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"Handcuffs" Clauses in International Commercial Contracts:

Basic Reflections on the Autonomy of the Parties to Choose the Proper Law for Their Contracts

Clever legal architects of international contracts sometimes succeed in inserting certain "handcuffs" clauses. Such clauses put a curb on all contractual partners in the exercise of their contractual remedies. Although of a binding nature for all signatories to the contract, the restrictive effects of such clauses are normally felt as handcuffs only by the other side of the contractual partnership.

So far as is known, handcuffs clauses have never been the object of a legal analysis. There are doubts as to whether such clauses are enforceable, and if so, to what extent. The purpose of this article, therefore, is to inquire how far the binding effect of such clauses may be recognized.

If one does not follow the doctrine of the *lex mercatoria,* the accuracy of which is questionable,[1] every international commercial contract is governed by a specific national law, *i.e.*, by its proper national law. The purview of such proper law

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1. For extensive references, *see, e.g.*, Otto Sandrock, *How Much Freedom Should an International Arbitrator Enjoy?*, 3 THE AMERICAN REVIEW OF INTERNATIONAL ARBITRATION, 30, 46, (1992) *reprinted in* OTTO SANDROCK, INTERNATIONALES WIRTSCHAFTSRECHT IN THEORIE UND PRAXIS/INTERNATIONAL BUSINESS LAW IN THEORY AND PRACTICE 439, 455, (1995) *Die Fortbildung des materiellen Rechts durch die internationale Schiedsgerichtsbarkeit, in* RECHTSFORTBILDUNG DRUCH DIE INTERNATIONALE SCHIEDSGERICHTSBARKEIT, Kar Heinz Böeckstiegel ed., 21, 51-60 (1989).

is not international, but restricted to the *imperium* within which the respective national legislators may exercise, and have exercised, their legislative powers. The question, therefore, whether a handcuffs clause is enforceable, and if so, to what extent, can only be answered on the basis of a specific national law.

The validity of handcuffs clauses depends, however, upon the different national legal systems and upon certain basic principles of contract law. These basic principles are more or less similar to each other within at least that part of the world commonly regarded as belonging to "Western" civilization. The present analysis, therefore, examines the validity of such clauses on the basis of Western national systems of law.

I. Examples and Purposes of Handcuffs Clauses

When trying to demonstrate the purposes underlying handcuffs clauses, it is useful to first present a few examples of such clauses.

A. Examples of Handcuffs Clauses

Handcuffs clauses share one characteristic feature with other types of contractual clauses: legions of different kinds of them exist. Human inventiveness is unlimited, and remains so with respect to the type of clauses here under consideration. Three examples of such clauses follow:

1. Claims for the fulfillment or for any other implementation of this contract, claims for damages allegedly arising out of a breach of this contract, and any other claims in connection with this contract can only be raised between the parties and against a third party if and insofar as this contract provides for it. Claims, therefore, cannot be raised on the basis of a statutory provision or of any other rule of law embodied only in the law chosen by the parties as proper law of contract.
2. (Dealing with a handcuffs clause attached to an arbitration clause): In specific stipulations, this contract provides for certain remedies that may be exercised by the parties in case their contractual rights may be hampered or violated by their partner's behavior. Claims for the enforcement of such remedies may be introduced before an arbitral tribunal (then such arbitral tribunal is specified as to its composition, its seat, etc.). The parties to this contract agree, however, that neither the aforementioned arbitral tribunal nor any state court whatsoever shall have jurisdiction to adjudicate claims introduced with remedies not specifically provided for by this contract, but deriving solely from the proper law of contract.
3. The remedies agreed upon in this contract are exclusive and do not permit the parties to recur, for the enforcement of their contractual rights, on any remedies regulated outside of this contract in any statutory or nonstatutory rule of the proper law of contract.

