be seldom resorted to. A recent Nordic dissertation by Svante O. *Johansson* points out the complexity of the instrument in practical terms.[221]

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219 Information relating to the condition of the cargo prior to or at the time of shipment would be relevant since the transport document is *prima facie* evidence of the latter stage; what happens after the issue of the document affects the liability of the carrier, and the state of the cargo recorded in the document is a legitimate point of comparison. In multimodal carriages with transshipments and where separate transport documents were to be issued each time, electronic recordings of events that can possibly cause damages (such as the shifting of cargo) could play a legal role.

Recordings of the state of the cargo at each stage of a multimodal carriage would have an impact on the application of the network liability by incorporating the relevant liability regime applicable to the mode of transport where the damage occurred.

220 As noted above, there is equally a potential conflict between retention of title clauses and rights based on the holdership of the bill of lading. See *Cour de Cassation de France, 1.10.1985, Cooppérative Agricole d´Esternay v. Margarine Verkaufs Union, ETL 1986.I. pp. 91 et seq. and 99*, as well as Chandler, III in Transfer of Ownership, pp. 424-425. In the French case, the court found, first, that a clause reserving title may not be invoked against third party purchasers in good faith and, second, that a negotiable inland bill of lading constitutes title to the goods, which it specifies for its holder in due course.

221 Svante O. Johansson, Stoppningsrätt under godstransport, Stockholm 2001.

Stoppage in transit is an exception to the rule, according to which only the party who has the right of control can stop the carriage of goods,[222] and to some extent their delivery to the consignee. Stoppage in transit is normally based on sales law, as is the possibility for the seller to retain title. Both aim at protecting the seller against a buyer, who does not honour his obligations. The right of stoppage in transit allows the seller to interfere with the relations arising out of a contract of carriage. Retention of title clauses give rights against the other creditors of the buyer, but their scope as regards possible subsequent indorsees varies.

I wish to make the suggestion that these rights represent an element external to the normal course of a tranportation. Stoppage in transit and retention of title are rights which are based, in addition to the relevant retention clause, on applicable national law, and which may affect the rights of the consignee where electronic bill of lading systems are used. These systems could purport to be comprehensive in the sense that both the contract of sale and the contract of transport are concluded or recorded using them, in addition to other contracts such as those relating to documentary credits. In theory at least, a central registry such as the Bolero Title Registry or any rules of procedure within the meaning of Article 2.4 of the draft Instrument on Carriage of Goods [wholly or partly] [by Sea], could eventually be developed to record even such rights as retention of title, a reservation for the right to use stoppage in transit where goods remain unpaid, and potential pledges liens on the goods.[223] All this could done at least on an informatory basis (which could partly wipe away the good faith of the consignee). Where non-negotiable transport documents are used, the position of third parties is even more vulnerable.

The laws on sale and transport could be adjusted to reach a satisfactory solution to the problem. The primacy of transport law obligations generally seems to prevail, at least when negotiable transport documents are used. The argument is generally that the carrier should not become an umpire in a sales agreement, even as regards such elements as the receiver´s good faith.[224] This is of course a valid argument.

However, it is not beyond imagination that technology might change the world even in this respect. What if the carrier is connected to the same electronic bill of lading registry as the parties who have also recorded their sales contract in

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222 Report of Working Group III (Transport Law) on the work of its eleventh session, Doc A/CN.9/526, para 131. This view appears to be close to Grönfors´s view (Grönfors 1982, pp. 316-317) of Swedish law: Grönfors holds that rights based on stoppage in transit are an exception to the normal rules to the entitlement to the goods (as interpreted by Tiberg, p. 551), see *infra*.

223 Doubts could legitimately be expressed whether this would be reasonable, bearing in mind the costs of introducing the relevant rules and technical solutions.

224 For instance Ramberg 2000, p. 45, and Tiberg, p. 556.

the registry? It would be technically possible to record and verify many rights[225] affecting the goods, should the system be developed to provide such comprehensive information. The question then arises of what the right and justified order of priority would be under international sales law: should the merchantability of the goods, reached by the use of bills of lading, always take priority over the duty of the buyer to respect his obligations? If yes, should the right of stoppage be discarded altogether if its practical scope remains limited, as suggested by Johansson.[226] In such a case, the rules relating to the right of control should remain at hand to the seller.

Carriers may, even in the traditional documentary system, be confronted with conflicting claims where holders of separate originals of a bill of lading come to claim delivery.[227] In an electronic system subject to the guarantee of singularity[228] this type of collision should not occur.

Many carriages take place without the use of bills of lading. In those cases, the seller can exercise the right of stoppage until the buyer has the goods in his possession.[229] This happens even if the seller no longer had a consignor´s copy or ´duplicate´ of the consignment note in the case of road, rail and air transport.

Under national law are different approaches imposing obligations on the carrier. Under English law, obligations are imposed on the carrier under sales law.[230] In the United States, stoppage in transit is regulated by the Pomerene Act as regards outbound shipments, and by the Uniform Commercial Code, Article 7, as regards inbound shipments. The revision of the Nordic Maritime Codes[231] in the early 1990s has maintained a provision which is very much in line with

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225 Where the seller resorts to stoppage in transit, he is supposed to have legitimate reasons. If the buyer uses the rights based on the possession of a bill of lading in contravention to the seller´s right of stoppage, this constitutes a breach of the contract of sale (Tiberg, p. 551). The seller´s invoking of stoppage could very easily be recorded in an electronic system. The buyer, who would be able to verify the rights affecting the goods, could be presumed to have knowledge of them. The rights of stoppage in transit or retention of title would be governed by their own proper laws. It is conceivable to require that the right of stoppage exists under the relevant sales law and has an effect on contracts of transport in order to become enforceable on carriers subject to a different contract statute (cf. Tiberg, p. 557). It is again a matter of policy whether to give priority to (foreign) sales law as against domestic transport law, which would not let sales law affect the carrier´s obligations under the contract of transport.

226 See Johansson, pp. 444 *et seq*.

227 See e.g. the Finnish Maritime Code Chapter 13, Section 53.

228 For the guarantee of singularity under the UNCITRAL Model Law on Electronic Commerce, see Articles 17 (3) to (5) of the Model Law and Chapter VI 3.1, *ante*.

229 Grönfors 1982, p. 317.

230 The English Sale of Goods Act section 46(4) provides that "when notice of stoppage in transit is given by the seller to the carrier or other bailee or custodier in possession of the goods, he must re-deliver the goods to, or according to the directions of, the seller;...". According to Debattista (Transfer of Ownership, p. 147) this provision is in conflict with the carrier´s common law obligation to deliver the goods to the holder of the bill of lading, or even to the defaulting buyer. Debattista does not suggest how the problem should be solved.

231 See for instance Chapter 13, Section 57 of the Finnish Maritime Code.

Article 71(2) of the CISG, and which regulates the relations between the carrier and his counterparts under the contract of transport. However, it is expressly provided in the Codes that the right of stoppage cannot be invoked against an indorsee of the bill of lading acting in good faith.[232] Article 71(2) of the CISG is not as specific in this respect.[233]

The reason for placing a rule from the global sale of goods into a maritime context, which seems to be relatively unique in the light of the CISG, is said to be to make it perfectly clear that the possession of a bill of lading with proper indorsement plays no independent role in the relations between the seller and the (original) buyer and an intermediary carrier.[234] The contract of sale would thus take precedence in relation to the carrier´s delivery obligations under the contract of carriage.

The picture is, however, far from clear and obvious. As the CISG is applicable to exports from Finland, Sweden and Norway in the absence of a choice of law clause to the contrary, there is a potential conflict between the two above mentioned statutory provisions of these countries.[235] There are authorities who suggest that the right of stoppage in transit provided by the sales laws shall not affect the rules applied to the carrier´s delivery obligations under the rules applicable to the carriage of the goods or, in any event, that the carrier shall not

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232 According to the *travaux preparatoires* of the Finnish Maritime Code however, no substantive change has been intended with this provision as compared to the Code emanating from the 1930s (HE 62 – 1994 vp at 56).

233 There is, however, a more elaborate provision in the Uniform Law of International Sales, namely its Art 73 (3), which requires the seller to show that the holder of the document of title "knowingly acted to the detriment of the seller". Article 71 of the CISG is said to be derived from the ULIS provision (Bennett in Bianca-Bonnell, p. 516). Since paragraph (3) was deleted, the relationship between the seller and a *bona fide* third party holder of the document of title is not clear. One view held is that the seller cannot claim the goods from such a third party on the basis of the Convention, but might do so under the applicable national law (Jelena Vilus in Dubovnik Lectures on pp. 242-243 referring to T.C.Hartley, The Uniform Law on the International Sale of Goods and the Draft Convention on Contracts for the International Sale of Goods prepared by UNCITRAL, vol II, London 1979, p. 7/3). The rationale of the deletion of paragraph (3) was apparently to eliminate a provision addressed to the carrier. As the CISG should be interpreted while bearing in mind its international character, the idea of national law supplementing it in relevant points should not be a desirable approach.

234 Honka, p. 137.

235 The practical significance of the problem is reduced by the fact that bills of lading are not often used in transportations to and from these countries. Ocean bills of lading may be used only after transshipments following feeder traffic to the main northern European ports due to which the applicable maritime law will be that of the continental European country of transshipment. A bill of lading could still be issued in the Nordic country concerned, which would cause choice of law problems for the period after the transshipment.

If no bill of lading is used, the conflict between the sales law and transport law could become acute, if the seller has given up his right of control by a NODISP clause but wishes to use his right of stoppage. The consignee might have transferred his rights to a third party.

incur any liability against the seller where the carrier chooses to deliver the goods to the holder of the bill of lading.[236]

I believe the inclusion of the said provision in the Maritime Codes is an interesting measure used towards reaching an interaction between two linked legal relationships. However, such an interaction undermines the role of documents of title in international trade, where the delivery of documents constitutes a ´constructive delivery´. The seller using his right of stoppage for unjustified or vexatious reasons could undermine the independence of the documentary transaction.

The seller is normally not able to invoke Article 71 of the CISG in cases where documentary payment methods, in particular confirmed letters of credit, are used. This applies to cases where the buyer´s non-performance relates to the payment of price. Paragraph (3) of said provision adds that a party suspending performance, whether before or after dispatch of the goods, must immediately give notice of the suspension to the other party and must continue with performance if the other party provides adequate assurance of his performance. This duty to give notice extends to cases of stoppage in transit. In Chapter V.5., *ante*, it was noted that the carrier can in practice deliver the goods to a party surrendering the bill of lading, and the seller would have to apply, in such a situation, for a court injunction to stop delivery. Conversely, the obligation to obtain an injunction could theoretically be imposed on the buyer[237] as a holder of the bill of lading, who should try to restrain a carrier from complying with instructions based on the right of stoppage in transit.

It is natural, however, that the arrangement envisaged in the Nordic Maritime Codes would create some practical difficulties. In particular, the carrier finds himself in a difficult position, should the seller decide to use his right of stoppage in transit.[238]

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236 Johnsson in Transfer of Ownership, p. 386, Ramberg, Konossement och köpavtal, in Festskrift till Kurt Grönfors, 1991, p. 364, Tiberg, pp. 548-558; a different view is taken by Grönfors in Sjölagens bestämmelser om godsbefordran on pp. 316-317. See also the case *Supreme Court of Sweden (Nordisk Tekstil Væveri Aktieselskab v. Tedder Käder Aktiebolaget konkursbo), Nytt Juridiskt Arkiv 1985, p. 879*. The Swedish discussion is based partly on the Swedish Maritime Code from the 1930s. The revision done in the 1990s namely did not aim to change the law in this respect (see the Finnish HE (gov.prop.) 62 – 1994 vp. at 56). It should be added that the discussion relates partly to the Nordic Sale of Goods Acts that are influenced by the CISG and apply, in addition to domestic sales, to sales between the Nordic countries. In the Swedish Sales Act, the right of stoppage is bilateral: the buyer who has paid in advance can resort to this right.

237 In addition to the actual buyer, certain other parties such as an indorsee could be mentioned as an interested party.

238 Under American law, the carrier has to undergo an ´interpleader´ procedure to find out who has rights to the goods (Tiberg, p. 550). Under American law (the Pomerene Act and the UCC), the carrier or bailee may insist upon the production of the original negotiable document before acting. In order to maintain the stoppage, a civil action must be initiated in court so that the rights of the parties may be adjudicated (Chandler, III in Transfer of Property, p. 425).

First, costs are incurred as a result of the seller using his right.[239] Second, the law is silent as to what extent the seller must furnish evidence to justify the use of stoppage or if is it sufficient only to give notice to the carrier.[240] In comparison, a court giving an injunction based on the right of stoppage in transit is designed to receive such evidence. If the claim is unjustified, the seller has to indemnify both the buyer and, it is assumed, the carrier. Third, when goods have arrived at their destination, and both stoppage and delivery are claimed, the carrier has to decide which claim to honour. Even the carrier´s possession of the goods at a terminal of the port of discharge may be put in doubt.

The above should suffice to demonstrate the interaction between the CISG and maritime transport law in respect of stoppage in transit. As observed, there are discrepancies between these regimes at the national level. The situation is not any easier in cases where several legal systems are concerned. The law applicable to stoppage in transit (or retention of title) is very often other than that applicable to the contract of transport. Resolving discrepancies in predominant international instruments relating to the contracts of sale and transport would therefore be worth considering.[241]

VIII.9.3 Loading and discharge in two legal relationships

As said, the contract of sale and the contract of transport are separate contracts. These contracts deal predominantly with different matters. However, this is not the case in every respect. The contract of sale frequently contains at least some provisions relating to how the contract of transport is to be concluded. These

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239 In one Swedish case (*NMCases 1992.58; West of Sweden Court of Appeal (Sonja)*), the carrier could not obtain the right to claim additional expenses incurred from the seller. Under English law, however, costs incurred by the carrier for the redelivery are to be borne by the seller (Sale of Goods Act section 46(4)).

240 In the latter case the position of the carrier, in terms of whether or not to follow the instructions of the seller, resembles that of a bank receiving a claim under a demand guarantee.

241 This could mean e.g. adding a provision to transport conventions such as the outcome of the UNCITRAL draft Instrument on Carriage of Goods [wholly or partly][by Sea] admitting such an interpretation of the CISG that its Article 71(2) has certain agreed predominance in relation to obligations based on contracts of transport.

Johansson suggests however (on p. 452) that there is a general understanding that the contract of sale should not affect the contract of transport. Using this assumption, Johansson goes on to develop an approach according to which the use of stoppage in transit should be tied more closely to the right of control. Although this approach is logical and well-presented, it would lead to an increased legal fragmentation of the supply chain, and one can ask whether the separability of the various legal relationships is justified in an environment where the possibility of obtaining information by the parties involved is increasing substantially. The right of stoppage in transit is designed for exceptional situations whereas the right of control is more of an everyday means.

A more logical way in my view would be to build on the good faith requirement for the parties and recognise that the contract of transport in most cases is a contract ancillary to the contract of sale. I am not prepared however to give precise suggestions. In any case, I agree with Johansson in that CISG 71(2) would need clarification. Since it is very difficult to amend the CISG, bodies like the CISG Advisory Council could shed some light on the Article.

provisions are normally part of the stipulations of the trade term referred to by the parties in the contract of sale. In other words, the contract of sale at times defines to some extent what kind of a transport contract has to be concluded by one of the parties.

To give an example, a CIF seller "must contract on usual terms at his own expense for the carriage of goods to the named port of destination by the usual route in a seagoing vessel...".[242] The requirement for ´usual terms´ brings in standard conditions of carriage. These invariably address the division of tasks, liability and costs in relation to loading and discharge. At the same time, the same issue is addressed by the relevant Incoterm referred to in the contract of sale. The parties, between whom the division is made, are of course different. However, the contract of sale may require a division between the seller and the buyer, which cannot be enforced on the carrier by the party concluding the contract of carriage with the carrier. On the other hand, the contract of transport is generally more precise than the contract of sale.

Sometimes the parties, knowing the conditions of carriage, may even agree on the ultimate division of costs in their contract of sale. The term ´CIFFO´ namely contains two relevant elements in this respect: the seller is to pay the main carriage, but instead of the ´usual terms´, a condition is implied that the carrier (and the seller) bears the discharge costs at the ship´s end of discharge. Another possibility is to use conditions of carriage designed to be in conformity with the Incoterms.[243]

VIII.9.4 Conclusions

In order to facilitate the use of electronic trading systems, and to lower the psychological barriers of using electronic instruments, discrepancies between the relevant contracts should be brought to a minimum. After all, many disputes and unnecessary correspondence could be avoided if interaction between the basic legal instruments is secured.

Supply chain management calls for cooperation from all parties concerned so that an effective network can be construed. In a network, a contract of carriage is ancillary to the contract of sale. The liability regime with the nautical exception - coupled with stringent P&I clubs, stresses the separateness of the contract of

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242 CIF INCOTERMS2000 A3(a).

243 In 1996, the Finnish Section of the ICC published Standard Shipping Terms 1996, which were prepared by a working group representing both shippers and shipowners and other interested parties. The working group was chaired by Mr. Asko *Räty*. These terms have both a loading and a discharging component. They are in chronological or logistical order as regards the possible place of delivery to the carrier, or to the consignee at the port of discharge. The terms are the GATE TERM, the WAREHOUSE TERM, the TACKLE TERM and the SHIP TERM (FREE IN). For the Standard Shipping Terms 1996, see Kuusniemi in Honka, pp. 217-268.

The Standard Shipping Terms 1996 led to the ICC Commission on Maritime Transport undertaking a study to determine the feasibility of establishing similar terms at an international level. Such terms would in essence amount to a set of standard liner terms (Guide to Export-Import Basics, 2nd edition, Vital knowledge of trading internationally, ICC Publication No 641, pp. 256-257).

carriage as does the multiple liability regimes for various transport methods. Efforts to promote a simple liability regime for multimodal transport, such as the UNCTAD/ICC Rules for Multimodal Transport Documents or the discussions going on under the auspices of UNCITRAL at the moment, are also useful for supply chain management and holistic business models.

Finally, a holistic approach coupled with the opportunities afforded by electronic commerce invites a reassessment of traditional rules relating to conflicting claims for the goods. A claim for delivery based on good faith possession of a document of title is generally effective against claims based on stoppage in transit or retention of title. Similarly, good faith creates estoppel for the carrier to defend himself by facts recorded in the bill of lading. In an electronic environment, good faith can be eliminated by appropriate recordings in the central registry, where the ´documents´ are situated. If abstraction is maintained (allowing the B/L rules to exist) in such circumstances, it is an intentional decision for market needs.

VIII.10 Transfer and creation of property rights by electronic means of communication

Chapter V.8., *ante*, dealt with the legal harmonisation of rights *in rem* in tangible goods and security interests. This area invites scrutiny into holistic trade law models as well. The use of electronic trading platforms for all-embracing commercial purposes highlights the importance of looking into the question of how property rights and security interests could be created and transferred by electronic means in a manner that third parties could be bound by the transactions as well.

Rights in relation to tangible goods or intangible property such as negotiable instruments may be subject to form requirements. In particular, the creation and especially perfection of security rights often attracts writing requirements.When states implement legislation based on the UNCITRAL Model Law on Electronic Commerce, most of these general problems relating to the basic legal infrastructure will disappear.

Some other problems need be resolved before the establishment of electronic equivalents to paper-based registration systems can take place. There are legal requirements for record-keeping, the adequacy of certification and authentication methods, a possible need for specific legislative authority to operate electronic registration systems, the allocation of liability for erroneous messages, communication failures, and system breakdowns. Moreover, the incorporation of contractual terms calls for attention. Finally, the requirements of privacy (data protection) and, in some cases, confidentiality need to be resolved.[244]

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[244] Transfer of rights in tangible goods and other rights, UNCITRAL Secretariat Note, Doc A/CN.9/WG.IV/WP.90, para 31.

VIII.10.1 Can you create rights in rem contractually?

The question posed in the above subtitle is, as the reader notes, somewhat absurd. This is because a right *in rem* applies, by definition, against the world at large. It gives protection to the person protected by such right in the goods against other creditors interested in the goods. A contractual right applies in principle *inter partes*, and if a party to a contract goes bankrupt, the other party with contractual claims has normally only the status of an unprivileged creditor. However, if the party enjoying contractual rights goes banktrupt, the banktruptcy estate can normally stand in his place.

In many or most jurisdictions exists in principle a *numerus clausus* of rights *in rem*. This means that rights enjoying protection against third parties are limited in number and stipulated generally by law. In Germany, this is the case.[245] In Finland, there are at least two rather opposite views on this.[246] New rights can only be created by way of legislation, which defines directly or indirectly the position of various parties concerned, such as third parties in general. However, where rights *in rem* of a foreign origin enter the picture, courts in a given country have to determine their position in relation to other rights in the goods. Courts may reject foreign rights *in rem* being inconsistent with their legal systems, or may transpose them into their own system and try to find a ´functional equivalent´ among the *numerus clausus* as is the case in Germany. However, should rights *in rem* established under the *lex contractus* be admitted as such, the principle of *numerus clausus* would be broken.[247] Rights not known to the national legal order of the country of jurisdiction could be enforced against third party creditors there. The recent European Insolvency Regulation requires in Article 5 that the ´State of the opening of proceedings´ shall respect foreign rights *in rem*.[248]

Yet the question is legitimate and relevant since, in the absence of any binding and uniform legal framework, electronic commerce in the field of international trade and more notably maritime transport is promoted by way of contractual arrangements such as the *Bolero System*. Such contractual arrangements are recognised in the UNCITRAL draft Instrument for Carriage of Goods [wholly or partly] [by Sea] as rules of procedure which define the rights and obligations of the parties in detail. The question of how such rights could

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245 Wilhelm, para. 242, p. 146; Koulu, Nykyaikaiset kirjaamisjärjestelmät, p. 150.

246 Wirilander, pp. 46-47, considers that numerus clausus does not apply in Finland, because statutory law has dealt with rights *in rem* in an insufficient manner, and there has been an opportunity for such rights to emerge under customary law.

Tepora, on the other hand, considers (in Oikeustiede 1988, p. 284) that there exists a *numerus clausus* in Finnish law. A party cannot create a legal category of rights which would restrict a third party´s rights beyond what the property law rules allow.

247 See Wilhelm, para 303, page 179, referring to Stoll, RabelsZ 32 (1968), 450, 461.

248 The creditors protected e.g. by a mortgage or a lien can satisfy their claims in respect of goods situated in the territory of a Member State of the Union other than that of the State of the opening of the proceedings under the legal rules applicable there. Apparently the nature of rights *in rem* is defined under that other law. The background ideology of the Regulation is the respect of the *lex situs* of the property as well as the legitimate expectations of the rightholders there. For the Insolvency Regulation, see Koulu, Konkurssi Euroopan unionissa, Helsinki 2000.

apply to *ultra partes* relations could be asked as some jurisdictions such as Germany maintain *numerus clausus* of rights *in rem*. The answer is that such recognition should be created by an international legislative instrument.[249]

Proprietary rights in goods under the international sale of goods are, however, also created by issuing documents of title. Under English law, documents of title are created by established commercial custom, which requires a substantial period of time.[250] There is therefore, in fact, a *numerus clausus* in respect of documents of title. The same apparently applies in Germany[251] and in France[252]. However, in the Netherlands parties may designate a commercial document as a document of title quite freely.[253]

Where documents of title are freely established, there is the possibility, in principle, of introducing new rights *in rem*. This is what the UNCITRAL draft Instrument for Carriage of Goods´[wholly or partly][by Sea] should do. So far it only deals with the ´negotiability´ of the document vis-à-vis the carrier, i.e. it tackles only the relationship based on the contract of transport.

An international instrument could give contractual arrangements the capacity of being able to constitute electronic documents of title. Such documents of title should have effects as against third parties, i.e. the world at large. The legal effects of such documents of title could be defined to the extent textbooks define them. There is a statutory definition of a document of title in section 1(4) of the English Factors Act 1889. According to *Todd*[254], however, a document of title within the meaning of that provision does not transfer constructive possession of the goods. Therefore any definition should cover the principal uses of documents of title, including transfer of ownership[255], transfer of indirect (constructive) possession, and its use of pledging the goods effectively. National

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249 The European Insolvency Convention contains in Article 5(3) a provision stating that "(t)he right, recorded in a public register and enforceable against third parties, under which a right in rem within the meaning of paragraph 1 may be obtained, shall be considered a right in rem". It is unclear whether this provision could in some instances cover rights recorded in registries such as the *Bolero Title Registry*. The meaning of the words ´public registry´ should be analysed. Moreover, it is not excluded that in some jurisdictions rights created contractually could be enforced against third parties.

250 Todd, p. 168.

251 Thorn in Transfer of Ownership, p. 190.

252 In the case *Cour de Cassation de France, 1.10.1985, Cooppérative Agricole d´Esternay v. Margarine Verkaufs Union*, ETL 1986.I., pp. 91-101, it was argued that Article 34 of the French constitution providing "la loi determine les principes fondamentaux du régime de la propriètè, des droits réels et des obligations civiles et commerciales" prevented instituting a document of title by a governmental decree. The court did not follow this argumentation. Yet, the principle seems to exist.

253 Zwitser in Transfer of Ownership, p. 253. See Chapter VIII.3.4.1., *ante*.

254 Todd, p. 106, footnote 22.

255 The *Bolero Rulebook* approach could be followed in this respect: the transfer of a document of title passes property in the goods if this is provided for in national law, or it is the intention of the parties to transfer property. The intention may be inferred. For instance, retention of title ceases to have effect when the document of title is transferred against payment or draft (documentary credits and collections). Consequently, title passes through agreement. Where the document of title is transferred before payment is made, the conflict between the original seller retaining title and a *bona fide* new third party buyer has to be resolved. It is a situation similar to one in which the right of stoppage in transit is used. The legislator may consider whether to address this problem.

law would remain determinant as to the ultimate property law effects such as the ranking of the pledgee among the creditors of the owner of the goods. National law could also maintain its own regime of documents of title outside the convention-based regime.

The problem that the transfer of property rights is usually covered by sales legislation such as the English Sale of Goods Act 1979 still remains. Should an international agreement be attainable in the field of transfer of property in general, and as it makes no sense to limit it to electronic transactions only, the agreement could be created through a protocol to the CISG which is presently silent on the issue of the transfer of property. However, where a transport law instrument simply reiterates the practices that already exist in the paper-based world, it could also be created through amending UNCITRAL´s transport law instrument. There are examples of transport law that determine to some extent issues relating to sales law.[256] Such inclusion would be a representative of a ´holistic´ approach to the laws of international sales, transport and finance.[257]

The effects of negotiable transport documents or documents of title would have to be created and maintained through ´rules of procedure´ such as the Bolero Rulebook. There is the problem that electronic bill of lading systems require adherence to the legal and technical particulars of the system. I wonder whether it would be possible to create legal ´interfaces´ between such closed systems and the rest of the world by resorting to rules of conversion from electronic records to paper and *vice versa*. International organisations could try to verify minimum requirements for such trading systems and possibly publish model rules of procedure.

VIII.10.2 How to tackle conflicting rights *in rem*?

In an ideal world, rights affecting tangible goods in the course of an international sale of goods transaction should be harmonised. But, as we know, very little harmonisation exists in this field. The CISG does not regulate the transfer of ownership or other property rights. However, it has been able to introduce the right of stoppage in transit to certain continental jurisdictions, that right being close to property rights, at least in operative terms. I will express some basic observations, with full respect to the complexity of the issue, which has not been examined in full by UNCITRAL as yet.

Since no harmonisation of substantive law is attainable in the foreseeable future, one should perhaps try to tackle the problems through the harmonisation of conflict of laws principles applicable to property and security rights affecting tangible goods in international trade. The scope of application of this law could

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256 The treatment of stoppage in transit in the Nordic Maritime Codes and the Hague-Visby Rules using the concept of ´document of title´ serve as examples. Another example is the US Pomerene Act which governs the relations between the shipper and the consignee.

257 European Community legislative acts have often a tendency of combining different types of elements, the most obvious example being Directive 2000/31/EC on electronic commerce.

govern e.g. priority conflicts.[258] The *lex contractus* would be, in most cases, a more suitable statute than the *lex situs*. This should be the law governing the relations between the parties of the contract of sale, which would also have an effect for third parties. In international trade, parties are free to choose the law that governs the contract. Such a problem may arise that parties would choose a particular law especially to the detriment of creditors. Therefore a system in which mandatory provisions of e.g. the countries where the parties have their seats should be respected.[259]

An international convention could also follow the example of the EC Insolvency Regulation in that foreign rights *in rem* are respected. In trade policy terms, a ´mutual recognition´ of foreign rights *in rem* could be granted to other convention states. In the enforcement of foreign rights, in cases in which this involves a procedural dimension, a full equation would probably not be possible. Where a foreign right in *rem* is alien to the national legal system, it would be perhaps too much to ask countries to apply a ´functional equivalent´ in their legal system, although Germany appears to be doing so already. In many countries, equivalence is simply lacking.

VIII.11 Creating document of title equivalents with book-entries

Under the new system, rights in tangible goods will potentially be created by registration instead of possession of a physical document of title. Therefore it is useful to take a look into the availability of registration systems.

VIII.11.1 Possible types of registries

Chandler[260] distinguishes between three types of registries. A government registry may normally be used for registering transfers of ownership and mortgaging real

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258 United Nations Convention on the Assignment of Receivables in International Trade from 2001 is an international legal instrument containing both substantive, conflict of laws and jurisdictional provisions. The law applicable to priority is the law of the assignor´s location. In addition, the main insolvency proceeding with regard to the assignor will be opened in that jurisdiction. This reconciles to some extent the conflicts between secured transactions and insolvency laws.

259 In the assignment convention, the applicable priority rule may be set aside if its application is manifestly contrary to the public policy of the forum state. This applies in case there are secondary proceedings.

260 George F. Chandler III, Maritime Electronic Commerce for the Twenty-First Century, ETL, 1997, pp. 656-658.

estate.[261] A central registry is one type, where a private group conducts its transactions over a private network accessible only to its members. Banking networks such as SWIFT, networks devoted to stock trading and the *Bolero System* serve as examples of a central registry. A central registry requires considerable staff to enforce system rules and to maintain security, which is a significant cost factor for participants. The costs are borne by the participants of the system on the basis of a membership fee system, although nothing prevents the costs of the system from being levied on a transactional basis. The legal system for central registries is based on rule books (or, as they are called by the UNCITRAL Draft Instrument on Transport law, ´rules of procedure´). These rules establish the allocation of risk for system malfunction and the insurance obligations of the registry and the user.

Finally, a private registry could be conducted over open networks, and the issuer of a document of title (or other person bearing the responsibility for the safe delivery of the property) has the duty to administer the transfer or negotiation process. An example of a private registry is the system based on the CMI Rules on Electronic Bills of Lading, which vests the tasks of the registrar to the carrier as issuer. Liability for delivery to an unentitled party parallels the paper practice. Costs are borne by each user, but these should not be significant since complexity is avoided, and no additional staff should be needed to run the registry.[262]

A central registry system is more secure than a private registry, since it contains no open channels of communication. All trading parties are registered users[263] of a mainframe computer maintained by the central registry, and the parties can access the mainframe from their places of business (in the case of the carrier, from the terminal). All transactions are recorded centrally on the

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261 For a government register "gone electronic", see Matti Ilmari Niemi, Finland´s New Electronic Title and Mortgage Register, in Property Law: Current Issues and Debates, Edited by Paul Jackson and David C. Wilde, Aldershot 1999, pp. 333-344.

See also the Land Registration Reform Act 1990 (Ontario). In the Ontario system, transactions through the automated real estate registration system are governed by a Document Registration Agreement, available to be signed by the parties. This Agreement only deals with the rights and obligations of the parties in respect of the act of registration and not with the rights and obligations of the seller and purchaser under the purchase agreement. Section 9 of the standard Document Registration Agreement gives the purchase contract a priority in case of conflict. There are statutory provisions relating to the content of electronic documentation used in connection with the registration.

