Intersections and Passing

Consideration about application of conflict-of-law rules, uniform law rules and of non-state rules of legal regulation

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I. Introduction

Explanation: The name opening our paper is not purposeless. It pursues a specific aim – to show existence of various groups of legal rules regulating or being able to regulate contracts including a foreign (international) element and in the same time to point out existence of horizontal[1] and vertical relationships between these rules. In consideration of the required scope of the paper, it is possible only to outline these issues, namely even in a situation when we limited the subject-matter of the paper to the issues of a single contractual type – international purchase agreement.[2]

Justifying the need: At the first sight, the area of legal regulation of private legal relationships with an international element represents an ill-arranged and non-transparent network of legal rules in terms of their various origin (their sources) and various nature (their sources and manner of creation). It is difficult for a person not being devoted to the concerned area to find a clear application rule for them and hence identify mutual relationships and subordinations. This comes in addition to the various view of the law determination before general courts and before arbitrators. The issue of conflict law is in addition sensitive to the approach of the procedural international law. This relationship may fundamentally affect the hearing of a specific case. Hence this respect cannot be left out either.

Aim: The objective of the paper is to point out to existence of individual groups of rules and methods of regulating the monitored relationships, their mutual relations, namely in relation to what applies before the courts in the Czech Republic. In consideration of the different theoretical starting points in arbitration, we shall put these issues aside.[3] The expression "monitored groups of rules" shall mean:

- conflict-of-law rules as rules determining law in private legal relationships with an international element,
- uniform law, i.e. uniform substantive legal rules directly regulating rights and obligations of the parties,
- the lex mercatoria[4] as the law of international merchants, which differs from the two foregoing groups by its origin. It is not based on legislative activities of a state or states. These rules come into existence either spontaneously, in practice, or they represent a result of activity of entities other than the state (ICC in Paris, business unions, academic activities). It is considered to include also rules, which are indeed created by international organizations but are not included in an international treaty (UNIDROIT Principles of International Contracts).

II. Private International Law – a Universal Solution?

Introduction. The starting point of our thoughts is one the components of the private international law – the conflict of law rules. The reasons are the following. In contrast to the uniform material, substantive law, the conflict law is not able to settle relationships with an international element in a uniform manner at this stage of its development.[5] However, it is capable of solving them in a complex manner, in their full extent. In contrast to the law of non-state origin (the lex mercatoria), no doubts are cast on its existence. Hence it is possible to use it as a starting point for thoughts about the basic possible applications of both other groups of rules.

Let us remind ourselves of the function performed by this discipline[6]: to determine the legal system, by which the legal relationship with an international element will be governed. This definition, following for example from the Czech Private International Law Act (hereinafter referred to as "PILA"), is narrower than the doctrinal approach to the private international law.[7] It even anticipates the applied method – i.e. the method ensuing from the hypothetical collision of legal systems when examining the legal relationship. The conflict-of-law rule and the connecting factor included therein form a connection between the examined legal relationships and the subsequently applied legal system. This predominantly European, continental approach maintained from the times of Savigny represents only seemingly simple and trouble-free set of rules. The effect of procedural law on one side and the development in the doctrinal area on the other side including the influence of the American approach bring about the differences. These are demonstrated not only in the formulations of the conflict-of-law rules but also in other issues like examination of the foreign law that is to be applied on the basis of the conflict-of-law rule, its ascertaining etc. This applies not just to national systems of the conflict law but it may affect also the system of the unified conflict law. This approach may have its influence also on the other groups of rules, which we monitor. Therefore it is suitable, before we proceed to define the relationship to the other monitored groups of rules, to mention the relationship the procedural and conflict law from the points of view of the Czech law.

Interaction of the substantive, conflict and procedural rules of law. The issue of interaction of the conflict and procedural laws has a fundamental importance for the area of applying a foreign legal system. A conflict-of-law rule and the substantive law applied on the basis of such rule's reference are used in a specific decision-making process. It is not possible to think of law treatment separately from a specific procedural framework. The conditionality of application of conflict-of-law rules and substantive legal rules by the standards specified within the law of the forum is indisputable. Issues of this type, as we state hereinbelow, affects in the specific case the course as well as the final result of the proceedings. Since 1989, when on the departments addressed also this issue in Santiago de Compostela, a number of articles as well as publications have appeared which have been trying to examine these very issues on comparative basis.