1. *The Factual Settings in which Handcuffs Clauses Are Most Often Used*

Handcuffs clauses are hardly discovered in international commercial contracts when the parties to such contracts belong to the same legal culture. Such clauses, rather, are encountered in contracts between parties stemming from different cultural and legal backgrounds. Their origin is in the concern of one party to avoid being subjected to a system of laws with which it is wholly unfamiliar. Such concern creates mistrust, and that mistrust leads to efforts by the concerned party to tame the mysterious unknown by making use of a handcuffs clause precautiously inserted into the contract.[2]

A common scenario accompanying such insertion of a handcuffs clause into an international contract is the following: A company from an industrialized country is trying to obtain a contract for works to be carried out in a developing country or in a newly industrialized country. The party offering that contract insists upon the choice of its own national law as the proper law of the contract. The contractor from the industrialized country, keen on obtaining the contract, has to acquiesce this demand. Thus, the national law of the contract awarder is adopted, in a choice of law clause, as the law governing the contractual relations between the parties.[3]

The company from the industrialized country, however, is wholly unfamiliar with even the most fundamental principles of the proper law of contract so chosen. The leading principles of the proper law may even originate from a religious code of conduct, a code the company has never confronted. The proper law of contract may also still be in a stage of development and certain parts may present themselves in a more or less cryptic state.[4]

To contain such danger of the unknown, the company from the industrialized country tries to take care that the respective rights and duties of the parties are meticulously outlined in the contract itself, thereby rendering the contract more or less self-sufficient. Any recourse to the statutory or nonstatutory rules of the proper law shall thereby be made redundant. The contract may thus develop into a complete legal system of its own.[5] In the view of the contractor, the ideal

2. As to a similar problem in international arbitration, *see* Giorgio Bernini, *Cultural Neutrality: A Prerequisite to Arbitral Justice*, 10 MICH. J. OF INT'L L. 39, 56 (1989).

3. For a list of examples confirming this trend, *see* MARTIN BARTELS, CONTRACTUAL ADAPTATION AND CONFLICT RESOLUTION, 106-08 (1985).

4. Compare the famous award in the so-called Abu Dhabi-Arbitration Petroleum Development (Trucial Coast) v. Sheikh of Abu Dhabi, 18 I.L.R. 144, 149 (1951), in which the parties had chosen the law of Abu Dhabi as their proper law of contract and in which Lord Asquith of Bishopstone stated, "*But no such law can reasonably be said to exist.*" However, the situation in Abu Dhabi, as well as in most of the other developing countries, has fundamentally changed since then not to speak of the newly industrialized countries.

5. Compare L.G. Telser, *A Theory of Self-Enforcing Agreements*, 53 J. BUS. 27-44 (1980); A. Verdross, *The Status of Foreign Private Interests Stemming from Economic Development Agreements with Arbitration Clauses*, 9 *Oesterreichische Zeitschrift für Öffentliches Recht* (1958/59); *id. Gibt es Verträge, die weder dem innerstaatlichen Recht noch dem Völkerrecht unterliegen?*, 6 ZEITSCHRIFT FÜR RECHTSVERGLEICHUNG, 129-34 (1965).

solution would be that, if a dispute between the parties arises, the rules of the proper law of contract would never have any chance at all of coming into operation.

Still, lawyers always experience that their contracts, as perfect as they may seem to be, can never be wholly immune from the complexity of life, particularly when unforeseen and unforeseeable developments take place. No wonder, therefore, that contractors from the industrialized world attempt to take all precautions against eventual risks still lurking in the future with respect to the *lex contractus* so unknown to them. One of the tools susceptible of so taming the future is handcuffs clauses.

Therefore, that handcuffs clauses share some characteristics with so-called stabilization clauses is obvious.[6] Whereas the latter try to take precautions against those risks that result from future statutory enactments set into force within the proper law of contract, handcuffs clauses try to cope with uncertainties arising from gaps in the contractual provisions: the contractual parties may have overlooked a problem when they drafted their contract. In contrast to their expectations, the contract is not at all self-sufficient, but shows certain lacunae that have to be filled by rules of the proper law. Such rules may provide one of the parties with a contractual remedy wholly unexpected by its contractual partner and cause, in the view of the latter, uneven contractual relations. In such a situation, a handcuffs clause precautiously inserted into the contract at the time of its conclusion will appear as some kind of a life buoy.

This scenario is, however, not at all unique to contracts that tie together companies from industrialized regions of the world on one side and companies from developing countries or newly industrialized countries on the other. The same conflict of interests may surge when companies from whatever countries—be they industrialized, newly industrialized, or still in the stage of development—are contracting with each other. Whenever one or the other of the contractual partners, or both of them, try to make a contract self-sufficient, the feasibility of a handcuffs clause may be discussed.