262 Ibid.

263 *Todd* (1998, pp. 164-165) describes the the procedure in a central registry system in detail: Each trader, financial institution and carrier has a unique *user-id* (user identity), and a secret password. The carrier could inform the system of the *user-id* of the shipper. However, the shipper has to be a member of the system. The shipper could then use his identity symbol and password to access the system to notify it of the *user-id* of the buyer of the goods as the consignee or holder of an electronic document of title or of the bank acting as pledgee of the goods. Only the current holder has the right to deal with the goods. As the machine would store the data, it could also control access to that data. Access to data can be given to a bank to examine the document well in advance of an actual transfer. For a documentary credit, the bank needs the presentation of documents, including, as the case may be, the delivery of a document of title, which it then holds as a pledge.

mainframe computer. The computer can also store all the details that are typically entered on bills of lading, including cargo descriptions and the terms of the contract of carriage. This is a logistical benefit since the same information needs neither re-keying nor otherwise repeating if reference methods are used.

The disadvantage of the central registry system, in addition to its costs, is its inflexibility. It requires all parties to a transaction to be members of a group. The use of documentary credits is useful particularly when the parties do have little information of and confidence in each other. In becoming members of a group that transacts business electronically based on preset rules of procedure, parties may well be considered more reliable, in which situation the more sophisticated functions of the system, such as those representing an electronic letter of credit, may become futile. A central registry advocated on a commercial basis may, if very successful, reach a very central position in the market. Thereby its rules of procedure might become the ´law´ one day.

VIII.11.2 Creating rights through book-entries – parallels

Electronic systems build on the legal framework of the transfer of rights in tangible goods. If this infrastructure is very complicated, advanced systems do not provide much assistance. Where the law requires physical delivery of goods for the purpose of transferring property or perfecting security interests in such goods, there is a need to amend the laws relating to these functions in order to create binding legal effects.[264] Electronic messaging is namely just a medium of transferring information, unless it has been empowered to perform other tasks.

Where the law provides or allows for the transfer of property rights or for perfecting security interests by symbolic delivery, the replacement of such a symbolic delivery by electronic means is possible by instituting an electronic system. An act, usually a transfer of the physical possession of a document of title, confers to the transferee a means of claiming control of the goods. At the same time, the act creates indirect (constructive) possession of the goods for the transferee or secured creditor. As the Note of the UNCITRAL´s Secretariat suggests, "the law could attribute the same effect to the entry of the transfer agreement into a registry system administered by a trusted third party or to an acknowledgement sent by the party in physical possession of the goods that these are held to the order of the transferee or secured creditor".[265] Thus, equivalent effects could be created by using either a central or open registry system.

Differences exist between registrations based on legislation and those based on contractual arrangements such as the *Bolero Title Registry*. The first are generally valid against third parties, whereas the latter necessarily not.

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264 Transfer of rights in tangible goods and other rights, Doc A/CN.9/WG.IV/WP.90, para. 33.

265 Ibid, para. 34.

Sometimes systems of rights registration start on a contractual basis but turn into statutory systems. In Finland, rights *in rem* relating to housing were first established by contractual arrangements in connection with the RS system[266]. This contractual arrangement was later codified in the Housing Sales Act[267], which made it easier for third parties to gain rights in respect of the property rights in the system. This arrangement, which is based on paper documentation, might provide parallels for the transition to electronic trade documentation. One can note, for instance, that this system is based on the idea of a private registry since one of the banks involved acts as a depository of the documentation.

Dematerialised securities recorded and sold electronically in stock exchanges form an example of a central registry system. Dematerialisation, as portrayed in Chapter II.2.4.3, *ante*, has become a key ingredient of modern trade in securities by settlement systems. The experiences from those systems give points of comparison to bill of lading registries. Both systems are designed to reduce the paperwork, expense and risks associated with physical documents. Stocks represent part of the share capital in a commercial company whereas a bill of lading entitles the holder to claim delivery of goods which are in the custody of the carrier. One may also recall that certain raw materials and commodities are traded in specialised exchanges, which may be gradually electronised.

Electronic warehouse receipts are used in some jurisdictions within the United States.[268] These receipts relate to agricultural commodities such as grain or cotton. They are computer records of the information that is required on a paper-

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266 The system concerns houses under construction and the shares in the company that is established to own and run the house. The shares of this company are sold to the public and give their holder a right to occupy an apartment in the house. Before the system was established in 1972 among Finnish banks, there had been problems such as the double pledging of shares. The system then established a presupposition that one of the banks would act as a depositary of the relevant binding documentation relating to the company and its finances. The depositary also organised the printing of the share certificates, and kept them in custody for the benefit of the owners or secured parties, until the construction had been terminated and these parties, notably the buyers, had met their obligations. The depositary has comprehensive non-documentary responsibilities as well. The system was created by a tri-partite agreement between the founders of the housing company, the company itself and a bank. The system established preliminary security rights (the pledge to secure repayment for the purchase price) for the buyers of an apartment to the shares of the company. The property in the shares was transferred to the buyer of the apartment, once the construction authorities had approved the completion of the construction and the buyer had paid the purchase price. Perhaps the signifance of the early stages of the RS system was that contractual arrangements were created to manage and improve the position of the shares bearing entitlement to apartments under construction. The system functioned on the basis of paper documents, but could also be transformed into an electronic medium.

(Erma, Kärävä & Riihimäki, Pankkitoimen lakiasiat, 9. painos, Jyväskylä 1988, pp. 210-218, Kärävä, Riihimäki & Kärävä, Pankkitoimen ja taloudenpidon lakiasiat, Helsinki 2002. pp. 427-434).

267 Asuntokauppalaki 843/23.9.1994 (Finnish Housing Sales Act) Chapter 2. See also HE (gov.prop.) 14/1994.

268 The system is government regulated and based on legislation. Public warehouses on agricultural commodities typically operate under licences issued by the United States Department of Agriculture under the United States Warehouse Act. Specific regulations governing electronic warehouse receipts are contained in federal legislation (US Code of Federal Regulations § 735). There is a central filing system for electronic warehouse receipts for cotton.

based warehouse receipt. For each receipt, there is a ´holder´ who can transfer the receipt to a subsequent holder. An electronic warehouse receipt may only be issued to replace a paper receipt if the current holder of the warehouse receipt agrees. There are provisions to guarantee the singularity of the receipt.[269]

The Bank for International Settlements conducted, in 1995, a study[270] on issues of cross-border securities settlements. It was found that there are generally two types of legal systems as to the relationship between paper securities and electronic book-entry systems[271].

One system applies the conventional legal framework for securities to book-entry systems by presuming the existence of physical securities. These securities may simply be demobilised and held by the depository, although this may not

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269 Transfer of rights in tangible goods and other rights, Doc A/CN.9/WG.IV/WP.90, paras 61 to 74.

270 Cross-border Securities Settlement (Bank for International Settlements, March 1995).

Note of UNCITRAL Secretariat, Doc A/CN.9/WG.IV/WP.90, paras 56, 57, 59 and 60.

The above study lists certain other problems in connection with cross-border securities settlements. Depository receipts are issued in one country to establish entitlement to a security held in custody in another country. The legal nature of these receipts is not always clear.

Moreover, cross-border securities settlements may involve systemic risks, conflict-of-laws problems, difficulty in establishing finality of delivery and payment and problems related to the participants of the system. For tackling some of these problems within the EU, see Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement finality in payment and securities settlement systems, OJ L 166, 11.6.1998, p. 45. According to that Directive, the law applicable to book entry securities provided as collateral is the law of the jurisdiction where the relevant register, account or centralised deposit system is located.

For the regulation of the governing law at an international level, see the presentation by Phillippe Dupont ´Regulatory Aspects of the draft Hague Convention on the Law Applicable to Certain Rights in Respect of Securities held with an Intermediary´; for the IMF Seminar on Current Developments in Monetary and Financial Law, Washington, D.C., May 7-17, 2002, http://www.imf.org/external/np/leg/sem/2002/cdmfl/eng/index.htm, visited on 25.3.2003. See also Directive 2000/47/EC of the European Parliament and of the Council on financial collateral arrangements, OJ L 168, 27.6.2002, p. 43, which also regulates pledges or charges in support of obligations under financial market transactions. According to Article 9 of that Directive, the law of the country in which the relevant book entry account is maintained shall govern

- the legal nature and proprietary effects of book entry securities collateral;

- the requirements for perfecting a financial collateral arrangement relating to book entry securities collateral and the provision of book entry securities collateral under such an arrangement, and more generally the completion of the steps necessary to render such an arrangement and provision effective against third parties;

- whether a person´s title to or interest in such book entry securities collateral is overridden by or subordinated to a competing title or interest, or a good faith acquisition has occurred;

- the steps required for the realisation of book entry securities collateral following the occurrence of an enforcement event.

In principle, the transfer of property rights or the creation of proprietary rights is left to party autonomy or national law, and only those aspects of a transfer which affect third parties (such as publicity) are made subject to mandatory connecting factors (cf. Wilmowsky, p. 6).

271 Book entry means the record of issuance or transfer of the securities in the depository´s accounts.

necessary. This system relies on a legal fiction to fit book-entry securities into paper-based legal institutions. The law pretends that the securities exist in physical form. Ownership rights and the transfer and pledge of book-entry securities are explained by using terms like ´possession´ and ´delivery´ through the mechanisms of immobilisation or global certificates, in which physical securities are deemed to be deposited and kept in interchangeable (fungible) form.[272]

The other system builds a new legal framework for dematerilised securities that are issued solely in electronic form. Legally, this arrangement may find various forms. The interchangeable nature of the securities may be explicitly recognised in a manner which redefines the investor´s property interest. He may be a co-owner of all the securities of the type he has purchased that are held by the intermediary.[273] The investor can claim his stock property solely on a proportional basis.

Another model makes the investor the debtor of the intermediary. In that case, the deposit of securities becomes analogous to a bank deposit. The investor´s position may be secured with the specific assets held for the investor that serve as collateral for the claim. The investor may also become part of a preferred class of creditors, with a claim that is secured generally by all securities held by the intermediary for customers.[274]

The study made by the Bank for International Settlements identified some points of conflict lying in the way of an effective cross-border settlement system. The involvement of several intermediaries adds new relationships and risks, such as insolvency or fraud. Accounting practices and safekeeping procedures, such as the separation of the investor´s assets from the assets of the depository are often the key to protecting the investor´s interests. Furthermore, the varying legal treatment of dematerialised securities may cause problems since countries relying on a traditional notion of securities being possessed in that context may not recognise foreign dematerialised securities as such. Such securities may simply be interests that are something other than traditional securities.[275] One could draw some parallels to a situation in which two countries do not have equivalent rights *in rem*. In Chapter V, *ante*, certain approaches to that problem were presented.

In another study[276], the redefinition of legal concepts traditionally applied in securities transactions was examined. One redefinition classified investment securities as intangible property instead of being tangible like physical shares. When securities become intangible and are not individualised, rights in them may no longer be regarded as property rights. The introduction of an intermediary between the issuer of the securities and their holder has raised the question as to

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272 Doc A/CN.9/WG.IV/WP.90, para. 56.

273 Investment funds generally operate on this basis.

274 Doc A/CN.9/WG.IV/WP.90,, para. 57.

275 Ibid., para. 59.

276 Conseil National du Crédit et du Titre, Problèmes juridiques liés à la dématerialisation des moyens de paiement et des titres, Paris, Banque de France, 1997, as referred to and summarized in the Note of UNCITRAL Secretariat, Doc A/CN.9/WG.IV/WP.90, para. 58.

whether the book-entry would simply be a means of evidencing the rights of the holder or whether it was constitutive of such rights. Finally, when paper documents are no longer used, the relationship between the investor and the depositary of the certificates may no longer be assimilated with the relationship between a bailor and a bailee.[277]

One can generalise that this kind of redefinition or erosion of property rights has not taken place in the international sale of goods even if electronic equivalents of a document title are used. Electronic bill of lading systems imitate the functions of a paper bill of lading, although the systems use the combination of several message types to replicate those functions. The rights created in a sale of goods transaction are either property rights such as the possession or ownership of the goods, or contractual rights relating directly to the goods, such as the right to claim the goods from the carrier. Moreover, legislation or jurisprudence in many countries (such as the UK and France) has moved in the direction of making it possible for the parties of an international sale transaction to own a unidentified part of a bulk cargo. Therefore, if a ship´s delivery orders, which are often used to claim delivery in respect of such cargoes, were treated as documents of title, their electronic equivalents could indeed transfer title, and not any contractual or *sui generis* right that would emerge in its place. The dematerialisation of international trade documents would not easily change the nature of the rights represented by them, since such dematerialised documents relate to rights in tangible goods, i.e. property or security rights in the traditional sense of the word.

VIII.11.3 The use of a central registry and applicable law

The benefit of a central registry system, containing a documentary credit facility and operating under one selected national law, is that several contractual relationships, for instance, those involved in a documentary credit arrangement, the contract of sale, insurance, and the transportation of goods, could be agreed to be governed by the same law, which is the English law in the *Bolero System*.[278] This possibility is obviously not limited to the use of a central registry, but the use of a central registry adds a useful connecting factor to the legal relationships covered by the registry, which may provide legitimity to the choice of law in some jurisdictions.

Usually, this agreed law should prevail.[279] However, should the national laws to which the transactions relate, contain form requirements as to those transactions, their legitimacy could be jeopardised. The mandatory nature of national transport laws set limits to party autonomy. Rights *in rem*, if it is not

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277 Ibid.

278 This is not presumed by the system, see *supra*.

279 A choice-of-law would have to be be made to the substantive national law of an agreed state, and not to the rules of the private international law of that state.

possible to subject them to *lex contractus*, could be subject to their own law, usually the *lex situs*. An international choice-of-law convention could at least designate this law to add predictability.

In one legal system, there is (hopefully) one comprehensive idea of the principles applicable to a trade transaction with all its dimensions. It is obviously practicable to establish the registry in a jurisdiction which is well-developed in questions of international trade. English law has been confronted with questions relating to international trade for centuries, which has also given rise to the establishment of an affluent legal profession in the City of London.[280] English law is rich in detail providing, usually through case law, solutions to a multitude of questions encountered by the international trading community throughout the years. Yet English law remains somewhat difficult for a continental lawyer, such as the writer of this study. The existence of common law, customary law, equity, statutory law and European law all side by side sounds often incomprehensible. Documents of title established first by common law and, second, by statute, and in way that a uniform system may not have been created, serve as an example.

The best results would be achieved through international harmonisation. International law-making agencies have projects covering the area of property and security rights which are usually considered together with insolvency law. The EU has its Insolvency Regulation. The Hague Conference on Private International Law is considering the feasibility of a new international convention concerning the law applicable to proprietary interests in investment securities held by intermediaries such as custodians, prime brokers and clearing houses.[281] UNCITRAL Working Party VI (Security Interests) is preparing a legislative guide on secured transactions. Finally, the United Nations Convention on the Assignment of Receivables in International Trade from 2001 has provisions on the conflict of laws on priority rules. The idea of harmonising property and security rights is not necessarily so distant. The above instruments constitute useful models and some ideas have crystallised.[282] One can designate the jurisdiction and conflict of laws rules relating to priority and add some substantive provisions.

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280 This status of English law and lawyers is enhanced by the fact that English law may be selected to govern the contract even if there is no legal connection to it. The following observation of Lord Wright (on page 291) in *Vita Foods Products Inc. v. Unus Shipping Co. Ltd. [1939] A.C. 277* is famous:

"connection with English law is not as a matter of principle essential...parties may reasonably desire that the familiar principles of English commercial law would apply".

It is true that a legal system with rich case law adds predictability.

281 See Ali, para. 10.01, page 293, note 1, and the references contained therein. Directive 2000/47/EC of the European Parliament and of the Council on financial collateral arrangements, OJ L 168, 27.6.2002, p. 43, which also regulates pledges or charges in support of obligations under financial market transactions.

282 For instance, there seems to be some understanding that rights represented by documents of title have priority over rights simply recorded (this is the prevailing view in the UNCITRAL legislative guide, and it has been adopted by the EBRD Model Law).

VIII.12 Conclusions

A holistic approach which emphasises the logistic benefits of seeing an international trade transaction as a chain of interrelated transactions and services has been introduced in various models and Internet trading platforms. So far, it has been more a logistic than a legal phenomenon. Work in the technical field towards interoperability and convergence continues in parallel with legal harmonisation. Emphasising harmonisation in each area and interaction between various legal relationships represents a holistic approach in the legal field.

All in all, a coherent substantive legal infrastructure is needed to make Internet trading platforms that serve trade and logistics more useful. Many possibilities exist to further this idea. One can imagine, as an ultimate result of holistic develoment, that one day a single platform could eventually cover all contracts in a transaction. It would facilitate electronic management of sale, transport, insurance, risk mitigation by documentary credit equivalents and interfaces with public authorities. Moreover, it would facilitate electronic recording and the transfer of property, security rights and contractual rights such as the exercise of stoppage in transit and the assignment of contracts. The legal framework would be sufficiently predictable by virtue of conflict of laws rules and harmonisation of substantive law. Various platforms could be interconnected just like telephone operators are today. Even dispute resolution services could be included.

The holistic approach described above is very ambitious and confronts difficulties especially in an economic downturn.[283] Perhaps a long-term perspective would be useful. It took centuries for commercial custom to create the present day commercial instruments, negotiable instruments, bills of lading and documentary credits. On the other hand, developments are faster today. The Internet came into commercial use around ten years ago and now constitutes an integral element of our everyday life.

An understanding of the interaction between trade, transport and finance should be seen as a general ideal to strive for in discussions leading to new international trade instruments.[284] I have some thoughts about how interaction between contracts and instruments governing them could be safeguarded in Chapter X, *post*.

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283 See Kim Christensen, Will the eUCP help electronic trade grow up?, DCI, Vol 9 No 1, Jan-March 2003, pp. 3-4.

284 A good example of a holistic approach on the legislator´s side is the English Law Commission, which has considered it the be important to safeguard interaction with UCP500 when the English Marine Insurance Act 1906 is revised in order to allow for the use of electronic insurance documents to a greater extent than it has done so far.

IX SETTLEMENT OF COMMERCIAL DISPUTES IN THE ´ELECTRONIC AGE´

This chapter is intended to deal expressly with the settlement of letter of credit disputes, including the disputes relating to standby letters of credit and contract guarantees. However, many observations are equally applicable irrespective of the subject-matter of the dispute. Emphasis will lie predominantly on arbitration since there are parallels and connections between the developments and problems in electronic contracting and international commercial arbitration today. Letter of credit arbitration as such is a relatively marginal topic, but is suitable to illustrate how the procedural technicalities contained in arbitration laws and conventions can be applied in an electronic documentary environment.

One of these parallels is the need for adapting form requirements to a new environment. For instance, general contract law addresses questions relating to the formation of contracts in general, whereas arbitration law determines the specific question of whether international conventions accept electronic agreements to arbitrate.

Secondly, the law applicable poses problems for international contracts in general and arbitration in particular since the localisation of the parties, the performance, the dispute or the proceedings may all be problematic.

Thirdly, both general contract law and the law of arbitration are based to a varying degree on the notion of party autonomy. Parties may agree on the terms of their contract and subject it to a particular law, or decide not to subject it to any law at all but to the general principles of law or *lex mercatoria* or, slightly more generally, to ´rules of law´. Arbitration is a method of setting contractual disputes, and is particularly useful when the parties wish to detach or insulate their contractual arrangements from national laws.

Electronic trading platforms which operate in the field of international trade and transport could be regarded as semi-autonomous legal frameworks. In Chapters VI, VII and VIII, *ante*, I have tried to portray the multitude of legal rules applying e.g. to the *Bolero System*, which is the most sophisticated integrated trading platform in operation. The dispute settlement method chosen in the Bolero Rulebook is, however, litigation.

One can ask why a study concerning international trade and transport law contains a chapter on dispute settlement, in particular arbitration. From a logistical viewpoint one answer is obvious. Each standard document form contains a provision relating to dispute settlement. As a rule, international standard contracts contain an arbitration clause. By entering into an agreement evidenced by such a standard contract, in fact two contracts are made, one for sale and one for arbitration. The law should not require two contracts to be concluded separately because form requirements for each contract do not match.

Private dispute settlement methods, including arbitration, are in a constant state of development. The idea of ´procedural logistics´ is not that far-fetched. The speed and costs of arbitration are frequently discussed topics. The next step would be to add the ´logistics´ of dispute settlement to the logistical chain starting from the conclusion and formation of the contract and ending with a succesful delivery and settlement or, in an unfortunate case, with a dispute settlement procedure.

An efficient dispute settlement could be of help in maintaining business relations. When new technology is used to replace traditional trading patterns e.g. by storing electronic records in a central registry, an interest in effective dispute settlement mechanisms may rise also because of the contractual complexities of the systems used. Moreover, the systems are there to replace and store traditional trade documentation. Where a dispute arises out of the role of documentation, concerning inter alia delivery based on a bill of lading registry, or conformity of electronic records presented in accordance with the *eUCP* or other rules applied by the trading platform, an online dispute settlement system connected to the service might prove to be useful.

Finally, and this is by far the most important argument for covering dispute settlement as well, arbitration practice has largely generated the *lex mercatoria* rules that are presented in legal literature. The choice of the substantive legal rules to be applied to a dispute is done on a more liberal basis than is the case with litigation, see *infra*, as well as Chapter X, *post*.

IX.1 Litigation vs. out-of-court dispute settlement

There is a volume of case law on documentary credits. A substantial part of this case law, however, deals with issues not covered by the UCP such as the fraud exception and the use of injunctive relief. Such matters invariably require the intervention of state courts. For instance, although arbitrators may be able to order interim and conservatory measures, the nature of arbitration is mainly

contractual, and arbitrators may not, as a rule, issue post-award attachments or, applying English law terminology, *Mareva* injunctions.[1]

Arbitrations regarding letters of credit exist, but I submit, without making any extensive survey on the cases reported in arbitral practice, that the existence of the Opinions of the ICC Banking Commission could reduce the number of disputes regarding the UCP rules themselves that need be litigated or taken to arbitration. Disputes relating to the underlying transactions may contain elements relating to the accompanying use of documentary credits, demand guarantees or standby letters of credit, although the key subject-matters in dispute normally relates to the performance of the parties in the underlying relationship. Arbitration, in its accelerated forms, might be appropriate for disputes of lesser magnitude concerning inter alia the conformity of documents such as bills of lading, and particular expertise is needed to address these issues.

What makes the case law on documentary credits also interesting is that it can usually be applied equally to commercial and standby credits as well as to guarantees payable on first demand as the basic doctrines applicable to them such as the autonomy of undertaking and the doctrine of strict compliance are virtually identical.

In any case, the benefit of litigation and arbitration to other methods of dispute settlement is that an enforceable award can be obtained using these methods, whereas other methods of dispute settlement such as conciliation[2] or Alternative Dispute Resolution (ADR)[3] are often preferred to maintain good working relationships in business relations.

As stated already in Chapter II.8., issues relating to litigation in electronic commerce are generally not treated in this study outside the question of the admissibility of evidence in electronic form. Some issues relating to the core issues of this study, such as enjoining payments under documentary credits and demand guarantees based on the fraud exception, require the use of national

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1 Ali Yesilirmak, Interim and Conservatory Measures in ICC Arbitral Practice, in ICC International Court of Arbitration Bulletin Vol 11/No. 1 – Spring 2000, p. 33. ICC arbitral practice: the Interim award (1990) in case 6251 on the Mareva injunction (an order restraining the defendant from removing his assets from the jurisdiction) and the final award (1995) in case 7828 on attachment.

2 A practically synonymous expression for conciliation is ´mediation´ (Bühring-Uhle, p. 216). For an international legislative approach on conciliation, see the recent Model Law on International Commercial Conciliation of the United Nations Commission on International Trade Law, United Nations General Assembly Resolution 57/18, 52nd plenary meeting 19 November 2002 (A/RES/57/18, 24 January 2003).

3 ADR is generally understood to refer to any type of procedure that constitutes an alternative to litigation. Within this wide concept, arbitration is one form of ADR. However, questions relating to arbitration have been regulated by legislation and international agreements for almost a century, and international commercial arbitration has established formalistic procedures, whereas ADR and conciliation are still in relatively early stages of development. Therefore, arbitration is not treated as a sub-category of ADR in this study. See also Bühring-Uhle, p. 261, who includes arbitration in ADR in a domestic setting, but excludes it as regards international arbitration.

On ADR, see Bühring-Uhle, pp. 261-363, and ADR International Applications, Special Supplement – ICC International Court of Arbitration Bulletin, ICC Publication No 640E, Paris 2001.

courts. On the other hand, legal matters involving mandatory elements such as those of maritime transport liability can be settled by arbitration. Furthermore, this study follows the trend of emphasising the role of out-of-court procedures. In any case, the treatment of normal civil proceedings and the jurisdiction of national courts would expand the volume of this text further, and I have chosen to leave litigation out.

IX.2 The interpretation of the UCP and the DOCDEX-procedure

Special out-of-court dispute settlement systems regarding documentary credit have been developed. They deserve attention as methods of interpreting uniform rules of international nature. Just like the UCP are unique in that they are a set of autonomous rules of the business community, an independent out-of-court settlement system for documentary credits serves as a showcase for the interpretation of such autonomous rules by the business community itself.

The courts of each jurisdiction may interpret UCP 500 in accordance with their own national law. This may lead to differences in interpretations. The ICC Banking Commission has had a practice of rendering opinions on queries relating to the use of the versions of UCP. The opinions are regularly published. According to the standard disclaimer, however, the replies given to the queries "are not to be construed as being other than solely for the benefit of guidance and there should be no legal imputation associated with the replies offered". Despite this disclaimer, it is convenient and legitimate for the industry to rely on these opinions in order to reach further uniformity in application. The banking commission opinions are designed to give guidance what the standard international banking practice is in a given case. In addition to the UCP, the ICC Banking Commission has rendered opinions on other banking rules of the ICC including the Uniform Rules for Demand Guarantees URDG 458. The queries regarding ISP98 are, however, forwarded to the ´Council for the International Standby Practices´.

The ICC Commission on Banking Technique and Practice examines queries put forward by the banking industry regarding the application of the UCP. Its opinions are published regularly and constitute recommendations on the proper use of the UCP.[4] In 1997, the ICC adopted Rules for Documentary Credit Dispute Resolution Expertise (The DOCDEX Rules). The service is available in connection with disputes relating to documentary credits incorporating the UCP as well as the application of the UCP or of the Uniform Rules for Bank-to-Bank Reimbursement under Documentary Credits (URR 525). DOCDEX is made available by the ICC through its International Centre for Expertise under the

[4] The opinions, in addition to other relevant documentary credit rules and texts are electronically available within the ICC in the DEXPRO service.

auspices of the ICC Commission on Banking Technique and Practice. DOCDEX decisions are taken by three appointed experts after consulting the Technical Adviser of the ICC Banking Commission.

A DOCDEX decision is not an arbitral award and is not, unless otherwise agreed, binding on the parties to the dispute. A binding decision is not enforceable as such, but implies a contractual agreement to be bound by the end result of the dispute settlement procedure.

A Panel of Experts is also available for Incoterms queries. Guidance is an efficient method for avoiding unnecessary conflicts relating to international trade law instruments. At the end of Chapter VII, *ante*, I raised the issue of amending the ICC rules by a provision similar to Article 7(2) of the, CISG which would refer to the internationality of the instrument in question, an that this should be taken into account in its interpretation.

IX.3 Letter of credit arbitration

Arbitration has many advantages as compared to litigation. An arbitral award can usually be rendered in a shorter time-scale than a court judgement, which may be delayed by appeal procedures. Arbitrators are normally familiar with business matters and more expertise can therefore be required of and expected from them. Moreover, letter of credit disputes are international in character, and it may be useful to conduct the proceedings in English or other international languages. Finally, letters of credit are used internationally and more often than not in connection with business partners in countries, where only arbitral awards but not court judgements can be enforced.

On the other hand, arbitration is, in principle, more expensive than litigation since the arbitrator(s)are entitled to a fee.[5] If the amount in dispute is relatively small the costs may become disproportionate to the size of the dispute. Even in such a case, an arbitration clause in the credit could act as a "deterrent".[6]

Arbitration is often divided into institutional and *ad hoc* arbitration. The difference is that in institutional arbitration the procedure follows the established rules of a particular arbitral institution[7]. Moreover, the institution normally has a role to play in the appointment of arbitrators. Many model or standard form

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5 Various arbitral institutions provide guidance as to the arbitrators´ fees charged in arbitrations conducted pursuant to their rules.

6 As put forward by William W. Park in the Foreword (p. ix) of the work of Christian, Bühring-Uhle, Arbitration and Mediation in International Business, The Hague 1996, "Arbitration exercises an *in terrorem* effect as a back-up when the parties are unable to reach an agreement".

7 Such as the ICC Court of International Arbitration, the London Court of International Arbitration, the American Arbitration Association, The Arbitration Institute of the Stockholm Chamber of the Commerce, or the Board of Arbitration of the Central Chamber of Commerce of Finland.

contracts refer the differences arising out of the contract to institutional arbitration. In *ad hoc* arbitration, parties may agree to the procedural rules to be applied, in the absence of which the procedural rules will, as a rule, be determined by the procedural law of the place of arbitration. Thus the arbitration statute (if any) of the place of arbitration applies.[8] A special case classified normally as *ad hoc* arbitration is arbitration under the UNCITRAL Arbitration Rules. Many arbitral institutions have accepted the role of acting as appointing authorities provided for in those Rules. UCP500 does not contain an arbitration clause.[9] There is only a note after the last article (Article 49) in the booklet, drawing the attention of the contracting parties wishing to use ICC Arbitration to the fact that they should agree on arbitration in a contract, or, in the event no single contract document exists, in the exchange of correspondence between them to comply with the requirement of a written agreement to arbitrate laid down in Article II(2) of the New York Convention.[10]

A letter of credit, in its more complex form (not to talk about negotiable or transferable credits), involves four contractual relationships, including the underlying contract. In all these relationships, there has to be a separate agreement to arbitrate, which could be, it is submitted, implicit between the issuing and the advising or confirming banks. Moreover, the relationship between the beneficiary presenting the documents and the issuing or confirming bank, as the case may be, receiving and examining them is not a contractual relationship in a strict sense. Therefore it is difficult see how a dispute between the beneficiary and the confirming bank concerning, for instance, the legitimacy of the rejection of documents could be examined by arbitrators without an express agreement to arbitrate entered into after the dispute has arisen. Special care must be taken in drafting an arbitration clause for a letter of credit, since the dispute may implicate more than two parties. For example, if a controversy involves an applicant or beneficiary, as well as the issuing and confirming banks, the arbitration clause should provide for consolidation of all claims before a single arbitral tribunal.[11]

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8 Harmony is sought in international arbitration by the UNCITRAL Model Law on International Arbitration.

9 For comparison, URDG 458 has a jurisdiction clause in favour of a competent court of the country of the place of business of the guarantor or the instructing party, whereas URCB 524 provides for ICC Arbitration. URC 522, however, is in line with UCP500 in this respect. ISP98 does not have an arbitration clause as such either. In its Preface it mentions expressly two arbitral regimes, the ICLOCA and the ICC. As the ISP98 was originally created by the Institute of International Banking Law and Practice, Inc. in the United States, which maintains under its auspices the International Centre of Letter of Credit Arbitration, a slight emphasis in favour of the latter regime can perhaps be observed.