As shown by comparative studies, there is a high probability of the different "procedural" understanding of the conflict-of-law rules and their understanding on the basis of the applied legal system.[8] Only briefly on how this relationship may be characterized in terms of the Czech law:

1. **Are conflict-of-law rules of the forum applied to relationships, which fall under the applicability of the private international law, ex officio or facultatively, i.e. according to the judge's discretion or only on the motion of the parties?** It is unquestionable that rules of the conflict law form a part of the Czech law, or the law applicable on the territory of the Czech Republic respectively. Hence there is not reason – unless they determine liberty of their application themselves – to treat them in a manner different from other legal rules, i.e. they are applied in the extent of their applicability (Section 1 of PILA). Neither the Czech literature nor the known cases resolved by the Czech courts mentioned a consideration of facultative application of conflict-of-law rules. The fact that the conflict law would not be applied and this resulting into application of another law should in case of review lead to cancellation of the judgment.
2. **How is the foreign law treated - as the law or as a fact to be proved?** From the point of view of the Czech law, the foreign law is considered law and hence the principle *iura novit curia* applies also in this case. The new draft private international law act expressly mentions this principal.[9] Nevertheless, the doctrine never cast doubts on treatment of the foreign law as the law. Hence the judge has been obliged to ascertain the contents of the foreign law by all available procedural means.
3. **It is possible to review incorrect application of the foreign law by Czech courts?** The Czech doctrine mentions application of law as it is applied in the concerned state, to which is belongs. These days, this principles is mentioned expressly also in the new draft act. In the event of incorrect application of foreign law, the current doctrine as well as literature approve of the review. There is however no case known as yet from judicial practice.

In the context of the relationship to the groups of rules, which we monitor, the following questions may be put:

1. If the subject-matter of interest of the private international law is to settle conflicts, how can we define these conflicts? Are they conflicts of legal systems of states and has there been a move towards the practice before certain arbitrators and this conflict may be understood also as a conflict between state legal systems and the group of rules of non-state origin? The standpoint to the question will help us take a stand to the lex mercatoria as the so-called law of international merchants. It will allow us to state whether the lex mercatoria or non-state means are directly applicable or only in the context of mandatory rules of the applicable law (determined by the parties by means of the choice of law or otherwise).

2. What is the relationship between various sources of regulation of the conflict-of-law and substantive rules? Is the method of regulation important too? In consideration of the various sources of regulation of the international purchase agreement, this viewpoint is naturally important too.

ad 1. The issue of applying the lex mercatoria or individual rules of non-state origin accompanies the area of relationships with international element as of the sixties of the last century. A number of works[10] has provided their opinion both on the issue of rivalry between the conflict law and the lex mercatoria and on the issue of possible application of the lex mercatoria or individual rules when applying the conflict-of-law method. The fact is that until the end of the last century, discussions addressed almost exclusively proceedings before arbitration courts.

As concerns the Czech law, the provision of Section 9 of PILA did not admit any doubts on application of the state law. The doctrine was negative also as regards the option of direct application. The only possible application of individual rules of non-state origin was their application within mandatory rules of the applicable law. The situation did not change after accession to the Convention on the Law Applicable to Contracts[11]. Neither language versions nor the literature to the Convention allow direct application of the lex mercatoria or individual means of non-state regulation.

An improvement in this issue is brought about only by the so-called Green Paper[12]. Therein the Commission – for the sake of the future conversion of the Convention into a Regulation – put also questions concerning the possible direct application of international treaties (for example those which have not become valid) and trade terms. The draft regulation of 2005[13] did not allow application of the lex mercatoria but it permitted application of individual non-state regulations like the UNIDROIT or PECL Principles of International Contracts. The proposal clearly reflected the effort to make use of the work of Landa's groups. It is a fact that following discussions, representatives of the states did not recommend this solution. Rome I Regulation does not include this option anymore, not in relation to the lex mercatoria or even to the above-mentioned sets of legal standards. Only the preamble of the new Regulation expressed the will to consider the option of their application in the future[14]. Even though it does not follow from the wording that direct application is concerned, it is obvious that it should be this one. Indirect application, i.e. within the mandatory rules of applicable law, is beyond controversy possible even today.