2. *Handcuffs Clauses v. Choice of Law Clauses*

It thereby becomes evident that whenever a handcuffs clause is invoked by a party, a reliance on that clause usually provokes a conflict with the choice of law clause that, within the contract, appears on equal footing with the handcuffs clause. Whereas it is the purpose of the choice of law clause in general to call

6. As to these clauses *see* George Rene Delaume, LAW AND PRACTICE OF TRANSMATIONAL CONTRACTS, § 2.07, 44-49 (1988); Timothy B. Hansen, *The Legal Effect Given Stabilization Clauses in Economic Development Agreements*, 28 VA. J. OF INT'L L. 1015-41 (1988); S.K. Chatterjee, *The Stabilization Clause Myth in Investment Agreements*, 5 J. INT'L ARB. 97-111 (1988); N. David, *Les clauses de stabilité dans les contrats pétroliers—Questions d'un Practicien*, 113 JOURNAL DU DROIT INTERNATIONAL (CLUNET) 79-107 (1986); Th. Wälde, *Stabilité du contrat. Règlement des litiges et renégociation, Revue de l'arbitrage* 203-38 (1981).

into operation all rules of law of the *lex contractus*, it is the object of handcuffs clauses just to prevent the coming into operation of some of them. Since both clauses appear in one and the same contract, it will eventually be the task of the judge or of the arbitrator to decide how the conflict between them will be solved.

In abstracto, several solutions of that conflict seem feasible. One might first think of applying the rule *lex specialis derogat legi generali*, which certainly is a general rule common to all systems of law originating from the European Roman law tradition. Then the handcuffs clause as the special clause would have to take precedence over the choice of law clause carrying a general character. Or one might classify that conflict as a matter pertaining to the interpretations of contracts, more specifically as a problem as to how conflicts between contractual clauses that contradict each other may and must be solved. A third course of legal reasoning, also compatible with all systems of law of the European-Roman tradition, would be to inquire whether at all, and if so, to what extent, handcuffs clauses can be reconciled with the public policy provisions or mandatory rules of the *lex fori* and/or of the proper law of the contract.

The following legal analysis will show that only the last-mentioned legal tool is useful in the present context. The starting point for that analysis must be the examination of the legal nature of said clauses.

II. The Legal Nature of Handcuffs Clauses

At first sight, handcuffs clauses apply to remedies and not to rights. These clauses restrict all contractual partners in making use of procedural remedies that the proper law of the respective contract would put at their disposal. One might be tempted, therefore, to characterize handcuffs clauses as procedural stipulations being governed by the *lex fori*.

Such characterization would, however, at least not be fully correct. Though these clauses exclude the operation of procedural remedies that, in the absence of such clauses, would be available to the parties under the *lex fori*, that exclusion reaches far beyond the *lex fori, i.e.*, into the proper law of contract. They prevent the parties from exercising certain substantive rights that in their absence would be at their disposal. It would therefore be incorrect to qualify handcuffs clauses as covenants of only a procedural nature. Handcuffs clauses are double-natured, operating both on the level of procedural and substantive law.

One has to therefore look for grounds invalidating these clauses not only in the sphere of the *lex fori*, but also in the sphere of the proper law by which they are governed.[7] As demonstrated above, their purpose is not only to affect the remedies, but also the substantive rights of the parties.

7. It is true that, in theory, a handcuffs clause could also be void for a violation of a public policy provision of a third state whose laws are neither identical with the *lex fori* nor with the *lex contractus, i.e.*, the proper law of the contract. For in certain instances, a judge may pay tribute to public policy provisions of third states that, in the view of that judge, would emphasize claim

III. Nullity Resulting from the Public Policy Provisions of the *Lex Fori*

A. Basic Considerations: A Justification of the Autonomy of the Parties to Choose the Proper Law for Their Contract

In the doctrine of conflict of laws, the autonomy of the parties to choose a proper law for their contract is justified by the consideration that, in principle, all national systems of law are equal as between each other and therefore interchangeable. In commercial contracts, the national private (not public) laws that would apply in the absence of a choice of law by the parties may thus be replaced by the parties through a choice of law clause by another national law. The law chosen is supposed to be as equitable, just, and effective as the law by which the contract would be governed in the absence of such choice of law clause.[8] It has been argued further that the parties must know which national system of law will most appropriately serve their contractual needs.[9] For these reasons, the principle of the autonomy of parties to choose their proper law of contract is recognized almost worldwide.