10 The Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York 1958) has been ratified, as of 16 April 2004, by 134 countries. It provides, in Article II(1) that "Each Contracting State shall recognize an agreement in writing under which the parties undertake to submit to arbitration all or any differences which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not, concerning a subject matter capable of settlement by arbitration". (emphasis added)

11 William W. Park, Making Sense of Financial Arbitration, Arbitration, Finance and Insurance – Special Supplement 2000, ICC International Court of Arbitration Bulletin, p. 11.

Another word of caution is necessary here. By submitting an undertaking by a bank to pay against stipulated documents to a lengthy and costly procedure, the outcome of which is unclear, the value of the credit as security for the seller might be reduced. The same applies as regards the value of the contract guarantee for the buyer if dispute settlement can easily be invoked. The autonomy of the bank's undertaking could be seen to be in jeopardy.

As appears from the reports relating to the development of trade credits in the 1990s, the whole idea of the traditional documentary credit was sometimes challenged in exchange for a ´new animal´ product. Encouraged by the non-conformism of some of those reformists, one could continue the ´brainstorming´ and suggest investigating the launch of new electronic dispute settlement methods for documentary credit or contract guarantee disputes, this without continually bearing in mind the need for preserving the absolute autonomy of the credit or guarantee, as the need to resort to arbitration makes the credit or guarantee conditional or accessory in principle. The availability of an effective dispute settlement could partially replace the need for the autonomy and abstraction of the bank´s undertaking. Particularly cases in which the good faith of the parties is put into question, such as that involving the fraud exception, could benefit from an instant dispute settlement procedure that would not necessarily have to go to the merist beyond a *prima facie* hearing. I agree, however, with those critics who say that the business community, in particular the beneficiaries, would not welcome such a product wholeheartedly. Nevertheless, I shall elaborate on this issue somewhat below.

IX.4 Settlement of documentary credit disputes through electronic means

Electronic dispute settlement systems could be useful methods to settle disputes relating to documentary credits and contract guarantees since gains could be achieved both in terms of the length and costs of the proceedings.

IX.4.1 L/C disputes possibly amenable to online settlement

Electronic credit disputes could often be ´documentary´ rather than contractual by their nature. The confirming (or issuing) bank is obliged to pay upon presentation of electronic records which appear on their face to be in conformity with the terms of the credit. In ´pure´ documentary credit disputes, the verification, interpretation and evaluation of the content of documents would be the essence of the proceedings. Written procedures would therefore be appropriate for these kinds of disputes in general. It is also natural that electronic communications would be used to transmit the electronic documentation forming the subject-matter or evidence of the dispute.

A fast-track[12] dispute settlement procedure for pure documentary problems could still be costly in relation to the amount in dispute, but this factor could be compensated for by reduced fees in a vast majority of electronic presentations. The reduction of fees could be achieved through automated examination of presented records, and the existence of an effective dispute settlement system could boost confidence in such systems.

Another imaginable use for online dispute settlement systems would be to detect an abuse of the system. Writing this, I am fully aware that the ICC´s first rules for contract guarantees (URCG 325) were a failure because they were not designed primarily for the pure on first demand guarantees which the beneficiaries required.

Still, one should recall that the approach adopted by the UN Convention for Independent Guarantees and Stand-By Letters of Credit is an objective evaluation of circumstances that may call for the use of a fraud exception for not honouring a demand for the guarantee sum or presentation of documents under a commercial letter of credit. Under the Convention, the bank concerned has in some cases discretion whether to pay or not.

An external dispute settlement body acting on a fast-track basis could be used to evaluate the existence of the criteria established by the Convention in a given case. However, even if restricted to clear abuse cases, this kind of examination would inevitably undermine the independence of documentary credits and demand guarantees. The reason is that the main contract would fall under scrutiny to some extent. Such scrutiny would not, however, go to the very root of the matter due to which the costs and length of the proceedings could be maintained at a moderate level, all this preserving the independence of the credit or guarantee to some extent.

One can ask whether such a procedure would be effective. Arbitrators would namely not have the same arsenal of procedural and interim measures as a state court would. However, if the bank´s duty to pay were subjected to a dispute settlement agreed initially upon between all parties concerned, the procedure would be far less cumbersome than resorting to state courts. Secondly, the Convention could be incorporated into the terms of the credit or guarantee already before having been implemented in the national legislation of the relevant country.

Electronic dispute settlement, possibly online arbitration service, could also form part of an electronic trading platform such as the *Bolero System*. In its present form, no dispute settlement mechanism has been added to the service.[13] On the

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12 For fast-track arbitration developed under the auspices of the ICC, see Improving International Arbitration, The need for speed and trust, Liber Amicorum Michel Gaudet, ICC Publication No. 598, Paris 1998.

The Arbitration Institute of the Stockholm Chamber of Commerce has adopted special ´Rules for Expedited Arbitrations´ (latest version in force as from 1 April 1999).

13 For disputes arising out of the Rulebook, there is a jurisdiction clause for English courts. TEDI Interchange Agreement contains a jurisdiction clause as well – for Japanese courts.

contrary, some electronic trading platforms designed for consumers, such as *eBay,* provide an online dispute settlement mechanism. Where the dispute relates to electronic documentation stored in the system and to its functions, online dispute settlement systems could add value to electronic trading platforms. A dispute settlement system could be resorted to in a case where conflicting claims were presented in respect of the goods, especially when the platform would, one day, be equipped to record property and security rights.

With these special observations regarding documentary credits and contract guarantees, I would like to turn to the procedural issues of online dispute settlement, in particular online arbitration.

IX.4.2 Online dispute settlement systems in general

The possibility of using speeded-up procedures in electronic form to settle commercial disputes has been a much discussed topic not only in the business community and among lawyers, but even among legislators. This has involved both out-of-court dispute settlement and, to some extent, traditional court procedures, especially documentary summary proceedings such as debt collection.

The EC Directive´s call for the Member States to allow alternative dispute settlement systems for online disputes is worth noting. Article 17 of Directive 2000/31/EC on electronic commerce calls for Member States to ensure that their legislation does not hamper the use of out-of-court dispute settlement schemes, available under national law, including appropriate electronic means. Recital 52, in turn, invites Member States to examine the need to provide access to judicial procedures by appropriate electronic means.[14] An example of such an examination could be the UK Lord Chancellor´s Department Consultation Paper "Resolving and Avoiding Disputes in the Information Age" already drawn up in 1998.[15]

Online out-of-court dispute settlement systems have existed for almost a decade now. Some notable early projects include the World Intellectual Property Organisation (WIPO) Domain Name Dispute Resolution Process[16], the Virtual Magistrate Project[17] of the Illinois Institute of Technology, and the

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14 In Finland, the law relating to the use of electronic communications and automated data processing in courts entered into force on 1 December 1993 (Laki sähköisen viestinnän ja automaattisen tietojenkäsittelyn käyttämisestä yleisissä tuomioistuimissa (594/93).

15 see http://www.open.gov.uk/lcd/consult/itstrat/civcon.html, visited on 27.4.2002.

16 see http://www.arbiter.wipo.int/domain_name/index.html, visited on 27.9.2001.

17 see http://www.vmag.org, visited on 25.3.2003.

"Cybertribunal" of the University of Montreal.[18] Today, there are dozens of online dispute settlement systems around the world.[19]

Many online dispute settlement systems are designed for settling consumer disputes and may be expected to provide fast and cheap alternatives to litigation. These systems represent mainly ´alternative dispute resolution´ (ADR) as opposed to arbitration.[20] Online dispute resolution, with or without arbitration, is regularly referred to as ODR.[21] Mediators and arbitrators are called ´third party neutrals´, and one suggestion describes technology as a ´fourth party´, something that influences the process of communication and negotiation and adds value to the third party roles of mediators and arbitrators. This fourth party need not replace the third party, but can do so, in the sense that the third party will increasingly be working solely with an electronic ally or assistant.[22]

The European Union has actively promoted ADR techniques for consumer disputes.[23] This study refrains from addressing either consumer issues, or ADR in general as being a more consensual dispute settlement technique, although the ICC ´DOCDEX´ procedure referred to *supra* could, of course, be regarded as a special form of ADR.

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18 Centre de recherche en droit public, Faculté de droit, Université de Montreal, see http://www.cybertribunal.org, visited on 17.9.2001; this early service appears to have been terminated.

19 A list of these systems can be found at http://www.ombuds.org/center/onlineadr.html, visited on 20.3.2004. In Europe, the federation of the continent´s chambers of commerce - ´Eurochambers´ - is maintaining a service, which can be found at http://www.onlineconfidence.org, visited on 20.3.2004. In the United States, one could name http://www.cybersettle.com, visited on 25.3.2004.; and in Asia http://www.disputemanager.com, visited on 25.3.2003. Users enter the services with user ID´s and passwords and pay the for service with their credit cards. The ´mediator´ can be a physical person or just software (Marjut Reivilä: Välimies voi olla verkossa (arbitrator can be in the net, KauppalehtiExtra, Informaatiotekniikka, p.31).

20 Traditional arbitration with adversarial and formal procedures is ill-suited to consumer disputes, since the costs may in most cases exceed the amount in dispute. Moreover, consumer legislation (e.g. the Finnish Consumer Protection Act 1978/38, Chapter 12 Article 1d) may require that the agreement to arbitrate is concluded only after the dispute has arisen. In most European jurisdictions, an arbitration clause contained in standard contract terms and binding the consumer to submit a dispute to arbitration is likely to be regarded as unfair. In the United States, by contrast, consumer arbitration clauses are usually enforceable. (E-Commerce and Development Report 2003, p. 179).

21 For ODR, see UNCTAD E-Commerce and Development Report 2003 Chapter 7, pp. 177 ff. and Tapio Puurunen, Resolving International Business-to-Consumer Electronic Commerce Disputes through ODR – Caveats to Privatizing Justice (to be published in a dissertation shortly).

22 E-Commerce and Development Report 2003, p. 188, referring to Katsh, E. and Rifkin J., Online Dispute Resolution: Resolving Conflicts in Cyberspace, San Francisco 2001.

23 See Commission Recommendation 257/98/EC of 30 March 1998 on the principles applicable to the bodies responsible for out-of-court dispute settlement, OJ L 115, 17.4.1998, p. 31; Commission Recommendation of 4 April on the principles for out-of-court bodies involved in the consensual resolution of consumer disputes, OJ L 109, 19.4.2001, p. 56; as well as Communication from the Commission on widening consumer access to alternative dispute resolution, of 4 April 2001, COM (2001) 161 final; and Green Paper on Alternative Dispute Resolution in Civil and Commercial Law COM(2002) 196 final of 19 April 2002.

IX.4.3 Focus on online arbitration

In contrast, this study will examine the use of electronic records and working methods in arbitration, as these questions are predominantly formalistic issues subject to parallels or similarities with the law of electronic contracting. Online arbitration services are emerging, although their use may still be fairly limited due to the much greater magnitude of amounts in dispute in business relations than in consumer relations, and because some legal questions may still remain open. For example, the American Arbitration Association (AAA) has already had an online arbitration system in operation for some years.[24]

Arbitration could more easily be adapted to electronic procedures than court litigation, due to the opportunities afforded by fast evolving rules of arbitral institutions and the possibility for the parties to agree on procedural rules. Electronic or online dispute settlement in the form of arbitration raises, however, some legal questions, answers to which are sought in the rules of arbitral institutions and under UNCITRAL auspices.

As the use of arbitration can be regarded as another dimension of party autonomy, parties involved in a commercial dispute may choose the procedure under which the dispute will be settled. Parties may refer to the rules of a particular arbitral institution, they may refer to arbitration in general, or they may provide detailed rules on how the proceeding will be conducted. This agreement can also be concluded after the dispute has arisen.

More often, however, an agreement to arbitrate is contained in the general commercial contract. Standard form contracts used in international trade almost invariably contain an arbitration clause. The general contract thus contains a provision which constitutes an independent agreement subject, in principle, to a separate legal regime. The autonomy or severability of the arbitration clause is the conceptual cornerstone of international arbitration.[25]

Even if the contract as such were invalid, the arbitrator would not be deprived of his jurisdiction, which is conferred by a clause deemed to be autonomous or separable, to decide the issue of invalidity and its consequences. The determination of the validity of the arbitration agreement is one of the first measures to be taken by arbitrators. In an electronic commerce context, the problem lies with the form requirements imposed by the legal regime applicable to the online agreement to arbitrate.

Another issue is the actual procedure. Although parties are in principle free to agree on the procedure, they regularly opt for the rules of arbitral institutions. These rules, together with legislation based on international agreements and models, normally determine the scope of electronic proceedings as well.

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[24] See http://www.adr.org, visited on 29.4.2002. The ICC is mentioned to be investigating the issue at the moment, see E-Commerce and Development Report 2003, p. 181.

[25] Craig, Park & Paulsson § 5.04. The autonomy principle is a substantive matter whereas the jurisdiction of the arbitrators to decide whether the dispute falls within the scope of the arbitration agreement (the so called *compétence-compétence* or, if one prefers German, *Kompetenz-Kompetenz*) is a procedural issue. For the acceptance of the autonomy principle and it relationship with the *compétence-compétence*, see *op.cit.*, note 16.

Finally, as the benefit of arbitration is an award that is recognised and can be enforced practically throughout the commercial world on the basis of the New York Convention on the Recognition and Enforcement of Arbitral Awards of 1958, it is opportune to examine, if form requirements for arbitral awards that would hamper electronic procedures exist.

IX.5 Towards ´electronic arbitration´

As explained above, the notion of ´electronic arbitration´, or other form of electronic dispute settlement, is of course inaccurate and useless as such without going into details of such procedure where the devil is said to lie. Attention is paid therefore to the questions relating to arbitration agreements, the place of online arbitation and applicable law, the conduct of arbitral proceedings using the Internet as well as the possibilities of rendering arbitral awards electronically.[26]

IX.5.1 Electronic commerce and arbitration agreements

The principal question under discussion at the moment is whether arbitration clauses in online contracts satisfy the writing requirement of the New York Convention (NYC).[27] It may be recalled that Article II(2) of the NYC allows for an arbitration agreement to be formed by the exchange of telegrams. The

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[26] See also the presentations of Andrés Moncayo von Hase, ´Arbitration and e-commerce related disputes: legal barriers and challenges´ and of Maurice Schellekens, ´Arbitration boards and e-commerce´ in International Colloquium, Internet law: European and international approaches, 19-20 November 2001, Paris, http://droit-internet-2001.univ-paris1.fr/ve/, visited on 9.3.2003.

[27] Confusingly, provisions relating to arbitration may be found in sectoral international conventions as well. For instance, Article 22 paragraph 1 of the United Nations Convention on the Carriage of Goods by Sea, 1978 (the Hamburg Rules) states that "... parties may provide by agreement evidenced in writing that any dispute that may arise relating to carriage of goods under (the) Convention shall be referred to arbitration". (emphasis added) It would be desirable that such independent formulations in sector-specific conventions are avoided.

The Hamburg Rules give the parties the right to agree on the place of arbitration and provide a number of places where arbitration proceedings should be instituted. These are the place where the plaintiff has his principal place of business, or, in the absence thereof, where the defendant has his habitual residence, where the contract of carriage was made provided that the defendant has there a place of business, branch or agency through which the contract was made, and where the port of loading or the port of discharge is situated. Arbitrators shall apply the Convention as substantive law. The Hamburg Rules rules are silent about procedural rules. It is submitted that general procedural rules apply, i.e. *lex fori* of the place of arbitration.

Although the Hamburg Rules are not widely applied, the Nordic Maritime Codes, for instance, contain provisions emanating from those Rules. These provisions include generally speaking the rules relating to arbitration.

The Hamburg Rules were agreed approximately during the same period as the UNCITRAL Arbitration Rules and the Model Law on Arbitration. As the fundamental procedural rules come from the applicable procedural law, that law will eventually determine the possibilities for a delocalised arbitration.

UNCITRAL Model Law on International Commercial Arbitration, which is the foundation of a notable number of modern national arbitration laws[28], has extended this to the exchange of telexes or other means of telecommunications which provide a record. One of the more recent arbitration statutes, the English Arbitration Act of 1996, has replaced the words "in writing" by the words "recorded by any means".[29] Moreover, jurisprudence has extended Art II(2) of the NYC to telex, and there is support for including facsimile in the means allowed by Article II(2) of the NYC as well.[30]

Although my intention is to concentrate on arbitration, it is still relevant to compare the requirements for an arbitration clause to those of choice of jurisdiction clauses. The most citable requirement for jurisdiction clauses is contained in Article 17 of the EC Regulation on Jurisdiction and Recognition and

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28 UNCITRAL Model Law on International Arbitration, as adopted by the United Nations Commission on International Trade Law on 21 June 1985, United Nations document A/40/17, Annex I.

Legislation based on the UNCITRAL Model Law on International Commercial Arbitration has been enacted in Australia, Bahrain, Belarus, Bermuda, Bulgaria, Canada, Croatia, Cyprus, Egypt, Germany, Greece, Guatemala, Hong Kong Special Administrative Region of China, Hungary, India, the Islamic Republic of Iran, Ireland, Kenya, Lithuania, Macau Special Administrative Region of China, Madagascar, Malta, Mexico, New Zealand, Nigeria, Oman, Peru, the Republic of Korea, the Russian Federation, Singapore, Sri Lanka, Tunisia, Ukraine, Scotland (within the United Kingdom), some States (California, Connecticut, Oregon and Texas) within the United States and Zimbabwe. (see the UNCITRAL Web-site http://www.uncitral.org/english/status/statues-e.htm, the latest update 16 March 2004). Moreover, many modern arbitration laws, such as the Finnish, Swedish and English Arbitration Acts have been significantly influenced by the Model Law.

Before adopting the Model Law, UNCITRAL had already developed its own Arbitration Rules, see Arbitration Rules of the United Nations Commission on International Trade Law, Resolution 31/98 adopted by the 31st United Nations General Assembly on 15 December 1976. For the UNCITRAL Arbitration Rules, see Matti Pellonpää and David D. Caron, The Uncitral Arbitration Rules as Interpreted and Applied, Selected Problems in Light of the Practice of the Iran-United States Claims Tribunal, Helsinki 1994.

29 The Finnish Arbitration Act (697/92) of 1992 requires (in § 3) an arbitration agreement to be concluded in writing. However, the requirement is to be construed broadly. An agreement to arbitrate is also considered to be made in writing when the parties have by exchange of telegrams, telexes or other documents produced by similar means determined that the dispute shall be settled by arbitrators. Gustaf *Möller* considers that this requirement is always fulfilled when there is an exchange of communications which are in writing. This would include telefax, EDI as well as other modern technology. A relevant issue is that the methods used produce a record (see Gustaf Möller, Om formkravet vid skiljeavtal, Tidskrift utgiven av Juridiska föreningen i Finland 1994, pp. 221-236). Möller does not mention e-mail, but it follows in my view from his argumentation that an arbitration agreement concluded through an exchange of e-mail messages suffices to meet the requirement of the Act.

The Swedish Arbitration Act 1999 does not contain form requirements as to an agreement to arbitrate (see Section 1 of the Act). Section 48 contains rules as to the law applicable to the arbitration agreement in case it has an international connection. In such a case, the agreement shall be governed by the law agreed upon by the parties. Where no such agreement exists, the agreement shall be governed by the law of the country in which, by virtue of the agreement, the proceedings have taken place or shall take place.

30 Richard Hill, New paths for dispute resolution in Improving International Arbitration, The need for speed and trust, Liber Amicorum Michel Gaudet, ICC Publication No 598, p. 65 and the references included therein.

Enforcement of Judgement in Civil and Commercial Matters.[31] That provision stipulates that an agreement conferring jurisdiction to the courts of a state (subject to the Regulation) shall be "either in writing or evidenced in writing; or in a form which accords with the practices which the parties have established between themselves; or in international trade or commerce, in a form which accords with a usage which the parties are or ought to have been aware and which in such trade is widely known to, and observed by, parties to contracts of the type involved in the particular trade or commerce concerned".[32] As one can note, a choice-of-court clause, at least in the EU context, is subject to slightly less stringent form requirements than arbitration agreements.

The most imaginable means of concluding a contract electronically, which includes an arbitration agreement, are probably the exchange of e-mail messages for the acceptance of an offer which is contained on an Internet site and which refers to such terms and conditions that include an arbitration clause. As for e-mail messages, these are capable of producing information that will satisfy the rules of legal evidence in Anglo-American law provided that e-mail systems are properly implemented and operated.[33] As regards the requirements laid down by the NYC, a comparison between the operational qualities of e-mail messages and telegrams could be made to equate these two means of communication, and the same goes for accepting an offer on the Internet.[34] Richard *Hill* considers that if

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31 Council Regulation (EC) No 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgements in civil and commercial matters, OJ L 12, 16.1.2001, p. 1. This Regulation applies within the European Union, but likewise in the Lugano Convention states, i.e. Norway, Iceland and Switzerland.

No similar rules on the recognition and enforcement of judgements exist so far at the international level. However, the Brussels Convention of 1968 establishing the solutions of Regulation 2001/44/EC has given inspiration to the Hague Conference of Private International Law for its draft Convention on Jurisdiction and Foreign Judgements in Civil and Commercial Proceedings, adopted by the Special Commission on 30 October 1999, available online at http://www.hcch.net/f/conventions/draft36f.html, visited on 1.4.2004. On the impact of the Internet on the recognition and enforcement of foreign judgements, see Féral-Schul, Christiane, ´The Implementation of Court Rulings´ at the International Colloquium, Internet law: European and international approaches, 19-20 November 2001, Paris, http://droit-internet-2001.univ-paris1.fr/ve/, visited on 9.3.2003.

32 The Bolero Feasibility Study 1999 assumes that the jurisdiction clause contained in the Bolero Rulebook agreed upon is valid. Indeed, it is in ´writing´, and Member States of the Union have implemented Directive 2000/31/EC on Electronic Commerce which obliges the Member States to authorise contracting by electronic means.

33 Hill in Liber Amicorum to Michel Gaudet, p. 65.

34 Ibid., According to Hill in the cited writing, the important differences between e-mail and telegrams are:

- it is relatively easy to forge an e-mail while the telegraph office (a third party) is able to verify the identity of the sender should this be requested;

- e-mails transmitted over the Internet are not inherently protected against inadvertent or deliberate changes, while it is practically impossible to change a telegram during its transmission; and

- e-mails may fail to be delivered whilst telegram companies can be assumed to deliver the telegram with a very high degree of certainty.

These problems can, however, be mitigated through the use of encryption or suitable business practices such as the actual verification of the message and its sender.

See also Hill´s analysis of telegrams, telex, telefax and e-mail at transmission and reception in Chapter IV.4.1., note 31, *ante*.

the seller´s offer in the Web contained an arbitration clause, then an arbitration agreement would be validly formed in accordance with Article II(2) of the NYC, provided that the portion of the offer containing the 'submit', 'transmit', 'accept' or similar function clearly and conspicuously referred to the existence of an arbitration clause among other terms and conditions. Should a clear and conspicuous reference be missing, this could lead to objections on the basis of the lack of informed consent from the buyer. Although jurisprudence might be turning towards a wide interpretation of the writing requirement provisions of the New York Convention and the Model Law, UNCITRAL has seen the need to to start revision with a view to effecting the necessary changes in the text, or at least to provide interpretative guidance for those who apply the relevant provisions. The UNCITRAL Working Group II (Arbitration and Conciliation) has been preparing uniform provisions on the written form for arbitration agreements to provide clearer rules on when a written agreement to arbitrate exists between the parties and to provide a more flexibile interpretation of the strict form requirement contained in the New York Convention, so as not to frustrate the expectations of the parties when they have agreed to arbitrate.[35] This could be done through a model legislative provision[36] revising Article 7(2) of the UNCITRAL Model Law on International Commercial Arbitration and an interpretative instrument[37] regarding Article II(2) of the New York Convention.

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35 Doc A/CN.9/WG.II/WP.118.

36 The Secretariat draft model legislative provision revising Article 7 of the Model Law for the basis of discussions in the Working Group (in Doc A/CN.9/WG.II/WP.118) is the following (the square brackets belonging to the draft):

"Article 7. Definition and form of arbitration agreement

"Arbitration agreement" is an agreement by the parties to submit to arbitration all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not. An arbitration agreement may be in the form of an arbitration clause in a contract in the form of a separate agreement.

The arbitration agreement shall be in writing. "Writing" includes any form that provides a [tangible] record of the agreement or is [otherwise] accessible as a data message so as to be usable for subsequent reference.

["Data message" means information generated, sent, received or stored by electronic, optical or similar means including, but not limited to, electronic data interchange (EDI), electronic mail, telegram, telex or telecopy.]

For the avoidance of doubt, the writing requirement in paragraph (2) is met if the arbitration clause or arbitration terms and conditions or any arbitration rules referred to by the arbitration agreement are in writing, notwithstanding that the contract or the separate arbitration agreement has been concluded orally, by conduct or by other means not in writing.

Furthermore, an arbitration agreement is in writing if it is contained in an exchange of statements of claim and defence in which the existence of an agreement is alleged by one party and not denied by the other.

The reference in a contract to a text containing an arbitration clause constitutes an arbitration agreement provided that the reference is such as to make that clause part of the contract.

[For the purposes of article 35, the written arbitration terms and conditions, together with any writing incorporating the reference or containing those terms and conditions, constitute the arbitration agreement.]

37 The instrument would refer to the text of Article 7 of the Model Law to be revised, and the notion ´agreement in writing´ contained in Article II(2) of the NYC should be interpreted to include the means provided for in that revised text.

The UNCITRAL Working Group has had doubts about the legal form in which the change should be effected.[38] In any event, notwithstanding the means how the changes will be introduced, there seems to be an agreement in the Working Party on the need to clarify the texts and safeguard a more liberal interpretation of the writing requirement for the arbitration agreement.

Attention has been paid above to the interpretation of international instruments addressing form requirements imposed on agreements to arbitrate. As has been noted, national laws substantially differ in this respect. The question then arises of which law determines the form requirements to be imposed on arbitration agreements. There is a relatively well-settled principle according to which the question of the law applicable to an arbitration agreement is independent of the law applicable to the merits. This follows from the principle of the autonomy of the arbitration agreement. Parties may expressly provide for the law applicable to the arbitration agreement. In the absence of such provision, an arbitrator or arbitrators will have to define the rules as to the form of the agreement. These rules may be based on a particular national law but may also be based on international instruments and commercial custom.[39] It is uncertain whether national courts would accept a UNCITRAL interpretative instrument regarding the form requirements imposed by the New York Convention, where challenges were made concerning the use of electronic communication methods. For arbitrators themselves, however, an interpretative instrument could, however, prove to be conclusive.

IX.5.2 Place of online arbitration and its implications

The place of arbitration normally has a practical importance to the parties and arbitrators due to the need of being present and providing evidence in that place. It may also have legal significance since it may determine the applicable procedural (i.e.´curial´) law. Parties are usually, provided that public policy provisions are respected, at liberty to determine the law applicable to the arbitration proceedings as, for instance, they can decide the law applicable to the merits of the dispute. The New York Convention leaves the parties entirely free in this respect.[40] Should the procedural law or the arbitration rules selected by the parties not cover certain issues, they may have to be considered under the law of the place of arbitration. These could include, for example, the validity of the

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38 According to several members of the Working Group, an interpretative instrument would not be sufficient for Article II(2) of the NYC, and an amending protocol to the Convention should be made. A suggestion has been made to create a Guide of Enactment of the new Article 7 of the Model Law. See the Report of the Working Group on Arbitration on the work of its thirty-sixth session (New York 4-8 March 2002), doc A/CN.9/508, para. 15.

39 Craig, Park & Paulsson, § 5.05. Reference is made to the case *Isover St. Gobain v. Dow Chemical France et al.* (1984, Revue de l´arbitrage 98), which concerned an unsuccessful challenge against an ICC arbitral award in which the applicable law to an arbitration agreement had been determined liberally.

40 The law of the place of arbitration, the *lex loci arbitri*, may, however, set limits to party autonomy. Belgian law, in an apparent attempt to attract more international arbitrations to take place on the Belgian soil, states, however, that it is not applied at all if excluded by the parties.

arbitration agreement, the constitution of the arbitral tribunal, or procedural matters such as the use of interim measures.What would the place of arbitration be, when no oral hearings are held and the proceedings are conducted through an exchange of electronic affidavits? Article 20 of the UNCITRAL Model Law on International Commercial Arbitration gives the parties a right to agree on the place of arbitration. This could be done, of course, on a fictitious basis. Failing such an agreement, the place of arbitration shall be determined by the arbitral tribunal with regard to the circumstances of the case, including the convenience of the parties.[41] Even though no oral hearings take place, the arbitral tribunal has to determine the place of arbitration at least when making the arbitral award, recalling that Article 31(3) of the UNCITRAL Model Law provides that the award shall state its date and the place of arbitration and that the award shall be deemed to have been made at that place.[42] One connection which the arbitrators may take into account is the geographical location of the server through which the arbitration takes place (the *lex loci server*). This approach could also be artificial, should more than one server be used in the arbitration, and should these be situated in different countries.[43] One could argue that online arbitration is delocalised and denationalised by nature. Doubts have been expressed whether national courts could accept this idea when applying the New York Convention.[44]

IX.5.3 The selection of the substantive law

One of the decisions that arbitrators may need to make is the choice of the substantive law applicable to the merits of the case.[45] Article 28 of the UNCITRAL Model Law on International Commercial Arbitration provides that "(the) arbitral tribunal shall decide the dispute in accordance with such rules of law as are chosen by the parties as applicable to the substance of the dispute".[46] Where the parties have failed to designate any law, the arbitral tribunal shall apply the law

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41 Notwithstanding this, the arbitral tribunal may, unless otherwise agreed by the parties, meet at any place it considers appropriate for consultation among its members, for hearing witnesses, experts or the parties, or for inspection of goods, other property or documents.

42 Section 10 of the American Arbitration Association´s Supplementary Procedures for Online Arbitration contain a similar provision giving the parties the right to choose the (formal) place of arbitration, and should the parties fail to designate this, the arbitral tribunal (the ´Arbitrator´) has to determine the place of arbitration.

43 Cf. Article 7(4) of the UNCITRAL draft convention on electronic contracting which makes the place of the server mostly irrelevant, doc. A/CN.9/WP.IV/WP.108.

44 Herman Verbist and Christophe Imhoos, Arbitration, Telecommunications and Electronic Commerce, A Summary of the Final Report of a Working Party of the ICC Commission on International Arbitration, ICC International Court of Arbitration Bulletin Vol 10/No 2 – Fall 1999, pp. 20-25. The Working Party was formed to examine issues relating to arbitration in the field of telecommunications and electronic commerce.

45 For the topic, see also ICCA 1994.

46 See also Article 33 of the UNCITRAL Arbitration Rules, which is similarly worded as Article 28 of the Model Law. However, the Model Law provision adds that "(a)ny designation of the law or legal system of a given State shall be construed, unless otherwise expressed, as directly referring to the substantive law of that State and not to its conflict of laws rules".

determined by the conflict of laws rules which it considers applicable. An arbitral tribunal does not have to apply the conflict of laws rules of the seat of arbitration.[47]

Article 28 of the Model Law adds that the arbitral tribunal shall decide *ex aequo et bono* or as amiable compositeur only if the parties have expressly authorised it to do so. Moreover, in all cases, the arbitral tribunal shall decide in accordance with the terms of the contract and shall take into account the usages of the trade applicable to the transaction.

Parties may also allow the dispute to be settled on the basis of the *lex mercatoria*. There may be an express authorisation to do this in the contract. For instance, the ICC Model Agency and Distributorship contracts anticipate this possibility whereas a similar provision was not taken into the ICC Model International Sale Contract (Manufactured Goods Intended for Resale).[48] Parties may also incorporate into their contract an instrument such as the *UNIDROIT Principles of International Commercial Contracts 2004* (see Chapter X.3.2., *post*), which represents certain elements of the *lex mercatoria* as understood by a respectable number of legal scholars. In the absence of a specific agreement, the arbitrators may nonetheless determine that this was the intent of the parties and submit the agreement to the *lex mercatoria*.[49] There have been various arbitral awards based

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47 According to Craig, Park & Paulsson § 17.02 at 326), "(t)he most frequent method used by ICC arbitrators to choose an appropriate conflict of laws rule is the cumulative application of the different rules of conflict of the countries having a relation to the dispute".