The following conclusion can be made: Neither the wording of the Rome I Convention or of the Rome I Regulation nor the provisions of the national law allow an option of direct application of the lex mercatoria or a set of legal standards of non-state origin. Their application is possible only within the mandatory rules of the otherwise applicable law (determined by choice of law of the parties or as a substitute law). Point 14 of the Preamble to the Regulation I does not mean any change in this respect. However, it shows a path to follow – a regulation with the same nature of rules as in the UN Convention on Contracts for International Sale of Goods – i.e. with directory nature of rules or an option of exclusion.

ad 2. The rules (conflict-of-law or substantial) we monitor can be included in various sources. A conflict of sources of regulation affected also by the purpose of the rules[15] requires at least the basic information on its perception in terms of the law valid on the territory of the Czech Republic. Hence in the concerned case, one may consider applying:

- **Rules of national and international origin (act v. international treaty).** This conflict is addressed in Article 10 of the Constitution. In accordance with this Article, published international treaties, whose ratification has been approved by the Parliament and which are binding on the Czech Republic, form a part of the legal order. If the international treaty determines anything differently from an act, the international treaty shall apply. In terms of the issue of private law, in which we are interested in, one may encounter rules of identical wording and different interpretation. This problem caused by differences in the accents on interpretation methods on international or national level accompanied by the emphasis laid on autonomous and uniform interpretation may cause problems. In this case, authors from the area of private international law tend to the preferential application of the international treaty.

- **Rules of national and European origin**. The basic principle of the European law is the application precedence to the national law established by judgments of ECJ. From this point of view an express provision in the new draft of PILA is very interesting. This provision expressly mentions the precedence of directly applicable provisions of the European law if they are inconsistent with the provision of law. This provision seems suitable to us not in cases where Regulations or

Directives are concerned but rather in issues included in the establishing Treaties. This would allow preferential application of another standard that specified in the new PILA.

- Conflict of rules of European and international origin. As concerns the issue of law applicable to contracts, which we follow up, this is a relationship between the Rome I Convention and the Rome I Regulation. This relationship is unambiguously solved in Article 24 of the Regulation. As concerns bilateral treaties on legal aid, the regulation of possible conflicts is included in Article 25 par. 2 of the Regulation.

- Conflict between international treaties. In the area of the purchase agreement, which we follow up, we may encounter this type of conflict only after the Rome I Convention became valid. In the past, the Czech Republic was not a party to a bilateral treaty including conflict-of-law rules. In the monitored area, the UN Convention on Contracts for International Sale of Goods and the Convention on Law Applicable to Contractual Obligations may hence get into conflict in the field international purchase agreements. The basic starting point for a solution thereof is the nature of the conflict as a conflict of international treaties. The very wording of both Conventions does not prevent application (Article 21 of the Rome Convention, Article 90 of the Vienna Convention) of the other one of them. The Czech literature points out the applied method and its ability of more effective regulation. Without any other considerations, it is applied preferentially within the scope of its applicability.

Conclusion: As concerns the issue of relations between individual sources as they have been mentioned, there are no problems either in the literature or in practice. As concerns the relationship between the Rome Convention and the Vienna Convention, the Czech court unambiguously solve it by preference of the rule, which includes uniform substantive rules.

III. Uniform Substantive Law and its Relations

Uniform rules of substantive law mean such rules, which are the result of universal unifications processes. It is true that after decades of efforts to create unified regulation, the results are limited. In the field of substantive law, the most pronounced is the activity of UNCITRAL. It is represented both by model acts and by international treaties. The most successful result is the UN Convention on Contracts for International Sale of Goods and the

Convention on the Limitation Period in the International Sale of Goods.

In the area, which we monitor, we may ask the following questions:

1. Is there in addition to the basic principle of preference of uniform substantive rules to the conflict-of-law one also another aspect of their mutual relationship?

2. As concerns application of the lex mercatoria or individual non-state means of legal regulation, what are the options of their application?

ad 1. At the basic level, we defined the relationship as a relationship of application preference of individual rules. Nevertheless, this statement has also other aspects just as regards our example of the international purchase agreement regulation. It is the following:

a) Special reference rules, which means the rules intentionally referring, together with the reference, to the law of the state as well as to CISG. I mean the case mentioned in Article 1.1.b). Even in the event when the conditions of Article 1.1.a) are not met and the Convention is applied directly and preferentially, its application is not excluded either. We may consider Article 1.1.b), which reflects the fact that CISG forms a part of the law valid on the territory of the state, to which refers the conflict-of-law rule. The rule thereby indirectly extends the applicability of CISG. The Czech Republic filed a reservation to this Article. This type of Convention shall not be applied before Czech courts.

b) Additional conflict-of-law rules. They shall be applied in cases when the Convention excludes certain issues from its regulation (Articles 4, 5) or where there are gaps in the regulation (Article 7.2). The conflict-of-law rules of the forum shall be applied either directly (Articles 4, 5) or where there are no general principles, on the basis of which it would be possible to regulate the relationship (Article 7.2).