This doctrinal approach also explains why the parties, by making use of said autonomy, are able to opt out of the mandatory rules of the substantive law applicable in the absence of their choice of law: The mandatory rules of the law chosen are, in their entirety, considered to be the equivalent of the mandatory rules of the law that would have been applicable without their choice of law clause. The faculty of the parties, therefore, to replace one national system of

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application. *See, e.g.*, Rome Convention, June 19, 1980, art. VII, para. 1., 19 I.L.M. 1492, 1494, on the Law Applicable to Contractual Obligations providing:

> When applying under this Convention the law of a country, effect may be given to the mandatory rules of the law of another country with which the situation has a close connection, if and in so far as, under the law of the latter country, those rules must be applied whatever the law applicable to the contract. In considering whether to give effect to these mandatory rules, regard shall be had to their nature and purpose and to the consequences of their application or non-application.

Id. In practice, the application of such third state public policy provisions would be very rare, however.

8. In the German doctrine of conflict of laws, this is (since Friedrich Carl von Savigny (1779–1861)) the basic approach underlying not only the rules on the law applicable to contractual relations, but all rules of private international law. The doctrinal closeness to the Dutch/Anglo-American doctrine of *comitas* is evident: if a judge of the *lex fori* acting on the doctrinal basis of a *comitas* applies the rule of law of another nation, the judge must assume that the foreign rule so chosen is, in balance, as equitable, just, and effective as the judge's own *lex fori*. Modern doctrines of conflict of laws, particularly in the United States (*cf.* the so-called better law approach), but also in Germany and in other countries, reject that doctrinal approach. In the view, however, of the majority of continental European writers, including the author of this article, the new "better law" approach has no merits. As to the doctrinal foundations of German conflict of laws, *see* G. Kegel, Internationales Privatrecht (§ 3, IX 143, 7th ed. 1995); *and* as to the doctrinal foundations of the Anglo-American systems, Fritz Alexander Mann, Foreign Affairs in English Courts, 134 (1986).

9. *See* Kegel, *supra* note 8, at 483.

law with another one also extends to the mandatory rules of the respective systems of law, that are also regarded as substitutable between each other.

Of course, the mandatory rules of Country A may, in detail, vary considerably from the mandatory rules of Country B. But despite such differences, the summary of what is mandatory in Country A is, pursuant to the basic doctrine underlying the principle of the autonomy of the parties, held to be equivalent to what is mandatory in Country B. Thus, the balance of what is permissible in the private law of Country A is considered more or less even with what can be agreed freely upon by the parties in Country B. The protection of certain participants in commercial affairs (for example, persons in need, the inexperienced, and the employee vis-à-vis his employer) can be achieved in many ways. It is not relevant by what means that protection is accomplished in the law chosen by the parties. It only matters that there is an appropriate protection at all, more or less equivalent with the protection granted by the law to which the contract would be subject in the absence of the choice of law clause.

B. A First Restriction to the Autonomy of the Parties to Choose Their Proper Law of Contract: The Public Policy Provisions of the *Lex Fori*

The autonomy of the parties to choose their proper law of contract does, however, have some limits. Certainly one of the most important barriers restricting the parties' choice of law faculty derives from the public policy provisions of the *lex fori*. That barrier is most significantly characterized by Article 7, paragraph 2 of the Rome Convention of June 19th, 1980, On the Law Applicable to Contractual Obligations [hereinafter Rome Convention]:[10]

> C. Nothing in this Convention shall restrict the application of the rules of the law of the forum in a situation where they are mandatory irrespective of the law otherwise applicable to the contract.[11]

This Convention, including Article 7, paragraph 2, has in the meantime been ratified by almost all members of the European Union, showing that the basic idea underlying that provision is a general principle of law more or less universally recognized by all national systems of law with Roman-European origins.

In the present context, a terminological remark must be premised: specific public policy provisions must not be confounded with normal or mere mandatory provisions or mandatory rules. The latter, as the larger *genus*, are defined as "containing a demand," "preceptive," "imperative," or "peremptory."[12] A legal transaction violating them would be void. There are common law rules, such as prohibiting a violation of bonos mores, or statutory common

10. *Supra* note 7, art. VII, para. 2.
11. *Id.*
12. Blacks Law Dictionary, 1114 (4th ed. 1951).

law provisions, and remedies against usury and deceit, or, finally, statutory prohibitions to charge compound interest. All these common law rules or statutory prohibitions may serve here as examples of normal mandatory prescriptions. Often, these prescriptions are centuries old and deeply embedded in our Western legal culture. Usually, they appear as integral parts of our Western common law systems. In European continental countries, they belong to their private law systems.