48 ICC Publications Nos 496, 518 and 556 respectively.

49 Craig, Park & Paulsson, Part III § 17.03, p. 333. In France, a government decree dated 12 May 1981 added new provisions on international arbitration to the Code of Civil Procedure. Pursuant to Article 1496 of the Code, the arbitrator applies to the contract the rules of law which the parties have chosen and, when no choice has been made, those which he considers appropriate (*celles qu´il estime appropriées*). This provision also gives recognition to French and foreign awards based upon the *lex mercatoria* or other non-national sources of law when the parties have not agreed on a decision based upon these sources (Lando 1985, pp. 756-757). A similar provision exists in Article 1054 of the Dutch Code of Civil Procedure. *Lando* concluded (in op.cit. on page 760) that the courts of most of the countries examined (France, Switzerland, Germany, Austria, England, The United States and the Nordic countries) would not set aside an agreement by the parties to apply the *lex mercatoria* or an award which, relying upon such an agreement, has been based on the *lex mercatoria*. Lando was not certain whether the courts would accept an award based on the *lex mercatoria* if the parties had not referred to it. French courts at least would recognise this.

Kühn thinks that special caution must be exercised in construing the intentions of the parties. According to him, one cannot usually assume that the parties wish to waive their right to agree upon a definite legal system. If the intentions of the parties are not clear, one should in most cases assume (especially under German law) that the parties wish to bind the arbitral tribunal to a law and legal system which has yet to be determined.

After the above arguments for and against were made, many institutional arbitration rules were amended to be in line with the French decree. Once the application of anational rules of law, in the absence of an express choice of law, is allowed by a contractual reference to institutional arbitration rules by the parties, the arguments against have, in my view, much less ground.

One should mention that the European Commission has, recognising that parties may, at least in some jurisdictions, submit their dispute to non-state law, invited comments from interested circles on whether this possibility should be allowed in the ´communitised´ revision of the Rome Convention on the Law Applicable to Contractual Obligations (Green Paper on the conversion of the Rome Convention of 1980 on the law applicable to contractual obligations into a Community instrument and its modernisation), COM(2002) 654 final, Brussels, 14.1.2003, pp. 22-23; see also Chapter X.2.3., *post*.

on the *lex mercatoria* and national courts have upheld these awards. The frequently cited *Norsolor* case[50] before the Austrian Supreme Court, the *Fougerolles*[51] case before the French Cour de cassation, as well as the case[52] in which the Court of Appeals of England recognised an award based on the *lex mercatoria*, serve as examples.

Recently, the ICC Rules of arbitration have adopted a rule very similar to the French decree from 1981. Article 17 (1) (Applicable Rules of Law) of the 1998 Rules of Arbitration provide that "(t)he parties shall be free to agree upon the rules of law to be applied by the Arbitral Tribunal to the merits of the dispute. In the absence of any such agreement, the Arbitral Tribunal shall apply the rules of law which it determines to be appropriate."[53] The idea has spread to the rules of some other arbitral institutions as well.[54]

When parties have expressly denied the use of anational sources of law, their use is not possible. Moreover, where each of the parties has based his pleadings upon national law, an arbitrator should not be permitted to apply the *lex mercatoria*. Should he do so, he would decide the case in a manner incompatible with the task conferred upon him, at least when the rules of arbitration do not give him discretionary powers as to the rules of law to be followed.[55]

A contract may refer to the *lex mercatoria*, or to principles of international commercial law, or to the usages of international trade. Such a provision may be exclusive, or it may be coupled with a provision in favour of a municipal law.

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50 ICC Case 3131/1979, ICCA Yearbook Commercial Arbitration IX (1984), p. 159.

51 Fougerolles v. Banque du Proche Orient, Cour de Cassation, 9.12.1981, 1982 Revue de l´arbitrage p. 183.

52 *Deutsche Schachtbau und Tiefbohrgesellschaft mbHb v. Ras Al Khaimah National Oil Co. And Shell International Petroleum Co. Ltd., [1987] 2 Lloyd´s Report, p. 246.*

53 The article contains rules about taking into account the provisions of the contract and usages as well as the powers to act as *amiable compositeurs* or to decide *ex aequo et bono*.

54 See for instance § 32(3) of the Rules of the Arbitration Institute of the Central Chamber of Commerce of Finland, which states:

"The arbitrators shall decide the dispute in accordance with the law.

If the parties have agreed that the law of a particular country should be applied to the dispute, the arbitrators shall base their award on the law of such country.

In the absence of such designation and if the case is connected with several countries and the parties have not agreed on the law or rules of law applicable to the substance of the dispute, the arbitrators may apply the law or rules of law, which they consider most appropriate. (Amended 29.11.2000)

If the parties have so agreed, the arbitrators may, however, decide ex aequo et bono."

It can be noted that the possibility of the parties to choose or the arbitrators to base the award on any rules of law is limited to international arbitration in Finnish Central Chamber of Commerce arbitration.

The Rules of the Arbitration of the Arbitration Institute of the Stockholm Chamber of Commerce (Article 24) and the Rules of the Expedited Arbitrations of the same Institute (Article 20) have a similar provision, but no requirement is made regarding the internationality of the dispute.

55 Lando 1985, pp. 756-757, Lando 1987, pp. 110-111. Since the publication of the article, the *lex mercatoria* has found shape, as referred to *supra*, in the UNIDROIT Principles for International Commercial Contracts and in the European Principles of Contract Law. Moreover, the past decade has seen many legislative references to non-statutory law, such as codes of conduct and model contracts.

Parties are at liberty to designate those rules of law that they deem appropriate and bind the arbitrators in this way. Where the rules are codified texts, the parties´ choice is close to contractual incorporation. In cases where only a municipal law is selected, many authorities deny the arbitrators the right to resort to the *lex mercatoria*. However, where a choice-of-law is missing, arbitrators can resort to it, nowadays often pursuant to provisions in institutional rules of arbitration.[56]

As in contracts, the application of the *lex mercatoria* in international awards is in certain instances combined with the application of a domestic law. The *lex mercatoria* and the domestic law may be placed at the same level, or the priority may be given to the general principles, or the arbitrator may use municipal law only to confirm the solutions drawn from the general usages.[57] Now that the ´codified´ *lex mercatoria* instruments such as the UNIDROIT Principles of International Commercial Contracts have evolved, and international conventions and model laws facilitate direct incorporation (the exclusive incorporation being subject to discussion), the side-by-side application of municipal law and the *lex mercatoria* may become more commonplace. It is arguable that a reference to an individual instrument together with a choice-of-law clause does not open the door to the application of the *lex mercatoria* yet, but a reference to international principles or usages in general does.

An arbitrator acting as an *amiable compositeur* deciding *ex aequo et bono* can apply the *lex mercatoria,* but an arbitrator having been empowered to decide according to the *lex mercatoria* cannot decide solely on the basis of equity.[58] However, parties may choose a combination of *lex mercatoria* and equity.

As a whole, the recent trends relating to substantive law applied to the merits of the dispute allow the *lex mercatoria* to be applied in several ways. Parties may agree on it in broad terms or more selectively and replace municipal laws by their choice completely or in part. Parties may decide not to designate a domestic legal system or any legal rules applicable to the merits, and the arbitrator can in principle choose any rules of law according to the rules of many arbitral institutions. Finally, the *lex mercatoria* can be included because the arbitrators are bound to respect the contract, which may be incorporating *lex mercatoria* instruments and usages that form parts of the *lex mercatoria* even according to narrower descriptions (see Chapter X.2, *post*).

The flexibility as regards the applicable law makes arbitration particularly useful a method for settling electronic commerce disputes. Arbitrators could creatively resort to international instruments facilitating electronic commerce (*lex electronica*), and not stick to cumbersome form requirements contained in a

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[56] Craig, Park & Paulsson however consider that "...as matters stand today in most countries, that ICC arbitrators run the risk of doing mischief if they declare *lex mercatoria* to be the governing law. The proper conduct would seem to be that of the tribunal in ICC Case 4650, which declined to accept *lex mercatoria* as the applicable law in the absence of any proof that the parties so intended".

[57] Goldman 1987, pp. 117-118.

[58] Lando 1987, p. 110.

particular national law connected to the transaction, unless such form requirements amount to matters of public policy, thereby undermining the possibility to enforce the award in the relevant country. [59]

IX.5.4 Arbitration proceedings and electronics

There are two apparent advantages of using on-line arbitration in lieu of normal arbitration proceedings. Firstly, the parties need not travel to the place of arbitration where oral hearings take place. This requires that the arbitration can be conducted without organising an oral hearing. Secondly, proceedings should be speeded up as documents and evidence can be exchanged almost instantaneously through electronic communications. The regulatory framework applicable to the arbitral proceedings should therefore allow communications in electronic form. Parties could establish such a framework by a contractual clause e.g. in an interchange agreement, unless such a clause is already redundant under the provisions of the applicable law. Outside these considerations, arbitrators have generally wide powers as regards evidence, and may therefore allow documentary evidence in the form of electronic records even if this were not provided for expressly in the contract or law.[60] Particular problems for online arbitration proceedings may arise in the proceedings themselves, or concerning the the form of the final arbitral award.

The question of an arbitral award in electronic form is also interesting as regards its presentation to trigger payment as a required document under an accessory contract guarantee (this is the case with Uniform Rules for Contract Bonds, URCB 524).

As regards the proceedings, distinction can again be made between *ad hoc* and institutional arbitration. In *ad hoc* arbitration, parties are free to agree on the rules for arbitration, subject to the limitations of the applicable procedural law, and bearing in mind the possibility that the final award is set aside in the country of enforcement on grounds mentioned in Article V of the New York

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[59] See Article V 2 (b) of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards.

[60] This principle is most clearly stated in Article 25(6) of the UNCITRAL Arbitration Rules, which gives the arbitral tribunal the task to determine the admissibility, relevance, materiality and weight of the evidence offered. Should the tribunal reject electronic records as evidence (based solely on reasons of form), one could ask, whether this would violate the public policy of the state of enforcement of the arbitral award. If basic electronic commerce legislation such as the US UETA or ESIGN were enacted there, such a case could perhaps be established. Reference is made to the Bolero Feasibility Study 1999, survey on the attitude of states regarding foreign form requirements (see Chapter II.9, *ante*).

See also the International Bar Association Supplementary Rules Governing the Taking of Evidence in International Commercial Arbitration, at http://www.ibanet.org/pdf/rules -of-evide-2.pdf, visited on 10.9.2003.

Convention.[61] Article 19(1) of the UNCITRAL Model Law namely gives the parties freedom, subject to the provisions of the Model Law, to agree on the procedure to be followed by the arbital tribunal in conducting the proceedings. They could therefore agree on arbitral proceedings without an oral hearing, in which communications and documentation are presented electronically.

To the extent parties have not validly agreed on the procedure of *ad hoc* arbitration, the procedure to be followed is normally determined by the arbitrator(s). Article 19(2) of the UNCITRAL Model Law gives the arbitral tribunal the right, failing an agreement by the parties and subject to the provisions of the Model Law, to conduct the arbitration in such a manner as it considers appropriate for consultation among its members, for hearing witnesses, experts or the parties, or for inspection of goods, other property or documents.[62] The arbitrators have discretion to decide whether to hold oral hearings or not. Article 24(1) stipulates that, subject to any contrary agreement by the parties, the arbitral tribunal shall decide whether the proceedings shall be conducted on the basis of documents and other materials. However, unless the parties have agreed that no hearings shall be held, the arbitral tribunal shall hold such hearings at an appropriate stage of the proceedings, if so requested by a party.

In institutional arbitration, parties have agreed to follow the rules of a particular institution. In each case, therefore, the rules of a particular institution have to be examined to see to what extent electronic procedures are possible. For one, the American Arbitration Association has adopted special Supplementary Procedures for Online Arbitration.[63] As regards other institutional arbitration rules, a close look has to be taken at them to see whether their wording explicitly or by implication facilitates electronic procedures.

According to the AAA Supplementary Procedures, the arbitral proceedings commence with the claimant making a request for arbitration. The AAA Supplement provides that the claimant shall submit the claim to the Administrative Site of the AAA. The word ´submit´ refers, inter alia, to the electronic transmittal of pleadings, exhibits, communications and other documents to the Case Site, which is an Internet site established to maintain case files with access limited to the arbitrators and the arbitral institution itself.

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61 This Article provides that the recognition and enforcement of the award may be refused, at the request of the party against whom it is invoked, only if that party furnishes to the competent authority where the recognition and enforcement is sought, proof that (inter alia):

(a) the party against whom the award is invoked was not given proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case.

Article V provides, furthermore, that the recognition and enforcement of an arbitral award may also be refused if the competent authority in the country where recognition and enforcement is sought finds that (inter alia):

(b) the recognition or enforcement of the award would be contrary to the public policy of that country.

62 A similar provision is in Article 15 of the UNCITRAL Arbitration Rules which state that "subject to these Rules, the arbitral tribunal may conduct the arbitration in such manner as it considers appropriate, provided that the parties are treated with equality and that at any stage of the proceedings each party is given a full opportunity of presenting his case".

63 The AAA Website – Rules'http://www.adr.org, visited on 29.4.2002.

The ICC Rules for Conciliation and Arbitration (the latest version is from 1998) provide, in turn, in Article 3(2) that notifications or communications may be made "by delivery against receipt, registered post, courier, facsimile transmission, telex, telegram or any other means of telecommunications that provides a record of the sending thereof". It should be therefore possible for the claimant to file a request for arbitration with the Secretariat of the ICC International Court of Arbitration electronically. Likewise, the Secretariat could notify such request electronically to the respondent. There are, however, no explicit practices on how this should be done.[64]

On the contrary, the AAA Supplementary Procedures provide, in Section 4.a., that after having received and reviewed the claim, together with the required administrative fees, the AAA shall establish a Case Site upon which the claim is immediately available. The AAA shall notify the parties by e-mail of the address of the Case Site. The arbitration shall be deemed commenced on the day the Case Site is established, as reflected in the confirmatory e-mails sent by the parties.

Should the respondent remain silent throughout the proceedings, the arbitral tribunal should make an *ex parte* award. Therefore the communication of the claim or request to the respondent is very critical in order to make the award enforceable against him, also bearing in mind the requirements of Article V of the New York Convention. The use of confirmatory e-mails appears to be very useful, if not crucial, to the succesful communication of the claim to the respondent. Should the respondent fail to send a confirmatory e-mail, the arbitral institution has to verify whether electronic proceedings can continue. Section 4.b. of the AAA Supplementary Procedures states therefore that if the AAA finds that notification to the respondent via e-mail is not possible, it may decide that the Supplementary Procedures should not apply. Similarly, Section 1.c. provides that the AAA may decide, due to the parties´ incapacity to participate in an electronic arbitration, or more generally in its own discretion, that the arbitration should not be conducted under the Supplementary Procedures. The ordinary AAA commercial arbitration rules remain solely applicable in that case.

In ICC arbitration, an arbitral tribunal is not obliged to organise oral hearings. However, conducting discussions in the form of electronic exchanges seems to require consent by the parties.[65] The AAA Supplementary Procedures

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64 In ICC arbitration, the establishment of the Terms of Reference is obligatory. There is a requirement that the Terms of Reference be signed. As the ´signature´ has traditionally meant a handwritten signature, this would mean that express agreement by the parties is necessary for the Terms of Reference to be drawn electronically. (Herman Verbist and Christophe Imhoos, Arbitration, Telecommunications and Electronic Commerce, A Summary of the Final Report of a Working Party of the ICC Commission on International Arbitration, ICC International Court of Arbitration Bulletin Vol. 10/No 2 – Fall 1999, pp. 20-25. The Working Party was constituted to examine issues relating to arbitration in the field of telecommunications and electronic commerce.)

It is arguable that Directive 1999/93/EC on a Community framework for electronic signatures would not change form requirements in rules to be incorporated contractually, although it equates electronic signatures with handwritten signatures required by national law.

65 Ibid.

are mainly based on electronic submissions (´submissions´ refers to pleadings, exhibits, communications, or other documents, however transmitted). Unless either party requests and the arbitrator (´arbitrator´ refers in Supplementary Procedures to a sole arbitrator or a panel of arbitrators) agrees to a hearing, the arbitrator bases the award on the submissions. So neither in ICC arbitration, nor in an arbitration subject to the AAA Supplementary Procedures can the parties resort to dilatory tactics by requiring an oral hearing.

The Rules of ICLOCA are generally based on the UNCITRAL Arbitration Rules. Article 15(2) of the ICLOCA Rules derogates from the approach adopted by the UNCITRAL Arbitration Rules in that it remains under the discretion of the arbitral tribunal whether to hold hearings for the presentation of evidence by witnesses, or oral argument, or whether the proceedings shall be conducted on the basis of documents and other materials. The ICLOCA Rules, like the UNCITRAL Rules, use the term ´in writing´ in many places (statement of claim, statement of defence, further written statements as well as the award) without also specifying this to mean electronic records. It is submitted therefore that, like in the ICC arbitration, an agreement by the parties is needed to make electronic exchanges the method of arbitration.

IX.5.5 Electronic arbitral awards

As regards the form of arbitral awards, there are requirements as to written form and signature existing in various national legal systems, as well as in Article IV of the New York Convention and Article 31 of the UNCITRAL Model Law on International Commercial Arbitration. There is further a distinction between an original and a copy. Article 31 of the Model Law provides namely that an arbitral award shall be made in writing and shall be signed by the arbitrator or arbitrators. After the award is made, a copy signed by the arbitrators shall be delivered to each party.

The requirement of a handwritten signature should be overcome by legislation equating electronic signatures with handwritten signatures. An electronic signature should be recognised by the law of the place of arbitration, in which the award has to be signed.[66] Moreover, electronic signatures may have to be recognised in the country of enforcement as well to be effective.[67] Article IV

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66 According to Article 31(3) of the UNCITRAL Model Law on International Commercial Arbitration, an arbitral award shall state its date and the place of arbitration as determined in accordance with Article 20(1).

67 Article V (d) of the New York Convention makes it possible to have the award set aside if the procedure was not in accordance with the agreement of the parties, or failing such an agreement, was not in accordance with the law of the country where the arbitration took place.

Even if the use of electronic signatures complies with the law of the country where the arbitration takes place, a country of enforcement without legislation on electronic signatures might interpret the New York Convention, as long as it is not crystal clear, and in particular Article IV thereof, as not enabling the enforcement of an electronically signed and rendered award, especially if it did not have the administrative means to deal with that award.

of the New York Convention requires the party applying for recognition and enforcement to supply the duly authenticated original award or a duly certified copy theof. In addition, the arbitration agreement or a copy thereof has to be furnished. For arbitration agreements, however, as noted earlier, UNCITRAL is preparing new legislative or interpretative instruments to facilitate the use of the electronic form.

As regards arbitral awards, the UNCITRAL Model Law on Electronic Commerce may offer a solution to the original vs. copy problem. It provides, as noted in Chapter IV.4.3., *ante*, that a document may be considered an original if two conditions are met. Firstly, there has to be reliable assurance as to the integrity of the information and, secondly, that the information is capable of being displayed to the person to whom it is to be presented.

Would a state court in a country having enacted legislation based on or comparable to the UNCITRAL Model Law on Electronic Commerce accept a document transmitted electronically as an original award? For this to happen, the court would have to satisfy itself that the award is signed by the required number of arbitrators[68] and that it is complete and unaltered. Third party authentication services might prove extremely valuable to guarantee the authenticity and integrity of electronic awards.[69]

Finally, one can mention it has been estimated that a vast majority of arbitral awards (over 90%) are followed without the need to resort to enforcement. The issuance of an award usually suffices to terminate the dispute.

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[68] The signatures of a majority of arbitrators suffice, provided that the reason for the missing signatures is indicated (Article 31 of the UNCITRAL Model Law on International Commercial Arbitration).

[69] For comparison, some older arbitration laws, such as the Finnish Arbitration Act of 1928, provided that a copy of each arbitral award must be stored in court archives. This provision contravened the principle of the confidentiality of arbitration and was removed from Finnish law in the 1992 Arbitration Act. Originally, the reason for providing for filing was not to make the awards intentionally public, but to store a copy of it with a view to protecting the interests of the parties that could lose their respective copies.

It might be useful to consider restoring the idea of a publicly kept register for arbitral awards in the case of awards rendered electronically. If facilities are created for storing court judgements in an electronic form, arbitral awards might easily be added to this system. Arbitral awards should be stored on a confidential basis, and only the parties and the administrator should have access to the award.

Alternatively, arbitral institutions might consider acting as Trusted Third Parties in arbitrations administered under their rules. In arbitrations under the AAA Supplementary Procedures for Online Arbitration, the arbitrator (i.e. the arbitral tribunal) shall submit the award to the Case Site, which then notifies the parties by e-mail that the award has been submitted. The Case Site shall then remain available to the parties for thirty days from the date upon which the award was submitted. It is available only to the parties and the arbitrator and does not serve as an archive of awards for retention and later enforcement.

Article 10 of the UNCITRAL Model Law on Electronic Commerce would lay down the requirements for effective retention by providing that a document is retained if "the information contained therein isÉusable for subsequent reference", if "the data message is retained in the format in which it was generated, sent or received", and if "such information, if any, is retained as enables the identification of the origin and destination of a data message and the date and time when it was sent or received".

X THE ´THIRD STAGE´: A MOVEMENT TOWARDS A UNIFORM SUBSTANTIVE LAW

In this study, I have tried to bring together a number of instruments and projects that have facilitated electronic commerce for the international sale of goods in recent decades. A modest attempt at summing up all these developments and trying to find a line of development in order to be able to make some predictions in that light will be made in this final chapter.

Although this distinction may be somewhat arbitrary, the legislation and other sources of law facilitating electronic commerce, including model contracts, could be divided into three stages in respect of their roles, or possible roles, in electronic contracting. The distinction is made simply in order to describe and understand the development process of the new legal infrastructure and is without any dogmatic significance as such. It has to be borne in mind, however, that the new legislation and rules govern not only the position of the parties exchanging electronic communications but also the validity, functions and importance of the instruments used by them, and the establishment and role of third party services which facilitate electronic communications and contracting. Furthermore, usages do not fit well into these three categories.

The first stage, or layer, comprising first and foremost the UNCITRAL Model Law on Electronic Commerce as well as legislation governing electronic signatures, could be described as measures of creating electronic functional equivalents for the basic legal concepts and tools available in the paper-based world while, at the same time declaring parity between electronic messages or tools and their counterparts on paper. The role of this legislation is therefore very technical. Another type of first layer regulations are acts which remove legal impediments such as form requirements contained in trade or transport legislation.

First stage regulations may already have some components that regulate contracting techniques. Although the UNCITRAL Model Law on Electronic Commerce pays particular attention to one particular contract formation

technique, incorporation by reference, it limits itself to safeguarding that electronic incorporation by reference is treated equally to an incorporation by reference in a traditional paper-based environment and leaves the questions of the formation of contracts to be governed by other legislative instruments. For instance, the US UETA has provisions on the relationship between the use of standard form contracts and the obligation to use electronic messaging. First stage regulation should be understood to be generally of a mandatory character.[1]

The second stage of electronic commerce regulation goes deeper into the formation of contracts and may even have provisions relating to the substance regarding the rights and obligations of the parties. Directive 2000/31/EC on electronic commerce contains many provisions concerning contractual and marketing techniques as well as rules facilitating the establishment of a proper infrastructure for electronic commerce. It strongly focusses on consumer protection as far as its contractual dimensions are concerned. The UNCITRAL preliminary draft convention on electronic contracting, as it stands at the moment, seems to be limited to contract formation issues, and of those solely between companies.[2] What is characteristic of it, however, is that it does not attempt to cover contract formation in its entirety. It leaves a role to the provisions of the CISG, to the UNIDROIT or European Principles of contract law, and finally also to domestic law provisions. The provisions for electronic commerce and the CISG are more mechanical, and one has to resort to the Principles or to domestic laws to include the psychological component within the framework of consensualism, i.e. to define when the wills of the parties meet and to find rules on the two defects of consent, fraud and threat. Furthermore, usages, especially those written down in codes of conduct, are of importance in a manner similar to the CISG. Second stage regulations are mostly directory (i.e. non-mandatory) law.

The third stage of electronic commerce regulation goes deeper in regulating the relationship between contractually communicating parties by providing for the law applicable to the legal relationship established by electronic means or by laying down substantive[3] provisions. This is the approach which American trading partner agreements have represented, and a similar contractual arrangement was recently discussed within the International Chamber of Commerce until it was finally abandoned. The substantive legal provisions relating to the transactions concerned may follow from the rules used in the paper-based world. For the notion of functional equivalence, basic recognition

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1 This is how Articles 1 to 10 of the UNCITRAL Model Law on Electronic Commerce are recommended to be implemented, see Chapter IV.4., *ante*.

2 Smedinghoff 2002 mentions (on page 25), as a US equivalent of the UNCITRAL project, a project by an industry group Electronic Financial Services Counsel (at http://www.efscouncil.org, visited on 25.8.2003) which has created in the summer of 2003 the Standards and Procedures for Electronic Records and Signatures (SpeRS at http://www.spers.org, visited on 25.8.2003).

3 The word ´substantive´ is used to point out provisions that regulate the parties´ rights and obligations under a contract in a manner similar to Part III of the CISG. On the other hand, UNCITRAL Working Party IV (Electronic Commerce) uses the notion ´substantive´ also to mean issues that are of traditional contract law and not necessarily specific to electronic commerce such as the formation of contracts.

for electronic transport documents has already been created in INCOTERMS 1990 and the CISG Advisory Council has created interpretations on electronic equivalents for notices and communications envisaged in Part III of the CISG.

Furthermore, it is also conceivable that a ´third stage proper´ will emerge – the use of an electronic medium leads to a reappraisal of traditional legal institutions, possibly after it is no longer recognised that certain rights were once transferred or that legal effects were created by means of paper, or even by means of messages replacing paper. Reference could be made to projects such as the anticipated SWIFTNet Trade Services Utility.

The paper-based world is still very much "alive and kicking". Therefore an alignment between paper-based and electronic worlds through creating functional equivalents is quite obvious. This is also necessitated by the need for the two forms of communication to coexist. However, as the years pass, and the electronic medium becomes predominant, it may not be that there will always be a piece of paper representing the same functions.

For the time being, nevertheless, legislators, including international organisations such as UNCITRAL, have not gone in the direction of making substantive laws particularly targeted to electronic transactions in the field of sale of goods, which seems to be a well-contemplated approach in the present-day situation.

X.1 The emergence and scope of the *lex electronica* at present

Having said the above, the notion of ´third stage´ in the title of this chapter relates in essence to the development of new uniform substantive law for the international sale of tangible goods. It is neither a new development nor unique to electronic transactions. Yet it is believed that the adoption of electronic methods of contracting will accelerate this development. So, in fact, the third stage of electronic commerce legislation would eventually be a reinforcement of the *lex mercatoria* in the wider senses of the word. Electronic commerce law, the *lex electronica*, will gradually form part of the *lex mercatoria*. This appears to be a popular opinion among writers.[4]

Fauvarque Cosson[5] "analyses the notion by quoting one description[6] regarding the integration of *lex electronica* with *lex mercatoria*, which both would be "hatched by the world of international traders and would govern relations between the members of that society, a law with an essentially traditional base derived from international trade practices but in which arbitration case law would also play a

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4 As analysed by Fauvarque-Cosson, p. 3. Similarly Johnsson, David – Post, David, Law and Borders – The Rise of the Law in Cyberspace, 1996, http://www.cli.or/X0025_LBFIN.htm, as referenceed to by Laine 1998, p. 49.

5 Ibid.

6 Pierre Mayer, Actualité du contrat international, Petites Affiches, special issue of 5 May 2000, p. 56.

big part". She also quotes another description[7], according to which the *lex electronica* "would arise from network users and would group together all the informal legal regulations applicable in the context of e-commerce". Fauvarque Cosson is not, however, in agreement with these ideas. *Lex electronica* with such a definition is too restrictive and since it presupposes limiting the field only to relations between professionals, since this definition only considers this law as originating from network users, this is comparable to self-regulation.[8] Fauvarque Cosson points out, quite rightly, that electronic commerce law consists of

> "(n)ot so much a plethora of regulations arising from practical experience (codes of good conduct, customary practices and other informal sources of law) but rather one of transnational legal rules. Although initially they took the form of legal instruments with only contractual value (recommendations, model agreements, standard law) they now include include various instruments endowed with the utmost binding force (conventions, European directives and future transposition laws)".

Fauvarque Cosson considers that the notion of *lex electronica* calls for "real legal pluralism" just as the case is with traditional substantive legal rules. She also contends that the *lex electronica* and cybercourts must not completely replace national laws and courts. It is still necessary to rely on domestic legal systems, and, consequentially, on choice-of-law rules, which according to her, however, must be adapted.[9]

The authors (Gautrais, Lefevre & Benyekleff) of the article ´L´émergence de la *lex electronica*´ define the scope of the *lex electronica* as comprising international conventions, model contracts, arbitral awards, usages arising from practice and, finally, general principles of law. They categorise the first three sources as institutional sources and the last two, usages and general principles, as substantive sources ("sources substantielles").[10]

I would also be in favour of a pluralistic concept of *lex electronica*. It comprises more or less all instruments of electronic commerce dealt with in this study: conventions, model laws, EC directives, and to some extent national statutes, uniform rules, general principles of law, generally accepted interpretations, model contracts, codes of conduct and arbitral awards. Like in the case of general commercial law, there is a tendency towards uniformity. However, electronic commerce law benefits from the fact that it is being created during an era when harmonisation is seen, or should be seen, as a necessity. Furthermore, *lex electronica* is almost invariably based on international models. Although practice inevitably adds discord, I believe the international legal community shares a desire for a uniform law in this area.

Individual instruments facilitating electronic commerce are, so far, inevitably inadequate. Additional rules must be sought somewhere. I suggest that similar

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7 L´émergence de la *lex electronica*, p. 548.

8 Fauvarque-Cosson, p. 3.

9 Ibid. It must be added that despite the fact that there are now statutes and a preliminary draft convention on electronic contracting, usages that are or are not included in codes of conduct have a recognised status. For instance, the UNCITRAL´s draft gives usages a role similar to that given by the CISG in the international sale of goods.

10 L´émergence de la *lex electronica*, p. 559.

methods could be used to those applied by arbitrators applying anational law, the *lex mercatoria* in traditional substantive commercial law disputes (see *infra*). Therefore there are practical reasons for referring to a concept that embraces law in its various appearances.

Judge-made law plays a preponderant role at common law and in European Community law whereas civil law systems give a leading role to statutory law. In commercial law, however, the use of arbitration and other out-of-court dispute settlement systems give adjudication a central role. Giving the adjudicators wide powers to apply and create rules is a relevant development. Coupled with the enhancement of out-of-court dispute resolution in electronic commerce arbitral practice may have notable effects.

Conflicts between various methods of bringing about legal rules have diminished substantially. It is perfectly normal for intergovernmental organisations to consider producing non-binding uniform rules or even model contracts. The choice between methods is made on the basis of legislative expediency and general legislative principles. For example, the emergence of consumer parties to electronic contracts has called for mandatory laws. Ideology gives way to pragmatism in legislative work, just as it has done in the general economy in the past decade or so.

In Chapter IV, *ante*, a look was taken into the various newly established rules on functional equivalence and contract formation. A tendency towards internationalism can be found there since, as said, new national legislation is almost invariably based on international models.

Although substantive contract law provisions are, as a rule, absent in the statutes and instruments already created for the facilitation of electronic commerce, it is tempting to make a reference to possible sources of uniform international commercial law, bearing in mind that international commercial contracts between business partners belong to the sphere of party autonomy and that parties can integrate into their agreements uniform elements created by the various formulating agencies of international commercial law.

The existence of a sound base of instruments for referencing and incorporation is particularly useful in electronic commerce, where the determination of applicable law may be particularly complex.

The development of instruments for electronic contracting in the form of conventions, model laws, guidelines and model contracts leads to the creation of necessary infrastructure for electronic transactions. Just as important, I believe, is the building of confidence in electronic commerce.

As already noted, conflict of laws is a particular problem in electronic contracting since traditional instruments do not address the problems specific to e-commerce. This is especially the case as regards consumer contracts, where there are well-established limits to party autonomy. In the international sale of goods between businesses, however, the uncertainty relating to the conflict of laws method may be greatly overcome by resorting to a uniform substantive law.

The law of electronic commerce is under constant development like any other field of law. Yet the instruments created so far, and those still under preparation, give rise to some general observations.

X.1.1 Limited changes needed to facilitate electronic commerce

One of the founding assumptions of UNCITRAL Working Party IV (Electronic Commerce) in drafting the preliminary draft convention on electronic contracting is that electronic contracts are not fundamentally different from other types of contracts.[11] In the United States, the drafters of the UETA (1999) found very few places where the existing rules of evidence, proof, contract formation, and other concerns were not adequate to cover electronic transactions.[12]

A generally accepted view seems to be that, as far as possible, instead of creating new norms for electronic commerce and Internet operations, existing principles, rules and procedures can and should be applied, in particular by way of interpretation, including the use of functional equivalents.[13] Creating specific rules for electronic commerce operations would create dual regimes for contracting, which is problematic since companies can use different contracting and communication methods interchangeably.[14]

This view can be contradicted by a view according to which the introduction of solid rules would eventually create the necessary confidence in electronic commerce, even for larger transactions. The rules for electronic communications are rather mechanical and thus more easily adapted to various legal cultures. States implementing uniform international rules would not need to limit themselves to electronic communications but could apply fundamentals such as the reception rule and its electronic equivalent to all contracts. The same goes for the parties making a contractual incorporation. Harmonisation proceeds in stages or layers, and partial harmonisation is better than no harmonisation at all. The benefits of partial harmonisation could spread their effects beyond the limits of the actual instrument. There is already a dual regime between international contracts regulated by the CISG and domestic contracts regulated by national law on domestic contracts. The CISG contract formation rules apply only to the sale of goods within the scope of the Convention.

When existing procedures are adapted to electronic commerce by way of producing functional equivalents, a mirror image of the past is created. Electronic commerce could, however, produce new business models and new legal institutions. The French study summarised in Chapter VIII.10, *ante*, explains how an erosion of property rights may take place when securities are no longer in tangible form but are dematerialised. Property rights may be replaced by contractual rights or debtor-creditor relationships. Such developments may have an impact on the position of third party creditors, or on the law applicable to the situation, just to mention two examples.

Mallon anticipates that the use of messages as substitutes for documents in electronic trading systems may one day give way to a common user database,

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11 UNCITRAL doc A/CN.9/WG.IV/WP.95 para. 11 referring to the work of Shawn Pompian entitled ´Is the Statute of Frauds Ready for Electronic Contracting´, Virginia Law Review, vol 85, p. 1479.

12 Gabriel, p. 3.

13 The CISG AC Opinion no 1, Electronic communications under CISG, 15 August 2003 represents such an interpretation.

14 This is an argument put forward by the International Chamber of Commerce.

where pieces of information are transferred by populating certain fields in the database, e.g. the carrier populates the field for descriptions of cargo.[15]

One may also recall the discussions in connection with ICC´s attempt to formulate an Electronic Trade Credit[16] in the mid 1990s. A common line of thinking was, even among such eminent characters of documentary credit law as Bernard *Wheble*, that traditional letters of credit should be replaced by a new instrument, which would copy the functions of a traditional documentary credit, but not be its exact equivalent in electronic form. After many attempts, the ICC ended up taking a traditional view by producing the eUCP, which regulates electronic presentations under UCP500. The discussion may not be over, as the launch of the SWIFTNet TSU indicates.

One of the most challenging tasks seems to be to the creation of electronic equivalents for documents of title and negotiable instruments. The legislators appear to be prone to leaving the job to the business community, which has responded to some extent. Yet, taking the contractual way cannot resolve the problems encountered with third parties. This could be one of the areas where a new substantive *lex electronica* could emerge through legislative involvement.

X.1.2 Most ´cognitive´ and moral parts of contract law outside the *lex electronica*

Contract formation by electronic means is generally not a mirror image of contract formation with traditional methods of communication. Contract formation rules in electronic commerce – to the extent they are taken to exist in contract practice and drafts for an international convention - remain very mechanical and generally leave many aspects to be resolved by other sources of law. Generally speaking, the ´cognitive´ dimension of contract law remains mostly outside the *lex electronica*. As exceptions one can mention that provisions on errors in communications found in the UNCITRAL draft convention on electronic contracting and that the notion of good faith is laid down in individual cases.[17] Consequently, the end result of any dispute relating to contract formation will depend on the entire structure of the applicable contract law.

It is obvious that electronic commerce law cannot build on psychological components, if one of the main purposes of the law is to facilitate the automatic formation of contracts, especially through electronic agents.[18] According to the science of today, machines are not conscious actors in the legal system. Our culture is based on the idea of dualism between spirit and materia, an idea represented, for instance, by René *Descartes* in the 17th century. If this dualism

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15 Mallon´s written interview 24 November 2003.

16 See Chapter VII.8.3., *ante*.

17 Especially in Article 13 (attribution of data messages) of the UNCITRAL Model Law on Electronic Commerce.

18 The UNCITRAL Working Party IV (Electronic Commerce) records (Doc. A/CN.9/548 para. 18) take note of this aspect and refer to national law provisions on error giving the negotiating partner´s knowledge of it a meaning and state that it is virtually impossible to prove awareness of a mistake on a side which is using automated processes to conclude the contract.

prevails, a conscious machine to which cognitive arguments would apply is impossible. A human mind can however be analysed and imitated to some extent by technical means.[19]

In particular, the rules relating to the attribution of data messages are particularly formal, but are deemed to be a necessity in order to achieve certainty and predictability in electronic communications. These rules incorporate some principles of agency in them, which is unique to electronic commerce. The rules of attribution are not concerned with questions of intent, but only with whether a person´s acts were causally connected to the creation or transmission of the electronic record or signature.[20]

Electronic contract law cannot be exhaustive or act alone but must be applied together with other rules of law. These are to be found in international instruments or in domestic law. Domestic law may of course include elements of international origin such as Part II of the CISG, and international legal principles may be used to supplement or interpret domestic law. Rules containing ´cognitive´ elements, as already said, and social elements such as the *Treu und Glauben* (good faith) principle of the BGB general clause will therefore come into play. Similarly, it is thought that domestic agency and other contract law may interfere to make the mechanical rules of attribution of data messages a rebuttable presumption, as the draft for the new Article 2 provisions of the Uniform Commercial Code suggests.

When parties are contracting electronically, they could add predictability in contract formation by referring to collections of international legal principles such as the UNIDROIT Principles for International Commercial Contracts or the European Principles of Contract Law.

X.1.3 Changing patterns of contract formation

As recognised e.g. by the drafters of the UNCITRAL Model Law on Electronic Commerce, the technique of incorporation by reference will be extensively used in contract formation. This method presupposes that there are reliable instruments, the contents of which are either well-known or can be verified with ease. The fact that reference techniques are already widely used in contemporary commercial practice by referring, for instance, to trade terms based on INCOTERMS 2000 speaks in favour of such development.

However, to avoid the pitfalls of contractual terms being altered unilaterally without informing the counterparty, repositories of commonly used contract clauses and other information can be established. In the Netherlands, a reference to general conditions deposited with a chamber of commerce is considered to be valid even in a paper framework. Should general conditions be available on the website of such a service provider, to which site a hyperlink is added in the

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19 For the possibility of the consciousness of machines, see the article ´Voidaanko robotille rakentaa tietoinen mieli?´ by Pentti A.O. Haikonen (Nokia Research Center) in Helsingin Sanomat 5 September 2003. Haikonen has also written a book entitled ´The Cognitive Approach to Conscious Machines´ (Imprint, Academic, UK, 2003).

20 Gabriel, p. 3, referring to Section 9(a) UETA (1999).

referencing electronic record, the situation should at least be equated with the use of a paper attachment where safeguards exist. Even where no hyperlink exists and the contract terms are not immediately available, incorporation by reference could be facilitated by repositories. Particularly suprising or onerous conditions could constitute an exception, depending on the applicable substantive contract law. The repositories could also record relevant case law and other information that helps to pave the way for the conclusion of a contract. Service providers such as trading platform operators need in no way guarantee the neutrality of the general conditions unless they had taken part in their drafting.

Electronic contracting facilities could bring into application standardised ´packages´of electronic contracting. For instance, *Paction*, the web application of the ICC Model International Sale Contract, forces the user to think about the ancillary activities and contracts which must be arranged in order to carry out the sale transaction, including the payment method and other services which may be provided by banks and other service providers. The use of Internet trading platforms based on the concept of a central registry could be coupled with functionalities such as the User Support Resources of the *Bolero System* to enable effective contract formation.

X.1.4 The role of self-regulation in electronic commerce law

The emergence of electronic commerce has largely taken place under the umbrella of self-regulation. The technical protocols of the Internet such as the domain name system are results of self-regulation. Interchange and trading partner agreements concluded between businesses have not been based on legislation. International organisations provided models such as the ICC´s UNCID Rules and took technical harmonisation measures in creating message standards, most notably EDIFACT.

Laine distinguishes between three models for the regulation of e-commerce. The ´Local Governance Model´ and ´World Governance´ represent vertical hierarchic governance whereas the ´Self-Regulation Model´ represents decentralised market-oriented regulation which works from the bottom up. None of these models will suffice alone, and governments can resort to them interchangeably.[21] One could obviously add the ´Regional Governance Model´, given the EC directives that were recently put in place.

As seen *supra*, the advocates of the notion of *lex electronica* or its equivalents that were created in the late 1990s usually gave self-regulation, including out-of-court dispute settlement systems, a leading role. The discussion on how to regulate the electronic marketplace still continues. However, by the turn of the millennium, legislation was put in place to govern e-commerce e.g. in the United States and in the European Union. The uniqueness of self-regulatory systems disappeared and started to coexist with legislation, which however also recognised self-regulation.

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21 Laine 1998, pp. 46-47.

I have perceived, in a somewhat unorthodox manner, the self-regulation of electronic commerce to mean any instruments not having been produced by governments in their legislative capacity (*acta jure imperii*).[22] Self-regulation can be national or international. Yet this does not seem to be the ´universal´ view on self-regulation, which is more technical. The UN/CEFACT Recommendation 32, E-Commerce *Self-Regulatory Instruments (Codes of Conduct)* lists namely four distinct types of legal solutions to provide legal certainty and security and to create trust in electronic commerce. These four are 1. national legislation, 2. international legal instruments, such as conventions, treaties, directives or alternative resolution schemes, 3. contractual solutions, such as Recommendations 26 and 31 of UN/CEFACT[23], and 4. the process of self-regulation including co-regulation.[24]

The UN/CEFACT view is that with self-regulation, businesses involved in electronic business voluntarily undertake to comply with certain rules of conduct when dealing electronically with others. Self-regulation can take different forms, e.g. adopting a code of conduct or participating in a national or international trustmark[25] scheme. However, this is not a contractual solution.[26] Legally speaking, the provisions of self-regulatory instruments are not enforceable contractually, but companies acting against them may easily be held liable for misconduct. The UN/CEFACT Recommendation is looking forward to a time when self-regulatory instruments meet certain basic criteria, and even to an international accreditation of self-regulatory instruments.[27] If this happens, the common principles contained in these soft law instruments may start crystallising into generally accepted legal principles (see *infra* on the legitimacy of the *lex mercatoria*).

Governments can promote the use of self-regulatory instruments and create ones for themselves for the management of e-government. The government can also act as a mediator. When the government assumes a regulating role but leaves parts of the scheme to be determined by the business community, one can talk about ´co-regulation´.

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22 So it is more or less the same as soft law. Messrs Jon *Bing* and Olav *Torvund* define self-regulation in a similar manner "as regulation prepared by someone other than the legislator, or someone who has obtained a delegated legislative right" (Self-regulation of Electronic Commerce in the Nordic Countries, p. 11).

23 The UN/CEFACT Model Interchange Agreement and the Model E-Agreement respectively, see Chapters III and IV, *ante*.

24 Another definition with a practical orientation is from the Swedish ICT Commission, which defines self-regulation in its report (available at http://www.itkomissionen.se) as "actions of systematized form, which will be taken by a company, a group of companies, a sector or the whole business life in order to clarify or solve problems in relation to consumers or other customers" (Self-regulation of Electronic Commerce in the Nordic Countries, p. 11).

25 Trustmarks are used to increase consumer confidence in the electronic marketplace. Companies commit themselves to following a certain code of practice in their activities and gain thereby the right to use the mark. Besides safety for consumers, these marks also establish practices and services for companies. For instance, the Norwegian *Nsafe* and the Danish *E-handelsmærket* offer dispute settlement, whereas the Finnish *SafeShop* offers insurance (Self-regulation of Electronic Commerce in the Nordic Countries, p. 14).

26 UN/CEFACT Recommendation 32, p. 2.

27 Ibid.

The rise of the Internet gave the opportunity to conduct electronic business technically without an interchange agreement. Legislative measures were needed to boost and regulate this development. However, legislative instruments also recognise the role of self-regulation. Article 16 of the Directive 2000/31/EC on electronic commerce obliges Member States and the Commission to encourage the drawing up of codes of conduct at the Community level, by trade, professional and consumer associations or organisations, which are to be designed to contribute to the proper implementation of the relevant articles of the Directive. The Commission has been working on a draft guideline which would tell what good self-regulation means.

One reason for self-regulation is that it is considered more flexible than traditional legislation since it can be changed and adapted to existing circumstances more easily than international conventions.

The UN/CEFACT Recommendation makes the Model Code of Conduct for Electronic Commerce of the Electronic Commerce Platform the Netherlands of 1999 a virtual benchmark of electronic commerce self-regulatory instruments.[28]

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[28] The principles set out in the framework for a code of conduct are the following ones:

- Signing parties shall state that they comply with the code of conduct;
- By giving definitions of certain terms occurring several times in the code of conduct, the signing parties shall increase the clarity and readability of the code;
- Signing parties shall clearly indicate the scope of their code;
- Signing parties shall focus attention on consumer relations;
- Signing parties shall focus attention on the way in which the code of conduct is enforced;
- Signing parties shall refrain from giving out misleading and/or incorrect information;
- Signing parties shall state that they recognise electronic communication and that they will accept electronic communication in legal proceedings (in court or otherwise);
- Signing parties shall assure the reliability of systems and organisation;
- Signing parties shall give clarity regarding demands for information and administrative organisation;
- Signing parties shall refrain from activities capable of jeopardising the availability of electronic information and communication systems;
- With regard to electronic signatures, the signing parties shall arrange what reliable forms and technologies they accept and use for electronic signatures, the verification of an electronic signature, the quality standards imposed on third parties, and the responsibility for the confidentiality of the electronic signature;
- Signing parties shall focus attention on the identifiability and origin of their commercial communications;
- Should a signing party apply an opt-in or op-out facility, it shall give clear information thereon;
- Optimal transparence of information is called for concerning the party offering services or products, concerning such services or products, the offer and the conditions applied (in total 20 items);
- Signing parties shall respect the privacy of the other party and shall indicate the way in which they will do so;
- To promote trust in their electronic commerce activities, signing parties shall indicate that they will respect the confidentiality of confidential information received from the other party and that they will take measures to ensure this confidentiality; and
- Signing parties shall respect intellectual property rights.

See also Annex II of the Report of the expert group on B2B Internet trading platforms, Final report to the Commission, 2003, which contains a checklist to assess whether a code of conduct for such a platform sufficiently meets the objectives of fair trade.

X.1.5 Are there general principles of electronic commerce law?

Electronic commerce law is part of other commercial law. Therefore the legal principles applicable to commercial law are equally applicable to electronic commerce. This leads us to ask whether electronic commerce itself contains general principles.

There are, in my view, no or few general principles that would be unique to electronic commerce. The basis for this assumption is that computerisation simply presents a new method for communication. The complicated or expensive technology does give, in any case, a chance to outline a few of working principles that appear to be common to the electronic commerce regulation instruments created thus far. These principles are practical necessities today and may wither away as preparedness to use electronic media grows. The principles are partly legal, partly operational. Doubt may therefore be expressed, whether the principles are such that they could be resorted to as sources of law without any authorisation from the parties.

Should such principles exist, they could be resorted to as an independent source of law in arbitration and perhaps in other forms of out-of-court dispute settlement. It should be remembered that common legal principles meet the criteria of even the narrowest descriptions of *lex mercatoria* (excluding, of course, those ´narrow´ views that consider it nonexistent). Finally, general principles are used to interpret and fill in gaps in international conventions. The UNCITRAL preliminary draft convention on electronic contracting contains in its latest form a provision similar to Article 7(2) of the CISG that refers to general principles on which the convention is based as a means of tackling unsolved questions concerning matters governed by the convention.[29]

The elevation of such principles is the task of arbitrators and legal literature. The principles may evolve in the course of technological developments. I will nevertheless point out some regularities that could gain the status of principles, unless they are admitted to have that status already. I certainly cannot be exhaustive – what is more important is the idea that such principles might exist, and if they do to discover what the method of establishing them would be and what their implications are.

To start, one has to mention the principle of functional equivalence, which is the drafting approach of the UNCITRAL Model Law on Electronic Commerce and lays down in essence the foundations for the documentary provisions in the eUCP and in INCOTERMS 2000. Functional equivalence means that electronic commerce techniques fulfil the same functions or purposes as the traditional paper-based requirement. Functional equivalence can be established by law (e.g.

[29] The latest draft is contained in Doc A/CN.9/WG.IV/WP.108, 18.December 2003. The relevant provision in the draft is Article 6(2).

the US UETA) to cover relevant areas such as evidence. Such provisions are affirmations that functional equivalence exists in these areas. Article 16 of the UNCITRAL Model Law on Electronic Commerce gives a non-exhaustive list of actions in transport law that are subject to the functional equivalence provision of Article 17(1). In Nordic countries, courts are presumed to reach the same conclusion by applying general principles of law, which effectively contain functional equivalence.

Functional equivalence is often, however, more of a legislative or drafting approach or technique rather than a principle. As a drafting technique, it should not be imperative. The electronic world, once it matures, could create ´new animals´ that need not slavishly imitate the paper-based world. The practical implication would be that electronic instruments would have to be assessed in accordance with principles applying to them, and the paper-based instruments would not serve as immediate analogies.

Obviously, electronic communication methods require special technology. The legal rules for electronic commerce are, as a rule, neutral as to the technical standards or methods of communication. This is largely because in this way they are not presumed to hamper technological developments. This inevitably leads to the relative superficiality of legal provisions, which in turn makes them more difficult to approach. The essential technical provisions laid down by the practice have to amend the general provisions.

The use of electronic media requires the consent of the parties. This principle may be found in legislation[30], but more particularly in standard rules. Such a provision is found in the US Uniform Electronic Transactions Act (UETA). INCOTERMS2000 requires consent from the buyer for the seller to be able to deliver an electronic transport document. Moreover, the use of electronic presentation of documents under the eUCP requires an agreement by the parties. Similarly, the draft Instrument of transport law under preparation in the UNCITRAL Working Party on Transport Law presupposes an agreement between the parties. The CISG AC also builds on this principle but adds that the consent has to apply in respect of the type, format and address of the electronic communication.[31]

This observation gives rise to the related issue that in business relationships there is a tendency to presuppose contractual arrangements to communicate electronically. An alternative would be to look for an implied agreement, which can be contested if the principle is fixed too rigidly. Parties may conclude an interchange agreement. Such arrangements are often a practical necessity, because the law may be silent on e-commerce issues, and technical aspects call for the adoption of necessary protocols.

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30 A provision to this effect is found in Article 8(2) of the UNCITRAL prelimary draft convention on electronic contracting as contained in Doc A/CN.9/WG.IV/WP.108. This draft provision should not be interpreted as denying electronic communications any validity in the case that there is no consent on the part of the addressee. National law shall determine whether an e-mail reply to an offer made by traditional mail should be taken into account or not. See doc A/CN.9/546 para. 43.

31 See Chapter X.1.5., *post*.

The draft Instrument of transport law presupposes that parties use ´rules of procedure´ such as the *Bolero Rulebook* in order to use electronic transport documentation, in particular those aiming to constitute documents of title. If legislation is to build on this prerequisite, the use of electronic negotiable instruments will require, in practice, that third parties enter such contractual arrangements or rules of procedure, or that their interface with third parties, such as users of other platforms, is arranged in some way.

A corollary to an agreement to communicate electronically would be a prohibition from using other means of communication. If such an agreement is an express one, courts in countries where freedom of contract applies would probably enforce it. On the other hand, where there is no express prohibition from using other media, an assumption should be that data messages are simply one more method for the parties to communicate, and so there is no obligation to use electronic media consistently throughout the contractual relationship even where the contract had been concluded electronically. This follows, in my view, from general contractual principles and the purpose of electronic commerce legislation.[32] Thus various notices required by law, e.g. a notice of non-conformity of the goods under Article 39(1) of the CISG, can validly be given by any medium.[33] The particular media has an impact, however, when requirements of singularity and uniqueness (being more or less equivalents of original in the paper-based world) for records or documents come into play.

If, under general contract law, rules forcing a party to communicate electronically are nonexistent, in practice, however, commercial terms often dictate a transition to an electronic means of communication. A car or a mobile phone manufacturer is usually a good persuader of its suppliers.

The use of an electronic medium may become obligatory in many ways. In public procurement, contracting authorities or entities could make electronic

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[32] A provision to this effect is contained in Article 9(1) of the UNCITRAL prelimary draft convention on electronic contracting as contained in Doc A/CN.9/WG.IV/WP.108. In integrated trading platforms, however, the consistent use of an electronic medium is a practical necessity.

[33] Cf. the ICC´s remarks contained in the Note by the UNCITRAL Secretariat, Doc A/CN.9/WG.IV/WG.101, which raised the problem of the status of GSM notices in the context of electronic commerce. As far as the CISG is concerned, written form is not needed, unless the contracting state concerned has made a reservation pursuant to Article 96 of the Convention to require written form for sales contracts. Jurisdictions which have adopted legislation equating electronic communications with writing allow for notices in the context of electronic commerce to be made by electronic means. The UNCITRAL Model Law on Electronic Commerce includes telefax within its scope. The question then remains, in my view, whether media using telephone technology produce a record equal to a written document.

communications (submission of tenders etc.) exclusive according to the brand new EC legislative package.[34] Public procurement deals are ultimately concluded as commercial agreements but the terms of the agreement are largely fixed in one of the alternative procedures, the purpose of which is to safeguard competition. The public procurement processes are in a way parts of the contract formation process. Similarly, in purely private contracts, a party inviting offers may fix the medium which is to be used. The issue of dematerialised equity and debt instruments provided by law in some countries, e.g. Finland, is non-voluntary as well.

There is a danger that emphasising the need of the parties to agree to electronic communication becomes a straitjacket. Computerisation has gained enough ground to let the EU allow stringent competition law effects be based on the requirement of exclusively electronic media in public procurement. The tendency of modern international legislation such as the CISG is not to lay down form requirements. If electronic contracts are like any other contracts, why then establish specific consent requirements for one method of communication? My prediction is that the requirement that the parties must agree to the use of electronic communications will water down in the future in jurisprudence, or that an implied agreement is interpreted to exist in most cases.

For the next decade or so, electronic trade documentation, once it gains ground, will coexist with paper documents. This coexistence will require rules on the interrelationship between the two methods of communication. Such rules are, for instance, the already mentioned guarantee of singularity and uniqueness provided for in Part II Chapter 1 of the UNCITRAL Model Law on Electronic Commerce. The Model Law provides rules on how to "drop down" from the use of electronic records to paper documents. Similar rules exist for electronic trading platforms. No uniform view exists as to who can choose the medium.

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[34] See Directive 2004/18/EC of 31 March 2004 of the European Parliament and of the Council on the Coordination of Procedures for the award of public works contracts, public supply contracts, and public service contracts, OJ L 134, 30.4.2004, p. 114 ; and Directive 2004/17/EC of the European Parliament and of the Council coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors, OJ L 134, 30.4.2004, p. 1.

According to Article 33 of Directive 2004/18/EC, contracting authorities shall use solely electronic means in accordance with Article 42 (2) to (5) to set up a ´dynamic purchasing system´ and to award contracts under that system. Article 42 deals with rules applicable to communication. The contracting authority may choose the means of communication, including an electronic medium.

The obligation of tenderers to use an electronic medium of communication is balanced by general requirements. Paragraph 2 of Article 42 states that "(t)he means of communication chosen must be generally available and thus not restrict economic operators´access to the tendering procedure". Furthermore, paragraph 4 adds that "(t)he tools to be used for communicating by electronic means, as well as their general characteristics, must be non-discriminatory, generally available and interoperable with the information and communication technology products in general use".

As soon as parties are capable of meeting these types of technical and commercial criteria, one could perhaps consider that an adequate infrastructure exists and recognise unauthorised electronic communications even in purely commercial relationships where no consent to their use could be said to exist.

Due to the lack of convergence of messaging technology and software, parties need to accept an adopted format e.g. by adding to their contract applicable specifications and appendices relating to the technical issues of interchange. A failure to act in accordance with such specifications may lead to substantive contractual consequences. For instance, where documents have to be presented under a commercial letter of credit in a specified technical format, the presentation in some other format will not qualify. Thus, as a matter of fact, the reduction of legal formalism will be replaced by technical formalism. Once the initiative towards the convergence of message standards succeeds, this phenomenon will gradually disappear and increase interest in electronic commerce.

Some basic rules of interchange are also so regular that they may amount to general principles. For instance, where the message is accessible to the receiver in his computer, it has been received by him. This fact has, as noted earlier, contract law implications. In my view, the reception rule should be regarded as a general electronic commerce principle, although it seems to be still contested by some participants of international lawmaking. The need to log and store data could easily be regarded as a principle, since electronic records cannot, practically speaking, be used as evidence otherwise, although these are equally standard contract law provisions. The demand is growing under e-commerce legislation that electronic contract terms and general conditions provided to the recipient must be made available in a way that allows him to store and reproduce them. The need for making the conditions available in all cases still remains an issue. On the other hand, the requirement to acknowledge receipt without a request to do so would not amount to a principle according to contemporary contract practice. Commercial practice, once clearly established, will gradually crystallise into unwritten, then perhaps written, legal principles.

X.1.6 Can electronic communication methods shape new substantive law?

In the introductory paragraphs of this chapter, the possibility of the emergence of a ´third stage proper´, that is, a new substantive law created for electronic commerce needs, was admitted. The next question would be whether such substantive law could apply outside the electronic commerce context. The International Chamber of Commerce, which participates in the work of UNCITRAL Working Party IV (Electronic Commerce), advocates the idea that no special framework just for electronic contracts should be created since different communication methods will exist side by side. However, should the rules designed for electronic commerce be pragmatic[35] enough, this would increase the use of electronic media.

It is assumed that the rise of electronic commerce will have some impact on substantive law in general. Electronic means of communication make it possible for the parties to communicate practically instantaneously. The Internet makes it possible to verify information even “on the spot”. When the amount of

[35] E.g. that incorporation by reference would be generally better recognised.

information increases during contractual performance, it may lead to increasing performance requirements and the elimination of the existence of good faith. These consequences of the technological revolution do not necessarily lead to the revision of the letter of the law, but impact how practical requirements e.g. in respect of contractual notifications evolve.

When the ABA Model Trading Partner Agreement was created in the late 1980s, the reception rule was chosen to govern the point of contract formation instead of the traditional Anglo-Saxon postal rule. The reception rule seems to be the predominant solution at an international level and, probably, at the EU level as well despite the doubts referred to *supra*.

The use of electronic signatures may ultimately lead to elevated requirements for form and authenticity in areas such as expressions of will in contract formation, where free assessment of evidence has prevailed in many jurisdictions. If one exaggerates and dramatises somewhat, history is creating a paradox in the flow of form requirements between the continents. The English Statute of Frauds from 1677 required a written form and a signature to conclude a sales contract. This Statute later became a part of many state laws in the United States, under the legal culture of which the concept of electronic signature, especially the sophisticated digital signature, was created. Thus, over three hundred years later, although the Statute of Frauds has been repealed in Britain, it has come back to the Old Continent in the form of an emphasis on the role of signatures and, in particular, digital signatures in legal transactions.[36]

It remains to be seen to what extent the ´advanced electronic signature´ envisaged in the EC Directive will be used in practice. Its use will add safety to commercial transactions, which goes beyond what has been the practice so far. Documentary credits are often used in dealings with countries that have bureaucratic foreign trade stipulations. Yet the UCP do not require, as a general rule, any signature in the invoice. Directive 2001/115/EC takes, on the contrary, a qualified electronic signature as a presumption.

The concept of the attribution of data messages, as contained in Article 13 of the UNCITRAL Model Law on Electronic Commerce and as relied on by electronic signature legislation, may add some elements of agency to the use of authentication methods.[37] Aspects of agency may also be connected with the notion of the ´originality´ of documents.[38] It could be that agency and electronic commerce laws could be intertwined.

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36 Cf. On the other hand, UCC Article 1, § 1-201(39)(19999 allows for a variety of methods for signing a document.

Legal history knows the phenomenon of the ´reception´ of foreign law. It is notorious that the French Code Civil found its way to the written laws of a number of countries. The same goes for the English common law in respect of the British Commonwealth. Reception can also take place in respect of legal institutions originally alien to the legal culture of the receiving country. Stoppage in transit was introduced to German and French laws by the CISG.

37 The legislators will have to determine whether to rely on traditional agency laws or laws regulating the question of who can sign documents on behalf of a company or other legal person or whether to create separate provisions for the use of electronic signatures. On this question, see Digital Signatures, p. 105.

38 See the Bolero Rulebook, Rule 3.11(2).

In the field of international trade and transport, the CMI Rules for Electronic Bills of Lading adopted in 1990 do not address the proprietary functions of bills of lading. This aspect could be tackled by legislation in the future. Electronic bills of lading or electronic bills of exchange to be created, based on a central registry, imitate even ´bearer´ instruments by electronic means by keeping confidential recorded ´to bearer´ transfers.

Another development might be a new idea of negotiability. The idea of functional equivalence presupposes that the functions of traditional trade instruments will be transformed into an electronic medium as such. Since possession of an instrument no longer exists as such, rights symbolised by an electronic instrument may start to transform from traditional property rights into something else, such as a debtor-creditor or other contractual relationship. This may already have an effect on the rights of third parties and the transferee.[39] Will there be legitimacy to protect the good faith of a transferee, maintaining at the same time the abstract nature of the instrument, if there exist claims on the rights symbolised by the instrument that could very easily be recorded and verified by book-entries into and searches from a central registry?

In letter of credit law, electronic presentation of documents authenticated by an advanced electronic signature could eradicate some fraud, in particular the forgery of documents. This would be a very significant development. Banks relieved from a manual scrutiny of the face of the document could, if there is demand, verify facts[40] from registries with the same level of diligence as when documents are checked.

One can wonder whether the consequences for the failure to deliver documents or electronic records with their data content in accordance with the requirements of law and contracts would be practically the same. Could we still talk about a separate obligation to deliver the documents, with a failure to do so amounting to a fundamental breach of contractual obligations? I believe it all depends on whether electronic records will eventually carry out the same functions as the possession of a piece of paper does today.