On the other hand, public policy provisions are also classified as mandatory rules. But they are more imperative than ordinary mandatory rules or prohibitions and form, within the general category of mandatory rules and provisions, a special kind. In general, public policy provisions embody the response of the modern legislators to certain situations in which their intervention was thought to be either necessary or at least useful. They enshrine certain policies pursued in a great variety of fields, *e.g.*, foreign policy, economics, cultural or environmental matters, and public health. Trading with the Enemy Acts, embargos, antitrust prohibitions, insider regulations, foreign currency restrictions, statutory rules prohibiting the export of objects belonging to the cultural heritage of a nation, environmental regulations, and rules prescribing certain hygienic minimum standards may be cited as examples. In European continental systems, these provisions are regarded to form part of their public laws.

Usually, there is little doubt as to their highly imperative nature. Public policy provisions have been characterized as having "an overriding effect"[13] of breaking the operation of not only all other rules of the *lex fori*, but also of all provisions of the proper law of contract, including their mandatory rules.

The language used in the Rome Convention cited *infra* has to be interpreted in light of the foregoing distinctions. Then, if that paragraph speaks of "rules of the law of the forum in a situation where they are mandatory irrespective of the law otherwise applicable to the contract,"[14] it becomes clear that the authors of the Rome Convention thereby meant the special public policy provisions of the *lex fori* as just defined.[15]

The consequences deriving therefrom are the following: though the parties to an international commercial contract are able to opt out of the normal mandatory provisions and rules of the law that would be applicable in the absence of their choice of law clause, they do not have any such power with respect to the public policy regulations of the *lex fori*. This holds true also for handcuffs clauses. Like all other contractual stipulations, handcuffs clauses are also subject to the overriding effect of the public policy regulations of the *lex fori*.

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13. CHESHIRE AND NORTH'S PRIVATE INTERNATIONAL LAW (P.M. North et al., eds., 12th ed. 1992).

14. *Supra* note 7, art. VI, para. 2.

15. Reference is made, in this context, to the Report on the Rome Convention submitted by M. Giuliano and P. Lagarde. A German version of that Report has been published in the 1986 Records of the German Federal Parliament. Drucksache des Deutschen Bundestages 10/503, *id.* at 60.

A handcuffs clause, therefore, cannot be enforced when it would frustrate any policy enshrined in such regulations. If and insofar as a handcuffs clause collides with the public policy of the *lex fori*, it has to be considered null and void.

C. One Example for Nullity of Handcuffs Clauses; One Counter-Example of Validity

An export prohibition may be used as an illustrative example in this respect: in one context, it may induce the nullity of a handcuffs clause; in another, such nullity might be doubtful or have to be denied.

Let us assume, first, that a contract provides for the delivery of military goods into a foreign country under a violation of an export prohibition. In such a case, a handcuffs clause could have been designed by the parties (presumably in bad faith) to prevent any of them from introducing a claim before the competent state court or the competent arbitral tribunal for the examination of whether the duty to deliver the goods is compatible with the export prohibition. There could hardly be any doubt that a handcuffs clause, under such circumstances would be null and void. Its operation would blatantly thwart the public policy of the state that issued the export prohibition: the parties would be prevented from obtaining a judicial pronouncement stating that the duty to deliver the incriminated goods is void and that the promise of one of the paries to deliver said goods cannot be enforced. Such consequences would certainly be unacceptable.

In spite of the handcuffs clause, therefore, each party could sue its contractual partner either before a competent state court or, when an arbitration clause would confer corresponding jurisdiction, before the competent arbitral tribunal and there seek as relief a pronouncement that its duty to deliver the goods would be null and void on account of the violation of the export prohibition.

That conclusion would, however, be doubtful or have to be denied if, after the seller would have delivered the goods and after the buyer would have paid the contractual price, one of the parties, *e.g.*, the buyer, would introduce a claim for the restitution of the price paid by it in return for the merchandise delivered.

Assuming further that the duty of the seller to deliver did in fact violate said prohibition statute and that the proper law of the contract would in fact thereupon allow the restitution of the contract price,[16] there would be no conflict between the handcuffs clause on the one side and the prohibition statute on the other. The statute only aims at the prevention of the delivery of the goods into the target

16. This is rather unlikely in legal systems deriving from the Roman law tradition in which the old principle *in pari turpitudine, melior est causa possidentis* governed that problem. *Cf.* § BGB 817 reading, in its translation into English:

> If it was the purpose of a performance that its recipient should, with the reception, violate a statutory prohibition or bonos mores, the recipient would be obliged to restitution. Restitution is excluded, however, if the performing party equally is accountable for such violation, unless the performance consisted in the assumption of a liability; a performance rendered in fulfilment of such liability has not to be surrendered.

country. It would not affect any other duty of the parties, *e.g.*, to restitute the price on the basis of an unjust enrichment in case of the nullity of the contract. Since the remedy of the unjust enrichment claim would be out of the purview of the prohibition statute, the handcuffs clause could fully unfold its power: the buyer would be prevented by it from seeking the restitution of the money paid under the void contract.