Together with the thus far relatively imaginary decline of the use of paper documents, documents as such seem to be losing some of their legal functions. The right to control the goods in transit covered by a non-negotiable transport document is, in the case of modern maritime transport codes, no longer tied to the possession of a particular copy of the transport document.

It is presumed that the transition to electronic commerce could eradicate, to some extent, the obligation of the seller to deliver (electronically) the relevant

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39 Cf. Article 9.1.9 of the UNIDROIT Principles 2004 of International Commercial Contracts, which gives an assignee in good faith the right to benefit from the assignment, if there is an agreement prohibiting assignment. However, the obligor may assert against the assignee all defences that the obligor could assert against the assignor (Article 9.1.13). Thus, in the contractual world not using documents of title, there would be no ´estoppel´.

40 E.g. they could check that an electronic negotiable instrument is recorded in a registry, the rules of procedure of which transfer title to the buyer or that the conditions of carriage incorporated by reference, or rather made available, contain certain elements required by the credit.

commercial documents. The transition to electronic means of communication may undermine the notion of a ´document´ as we know it now. For instance, in a transport contract, information about the status and condition of cargo could be obtained more often in real time, which reduces the essence of documents as carriers of information, at least in practical terms. It could perhaps be better to concentrate on the meaning of a document as "a set of data content recorded as such". This data content could in theory be amended throughout the course of the delivery process.

Finally, one must recall *Mallon´*s vision of the disappearance of electronic messages which identicelly replicate paper documents and which are being replaced by central databases where, particular fields are populated by users.[41] The disappearance of the document as a means of communication may lead to the readaptation of legal rules assuming the use of documents.

I believe that there could one day be a tendency to regulate, in lieu of the transfer of documents, the transfer of information – the data content - in connection with the sale. Therefore a failure by the seller to deliver information, e.g. by populating fields in a register, given by third parties (carriers, insurers, officials etc.) will be sanctioned in the same way as the failure to deliver the prescribed documents under contemporary law. But as long as traditional paper documents exist side by side with electronic records, no revised volume of the INCOTERMS will talk about information instead of documents and records.

X.2 The *lex mercatoria* as a source of international trade law

The question was posed above whether the *lex electronica* will shape new substantive law. One could also ask whether some aspects of substantive law will be enhanced by electronic commerce. An assumption made in this study is that incorporation of substantive rules, together with rules of communication, recording and contract formation (constituting today´s *lex electronica* proper) will accelerate the move towards harmonious sources of substantive law, in other words, the *lex mercatoria*.

X.2.1 How to define *lex mercatoria*

It is impossible to review all the definitions of *lex mercatoria* that have been suggested through some four decades. I will therefore mention just a few very representative and characteristic ones. The discussion on the emergence of a new *lex mercatoria* started namely in the early 1960s. Clive M.*Schmitthoff* argues in a

[41] These visions are reflected in the plans for SWIFTNet Trade Services Utility, see Chapter VIII.7.5., *ante*.

publication[42] that compiled the presentations in a major international conference on international trade law as follows:

> "If all sovereigns agree, subject to certain reservations, to recognise and admit the universal custom of the businessmen as a law-creating agency, the striking similarity in the law of international trade in all national legal systems,..., might, in fact, find its explanation in the derivation of that law from a common source. This new *lex mercatoria* might be the beginning of an autonomous international mercantile law which would be no longer fashioned by the principles of national law. The evolution of an autonomous law of international trade, founded on universally accepted standards of business conduct, would be one of the most important developments of legal science in our time."

Schmitthoff considered *lex mercatoria* to be an expression of both spontaneous and official unification by means of general conditions, trade usages, custom and international conventions. Even national law and case law would, in some instances, amount to *lex mercatoria*. Schmitthoff was an advocate of a wide conception of *lex mercatoria*.

Probably the most cited proponent of the notion of *lex mercatoria* is still Berthold *Goldman*,[43] who claimed that in international commercial arbitration, arbitrators and parties could detach legal relationships from applicable national legal rules and submit these relationships to the *lex mercatoria*. Goldman was, by and large, in favour of a narrower scope of the *lex mercatoria* than Schmitthoff. In his view, the *lex mercatoria* "comprises rules the object of which is mainly, if not exclusively, transnational, and the origin is customary and thus spontaneous".[44] In this way, it is made of usages of international trade which become customary rules and general principles of transnational law.

Lando[45] especially mentions public international law[46], uniform laws, the general principles of law, the rules of international organisations, customs and usages, standard form contracts and reported arbitral awards as sources of *lex mercatoria*, although he considers that it is not possible to provide an exhaustive list of all the elements.[47] Lando thinks that there can be combinations of *lex mercatoria* and national law. National law provisions cannot be of a mandatory character. However, ´directory´ rules, which can be derogated from by a contract, can fill in the gaps the *lex mercatoria* leaves open.

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42 Clive M. Schmitthoff, ´The Law of International Trade, its Growth, Formulation and Operation´ in Schmitthoff (ed.) The Sources of Law of International Trade, Norwich 1964, pp. 3-41.

43 This is justified since Goldman was one of the first proponents of the notion in his article (Goldman 1964).

44 Goldman 1987, p. 113.

See also references in Sandrock, O., Die Fortbildung des materiellen Rechts durch die Internationale Schiedsgerichtsbarkeit., note 7 on page 75.

45 The *Lex Mercatoria* in International Commercial Arbitration, (1985) 34 ICLQ, pp. 749-752.

46 The inclusion of public international law is criticised by Mustill (see *op. cit. infra*), who does not think it would constitute a sound basis for international commercial law. In my view, there are similarities in the methods and sources of public international law and the *lex mercatoria* since unwritten legal principles and usages play an important role in both of them.

47 Ibid., p. 749. Lando refers here to the works of Fouchard, ´L´arbitrage commercial international´ (1965) Nos 575-630, and ´L´arbitrage international en France après le décret du 12 mai 1981´, (1982) 109 Journal du Droit International (Clunet) 374, 394 *et seq*.

For Lando, the *lex mercatoria* seems to be as much a method of approaching legal problems as a uniform legal system. He states[48]

> "(s)ome authors have conceived the law merchant as the world law. However, it need not be the same all over the world. The arbitrator will tend to confine his investigations to those legal systems which are connected with the subject-matter of the dispute. Where they have a common rule or rules leading to the same result, the arbitrator will be obliged to follow the common core of these laws, although other systems may provide a different solution.

In Lando´s view, the arbitrator must often seek guidance from sources other than the law merchant, which usually means national laws.[49] Sometimes he must invent a new solution and thus act as a social engineer. In this way, an inventive arbitrator differs from legalists, who try to bring the case before them under the proper provision or precedent. Instead, he views the case in all its different aspects, weighs the opposing considerations, and makes his choice. The strict application of national laws, many of which may be connected to the dispute and lead to different results or be ill-suited to international business transactions, might in turn lead to unequitable results.

The theories on the *lex mercatoria* put forward found support in French-speaking Europe and partly in the Netherlands. Lawyers in Germany and in common law jurisdictions were generally hesitant, reluctant, sceptical or hostile towards the theory.[50] Lord Justice *Mustill´*s writing ´The New Lex Mercatoria: The First Twenty-five years´[51] is probably the most well-known critical account of the doctrine but, at the same time, also a very good analysis of the writings and case law up to the end of the 1980s. Therefore it has received attention in many writings thereafter.

Mustill reviews the characteristics of the *lex mercatoria* as put forward by the proponents of the doctrine. The *lex mercatoria* is anational meaning, first, that international commercial contracts are not, in the absence of an express choice of law, directly derived from any one body of national substantive law and, second, the rules of the *lex mercatoria* have a normative value which is independent of any national legal system. Mustill creates a distinction between legal

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48 Ibid., p.750. Lando uses the differences between the Danish Sale of Goods Act and the CISG as an example. Under Danish law, notice of late delivery had to be given immediately whereas under the CISG it must be given within a reasonable time. When the arbitrator can apply the *lex mercatoria*, he or she is not bound to rigid rules designed for domestic sales, but can take into account the international nature of the transaction. (After the article was written, Denmark implemented the CISG in its legislation and the problem no longer exists).

49 One of the working methods is the cumulative application of conflict of laws and substantive rules.

50 De Ly in Towards a European Civil Code, p. 41.

A typical Anglo-Saxon view is that of *Wood*, who states (on p. 20) that "(s)ome writers think that there is a special system of transnational commercial law known as *lex mercatoria* which is a synthesis of generally held commercial principles applying to transnational contracts and separated from any domestic system of law. In practice *lex mercatoria* is perhaps no more than an expression of the increasing uniformity of commercial laws in the major jurisdictions and of a judicial tendency to uphold international contracts."

51 4 Arbitration International (1988) pp. 86-119.

harmonisation and the *lex mercatoria* as understood by its proponents. The *lex mercatoria* is contractual, and such testing points of transnational law as status, capacity, consent and rights *in rem* (transfer of title in corporeal assets or pledge) [52] are usually not affected by it. The *lex mercatoria* is not invoked in cases of pure delict. The fact that the laws of all states cannot be taken into account has led to the relativisation of the doctrine and the emergence of a *´micro´ lex mercatoria*, which need not be the same all over the world.

A conspicuous distinction among supporters is how the *lex mercatoria* comes to govern an individual transaction. One concept is that of a standing body of legal norms, which automatically applies *ipso jure* to every transaction within its purview, unless excluded. The other approach is that ´the *lex*´ provides ´a repertoire of rules´ available to those parties who, expressly or by implication, choose to incorporate them into their dealings, and who, by the same token, choose to detach their contracts from national law. Another theoretical distinction is whether an arbitrator settling a dispute simply uncovers the *lex* as it is, or whether he creates law. Mustill further asks whether prior awards based on the *lex mercatoria* should be followed or not.

Mustill goes through the cited sources of the *lex mercatoria* on the basis of Lando´s list (see *supra*) and adds his comments to each of them. His practical addition covers the public policy of the country in which the enforcement of the arbitral award is sought. Mustill mentions 20 different principles[53] appearing in

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[52] Under English law itself, the creation of documents of title takes place through established custom, although conceptually such custom forms part of English law.

[53] These are (in edited form):

- *pacta sunt servanda;*
- an exception to this in long term contracts is *rebus sic stantibus*;
- another exception to *pacta sunt servanda* is the abuse of law and that unfair and unconscionable contracts should not be enforced;
- there may be a doctrine of *culpa in contrahendo*;
- a contract should be performed in good faith;
- a contract obtained by bribes or other dishonest means is void, or at least unenforceable; similarly a contract is unenforceable if it creates a fictitious transaction designed to achieve an illegal object;
- a state entity cannot be permitted to evade the enforcement of its obligations by denying its own capacity to make a binding agreement to arbitrate;
- the controlling interest of a group of companies is regarded as contracting on behalf of all members of the group, at least so far as concerns an agreement to arbitrate;
- ´gold clause´ agreements are valid and enforceable and in some cases either a gold clause or a ´hardship´ revision clause may be implied;
- where unforeseen difficulties intervene in the performance of a contract, the parties should negotiate in good faith to overcome them, even if the contract contains a revision clause;
- one party is entitled to treat itself as discharged from its obligations if the other had committed a breach, but only if the breach is substantial;
- no party can be allowed by its own act to bring about a non-performance of a condition precedent to its own obligation;
- damages for breach of contract are limited to the foreseeable consequences of the breach; >>

arbitral practice, which he considers to be a "rather a modest haul for 25 years of international arbitration".[54]

There is no uniform perception of what the *lex mercatoria* means among those who advocate it. As *Goode*[55], another critic, puts it "no two writers are agreed on its meaning". Goode states that to some "it denotes the totality of law governing cross-border transactions, whether derived from usage, general principles of law, conventions, uniform rules effectuated by contractual incorporation, or even standard-term contracts", and adds: "this is more or less what transnational commercial law is all about".

For *Goode* himself, the *lex mercatoria* should make up the prescription for unwritten commercial law. It would consist of customary commercial law, customary rules of evidence and general principles of commercial law, including international public policy.[56] In Goode´s argumentation, the *lex mercatoria* derives its force from the common understanding among commercial men, although there may be compilations of the *lex mercatoria*. In both situations, the *lex mercatoria* supplements or replaces the applicable domestic law as determined by the rules of the private international law of the forum state.

The view of seeing the *lex mercatoria* as a complementary source of law is also reflected in *Lowenfeld´*s arguments. He mentions some cases in his arbitral practice and adds that in each case "*lex mercatoria* supplies the solution to a particular issue, without necessarily governing all aspects of the transaction". In his view, "the *lex mercatoria* can furnish an alternative to a conflict of laws search which is often artificial and inconclusive, and a way out of applying rules that are

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<< -damages for non-delivery are calculated by reference to the market price of the goods and the price at which the buyer has purchased equivalent goods in replacement;

- a party which has suffered a breach of contract must take reasonable steps to mitigate the loss;

- a party must act promptly to enforce its rights, on pain by of losing them by waiver;

- contracts should be construed according to the principle *ut res magis valeat quam pereat* (it is better for a thing to have an effect, than to be regarded as void);

- failure by one party to respond to a letter written to it by the other is regarded as evidence;

- a debtor may in certain circumstances set off his cross-claims to extinguish or diminish his liability to the creditor; and

- a tribunal is not bound by the characterisation of the contract ascribed to it by the parties.

54 However Lowenfeld adds that "that could be said of the Ten Commandments or of the American Bill of Rights as well". He adds to the Mustill list the effect of unforeseeen events on a contract: classical contract law tends to think that a party is either completely discharged from its obligations or is fully liable, whereas the *lex mercatoria* as reflected in standard form contracts seems inclined towards suspending performance for the time of the interruption while preserving the underlying obligations, or towards apportioning losses from an occurrence that neither party caused or could have foreseen.

55 Goode, A New International Lex Mercatoria?, Juridisk Tidskrift 1999-2000, p. 253.

56 Ibid.

inconsistent with the needs and usages of international commerce and that were adopted by individual states with internal, not international transactions in mind".[57]

I personally prefer a comprehensive scope for the *lex mercatoria*, at the same noticing that it does not necessarily exclude the application of the law designated on the basis of conflict of laws rules. This is partly because the concept is more instrumental in that way. Arbitrators, conciliators (e.g. in ADR) applying law or, to the extent permitted by law, judges should be able to follow a line suggested by international instruments such as conventions, model laws, arbitral awards, international legal principles or interpretations on international instruments, to the extent this does not violate the parties´ express agreement. The rules of the arbitral institutions, at least those mentioned in this study, only require that the arbitrators follow ´rules of law´ when the parties fail to designate any sources of law. The advantage of the *lex mercatoria* is its flexibility and usefulness. Critics usually say that the *lex mercatoria* is vague whereas national law is developed. On the other hand, explicit *lex mercatoria* instruments may represent solutions that do not exist under national law as such. Especially when few legal materials exist under national law on new technical solutions or commercial concepts, international solutions should receive attention as models.

Counterbalancing the freedom as to the sources, the application of the *lex mercatoria* should be seen as a teleological method of interpreting legal rules in a manner that promotes uniformity in their appplication and consistency. Even state courts should follow this method when interpreting international instruments such as the CISG or the UCP.

X.2.2 The *lex electronica* as a part of the *lex mercatoria*

Key electronic commerce rules, such as the general admissibility of evidence in electronic form, may be regarded as general principles of law applied by the business community. Therefore the essence of the *lex electronica* could eventually be part of the *lex mercatoria*.

Where disputes are settled by arbitration, arbitrators are entitled, to a certain extent, to base their award on the *lex mercatoria*. This gives them an opportunity to use international legal materials on electronic commerce as sources of law. Parties could refer in their contract to the *lex mercatoria* or ´general principles of law´ with a view to giving the arbitrators freedom to choose the principles suited to the transaction. Even without this, as we have seen, arbitrators may apply general principles of law to some extent. A possible problem could concern form

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[57] Lowenfeld, p. 10. Lowenfelt cites Lando´s example of an unreasonably short time-limit for the needs of international trade contained in national law.

Goldman also sees the possibility of the lex mercatoria and national law existing side-by-side. For instance, questions of capacity could be resolved by national law, and other issues on the basis of the *lex mercatoria* (Goldman, Nouvelles réflexions sur la Lex Mercatoria 1993). See also Fouchard, Gaillard and Goldman on International Commercial Arbitration, Kluwer 1999.

requirements imposed by national law. As the assumption is, outside clear cases of illegality and where expressly contested, that parties expect their transaction to be valid, arbitrators could bring into application the rules of the UNCITRAL Model Law on Electronic Commerce, for instance, to supplement parties´ contractual arrangements such as an interchange agreement.

The discussion on the *lex mercatoria* arose when the law of international business transactions could no longer develop under a statutory framework. Party autonomy, and especially its procedural dimension in the form of international commercial arbitration, made it possible for the organs of the international business community to become recognised law-creating agencies. The emergence of electronic commerce law as applied to business-to-business relationships will also develop in the hands of the businesss community. This legislation generally gives way to party autonomy and out-of-court dispute settlement. Electronic commerce legislation is generally created with the intention to facilitate trade, not to create barriers. Therefore arbitrators and conciliators could easily apply the *lex mercatoria* method to dispute settlement and be inventors.

Furhermore, the *lex electronica* acts as a bridge to the use of harmonious substantive law. In fact, the notion has even been used to signify substantive Internet law.[58] In electronic commerce, the facilitating legislation is, as a rule, a result of international cooperation. This applies to the basic concepts and principles of contract formation. Therefore, there is no giant step to the use of uniform substantive law. Moreover, electronic commerce will be advanced frequently through the use of contractual arrangements, which are based on standardised models that bring uniformity with them.

X.2.3 The legitimacy of the *lex mercatoria*

The *lex mercatoria* is recognised as a source of law in arbitration, at least if referred to by the parties, whilst national courts generally apply national law in accordance with the conflict of laws rules of the forum. This distinction is slightly categorical since, for instance, trade usages are admissible sources of law in national courts, which is also justified by Article 9 of the CISG. National case law could therefore be seen as a supplement of the *lex mercatoria*.[59]

Where does the *lex mercatoria* then derive its legitimacy from? Parties are allowed to give the arbitrators the power to decide *ex aequo et bono* or according to the *lex mercatoria* itself. Arbitrators can in these situations disregard national laws including mandatory provisions, unless these are such laws which claim to be applicable irrespective of the law otherwise governing the contract.[60] Outside these situations they may use their party autonomy in not challenging the award. National courts give indirect recognition to the notion of *lex mercatoria* by refusing to set aside awards based on it.

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58 Matthew Burstein in Internet..., p. 28.

59 The website http://www.cisg.law.pace.edu/cisg/ (visited on 5.4.2004) contains CISG-based case law from various parts of the world.

60 Bonell 1996, p. 8. Bonell is referring to ´overriding´ mandatory laws within the meaning of Article 7 of the Rome Convention on the Law Applicable to Contractual Obligations. Another exception is transnational public policy.

National courts are bound by the prerogatives of national law. Harmonisation and unification bring international instruments such as the CISG within the ambit of national law. Parties are generally not allowed to make anational law such as the UNIDROIT Principles of International Commercial Contracts the (sole) law applicable to the contract in a manner that would be recognised by state courts. However, in accordance with the principle of party autonomy, parties can validly incorporate such principles contractually. Parties may expressly refer to a usage. An international soft law instrument can evidence such usage.[61]

There is a possibility that the clear distinction between arbitration and litigation could melt down as regards the possibility to apply anational law. There has been a suggestion[62] to amend the Rome Convention on the Law Applicable to Contractual Obligations to give the parties an opportunity to choose the UNIDROIT Principles as the governing law within the meaning of Article 3 of the Convention. The suggestion has been registered by the European Commission, which added it as one of the questions posed to the public in its recent Green Paper[63]. In the responses, business organisations generally have supported the creation of the possibility of choosing an international convention, but most governments have not. Still, it is an idea that, I believe, has not been raised for the last time. The other part of the Commission´s question concerned the incorporation of international conventions not in force in the *lex causae*. This possibility received support[64] and objections[65]. I believe these instruments could also be regarded as parts of the *lex mercatoria*, especially when they regulate with specificity issues not yet regulated under national law.

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61 See e.g. *S.A.Fabricom and S.A. Laurent Bouillet Ingéniere v. Générale de Banque and ACEC Union Minière*, 15 December 1992 (Revue de droit commercial belge 1993 II, p. 1055).

62 K.Boele-Woelki, ´Principles and Private International Law – The UNIDROIT Principles of International Commercial Contracts and the Principles of European Contract Law: How to Apply Them to International Contracts, Uniform Law Report 1996, p. 652.

63 Green Paper on the conversion of the Rome Convention of 1980 on the law applicable to contractual obligations into a Community instrument and its modernisation; COM (2002) 654 final, Brussels, 14.1.2003, pp. 22-23.

Question 8 reads: "Should the parties be allowed to directly choose an international convention, or even the general principles of law? What are the arguments for or against this solution?" For the question of parties choosing a convention directly, see X.5.2., *infra*.

64 The Netherlands considers that the choice of a convention in force between states other than that of the state of the forum or the *lex causae* should be allowed as a ´primary choice of law´ and the provisions of the Convention should even replace the mandatory provisions of the *lex causae*. Choosing general principles "will be regarded as less straightforward than a primary choice of law" (JAI/1031/03-EN/available at the commission´s website http://europa.eu.int/comm/justice_home/news/consulting_public/rome_i/news_summary_rome1_en.htm, visited on 19.2.2004).

65 The UK Government was opposed to both choosing an international convention and general principles of law. As regards conventions, it was said" (s)uch agreements do not generally contain the necessary supplementary rules covering matters as the formal validity of the contract, the burden of proof, the consequences of breach, the heads of damage recoverable and limitation". (statement available at the above Commission´s website, visited on 19.2.2004).

The *lex mercatoria* may be seen to have drawn its legitimacy from national law, as Goode has stated.[66] For instance, internationally accepted general principles of law are also part of one or other national legal systems constituting the objectively determined applicable law under traditional conflict of laws rules. The arbitrators are in fact applying a principle to be found in a relevant legal system; all that a choice of law clause does is to dispense with the need to identify the particular national legal system that is being applied.[67]

Lando represents the view that the *lex mercatoria* does not depend on the fact that it is made and promulgated by state authorities but that it is recognised as an autonomous norm system by the business community and by state authorities.[68] In the history of law, there have been many schools of law defining the nature of law. The historic school considered law to be a spontaneous phenomenon, born from the spririt of the people (Volksgeist). The sociologically oriented schools considered the law to be a social fact.[69] If the law is a social fact, it can, in principle, be examined empirically.[70] There are sociological, empirical and realistic schools of law, all of which give adjudication by courts and the implementation of legal rules (´law in action´) a role superior to written law (´law in books´).[71] Such schools give legitimacy to soft law as well.

In my view, the *lex mercatoria* represents first and foremost a useful repertoire of rules, which the parties or those responsible for adjudication may resort to. This resorting may take the form of a contractual incorporation or a complete substitution of the *lex causae* with these rules. The normative nature arises first from the usefulness and precision of the rules for a given situation. Those rules are being shaped all the time. There may be *´micro´ lex mercatorias* as dictated by the situation. The *lex mercatoria* could be compared to public international law. One could look at the obligation added to the CISG and other UNCITRAL Conventions, namely that "...regard is to be had to (its) international character and the need to promote uniformity in (its) application and the observance of good faith". The need to promote uniformity could be seen as a general objective

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66 Goode 2000, p. 266.

67 Ibid., p. 259.

68 Lando, (1985) 34 ICLQ, p. 752.

69 Goldman 1964, p. 190.

70 The *lex mercatoria* has been explained by applying the sociological theory of Georges *Scelle*, who argued that groups within society create their own legal rules, and for the business community this was the *lex mercatoria*. Another, jurisprudential theory of legal pluralism was developed by Santi *Romano*, who considered that legal systems are not monolithic but that various systems and subsystems coexist (De Ly in Towards a European Commercial Code p. 44; see De Ly, International business law and lex mercatoria, Amsterdam, 1992).

71 The sociological school of law in the United States included such names as Oliver Wendell *Holmes Jr*. and Roscoe *Pound*. The latter described jurisprudence as ´social engineering´ (cf. Lando *supra*) and emphasised the social effects of justice as the *Interessejurisprudenz* founded by Rudolf von *Jhering* during the 19th century did. The sociological school was followed by the school of realism.

The school of legal realism has given significance to psychological aspects, or have at least criticised doctrines which presuppose one deductible solution to each legal problem. The realistic school gained a strong foothold in Scandinavia at the beginning of the 20th century. The most well-known representatives of that school were Axel *Hägerström* and Alf *Ross*. One of the thoughts of that school of law was the relativisation of the concept of ownership. According to *Ross*, ownership could be divided into facts and consequences without having to define what ownership as a concept represents.

of the application of international trade law in general, and the scope of the obligation for such a teleological interpretation would be defined by the parties.

In addition, the emergence of the *lex mercatoria* may be part of the development procedure of law, with which I mean approximately the following course of events.[72] First, legal ideas emerge as solutions to individual needs, and these ideas find their way into individual judgements or contracts. They may also become parts of instruments of soft law including model contracts. Finally, they are codified in legislation, where this process has been found to be pragmatic.[73] The legislator seldom takes a solution out of a vacuum.

International conventions that have been agreed on universally almost certainly represent some form of common understanding among business or at least legal circles, although they may not be ratified. The fact that a convention has not been ratified, in turn, does not necessarily imply that it would be beyond such understanding. The reason may simply be the lack of resources under today´s fiscal policies in national administrations to look into these matters more closely (the disparate maritime transport conventions do not serve as good examples of understanding, however). In this path of development, legal positivism and formalism give way to an empirical conception of law. The binding nature of the law arises from the fact that it is observed, although this is a somewhat circular conclusion.

Despite the legal doctrinal dimensions of this discussion, a historical look into the development of law proves that there are, in any case, practical movements towards uniformity in international commercial law. This movement takes shape in the form of conventions, model laws, general principles of law, international standard form contracts and guidelines.

In the field of documentary credits, especially, a major part of the substantive law applicable to documentary credits has been harmonised through the cooperation of banks and other actors of the international business community under the auspices of the International Chamber of Commerce. It should not be forgotten either that important ´trading patterns´ such as those relating to the use of bills of lading or waybills, documentary credits, bills of exchange and the use of trade terms have evolved and been created in the custom of merchants through the centuries and have been adopted almost universally.[74]

There is a bounty of fruits of legal harmonisation or unification and thus no need to give the concept of *lex mercatoria* a purely ´metaphysical´ connotation. Legal harmonisation is a historical fact and is not a matter totally different from the existence of anational norms, since the fruits of harmonisation can be regarded as expressions of these norms. Harmonised instruments such as the CISG should be interpreted with regard to their international character.[75]

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72 Cf. the emergence of customary law on the basis of model contracts, X.4.4., *infra*.

73 In the US, the drafters of the UETA did not want to go into detail when addressing *transferable electronic records* hoping that contractual practice would show the way to go in future legislative efforts, see Brumfelt Fry, p. 5.

74 Grönfors, 1991, p. 28.

75 See Article 7 of the CISG.

A regional harmonisation exercise, European integration, may one day encompass the harmonisation of civil law. European Community law requires Member States to act in a manner which does not jeopardise the objectives of integration. The objectives pave the way for teleological interpretations of EC law. In the global context equally, the need for legal uniformity to lower transaction costs under the pressures of globalisation could become the driving force for a new legal order.

The business community itself is, by definition, a major creator of the *lex mercatoria*. The International Chamber of Commerce produced in its first two decades the Uniform Customs and Practice for Documentary Credits and the INCOTERMS. In the 1950s, the ICC suggested to the United Nations that a convention on the recognition and enforcement of foreign arbitral awards should be created. This led to the adoption of the 1958 New York Convention. Moreover, the success of the New York Convention gave impetus for the United Nations to establish the Commission of International Trade Law (UNCITRAL), presently a key formulating agency for international trade law. Not surprisingly, once the governments widely recognised international arbitration by adopting the New York Convention, views declaring the independence of the business community in norm creation through its own dispute resolution mechanisms grew more vocal.

The theory of the *lex mercatoria* is primarily a liberal theory aimed at freeing international commerce from the "particularities, parochialisms and anachronisms of national conflict and substantive rules and replacing these with uniform transnational rules".[76] The frontiers of states are, in an ideal situation, transparent. The ideology corresponds with today´s popular image of globalisation.[77] The EU´s push towards creating an internal market aims for similar objectives due to which parallels can be drawn between the *lex mercatoria* theory and European integration, most notably the harmonisation efforts of contract law.

The balance sheet of many multinational companies is larger than the economy of many individual national states. The freedom of the economic community to shape its own laws without major interference from governments is also akin to economic liberalism. In economic liberalism, the economy ends up in a balanced situation through its own means. The legal dimension of it would be that the fewer restrictions there are, the better the end result is for the entire society. Experiences like the *Enron* scandal in the United States may, however, discourage such beliefs.

Public international law is, in extreme cases, a result of the bargaining power of individual states. The same goes for the law between individual undertakings. A big manufacturing company can require its suppliers to be connected to it and with one another by EDI, use certain contractual terms in doing this or move to use electronic invoicing altogether. A long dominance in shipping and marine insurance gave the English Institute Clauses dominance in the field of cargo insurance.

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76 De Ly in Towards a European Commercial Code p. 44.

77 In Mustill´s view (p. 26), "(e)ssentially, the *lex mercatoria* is a doctrine of laissez faire".

The international business community needs harmonised trade practices. Harmonisation takes place in international organisations. Often, however, unity follows predominant commercial patterns rather than harmonised solutions established in international organisations. As the saying goes, "nothing succeeeds better than success itself". This can of course be problematic if the bargaining powers of the parties differ greatly.[78] The success of the Institute Clauses is no longer tied to the English maritime might. We can only wait for what may result from the establishment of the legal foundations of the *Bolero System* on English law.

National legislators, or supranational ones such as the EU, put limits to this law of the powerful by introducing competition laws and protecting the weaker party, even if a corporate party, with general clauses such as the UCC § 2-302. The EC Commission would like to safeguard that EU-wide standard contract terms to be promoted are sufficiently representative (see *infra*). Such measures, however, only partially restrain the rule-making activity of a dynamic international business community.

In fact, today´s governments see their role as merely being facilitators of commerce. The will of the legislator is generally to assist in the development of borderless trade, which is also one of the founding ideas of the European Union. It is submitted that intergovernmental organisations recognise this and partly shift their focus to non-statutory instruments. In terms of economics, dynamic companies are seen as engines of prosperity and development, and governments compete to attract them to maintain employment and the level of tax revenues.

These developments are behind the use of uniform legal rules. International conventions, model laws and sometimes even predominant national laws form part of transnational commercial law. Arbitral awards are a recognised source of anational commercial law. Moreover, in an increasing manner, self-regulation guidelines and contract practice embodied in model contracts establish the law. Every contract lawyer can therefore be seen as a ´grass-root legislator´. The *de facto* harmonisation through model contracts is sometimes referred to as ´modelling´.[79]

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78 Cf. Goldman 1964, p. 188: "les petits sont obligés de suivre les règles établies par les gros". Goldman adds at the end of his article: "il reste encore à veiller à ce que les intérêts don't elle poursuit la satisfaction demeurent suffisamment équilibrés pour garantir la légitimité de ses prescriptions. Mais ceci, aurait dit Kipling, est une autre histoire."

79 *Benabou*, p. 1 referring to A.Martin-Serf, ´La modélisation des instruments juridiques´ in ´La mondialisation du droit´ (under the direction of E.Loquin and C. Kessedjian), Centre for research on international markets and investment law (CERIMI), 2000, p. 178 ff.: "modelling, a means of standardization that comes from the bottom, that is to say the consumers of economic law, is opposed by its origin and nature to harmonisation, which is an approximation of legal systems based on a common political will, and it is also opposed to the unification of the various legal systems, the aim of which pursued by political authorities is to adopt identical rules" (translated).