This second example shows that when the compatibility of a handcuffs clause with the public policy provisions of the *lex fori* has to be examined, one cannot arrive at indiscriminate, sweeping conclusions for a whole category of cases; all cases must be individually examined on their specific merits.

IV. Nullity Resulting from a Violation of the Public Policy or the Mandatory Law Provisions of the Proper Law of Contract

A. Basic Considerations: Partial Choice of Law Clauses and the Prohibition to Go "Raisin-Picking"

From the above-mentioned considerations,[17] it follows that if a specific national system of law is chosen by the parties as their proper law of contract, that law, in principle, has to be applied *in toto*. Of course, partial choice of law clauses providing for the simultaneous application of two different systems of law to various parts of one and the same contract are permissible. Again, the Rome Convention[18] is an illustrative example for such a rule. Article 3, paragraph 1 of the Convention reads:

> A Contract shall be governed by the law chosen by the parties. The Choice must be express 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* (emphasis added).

That rule is also known to some conflict of laws systems outside the European Union.[19] There is a strong indication, therefore, that it may be equally qualified as a general principle of (private international) law recognized "by civilized nations."[20]

B. A Second Restriction to the Autonomy of the Parties to Choose Their Proper Law of Contract: No "Raisin-Picking" Allowed

The autonomy of the parties meets, however, a second restriction specifically developed for partial choice of law clauses. That restriction is of utmost impor-

17. *See supra* Part IV.A

18. *Supra* note 7, art. III, para. 1.

19. As to the the conflict of laws systems of the United States, *cf.* London Assurance v. Companhia de Moagens do Barreiro, 167 U.S. 149 (1897); Albert Armin Ehrenzweig & Erik Jayme, Private International Law 32 (1977); as to the "depecage" in general in the U.S. conflict of laws systems *cf.* Roger C. Cramton, David P. Currie & Herma Hill Kay, Conflict of Laws 358 (1987).

20. *See* art. 38 para.1 (c) of the Statute of the International Court of Justice. That expression, objectionable already when it was inserted into that provision, is wholly outmoded today.

tance in the present context: the parties can never split up their contract in such a way as to avoid the application of all mandatory law whatsoever. Raisin-picking is not permitted.[21] The parties would not be authorized, for example, to choose a certain system of law for one part of their contract and then stipulate that only the derogatory rules of that law shall apply to that part. They cannot split up the proper law chosen by them into mandatory and derogatory rules while adopting only the derogatory rules so chosen and repudiating its public policy or mandatory provisions. When they choose a proper law, be it only for a part of their contract, it is a take-it-or-leave-it proposition authorizing them to accept only the entirety of it and not only the provisions pleasing them and satisfying their contractual wishes.

That rule may be illustrated by an example taken from a contract on the purchase of the shares of a foreign company. It is known that some systems of law protect buyers of foreign securities against certain risks unknown and prejudicial to them through so-called blue-sky laws, whereas in other legal systems the rules pertaining to such risks have been integrated into other statutes, for example, into the general statute on company law or into the respective general civil code.[22] It would not be permissible then, under the above-cited rules on the partial choice of law clauses, for the parties to agree that their purchase contract should in general be governed exclusively by the company law and the civil code in effect in the home law of the acquired company if that law would be bare of any blue-sky regulations and that the transfer of the shares at the closing should be subject to the home law of the buyer (who knows blue-sky laws) to the exclusion of those blue-sky regulations. Or, if the parties have provided in a turn-key contract on the erection of an industrial plant or on the construction of a hotel, a hospital, or a water dam, that all matters pertaining to the erection or construction of such projects shall be governed by the laws of the host State A in which they are realized, whereas all deliveries of components through the contractor shall be subject to the domestic laws of the latter, *i.e.*, to the laws of State B, the parties must accept the mandatory law provisions of both States A and B with all their mandatory provisions without being able to exclude their operation by a specially tailored partial choice of law clause.

21. As to German conflict of laws, *see* the decision rendered by the German Supreme Court in 1936 (*reprinted in* 1936 *Juristische Wochenschrift* 2058, 2059) in which that court stated: it is not permissible "*that a contractual relationship is subjected to the legislation of a certain state with the proviso that a definite statute, whether already in effect or expected to go into effect and regulating a special problem, shall not be applied, unless such statute contains but suppletive rules of law.*" In French conflict of laws, that problem is dealt with under the heading of a *depecage* of a contract; *see* Henri Batiffol & Paul Lagarde, 2 DROIT INTERNATIONAL PRIVÉ, 274 (7th ed. 1983). As to English conflict of laws, *see Forsikringsaktieselskapet Vesta v. Butcher*, 2 ALL E.R. 488, 504-05 (Q.B. 1989); *aff'd* 3 W.L.R. 565, 587-88 (C.A. 1989), *aff'd* 1 Lloyd's Rep. 331, 347 (H. L. 1989).

22. This was the case in Germany, until its so-called *Wertpapierhandelsgesetz* (Statute on the Trade with Securities), July 26, 1994.

C. Consequences for Handcuffs Clauses

When applying these rules to handcuffs clauses, one first has to recall that handcuffs clauses normally reduce the purview of the proper law of contract.[23] There is even a conflict in terms of handcuffs clauses versus choice of law clauses. Secondly, handcuffs clauses have already been analyzed as being double-natured in affecting not only the remedies available to the parties in the competent courts or arbitral tribunals, but also in thwarting their substantive rights.

This shows that handcuffs clauses have at least one trait in common with partial choice of law clauses: they restrict the purview of the proper law of contract. Whereas partial choice of law clauses fill the gap with the rules of another system of law, handcuffs clauses leave that gap open in removing remedies and substantive rights otherwise available to the contractual partners. The parties are not authorized to stipulate partial choice of law clauses at their full liberty, but have to accept the application of the mandatory rules inextricably connected with their chosen laws. The parties are not allowed to go raisin-picking.

If, however, the parties have no power to repudiate, by partial choice of law clauses, the application of mandatory rules of the proper laws chosen by them, they should also not be able to annihilate the effect of such mandatory rules by inserting handcuffs clauses into their contracts. Therefore, handcuffs clauses should be treated equally with partial choice of law clauses. The restrictions applying to partial choice of law clauses should also therefore control the effect of handcuffs clauses.

D. Results: the General Doctrinal Rules

We therefore arrive at the following results: handcuffs clauses are null and void if and insofar as they restrict the parties in the exercise of those of their contractual rights and remedies that have been granted to them by a public policy or mandatory law provision of the proper law of contract. They are binding, enforceable, and effective, however, insofar as they exclude the exercise of substantive rights and remedies conferred upon them by any derogatory rule of the *lex contractus*.

Under the angle of the proper law of contract, the validity of handcuffs clauses therefore depends on their compatibility with its public policy provisions and with its mandatory rules.

E. Two Examples of a Valid and One Example of a Void Handcuffs Clause

The operation of these principles is best illustrated by a few examples:

a. It is general practice in international trade that the parties to international sales contracts replace the statutory rules of the proper law governing the

23. *See supra* sub 2.3 and 3.

liability of the seller for defects in the chattels sold by special stipulations in their contract that provide for other remedies.

If the parties to an international sales contract have chosen German domestic law (and not the U.N. Sales Convention) as the proper law of their international sales contract, it is common practice for them to derogate all remedies deriving from the section of the German Civil Code dealing with the liability of the seller for such defects (section 459 et seq.). That section of the German Civil Code is modeled after the remedies of ancient Roman law in providing that, in general, the buyer can, in case of a defect with the good delivered, either opt for the dissolution of the contract (while demanding the repayment of the price paid to the seller)[24] or demand a reduction of the contractual price to be paid, in proportion between the value of the chattel without the defects to its value with said defects.[25]

These statutory remedies are completely outmoded today. It is therefore common practice to substitute for them, in domestic as well as in international contracts, other remedies that better suit the needs of the parties by providing, for example, that either the seller has the option of removing the defect within a definite period of time or that the buyer may demand such removal. There can hardly be any doubt that handcuffs clauses of that kind are fully binding, enforceable, and thus of full validity in international sales contracts.

b. Another example for the full validity of a handcuffs clause is the following: unforeseen, unforeseeable, and unavoidable circumstances overcome the execution of an international long-term contract on the erection of an industrial plant and disturb the equivalence of the performances to be rendered by the parties. One of the parties therefore suffers a considerable hardship. The proper law of the contract, and not a special hardship clause,[26] would assist the aggrieved party in allowing it to demand the adaption of its contractual duties to that fundamental change of cicumstances.[27] But there is a handcuffs clause in the contract providing that all remedies granted by the proper law of contract shall be unavailable to the aggrieved party.