I do not fully agree with the conclusion. No contract lawyer has the desire to see legislators refraining from making his life a little easier by directory legal provisions that would save him from being too explicit and would save, at least in the case of paper-based contracting, some trees.

The diversity of forms of transnational commercial law may be described with the concept of ´soft law´. The notion was originally used in public international law in the 1970s. From there it found its way to European Community law. Today, it is not uncommon to see the concept mentioned in the context of private or commercial law as well. An instrument of soft law is not binding as such. It shows a direction towards which parties or jurors can go when seized with a legal problem. Soft law can fill gaps (*lacunae*) in law.

If a soft law instrument represents sufficiently common legal values, it may become part of written law one day. In this way, soft law crystallises and becomes ´hard´ law. As the Electronic Platform the Netherlands code of conduct[80] notes "(e)-commerce businesses committed to a code of conduct can be challenged by customers to comply with that code. It cannot be ruled out that the standardization based on the code of conduct will become so generally accepted that it will be also enforceable by law".[81] The procedure is quite similar to how trade customs emerge from practices between individual companies (see *infra*). Legislators can also use soft law instruments to tackle legal problems. If that measure is not sufficient, hard law may follow.[82] In fact, what the Commission has recently suggested as the working method in the field of contract law harmonisation largely follows the above ideas.

This leads to the conclusion that there will be solutions which are created at any place, be it an intergovernmental or non-governmental organisation, a government or a company or university, that take predominance within a period of time.[83] These solutions are created by numerous potential formulating agencies of international commercial law, the observation of which is as much an empirical as a formal exercise.

X.3 Some key sources of substantive law for electronic commerce

The following list of sources of law represents some major sources of transnational commercial law, in my view largely the new *lex mercatoria,* which will undoubtedly be the substantive supplement to the rules of the *lex electronica*, or rather vice versa.

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80 UN/CEFACT Recommendation 32, p. 8.

81 In marketing, many governments have well observed that the initiatives of code creation by the private sector are good marketing practice. It is very easy for governments to turn them into mandatory law or jurisprudence, and the business community should have no objections to that. Similarly, the business community´s own guidelines of ethical content for the activities of multinational enterprises in the 1970s formed a basis for the OECD to adopt similar guidelines on a governmental level.

82 Directive 2002/92/EC of the European Parliament and of the Council of 12 December 2002, on insurance mediation, OJ L 9, 15.1.2003, p. 3 followed a recommendation which was found to be inadequate.

83 Trudel, p.4, considers that, within the networks, ´landmark principles´ are established which must be relayed by other rulemaking areas. Trudel states that the Internet is replacing the traditional legal system´s operation in a "hierarchical, linear and arborescent (meaning same source) design". Trudel sees coregulation as a sign of interplay between governmental institutions and other "places and networks" which formulate law.

Substantive law naturally has many dimensions, and I am referring to sources with the primary contract, the contract of sale, in mind. My intention is not to present the individual provisions in detail, but to indicate the role and usefulness of each set or type of regulatory instrument.

X.3.1 The United Nations Sales Convention

The United Nations Sales Convention, referred to as the CISG, is undoubtedly one of the key sources in determining the substantive law for electronic commerce. As such, it could constitute a *lex mercatoria* instrument in itself, since "it can itself be regarded as the expression of international mercantile customs".[84] As already noted at the beginning of this study, the Convention applies to contracts of the sale of goods between parties whose places of business are in different states, when the states are contracting states, or when the rules of private international law lead to the application of the law of a contracting state. The issue of the scope relates both to the rules of contract formation (Part II)[85] and the substantive Part III, unless applicable otherwise.

In electronic commerce, the internationality of the sales transaction causes some additional problems, since the place of business is not always easily determined. It should be noted that the CISG does not define the place of business expressly, but that some rules have been established in legal literature. The analysis of UNCITRAL´s Secretariat draws a parallel between electronic commerce and more traditional means in stating that where parties to a contract concluded electronically clearly indicate where their relevant places of business are located, those places of business are to be taken into consideration in determining the internationality of the sales transaction.[86] Moreover, the same remark applies even in those instances in which a party has more than one place of business.

However, if the relevant place of business has not been clearly indicated by the parties before or at the time of the conclusion of contract, one has to see whether there are circumstances from which the location of the relevant place of business can be inferred. The analysis suggests that the internationality could be inferred from the e-mail address: "Recognizing the legal significance of an e-mail address being linked to a specific country through a domain name would have an advantage of necessarily making the parties aware that the contract may not be a domestic one".[87] An alternative approach, according to the analysis, would be to determine the internationality of an electronically concluded sales transaction under the Convention.

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84 As put forward by Audit, p. 2.

85 The application of the CISG contract formation rules in the electronic age was examined in Chapters IV.7.2.2. and IV.7.3., *ante*.

86 A/CN.9/WG.IV/WP.91, para. 8.

87 Ibid.; para. 10.

According to the note containing the analysis, this would apply as follows:

- where a party uses an address linked to a domain name connected to a specified >>

The Convention is not all-embracing in relation to the object sold or the nature of the sale in general. It does not apply to sales of goods bought for personal, family or household use, unless the seller, at any time before or at the conclusion of the contract, neither knew nor ought to have known that the goods were bought for any such use. Neither does it apply to sales by auction or on execution or otherwise by authority of law. Moreover, sales of vessels or aircraft, the purchase of electricity as well as financial instruments are excluded from the scope. (Article 2)

Contracts for the supply of goods to be manufactured or produced are to be considered sales contracts unless the party who orders the goods undertakes to supply a substantial part of the materials necessary for such manufacture or production. Similarly, the Convention does not apply to contracts in which the preponderant part of the obligations of the party who furnishes the goods consists of the supply of labour or other services (Article 3). The Analysis of the UNCITRAL Secretariat refers to the interpretation of commentators and courts according to which the sale of standard software can be considered a sale of goods, at least where the software is not custom-made.[88]

The Convention governs the formation of the contract of sale (Part II) and the rights and obligations of the seller and the buyer arising from such a contract (Part III). Although the Convention provides rules regarding contract formation as well as relatively comprehensive substantive rules it has to be read together

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<< country (addresses ending with ".at" for Austria, ".nz" for New Zealand and ".fi" for Finland), it can be argued that the place of business should be located in that country, and

- where the address does not, however, allow for a similar solution since a top level domain such as ".com", ".net" or ".net" is used, it can be argued that in such a case the contract should always be presumed to be international.

The UNCITRAL Working Group IV on Electronic Commerce has so far agreed with the conclusions of the analysis in respect of a place of business indicated by a party, however, keeping it a rebuttable presumption. On the other hand, in the present view of the drafters (which is indicated by reactions to Article 7 of the draft Convention on electronic contracting), the sole fact that a person makes use of a domain name or electronic mail address connected to a specific country does not create a presumption that its place of business is located in such country. Similarly, the location of the equipment and technology supporting an information system used by a legal entity for the conclusion of a contract, or the place from which such information system may be accessed by other persons, in and of itself does not constitute a place of business. (See doc. A/CN.9/WG.IV/WP.108, p. 9 and note 32, as well as Chapter IV.7.2., *ante*.

In addition to determining whether the contract falls under the Sales Convention, the places of business of the parties, or their location in general could have a bearing on the jurisdiction, applicable law and enforcement.

88 Ibid., pp. 7-8. The evaluation can be made on the basis of two different questions. The first asks whether software represents ´virtual goods´ or is merely a service. The second asks what a ´sales contract´ is, bearing in mind that transactions in ´virtual goods´ are in the form of licences, not sales. The status of a purchaser is different in these two cases.

A buyer of goods can dispose of them freely, whereas a licencee is under the control of the licencor in respect of the product concerned. The right in the virtual goods remains with the licensor, and there could be restrictions on transferring the software to a third party.

For these issues from a Finnish domestic sale of goods law perspective, see the recent Finnish Supreme Court case KKO 2003:88, as well as Matti Vedenkannas, Tietokoneohjelman luovutuksen luonne: tekijänoikeuden, käyttöoikeuden vaiko teoskappaleen luovutus?, Defensor Legis No 5/2002, pp. 862-879.

with other rules of law, and amendments by contract will serve the needs of the business community in electronic commerce.

Especially as regards the substantive rules contained in Part III of the Convention, contract practice usually amends or supplements them in some respects or even replaces them completely. This has been the case in the United States.

A uniform law cannot reach the degree of precision in respect of the detail that may be required by the commercial world. For instance, precise time-limits are missing and are substituted with notions of reasonability. Secondly, the consequences of a breach provided for in the Convention may not satisfy most sellers, since the Convention does not contain anything on the limitation of the seller´s liability. The presumption is that a seller is also responsible for consquential loss. Finally, sales laws do not usually contain fall-back provisions for a number of integral elements of standard commercial contracts, such as retention of title clauses, liquidated damages clauses applicable law and settlement of disputes clauses just to name a few.

The Convention does not generally deal with the validity of the contract or of any of its provisions or of any usage. Therefore such aspects as the capacity of the parties and rules on agency are to be found elsewhere. Neither does it deal with the effect which the contract may have on the property in the goods sold.

The Convention does not contain any rules on fraud, coercion or unconscionability. These subjective aspects of contract formation are left to be resolved by other rules of law. Finally, the observation of good faith has been left the status of a principle only.

The Convention however recognises that it is not complete and that gaps exist. It has produced a mechanism of gap filling and interpretation "in conformity with the general principles on which it is based" (Article 7(1)). The Convention can therefore be regarded as an autonomous system capable of generating new rules.[89] As examples of such general principle one often mentions the Convention´s tendency to favour upholding the contract and to favour performance to rescission.

Parties can, it is submitted, make the Convention applicable even when it is not ratified or excludes its own application. The effect of such incorporation can be simply contractual or can constitute, depending on the attitude of the *lex causae*, a choice of the law applicable.[90] Jurisdictions requiring e.g. a reasonable link between the law and the transaction can, however, pose problems in this respect. I believe that where the CISG is made the governing law, or is said at least to govern the relationship in accordance with its letter, then the principles

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89 Audit, p. 7.

90 As note *supra*, the Dutch Supreme Court has (in the cases *Hoge Raad, 26.5.1989, NJ 1992.105* and *Hoge Raad 5.1.2001, NJ 2001.391*) held that the parties were free to designate the Convention as the law applicable to their contract despite the fact that the Convention did not apply directly pursuant to Article 1(1).

on which it is made, including the method of gap filling by principles and the predominance of trade usages, come into play. An incorporation of the CISG has therefore the same type of effects as referring the case to the *lex mercatoria*.

One significant gap, which cannot usually be filled without recourse to national law, is the field of property rights in the goods. A retention of title clause is a standard component of any sale of goods agreement, and its validity and scope are usually determined by national law.

X.3.2 The UNIDROIT Principles of International Commercial Contracts

The *lex mercatoria* will undoubtedly include legal principles agreed on universally. In fact, the CISG already refers to the "general principles on which it is based".[91] Attempts have been made to define international contract law principles in detail. When compilations of widely agreed principles emerge, general principles become not only something metaphysical, but instruments that can be incorporated by reference.

UNIDROIT Principles of International Commercial Contracts have frequently been pointed out as a source of *lex mercatoria*.[92] These Principles may be looked upon as representing a system of rules of contract law common to the world´s main legal systems. Referring to the title[93] of another publication concerning these Principles, they can even be considered an international restatement of contract law in the the terminology of US legislation. They could be seen as representing a new *lex mercatoria*. This is even assumed in the Preamble of the Principles: "They may be applied when the parties have agreed that their contract be governed by general principles of law, the *lex mercatoria* or the like".

The work was commenced in 1980, the year of the completion of United Nations Sales Convention, by a group of eminent independent experts representing diverse legal systems, and was finalised in 1994.[94] The work is said to be "impressive by virtue of its ambitious and global character, since it comprises a body of rules (rather than ´principles´...) covering the entire general

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91 Article 7(2) of the Convention provides, as said, that "(q)uestions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based or, in the absence of such principles, in conformity with the law applicable by virtue of the rules of private international law".

92 For instance UNIDROIT Principles for International Commercial Contracts: A New Lex Mercatoria?, ICC Publication No 490/1. Paris 1995. See also a very recent ICC publication, UNIDROIT Principles of International Commercial Contracts, Reflections on their Use in International Arbitration, Special Supplement – ICC International Court of Arbitration Bulletin, Paris, June 2002.

93 M.J.Bonell, International Restatement of Contract Law, 2nd, enlarged ed., New York 1997. This comparison was made by Pierre Lalive, President of the ICC Institute for International Business Law and Practice in the Foreword of ICC Publication No 490/1.

94 The group was chaired by Professor Michael Joachim Bonell from the University of Rome.

spectrum of contract law, including contract formation, validity, interpretation, execution and non-execution – excluding only such matters as special contracts, prescription (cf. *infra*) and the transfer of property".[95]

At the time of the finalisation of this study, UNIDROIT came out with a new edition, UNIDROIT Principles of International Commercial Contracts 2004[96] now covering several new areas: the authority of agents, third party rights, set-off, the assignment of rights, the transfer of obligations, the assignment of contracts and limitation periods. Minor adjustments were made to the provisions and commentaries contained in the 1994 version, and the new text is generally not intended to be a revision of the old text.

The Preamble of the Principles indicates that parties can select the Principles as the rules that govern their contract. The Principles themselves could be given several roles. Firstly, they could be designated as the proper law of an international contract and would serve as the *lex contractus*.[97] A suggestion has been made to amend the Rome Convention on the Law Applicable to Contractual Obligations to allow the parties to choose either the UNIDROIT Principles or the Principles of European Contract Law as the law governing the contract.[98] As regards the present Convention, there are opposite views as to the possibility to refer to anational rules.[99] At the present stage of legal thinking, it can in any case be generalised that national courts require a contract to be governed by a national legal system, be it the *lex fori* or some other national law.

As mentioned *supra*, the Commission has at least put under discussion the suggestion of amending the Convention to allow parties to choose anational rules of law in lieu of state law. If concluded, such a revision could make the observance of a *lex mercatoria* provision binding on state courts as well. Reference to the Principles can already be made without reserving such a possibility in the Convention, but this reference is generally regarded merely as a contractual incorporation. Although state courts normally respect such an incorporation, the law governing the contract will still have to be determined on the basis of the private international rules of the forum. The Principles will bind the parties to the extent that they do not affect the rules of the applicable law from which the

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95 Foreword of ICC Publication 490/1 by Pierre Lalive, President of the ICC Institute for International Business Law and Practice.

96 Published in Rome in May 2004.

97 See The UNIDROIT Principles as *Lex Contractus*, With or Without an Explicit or Tacit Choice of Law:

- An Arbitrator´s Perspective, by Pierre Lalive, pp. 77-84; and
- The Perspective of the Counsel by Julian D M Lew, pp. 85-94; in ICC Arbitration Bulletin, Special Supplement 2002.

98 Burnstein in Internet..., pp. 33-34, referring to K. Boele-Woelki´s suggestion in ´Principles and Private International Law – The UNIDROIT Principles of International Commercial Contracts and the Principles of European Contract Law: How to Apply Them to International Contracts, Uniform Law Report 1996, pp. 652-678 (664-669).

99 De Ly in Towards a European Civil Code, p. 53.

parties may not derogate.[100] The revision of the Convention in the above described manner would change these practical consequences. [101]

In arbitration, on the contrary, where arbitrators are allowed to act as *amiable compositeurs,* which means that they can decide *ex aequo et bono*, the Principles can be applied by the arbitrators to the exclusion of any national law. The *lex mercatoria* or general principles of law may be applied in arbitration even when the arbitrators do not act as *amiable compositeurs* since it has been widely accepted that arbitrators even in such a case may apply anational rules in lieu of a specific national legal system.[102] The only limitation would be the application of those rules of domestic law which are mandatory irrespective of which law governs the contract (*lois d´application nécessaire*).[103]

It is interesting to note that during the years 1994-1998 there were 23 ICC arbitral awards referring to the UNIDROIT Principles in general, among which eight awards dealt with situations where the Principles constituted the proper law of the contract. All eight awards concerned arbitration at law and none *ex aequo et bono*.[104]

The point has been sometimes raised that a reference to the Principles should always be regarded as a mere contractual incorporation and should be at the same level as any set of uniform rules intended for referencing and thus have the status of contractual terms, which the parties are relatively free to determine in accordance with the principle of party autonomy. It has been argued that this would be the case since the Principles are far from being a complete body of contract law, not to speak of a fully-fledged legal system.[105] On the other hand, the Principles are modern and sophisticated, which is not the case with all national laws. Still, it is possible to refer to the latter with substantial exclusivity. When the Principles have been referred to and no national law has been chosen by the parties, arbitrators could easily infer that the intention of the parties was to exclude domestic law altogether.

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100 The Preamble of the Principles, p. 3.

101 A possibility afforded by a revision of a conflict of laws convention to refer to anational law could not as such elevate the UNIDROIT Principles to a level completely at par with national laws in the formalistic sense, since the rules replacing the Convention would simply allow parties to choose their own rules of law to govern their relationship. If uniform substantive commercial law were to be created under the framework of Community law (*acquis*), one would have to apply the ´Community method´ to enact it.

102 See Chapter IX.5.3., *ante*, in particular note 47. See also Hans Van Houtte, The Unidroit Principles as a Guide to Drafting Contracts, in The UNIDROIT Principles for International Commercial Contracts: A New Lex Mercatoria?, ICC Publication No 490/1, pp. 115-125. In this respect, compilations of arbitration practice such as the *UNIDROIT Principles of International Commercial Contracts, Reflections on their Use in International Arbitration*, Special Supplement – ICC International Court of Arbitration Bulletin, Paris, June 2002, are of great interest.

103 Article 1.4. Comment 3 of the Principles. See also Chapter II.8., *ante*.

104 Fabrizio Marrella & Fabien Gélinas, The UNIDROIT Principles of International Commercial Contracts in ICC Arbitration, ICC International Court of Arbitration Bulletin Vol. 10/No. 2 – Fall 1999, pp. 26-32.

105 Ulrich Drobnig, The Use of UNIDROIT Principles by National and Supranational Courts, in The UNIDROIT Principles for International Commercial Contracts: A New Lex Mercatoria?, ICC Publication No 490/1, pp. 223-232.

A further possibility for referencing to the UNIDROIT Principles is to use them as a means of supplementing and interpreting applicable domestic law.[106] Moreover, as another possibility, they have been used as a means of supplementing and interpreting international conventions, in particular the CISG.[107]

There are other uses for the Principles. They can be used as a guideline for drafting contracts. They are also valuable in providing guidance for the conduct of contract negotiations as well as laying down rules of liability for negotiations conducted or terminated in bad faith.

Even though the Principles were drafted to constitute a *lex mercatoria* or soft law instrument, their success has led to legislative efforts to incorporate parts of them into national laws.[108] This type of ´crystallisation´ of soft law instruments is of course convincing, but contains pitfalls, if the national legislator does not follow the development of the flexible soft law instrument, there being now a new version of the instrument albeit that it merely introduces articles for new areas.

The Principles overlap the CISG but can be used together with it as well, as contractually incorporated or as a gap filling instrument. Whenever the requirements for the application for the CISG exist, it will normally take precedence over the UNIDROIT Principles, unless the parties provide otherwise.[109] All in all, the UNIDROIT Principles are a more comprehensive instrument than the CISG and the potential scope of application is wider, extending to contracts other than sale. Article 1.6 contains prerogatives on how to interpret the Principles and to fill in gaps in them. The method is similar to the CISG, and it differentiates the Principles from contractual terms even if their status is similar.The Principles are suitable for electronic commerce since they do not require a contract, statement or any other act to be made in or evidenced by a particular form.

X.3.3 Principles of European Contract Law and new dimensions for *acquis*

Another set of contract law principles that may find its way to the regulation of commercial contracts is entitled the ´Principles of European Contract Law´. These are the product of work carried out by the Commission on European Contract Law, a body of lawyers drawn from all the Member States of the European Community, under the chairmanship of Professor Ole *Lando*. They are said to be "a response to a need for a Community-wide infrastructure of contract law to

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106 See François Dessemontet, Use of UNIDROIT Principles to Interpret and Supplement Domestic Law, in ICC Arbitration Bulletin, Special Supplement 2002, pp. 39-50.

107 See Michael Joachim Bonell, The UNIDROIT Principles as a Means of Interpreting and Supplementing International Uniform Law, in ICC Arbitration Bulletin, Special Supplement 2002, pp. 29-38.

108 See An International Restatement of Contract Law, pp. 235-238.

109 For the interrelationship between the UNIDROIT Principles and the CISG, see Bonell 1996, especially pp. 4-8.

consolidate the rapidly expanding volume of Community law regulating specific types of contract".[110]

The aims of the Principles are the facilitation of cross-border trade within Europe, the strengthening of the single European market, the creation of an infrastructure for Community laws governing contracts, the provision of guidelines for national courts and legislatures, and the contruction of a bridge between civil law and common law.

These common principles, mainly for the countries of the European Community, concern the issues of validity, the interpretation and content of contracts, the authority of an agent to bind his principal, performance, non-performance and remedies.

The Principles are designed for several purposes. Like the UNIDROIT Principles, they can be expressly adopted by the parties. Moreover, an arbitrator could find it to contain a modern formulation of the *lex mercatoria*.[111] However, the drafters of the Principles have, if possible, a more ambitious goal. The Principles provide a necessary legal foundation for measures taken and to be taken in the future by the organs of the Community.[112] They could be used in legal harmonisation between the Member States, or in legislative reform work within individual Member States.

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110 Ole Lando and Hugh Beale (Eds.), Principles of European Contract Law, Part I: Performance, Non-performance and Remedies, Prepared by the Commission on European Contract Law, Dordrecht, The Netherlands, 1995, Introduction. In 2000, an extended version, ´European Contract Law, Parts I and II´, was published, edited by the same editors (Kluwer Law International, 2000). See also ´Towards a European Civil Code´, Second Revised and Expanded Edition, The Hague, 1998.

111 For the similarities and differences between a *lex mercatoria* approach and the Principles of European Contract Law, see De Ly in Towards a European Civil Code.

112 Over recent years, discussion has intensified on a possible harmonisation of substantive private law, in particular contract law. The European Parliament has adopted a number of resolutions on the possible harmonisation of substantive private law. In 1989 and 1994 it called for work to be started on the possibility of drawing up a common European Code of Private Law. In its resolution of 16 March 2000 concerning the Commission´s work program 2000, the European Parliament stated "that greater harmonisation of civil law has become essential in the internal market" and called on the Commission to draw up a study in this area (OJ C 377, 29.12.2000 p. 323).

One may add that the Conclusions of the European Council in Tampere during the Finnish Presidency in 1999 requested an overall study on the need to approximate the legislation of Member States in civil matters in order to eliminate obstacles to the smooth functioning of civil proceedings. This means that, at least in principle, harmonisation is desired by the Member States as well.

The Commission later came forward with a Communication from the Commission to the Council and the European Parliament on European contract law, COM (2001) 398 final. In this Communication, the Commission puts forward a number of options for Member States to receive their input concerning the need for future harmonisation.

The harmonisers could indeed build on the academic work in this field. In addition to the Principles of European Contract Law Parts I and II, the ´Pavia Group´ has published the European Contract Code"– Preliminary Draft (Universita di Pavia, 2001) based on the work of the Academy of European Private Lawyers. This code contains a body of rules and solutions based on the laws of members of the European Union and Switzerland and covers the areas of contract formation, content and form, the interpretation of contracts and the effect, executions and non-execution of a contract, cessation and extinction as well as other contractual anomalies and remedies. Another important ongoing academic exercise in this area is the ´Study Group on a European Civil Code´, which covers areas like ´Sales/Services/Long Term Contracts´ and ´The Transfer of Property in Movable Goods´. >>

The Principles are by definition a set of principles for a geographically limited area. However, given the impact that European legal cultures have had on the development of legal cultures elsewhere and the role of the European Union as the largest trading bloc in the world, the European Principles could play a role in international trade as well.

The European Commission is increasing activity towards building an EU-wide contract law. According to its late Communication[113], the Commission will endeavour to improve the contract law *acquis communautaire* by establishing a ´common frame of reference´, which will guide the Commission and national legislators in further legislative measures. The objectives of the common frame of reference are 1) to allow the existing *acquis* to be improved and simplified and to ensure the coherence of the future *acquis*, 2) to allow the identification of common terminology for particular fundamental concepts or best solutions for typical problems, in order for the future *acquis* to be proposed, and 3) to form a basis for further reflection on an ´optional instrument´ in the area of European contract law.

The ´optional instrument´ would be a body of rules particularly adapted to cross-border contracts in the internal market. Parties to such contracts could refer to this instrument as the applicable law. Furthermore, it should be possible for the specific rules of such a new instrument, once it has been chosen by the contracting parties as the applicable law to their contract, to be adapted by the parties to their needs. The Commission is not yet sure how the relationship with national mandatory provisions should be settled. Moreover, the Commission invites comments about the interrelationship between the Optional Instrument and the CISG.[114]

<< For a recent Finnish assessment of the harmonisation of European contract law, see Wilhelmsson, Ole Landon kyydissä kohti eurooppalaista sopimusoikeutta (Towards A European Contract Law with Ole Lando), Defensor Legis No 3/2000, 440-451).

113 Communication from the Commission to the European Parliament and the Council, ´A more coherent European contract law´, An Action Plan, OJ C 63, 15.3.2003.

114 This is indeed a very good question. Since 20 out of 25 national laws of the Member States applicable to the international sale of goods after the 2004 enlargement are based on the CISG, there is no reason to reproduce it in a conflicting manner. It is already a ´common denominator´, and although the UK does not adhere to the CISG, one must bear in mind that a great Anglo-Saxon jurisdiction, the United States, has adopted the CISG.

The CISG does not cover services and possibly not the sale of software, it does not regulate transfer of property or many aspects of contract formation such as incorporation by reference, the effect of errors, and the battle of the forms. Finally it may need amendments as to electronic contracting. A European optional instrument could tackle the effect of electronic communications since the relevant directives (e-commerce and electronic signatures) did not cover contract formation in detail. It could for instance crystallise the reception rule at a European level. The optional instrument should be very much supplementary, updating instrument in relation to the CISG.

The above list includes items which presuppose the use of a legislative method equivalent to the Community method after the Intergovernmental Conference. For instance, the French constitution requires that the questions relating to property have to be regulated by law. Therefore the preparation of the Optional Instrument would have to result in a decision, regulation or directive most likely a decision. The new constitution would change the labels of these legislative instruments.

X.3.4 Customs and Usages

Like the ´academic´ principles examined *supra*, trade customs and usages play a role in regulating international trade contracts or interpreting the law formulated elsewhere. As noted *supra*, some writers have seen usages in a determinant role in regulating cyberspace. Here we are discussing the meaning and operation of usages in traditional substantive law, which according to my conclusions would largely remain intact with the emergence of electronic commerce. But as the *lex mercatoria* would include the *lex electronica*, forming analogies of the role of usages is inevitable.

First, one must clearly define what customs and usages are. It has been noted that there are few studies on usages, and even these are outdated.[115] Generally, the notions ´customs and usages´ are used to denote customary law. Custom is not, however, synonymous with usage, and the use of these notions varies between legal cultures.[116]

The United Nations Sales Convention recognises the role of usages in Article 9. Parties are bound by any usage to which they have agreed and by any practices which they have established between themselves. Moreover, the parties are considered, unless otherwise agreed, to have impliedly made applicable to their contract or its formation a usage of which the parties knew or ought to have known and which in international trade is widely known to, and regularly observed by, parties to contracts of the type involved in the particular trade concerned.[117] It has been said that CISG Article 9(2) is "significant in that it acknowledges that rules not made by states can be imposed upon the parties".[118]

In international arbitration, the status of usages is recognised by Article 28(4)[119] of the UNCITRAL Model Law on International Arbitration which provides, as already noted, that the arbitral tribunal shall take into account, in all cases, the usages of the particular trade in the transaction.

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115 L´émergence de la *lex electronica*, p. 554.

116 Goode quotes (in Commercial Law, p. 41 note 44) the work 12 Halsbury´s Laws of England (4th edition) and its title ´Custom and Usage´ and notes that a custom is a rule of a particular locality whereas a usage is a settled practice of a particular trade or profession. Some normative differences may be found in the treatment of the concepts, however, giving customs an upper hand. In the commercial law of civil law countries and the US, the distinction is practically non-existent. Generally, the notion ´custom´ has gradually given way to ´usage´, especially in international commercial law. The best example of this is that CISG Article 9 only mentions usages (See the analysis in L´émergence de la *lex electronica, pp. 555-558*).

117 Cf. the United States UCC § 1.105, which defines a usage as "any practice or method of dealing having such regularity of observance in a place, vocation or trade as to justify an expectation that it will be observed with respect to the transaction in question". This definition does not take into consideration the possibility that a usage may bind the parties even though, at the time of the conclusion of the contract, none of them were aware of the usage. For the definitions and role of usages, see the references in Lando & Beale, pp. 46-47.

118 Audit, p. 3. For the treatment of usages under the CISG, see Stephen Bainbridge, Trade Usages in International Sale of Goods: An Analysis of the 1964 and 1980 Sales Conventions, 24 Virginia Journal of International Law (1984) pp. 619-665, reproduced at http://www.cisg.law.pace.edu/cisg/biblio/bainbridge.html.

119 Similarly Article 33(3) of the UNCITRAL Arbitration Rules and Article 17(2) of the ICC Rules of Arbitration.

Both usages and practices will, when applicable to a contract, set aside the rules of law, as well as any set of contract principles, which would otherwise apply. However, usages and practices are only valid insofar as they do not violate mandatory rules of the law applicable to the contract or to the particular issue in question.[120] Moreover, usages do not bind the parties according to Article 1.8(2) of the UNIDROIT Principles whenever their application would be unreasonable. I believe this provision reflects a common understanding in different jurisdictions.

When considering examples of commercial usages or customs, one can refer to well-known rules such as INCOTERMS 2000 or the Uniform Customs and Practice for Documentary Credits created by the International Chamber of Commerce. However, these rules or contractual terms are, as a rule, incorporated into the contracts, and can by and large be regarded as terms of contract.[121] A custom, or rather usage, in the legal sense would play a role even in the absence of a contractual reference to it, and it would take precedence against non-mandatory provisions of law.

There is a link between usages and model contracts. A term in a model contract could namely reach such universal recognition that it would find its way into tailor-made contracts without a specific reference. After years of regular use, such terms could be considered to be custom and be applied without mentioning them. The development of a commercial custom has been described as a gradual process: it often starts as the business procedure of a few leading enterprises, then becomes a general practice in a particular trade, founded on parallel action, then it grows into a trade usage and eventually acquires the certainty and legal status of custom.[122]

X.3.5 Model contracts

The potential of model contacts (or standard form contracts) in the harmonisation of international trade law was already recognised some forty years ago, when an eminent lawyer considered that in the long run the unification of international trade law by means of model contracts may prove to be more fruitful than by means of international conventions.[123]

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120 Lando & Beale, p. 44.

121 The INCOTERMS have sometimes been regarded as custom. However, it should be noted that the use of INCOTERMS 2000 requires the selection of an individual trade term. One could consider that a selected trade term without reference to its source collection could be interpreted in accordance with the provisions of INCOTERMS 2000 on the basis that this interpretation represents custom. Moreover, some trade terms, such as ´DDU´ (Delivered Duty Unpaid), have not existed outside INCOTERMS at all, and it would be strange to consider them apart from their origin.

In the United States, some writers have given the UCP a significant status in defining the custom, see Chapter VII.5.2.,"*ante*.

122 Schmitthoff, The Unification or Harmonisation of Law By Means of Standard Contracts and General Conditions, (1968) 17 of The International and Comparative Law Quarterly, p. 551 (also in Select Essays in International Trade Law, Edited by Chia-Jui Ching, London 1988, p. 191).

123 Kopelmanas, International Conventions and Standard Contracts as Means of Escaping from the Application of Municipal Law, in The Sources of Law of International Trade (ed. Schmitthoff), London 1964, pp. 118-126.

The use of the Internet will make it increasingly easy to use model contracts to pave the way towards mutual satisfaction in a contractual relationship, or at least will make both parties equally critical to the provisions of the contract, which might cynically be interpreted as a sign of the neutrality of the terms.

Model contracts are accompanied by standard terms which have been prepared in advance for future regular use. Article 2.18 of the UNIDROIT Principles of International Commercial Contracts define standard terms as "provisions which are prepared in advance for general and repeated use by one party and which are actually used without negotiation with the other party".

This notion makes standard terms rather unilateral by definition. One could add that such standard terms exist which are prepared by an organisation predominantly representing either the sellers or the buyers in a particular industry. The older model contracts, particularly those sponsored by the great international commodity associations, showed a tendency to favour the members of those associations and to shift the economic balance to the advantage of the economically stronger.[124] In concluding agreements through the Internet, the seller normally asks a consumer as buyer to confirm the acceptance of his contractual delivery terms. The buyer cannot proceed unless he agrees with such terms and conditions (a ´click-wrap´ contract). This is practically a situation in which a *contrat d'adhésion* (standard terms which the buyer cannot influence) is offered to be signed or accepted otherwise.[125]

Model or standard form contracts have, however, another meaning, namely that of a model contract form. In this meaning, a standard contract is "a model contract or set of standard conditions in the written form, the terms of which have been formulated in advance by an international agency in harmony with international commercial practice or usage, and which has been accepted by the contracting parties after having been adjusted to the requirements of the transaction in hand".[126]

The opposite of unilateral standard terms is an ´agreed document´ approved by the parties in advance. For instance, a framework set of conditions may have been agreed between regular business partners, and each quantity of purchased merchandise will be acquired referring to those terms. More importantly, an agreed document can be a model contract of an international agency, the preparation of which was contributed by representatives of regular buyers and sellers.

The prerequisite for the use of model contracts is party autonomy. Parties are free to agree on the terms of their contract. Modern contract law imposes, however, some restrictions on the freedom of the parties especially with a view to

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124 Schmitthoff, The Unification or Harmonisation of Law By Means of Standard Contracts and General Conditions, (1968) 17 of The International and Comparative Law Quarterly, p. 551.

125 The attitude of courts towards click-wraps may be softening, see Matthew Burnstein in Internet..., p. 32 referring to *ProCD Inc. v. Zeidenberg 86 F.3d 1447 (7th Cir. 1996)*.

126 Ibid, p. 193

protecting the weaker party. The control of standard terms imposed by general clauses in national law aim predominantly at the protection of consumers as regards *contrats d´adhésion*, often excluding international commercial contracts.[127] The objective of consumer protection has also been recognised by Community law in an increasing number of legal acts which touch upon contract terms as well.[128]

The ICC published at the end of 1997 a model contract entitled ´The ICC Model International Sale Contract (Manufactured Goods Intended for Resale)´[129], which is based on the United Nations Sales Convention.[130] This is a new instrument which complements existing instruments such as the UN/ECE Terms and Conditions for the Supply of Machinery and Equipment Nos 188 as well as the various conditions put forward by the European Metal Industry Federation ORGALIME. The latter contracts are, however, mainly used to sell ´tailor-made´ (i.e. specific goods under the CISG) to an end-user, whereas the ICC Model Contract is designed for sales of consumer goods intended for resale and thus not yet to consumers or end-users themselves. Commercial services exist to facilitate the use of standard terms.[131]

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127 The UK Unfair Contract Terms Act of 1977 Section 26 excludes international contracts whereas the German AGB-Gesetz does not do this. The general clauses in Section 36 of the Contract Acts of both Finland and Sweden do not exclude international contracts from their application either, although such application might be considered exceptional. See Jan Hellner, The Vienna Convention and Standard Form Contracts, in International Sale of Goods, Dubrovnik Lectures, Eds. Paul Volken and Petar Sarcevic, New York, 1986.

Case-law may apply principles equivalent to general clauses in written law. French case-law makes suppliers fully responsible for hidden defects (*vices cachés*) (A more coherent European contract law, OJ C 63, 15.3.2003, p. 8).

128 Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts, OJ L 95, 21.4.1993, p. 29, 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, OJ L 144, 4.6.1997, p. 19, and Directive 2002/65/EC of the European Parliament and of the Council of 23 September 2002 concerning the distance marketing of consumer financial services and amending Council Directive 90/619/EEC and Directives 97/7/EC and 98/27/EC, OJ L 271, 9.10.2002, p.16 form an element of consumer protection in contractual matters.

129 ICC Publication No 556.

130 The General Conditions provide that any questions relating to the contract which are not expressly or implicitly settled by the provisions contained in the contract itself shall be governed :

- by the United Nations Sales Convention, and

- to the extent such questions are not covered by the Sales Convention by reference to the law of the country where the seller has his place of business.

It should be noted that the drafting group who prepared the ICC Model Contract finally rejected a *lex mercatoria* oriented provision, which would have made legal principles common to the jurisdictions of the seller and buyer a tertiary source of law after the contract and the CISG.

For the ICC Model Contract, see also Railas, ICC:n uusi sopimusmalli kansainväliseen irtaimen kauppaan, Defensor Legis N:o 2/1999, pp. 309-318.

The ICC Model International Sales Contract contains a *force majeure* clause. The ICC has, however, also produced an independent *force majeure* clause, which the parties can incorporate into their contract. There is also an ICC Hardship Clause for the adaptation of contracts in cases where changing circumstances render the performance of a contract so difficult that it amounts to hardship. Both clauses are published in the same booklet (ICC Publication No 650, Paris 2003).

131 See, for example, the site http://www.iaccm.com, visited on 18.8.2004.

It is not totally excluded in the light of the reported discussions that model contracts could become an instrument of harmonisation under the auspices of UNCITRAL as well. Likewise, the European Union seems to be considering following that path.[132]

X.4 ´Operational´ requirements for any new instruments and their making

Many new legislative instruments for the facilitation of electronic commerce have already been created. They share certain characteristics which are also vital for any new instruments to be created. An account is given of those characteristics, here and there coupled with some remarks based on an analysis of the materials examined in this study.

The basic question posed is whether a separate legal framework for electronic commerce is needed. As long as volumes, the diversity of contract types or the amounts at stake in electronic contracting remain low there is little incentive to create rules for just one method of communication. Many countries including the United States have implemented the UNCITRAL Model Law on Electronic Commerce in its original or in a modified form. However, even more countries have refrained from doing so. As regards contract formation, Part II of the CISG covers only contracts of sale and needs interpretation as regards electronic communications. The drafters of the UNCITRAL preliminary draft convention on electronic contracting currently under preparation are discussing the issue of to what extent contract formation by electronic means should be subject to a separate legal system.

Although those who say that electronic contracting involves the same issues as other means of contracting, harmonising electronic contracting is supposedly easier than trying to reach harmony in contract law more generally. This is because electronic commerce does not generally go into such fundamental substantive contract law issues as the adjustment of unconscionable contracts. Should success be achieved in harmonising this layer of contract law, it could spread its influence to contract formation procedures that use other methods of communication. New rules on contract formation could be make to be more media neutral.

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132 See Communication from the Commission to the European Parliament and the Council: A More Coherent European Contract Law, An Action Plan, Brussels 14 March 2003, OJ C 63, 14.3.2003, pp. 11-15. The Commission will promote the elaboration of EU-wide standard contract terms a) by establishing a website to facilitate the exchange of information of initiatives, and b) by offering guidelines on the use of standard terms and conditions. The Commission will apparently not produce standard terms itself. However, it aims to ensure that standard contract terms and conditions are jointly elaborated by representatives from all relevant groups including large-, small- and medium-sized industry, traders, consumers and legal professionals.

X.4.1 Preserve party autonomy

The move towards electronic commerce should not undermine contractual freedom more than is necessary. There are particular needs in the fields of consumer and investor protection. In the international trade between businesses, however, there are few areas that should be covered by mandatory legislation.

There are conflicting views as to whether electronic commerce laws should be made mandatory or not, the word mandatory meaning that the parties may not derogate from the provisions of these mandatory laws under a national legal framework (which may or may not allow derogation by choosing another law to govern the contract).

The UNCITRAL Model Law on Electronic Commerce provides, in Article 5, that derogation or variation of its provisions by agreement might not be permissible where any such variation or derogation would not be valid or effective under applicable law. The Model Law on Electronic Commerce, and especially Articles 1 to 10, presents minimum requirements for the recognition of functional equvalence, and there is reason for holding these provisions to be mandatory. On the other hand, the ´system rules´ subject to Articles 11 to 15 are designed to be of a non-mandatory character.

The UNCITRAL Model Law on Electronic Signatures allows a party to establish the reliability of an electronic signature by any means other than those referred to in Article 6, paragraph 3, of the Model Law. The drafters of the preliminary draft convention on electronic contracting prefer, at least for the time being, to make the Convention non-mandatory.

When it comes to regulating areas which are already covered by mandatory legislation such as the various conventions relating to carriage of goods, a replacement or amendment has to take place through a legislative instrument. The legislator can always determine to what extent the new legislation should become mandatory. I believe that all laws that purport to have effects on the law of property must be mandatory, at least as against third parties. The parties then would not be able to change the property law effects of an instrument by an agreement between them, unless the result is recognisable by the world at large, as is marking an instrument ´non-negotiable´.

X.4.2 Make new instruments apt for contractual incorporation

As noted *supra*, the European Commission has been inviting comments on whether parties should be allowed to choose a convention to apply to the contract directly irrespective of whether it has been implemented as part of the *lex causae*. The question is actually whether the convention so incorporated would constitute the governing law.

Should the answer be negative, there would be no chosen law, and the contract containing such a choice would be governed by the law applicable in the

absence of a choice pursuant to Article 4 of the Convention. This law would then determine the role of the non-state rules chosen by the parties.[133]

The Commission´s Green Paper refers to two cases before the Dutch Supreme Court, which granted the parties the right to designate the CISG as the law applicable to their contract. The effects of the designation varied in respect to whether the contract was purely internal or international. Should the contract have been purely internal, the rules of the Convention could not have derogated from the mandatory rules of the law applicable in the absence of the choice. However, as the contract was an international contract, the court acknowledged that the choice of the Convention ruled out the mandatory rules of the law applicable in the absence of the choice.[134]

Where the parties do not intend to replace the entire *lex causae* with an international convention, the possibility of incorporating an international convention directly should be allowed to the extent that it does not violate the mandatory rules of the laws applicable to the contract. International conventions and instruments are increasingly drafted so that they are to be incorporated directly.

The UNCITRAL Model Law on Electronic Commerce has been drafted so that parts of it can be incorporated into contracts directly without having to refer to a national law. The same has applied to the rules of maritime transport since the adoption of the Hague Rules (Brussels Convention) of 1924. The fact that the maritime rules were meant to be mandatory made it necessary for legislators to transpose the rules into their national laws.

The UN Convention on Independent Guarantees and Standby-Letters of Credit may be made applicable by the parties, even where it is not otherwise applicable in the absence of other recognised connecting factors. The same approach seems to be chosen by UNCITRAL in respect of the draft convention on electronic contracting and the draft instrument on the carriage of Goods [wholly or partly] [by sea]. This approach builds on the role of the instruments as potential *lex mercatoria* instruments which can be incorporated into contracts such as the Incoterms or the UNIDROIT Principles.[135]

X.4.3 Safeguard adequate interaction between legal instruments

An international sale of goods transaction consists of many contractual relationships covered by separate contracts. Many disputes arise because these instruments do not work well together. Sometimes the discrepancy is intended, e.g. in the case of independent guarantees, but often is not. The problem might

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133 COM (2002) 654 final, Brussels 14.1.2003, p. 22, referring to P. Lagarde, Le nouveau droit international privé des contrats après l´entrée en vigueur de la Convention de Rome du 19 juin 1980, RCDIP, 1980, 287.

134 COM (2002) 654 final, Brussels 14.1.2003, p. 23, referring to Hoge Raad, 26.5.1989, NJ 1992.105 and 5.1.2001, NJ 2001.391.

135 See, however, Chapter VII.5.5., *ante*.

become more acute as regards integrated electronic trading platforms, since companies might prefer to protect their sector-specific interest as compared to joining such systems in order to save costs.

X.4.3.1 Building parallels with software technology

The founding idea behind the ´electronisation´ of the international sale of goods is the interplay between the various contractual or administrative relationships involved in a sales transaction. As international organisations are, in good cooperation I assume, creating instruments for facilitating trade and transport law, there is a need to make the legal rules ´interoperable´, to borrow a word from computing. It is indeed tempting to see a parallel between the attempts to reach convergence in respect of XML-based message standards on the one hand, and attempts to find harmony in the regulatory world on the other. One day there will perhaps be enough progress in both, and the two parallel lines will merge in the applications of electronic trading platforms. In the legal world, interoperability means both the unification of substantive law or predictable conflict of laws rules and the interaction between predominant international legal ´solutions´ for each contract involved in a transaction. International e-commerce instruments, the CISG, the UNIDROIT Principles, the UCP, the ultimate UNCITRAL instrument for carriage of goods by sea (hopefully covering the land leg) and the INCOTERMS will represent some predominant solutions which will be applied extensively in everyday commercial life.

X.4.3.2 Harmonise definitions

A basic element of interoperability and interaction is that identical definitions of various concepts used in law (e.g. ´electronic record´) are included to the extent possible in the various instruments regulating electronic commerce. The terminologies connected to the use of electronic signatures should be as identical as possible. Otherwise the legal profession can easily make use of the divergences in definitions in their pleadings.

X.4.3.3 Build on the existing instruments

As electronic commerce spreads, new instruments in the form of model contracts, principles and legislation will increase. For each instrument, there is a drafting group consisting of experts and strong personalities who direct the instrument under preparation towards their own personal or business-related preferences. As the emphasis in international facilitation may be on private codes of conduct, the problem of mushrooming may increase. To the author´s personal liking, however, it would be advisable to try to build new instruments on existing instruments as much as possible to avoid conflicts. For instance, the ´system rules´ of Articles 11 to 15 of the UNCITRAL Model Law on Electronic Commerce provide clear-cut principles that can be added to electronic contracts by cutting and pasting, or simply by incorporating them by reference. Any derogations in new instruments from predominant instruments should be clearly pointed out.

By following the course suggested above, legal principles common to electronic commerce would be established faster and be able to gain recognition.

Moreover, for the disputes that inevitably emerge, it would be easier to find principles (forming parts of the *lex electronica*) that can be resorted to than to use excessive casuism in drafting each time.

A further guideline for drafters, related to the above considerations, is that one should not presume disharmony. It is easy to point out that predominant legal solutions are not followed everywhere. Still, as a drafting policy, harmony should be presumed.

X.4.3.4 Avoid discrepancies between the contracts of sale and transport

As elaborated in Chapter VIII.9, *ante*, an area where ´interoperability´ or interaction is relevant in practice is the relationship between the rules applicable to sale and those concerning transport. A traditional example is the situation in which C-Incoterms (i.e. CPT, CIP, CFR or CIF) are used. These trade terms are namely suggested for deliveries in connection with sales in which documentary credits are used. English law knows equally the concept of a ´CIF-contract´, which is regularly used in connection with documentary credits. The reason for the use of the CIF-term is that it is impractical for the seller to carry the risk during the carriage since the transport documents are presented to the bank for payment. Although the contract of carriage is made by the seller, the party carrying the risk (the buyer, the bank or a cargo insurer on their behalf) should be able to sue the carrier for negligence.

Another example of the interrelationship between the contract of sale and the contract of transport is the right given to the parties of a contract of sale to dispose of the goods whilst in transit. This right may be bound on transport documents or may apply independently on the basis of a contract or statutory provision. The inclusion of a provision from the world of contracts of sale similar to Article 71(2) of the CISG into the Nordic Maritime Codes represents an example of efforts to reach ´interoperability´ between the two regimes, at least in terms of information.

An interface where conflicts exist between the contract of sale and the contract of transport is the phase of loading or discharge of goods onto or from the transporting vehicle. INCOTERMS 2000 has regrettably moved towards fixed points of delivery, where, with notable exceptions, the risk (as well as tasks and costs) pass from the seller to the buyer. Such a point does not necessarily coincide with the point where the carrier´s liability attaches or ends under the contract of carriage. The availability of standard terms, which could be incorporated into the contract of transport and would match a given trade term under the INCOTERMS, could reduce the conflict. In some cases, the two regimes of abbreviations, trade terms and shipping terms, could be combined in the contract of sale (like today´s ´CIFFO´[136]) to overcome later conflicts between the sale and

[136] Cost Insurance Freight Free Out means that the seller procures and pays the main carriage including insurance in such terms that the discharge of the goods at the port of destination is for the consignee. The buyer as consignee already knows his obligations at the time he concludes the contract of sale.

transport regimes. A documentary credit can prohibit loading or unloading costs that are "additional" to the freight, such as a FIO clause[137]. These may not appear on the transport document. Generally, adding terms of the contract of sale to the contract of transport should be done with sufficient precision so that responsibilities are created for the carrier. Such an exercise is so complicated that caveats for attempts to merge two contracts are reasonable.

X.4.3.5 Tick the balance between abstract and accessory undertakings

Construing the future trade law system requires a choice between independent or abstract undertakings on the one hand, and accessory undertakings on the other. This is not, of course, a new issue since it has been debated for a long time, for instance, in the field of contract guarantees.

Abstract undertakings are frequently connected to the use of negotiable instruments or documents of title, but can exist independent of them. A tendency has appeared of moving away from the use of bills of lading representing rights in the goods as independent and protected by the good faith of the new holder in due course. Bills of lading are seen as cumbersome and costly. Electronic trading systems can replicate the functions of the bill of lading without logistical pitfalls such as the documents arriving at the destination later than the goods. It is therefore defensible that negotiable instruments and documents of title remain in the arsenal. Although the UNIDROIT Principles of International Commercial Contracts 2004 treat an unauthorised assignment of a right to an assignee acting in good faith partly in the same way as an innocent indorsee of a bill of lading (without estoppel, however), equivalents of traditional negotiable instruments will probably be more understandable, and they will likely be covered by instruments such as the UNCITRAL draft instrument on carriage of goods [wholly or partly][by sea]. As well, the role of the transfer of documents of title should not be forgotten in perfecting security rights.

However, the information society can introduce many changes. There may be conflicting rights relating to the goods in transit. Should all such rights be recorded in the same registry, it would be possible to redefine the priority of the rights, and make the priority order transparent to users, while, however, bearing in mind the necessary level of confidentiality.[138] Moreover, changes in the condition of goods could be recorded in real time in a register accessible (if so desired) by all parties concerned. Today´s electronic systems replicate the functions of the paper-based world in accordance with the functional equivalence approach. The question may, however, be asked of whether abstract undertakings such as that based on carrier´s estoppel are well-founded in an information society.

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137 ´FIO´ means ´Free in and Out´, i.e. the shipper has to bear the loading costs and the consignee the unloading costs, which are therefore free for the carrier.

138 The priority order should follow from one legal system that could be designated by an international convention.

Trade finance in the form of documentary credits is, in my view, rightly held independent of the problems in the underlying contract of sale and the intricacies of transport law. The same logic applies to standby letters of credit and demand guarantees. However, the information society could form certain basic assumptions that would render these instruments redundant. The possibilities offered by the Internet and the various databases and registries accessible through it could undermine the reasonability of the ´on their face´ scrutiny. In the case of commercial letters of credit, however, the documents to be presented electronically must be effective in their original function, e.g. in transferring title and possession, so that documentary trade payment methods are useful. Therefore absolutely abstract undertakings are useful in creating confidence and security for the beneficiary, although they are not necessarily logistically motivated.

X.4.3.6 Avoid unnecessary documentation

Streamlining trade documentation includes avoiding unnecessary documentation. Documentary requirements are imposed by both law and legal instruments used in international trade. For instance, one of the next versions of the Incoterms could recognise that the use of an invoice, or, in some cases, a transport document is not absolutely necessary as the same functions are fulfilled by other means. Commercial law cannot, however, act alone. Administrative and fiscal laws should be adapted to take efforts to streamline trade documentation into consideration. This issue should be mentioned here, although it is self-evident, since there is obviously still a long way to go.

A parallel to avoiding unnecessary documentation is the avoidance of unnecessary data content common to many trade facilitation efforts such as those relating to electronic invoices and, more recently, the SWIFTNet Trade Services Utility.

X.4.3.7 Avoid unnecessary regionalism

In trade policy, regional integration is a phenomenon that occurs simultaneously alongside multilateral trade liberalisation and bilateral treaties. Regional integration may pave the way for multilateral arrangements, and regional organisations can more easily handle negotiations with other countries and organisations. In legal facilitation, however, global solutions should be sought. If a global solution cannot be achieved, one could then resort to regional harmonisation.

A good example is the fraud exception in connection with demand guarantees and standby letters of credit. The UN Convention on Independent Guarantees and Stand-By Letters of Credit adopted in 1995 offers, as has been explained earlier, an option to extend its application to commercial letters of credit as well.

An unofficial Study Group for a European Civil Code, which prepares informal suggestions for European regulations on independent guarantees under the heading ´personal securities´, has considered presenting its own suggestions as regards fraud exception in connection with demand guarantees and standby

letters of credit, but not at all for commercial letters of credit. Professor *Drobnig*, who chairs the relevant Working Group, argued in a seminar organised in Helsinki in 2003[139] that the UN Convention has since 1995 been implemented only by five commercially insignificant states, which reduces the relevance of the Convention. In my view it would be better to draw support to a multilateral instrument than to replace it, unless there is something wrong with its substance.

It should also be recalled that demand guarantees and standby letters of credit are largely used in trade involving third countries e.g. those in the Middle East. Therefore universal legal solutions might be more appropriate and could be introduced more easily to contracts with partners in third countries. Furthermore, a demand guarantee, a standby letter of credit and, if needed, a commercial letter of credit may consist of four contractual relationships, each one of them potentially subject to a separate national law. It would not be an ideal situation to have two or more legal regimes, which would differ in determining the question of fraud in the transaction.

As commercial letters of credit and demand guarantees have many common features, such as the autonomy of the bank´s undertaking and the standard for examining the documents that trigger payment, and as the jurisprudence relating to the exception of fraud in connection with the two types of instruments is largely applicable to either side, it is not desirable to create a legal framework that only covers one side of the instrument. Analogy would have to be sought in any case.

Instead of creating legislation particular to regional standards, efforts should be made to implement the UN or universal instruments at a national level. That is what has already been done in the field of transport law.

X.5 The role and administration of international organisations

As noted *supra*, the activity of the International Chamber of Commerce in proposing the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards in 1958 opened the eyes of governments and led to the establishment of the United Nations Commission on International Trade Law UNCITRAL, which started its work in 1968. Only many years later, in 1992, UNCITRAL finally recommended the use of the INCOTERMS, which had already been in use in different versions since 1936. In any case, such a recommendation manifests the recognition of the idea that the legal framework for international trade is made of many components. In electronic commerce, the complementary nature of international legislation and private rules, including codes of conduct and model contracts, should be a well-balanced relationship.

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139 ´The Future of European Civil Law´ organised by the Private Law Institute of the University of Helsinki on 10 June 2003.

Today, it may be difficult to distinguish between the roles and products of ´public´ and ´private´ organisations, unless mandatory instruments are created, which creation requires the intervention of states. The European Union has taken the enhancement of electronic commerce as one of its primary objectives in order to make the ´Old Continent´ more competitive vis-à-vis the United States. Therefore, EC legislation is at an advanced stage in electronic commerce. However, Community law takes a positive attitude towards private initiatives and codes of conduct in electronic commerce.

Outside the field in which mandatory rules can be created, legal instruments such as model contracts and uniform rules are created both by private and public organisations. Private organisations may be composed of companies, but they may also be composed of practitioners or academics (such as the CMI). Academic efforts towards creating uniform contract law principles have been made under the umbrella of a publicly funded scientific organisation which led to the creation of the UNIDROIT Principles. Practititioners and courts may build on this doctrine. At the extreme, legislators may allow a choice to be made in favour of anational rules of law such as the UNIDROIT Principles. Should this possibility be allowed in private international law, national courts would have to allow direct references to such legal rules even to the exclusion of otherwise mandatory rules. However, developments are not so far along yet.

The need for interplay between inter-governmental organisations and the business community is generally recognised and takes place in practice. A practical observation of the path to this interplay is that very often the same experts and scholars appear in various forums in different roles.

The public highway for creating rules for international trade is slow. A number of conventions remain unratified, which is certainly frustrating for those involved in their drafting. It is submitted here that the use of electronic commerce in cases where the location of trading partners is not clear, coupled with the globalisation of business life, underlines the internationality of electronic business transactions. This factor adds to the desire to seek transnational solutions to legal problems. As a binding uniform legal framework is lacking, practitioners will find their legal norms among the arsenal of non-binding rules. As noted many times, legislators have partly recognised this trend. In this way, a new supranational law, the *lex mercatoria*, will gradually strengthen its position.

International commercial law creating agencies have frequently codified existing practices. This was the the case with the ICC's Incoterms and the UCP. This strategy reduces the risks of failure and crystallises existing practices. Organisations may be proactive and create legislation or rules ´from the front´.

This study is largely built on the idea of seeing an international sale of goods transaction as a chain in which everything should serve everything in an expedient manner. This idea is behind many projects that international organisations have been occupied with in the field of international trade in the past decade. When a comprehensive look should be taken, organisational structures need to facilitate it. International trade includes several group interests that are sometimes antagonistic towards each other.

The difficulties in doing away with the nautical fault exemption in the carriage of goods by sea serves as an example. Sectoral organisations easily see

the problems from a fractional point of view. On the other hand, such organisations that have a multi-commission structure representing experience with different problems of trade are better positioned to tackle multi-dimensional problems. On the public side, UNCITRAL is such an organisation, and on the private side is the International Chamber of Commerce[140], not to discredit any others. Joint working parties and task forces are useful instruments in reconciling various views. A multistructural organisation has to remain as neutral as possible in order to succeed.

Surprisingly, the European Union largely lacks forums where different angles to general problems could be presented. If the EU wishes to take a more active role in harmonising the civil law that affects the field of international trade, it should consider improving its mechanisms. The discussions leading to the adoption of the new constitution could have given guidance on the question of how the Community institutions would be equippped to tackle multidimensional issues. There were no prerogatives on this issue. The same problem has been discovered in national administrations.

X.6 Which regulatory instruments should be used?

Once the governments become technically prepared to consider the ratification of an international convention, the convention to be adopted may be already outdated in some respects. One may have a look at the surveys conducted by UN/CEFACT in 1999 and UNCITRAL in 2001 regarding international trade law instruments to find out the number of legal instruments not yet in force and already outdated as regards the dimensions of electronic commerce (these groups are usually silent on this issue).

This fact makes it tempting to use instruments like ´uniform rules´ designed to be applicable through incorporation into contracts. Such instruments are useful because they can be changed more easily in changing commercial and technical circumstances. Their use means, in principle, less legal security, since soft law instruments can be regarded as less binding. Legal security increases, however, when principles contained in soft law instruments are crystallised into hard law.

UNCITRAL´s various Working Groups have recently been confronted with the argument that non-binding uniform rules could replace the conventions under preparation.[141] The reaction has been that the two systems supplement each other. In maritime law, the existing legal framework is based on mandatory conventions, which cannot be deviated from by contractual arrangements, unless the legislator gives consent thereto. In some other respects, legislation can defend

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[140] The revision of UCP500 represents a good example of how different aspects are taken into account. In addition to the Banking Commission, the Transport, Insurance and Commercial Practices Commissions are involved in the drafting.

[141] See Working Group III (Transport Law), A/CN.9/WG.III/WP.29, paras. 126-129; Working Group IV (Electronic Commerce), Report on the work of its forty-first session , A/CN.9/528, para 31, referring to Note by the Secretariat incorporating ICC´s comments, A/CN.9/WP.IV/WP.101.

its place. Legislation can add security with regard to the basic elements of contract formation such as a uniform understanding of the reception of a data message (e.g. data being available) having contract law implications or of the effects of incorporation by reference of contract terms. Moreover, drafting legal texts is in no way easier for actors in a busy business environment than it is for full-time legal drafters. Very few companies can afford to have officers spending most of their working time to create legal infrastructure in abstract terms.

Furthermore, it is difficult to imagine the use of electronic negotiable instruments or documents of title spreading without being established in legislation first. The *Bolero System* is obviously an exception to this, but would certainly benefit from a sound legislative infrastructure. The notion of ´document of title´ of the Law Merchant (*lex mercatoria*) was recognised by English law over two hundred years ago, whilst the United States made bills of lading negotiable instruments through a statute at the beginning of the 20th century. Through a statute, effects on third parties can be secured, which is a major facilitation incentive. Legislation can interfere with the existing *numerus clausus* of rights *in rem* and with documents of title prevailing in some jurisdictions.

If there is a desire to establish certain uniform rules as trade customs, it will take considerable time. Yet the transition to electronic commerce may speed up the establishment of commercial customs and make them more universal.

There should, however, be nothing to prevent the incorporation of a regulatory framework created by an international convention into a contract, at least when such a framework is not intended to replace the *lex causae*. The famous ´Clause Paramount´ incorporating the 1924 Convention regarding the Hague Rules into contracts of carriage evidenced by a bill of lading serves as an example thereof, although its incorporation is actually mandatory for Convention States. Therefore, as said, the technique of drafting international conventions should facilitate direct incorporation into contracts as well.

As said earlier, this aspect has already been taken into account with the UNCITRAL Model Law on Electronic Commerce, the ´system rules´ part of which (Articles 11 to 15) is drafted in a manner to facilitate incorporation. The UNCITRAL draft convention on electronic contracting and the UN Convention on Stand-by Letters of Credit and Independent Guarantees use this technique. It is uncertain what role an incorporated convention text has in state courts, if it does not already form part of the *lex causae* through other connecting factors.

Governments and intergovernmental organisations have shown a willingness to be flexible before of the challenges posed by rapid technical development. In addition to this, states should respond with increasing solidarity when enforcing laws of other states. More than ever, the emphasis will be on the similarities of the legal systems, which is a natural basis for mutual recognition. Harmonisation then seeks to ensure that different legal systems can communicate.

The choice of legislative instruments is, after political tensions between different state ideologies have largely vanished, a matter of expediency. The choice is often between predictability and flexibility. As much as dispute resolution will take place outside state courts, it will benefit from the elements of flexibility and creativity, which in turn help to shape new legal rules - with the kind permission of sovereign national states.

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Mr. Heikki Vaara, Managing Director, Vaara & Partners, 25 February 2004.

Mr. Tapani Voionmaa, Corporate Counsel, Finnlines Oyj., 25 November 2003.

INDEX

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Electronic commerce may change international trade procedures and bring about cost savings. A regulatory framework for e-commerce and, more widely, e-business is currently being shaped by international organisations.

This doctoral dissertation analyses developments in various fields of law ranging from contract formation to documentary credits and dispute settlement. The approach is holistic and is based on efforts to introduce uniform sources of law for e-commerce transactions in international trade. Legal issues are presented in the context of technological and commercial developments.

This book covers a broad repertoire of rules of law predominantly of international origin, which are useful tools for practitioners in drafting contracts or for arbitrators or judges settling e-commerce related disputes and which are interesting for everyone looking at the challenges of this dynamic field of law.

The writer has multifaceted experience in law and rule making in an international environment as well as being a practitioner of law himself.