It could hardly be doubted that, by virtue of said handcuffs clause, the remedy of the adaption of the contractual duties would not be at the disposal of the aggrieved party. For when the parties inserted the handcuffs clause into their

24. This would be the *actio redhibitoria* under Roman law.

25. This would be the *actio diminutoria* under Roman law.

26. As to these clauses *see, generally*, C. M. Schmitthoff, *Hardship and Intervener Clauses*, J. BUS. L. 82 (1980); Delaume, *supra* note 6, at 57; Fontaine, *Hardship Clauses*, 1975 *Droit et Pratique du Commerce International* 512.

27. According to the never codified rulings of the German Supreme Court in Civil Matters (dating back to the years following the inflation of the German mark after the First World War) and with the support of the German doctrine, the aggrieved party can demand the adaption of the contractual obligations to the new circumstances in such a case. *See, e.g.*, P. Hay, *Frustration and Its Solution in German Law*, 10 AM. J. COMP. L. 345 (1961); H. Lesguillons, *Frustration, Force Majeure, Imprévision, Wegfall der Geschäftsgrundlage*, 5 DROIT ET PRATIQUE DU DROIT INTERNATIONAL 507 (1979).

contract, they must be deemed to have freely accepted the risk of an unbalance between their contractual performances supervening from a fundamental change in the cicumstances surrounding their contract. If, in such a case, the proper law of contract would take account of the fundamental change of circumstances and, like a *clausula rebus sic stantibus* clause, would seek to alleviate the fate of the aggrieved party, that rule of the proper law could not be qualified as a public policy or mandatory provision. It would rather be considered as being of a derogatory nature permitting said handcuffs clause to display its effects by removing from the hands of the aggrieved party the remedy to claim the adaption of the mutual contractual duties.

c. The result would be different, however, in other factual situations, for which the following might serve as a practical example: one of the parties to an international contract into which a handcuffs clause was inserted claims to have been the victim of a fraudulent misrepresentation committed by its contractual partner when entering into the contract. Such party therefore makes use of a remedy put at its disposal by the proper law of the contract, a remedy by which the aggrieved party can demand the dissolution of the contract and/or the payment of damages sustained during its execution. Its contractual partner, however, opposes the introduction of such remedy by relying on a handcuffs clause that would prohibit the exercise of that statutory tool.

The starting point for the solution of this conflict must be the following: the statutory or common law rights protecting the position of a party who, in such a manner, has become the victim of a fraudulent misrepresentation are of a mandatory nature.[28] The parties are bound by those rules without having the option of derogating from them. The effect of the handcuffs clause would be to suppress all rights and remedies deriving from the provisions just mentioned. In such a case, a party therefore cannot be deprived by a handcuffs clause of the protection accorded to it by the proper law of the contract. In other words, the handcuffs clause would be null and void.

This result appears persuasive. A party who agrees to the insertion of a handcuffs clause into the contract cannot be supposed to have waived the exercise of remedies against a fraudulent misrepresentation of which it could neither be aware nor protect itself and to which it therefore was destined to inevitably fall victim.

The same rule has to apply when a party exerts an illegal duress or an undue influence upon his or her contractual partner: a handcuffs clause could then never deprive victims of such illegal acts of their statutory or common law rights accruing to them.

28. *See, e.g.*, BGB § 123, which reads in its English translation: "*A person who has been caused by a fraudulent misrepresentation or by an illegal duress to effect a legal transaction, can rescind that transaction.*"

V. Conclusion

Handcuffs clauses do not present legal mysteries. On the contrary, the rules on their validity or invalidity are rather simple. All depends on whether either public policy provisions of the *lex fori* or public policy provisions or mandatory rules of the proper law of contract would be violated by their enforcement.

It is true, therefore, that handcuffs clauses do not guarantee the attainment of all ends that the parties, when inserting them into their contracts, seek to accomplish. Parties can rely on them to a limited extent only. But any protection, even of reduced volume, granted by these clauses certainly is valuable, and their use therefore can be recommended.