Conclusion: Mutual intersections of conflict-of-law rules and uniform substantive rules are a reality in the field of regulating private legal relationships with an international element. On one side, the create networks of regulations, which are difficult to understand of a laic, on the other hand, however, this compromise allowed adopting of the Convention.

ad 2) The issue of the relationship between Vienna Convention and the lex mercatoria has several aspects. This relationship was concisely described by Audit[16] who said that: "*Despite their differences, the Vienna Convention and the lex mercatoria do not compete for the status of being the exclusive source of law for international trade. Although the rules of the Convention are approved by states, they operate in conjunction with international trade usages and the principle of contractual autonomy*". Mutual relationships are allowed on the basis of:

a) The directory nature of the Convention as a whole as well as its individual rules (Article 6). On the contractual basis, it is possible to refer to any grasp-

able legal rule of non-state origin. In consideration of the wording of Article 4, it remains questionable however whether a direct reference to the lex mercatoria as a whole would be valid. In our opinion, such type of reference would be "verified" by return by means of the conflict-of-law rules of the forum. Hence a direct replacement is not possible on the level of substantive law.

b) The regulation of international trade usages in Article 9. This type of a non-state mean can be applied both on basis of an inclusion directly to the contract or on the basis of hypothetical will of the parties. Also in this case, only individual rules may be grasped, specifically those one, which may be qualified as trade usage or international trade usage, not as the lex mercatoria as a whole.

Conclusion: The Vienna Convention allows an extensive application of individual non-state means of legal regulation. Application of the lex mercatoria while applying the principle of autonomy of the parties' will is not possible. Such clause would be verified by return via the national legal system due to Article 4.

IV. Existing and Potential Relationships

In this paper, we made an attempt to indicate various levels of and mutual relationships between legal rules intended to regulate private legal relationships with an international element. We can state the following:

- Basic construction line consisting of the state law. As concerns both the sources and the methods of regulation, the application hierarchy is clear.
- Effect of autonomy of the parties' will. It affects application of rules of non-state origin both in terms of the conflict-of-law method and in terms of the direct method. Specifically, we can mention the following:

a) Influenced application of uniform substantive rules, namely as concerns the exclusion of application of the rule as a whole and as concerns exclusion of an individual rule (see Article 6 of CISG). Application of another rule (created by will of the parties, a non-state rule of legal regulation, the lex mercatoria as a whole) is however limited by Article 4 of CISG.

b) Option to choose the state law without restrictions (see Article 3 of the Rome I Regulation and the Rome I Convention). Nevertheless, application of rules of non-state origin is possible only within mandatory rules of the applicable law (state).

Direct application of the lex mercatoria is in all cases determined by the standpoint of the state law, whether upon application of the conflict-of-law method or the direct method.

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[1] Horizontal relationships shall mean the case when the rules of the same legal force get into conflict and it is necessary to decide on the application precedence.

[2] Similar representation of the said groups of rules may be noted also in relation to another contractual type – international contract of carriage.

[3] The proceedings before arbitrators differ in a number of aspects. The doctrine reflected in the regulation, opinions of arbitrators sharing various theoretical positions, greater extent of autonomy of the contracting parties' will, less intensive relationship of arbitrators to the territory of the state, in principle non-reviewable decision-making about the law applicable in the proceedings before arbitrators, all this requires for the different commentary of this subject matter. See: Rozehnalová, N.: Rozhodčí řízení ve vnitrostátním a mezinárodním obchodním styku. Praha:ASPI CODEX. 2008, p. 54–60.

[4] There are severel approaches to the conception of lex mercatoria. See for example: Goldmann, B.: Lex mercatoria, Forum international No.3, 1983. Goldštajn, A.: The New Law Merchant Reconsidered, Festschrift Schmitthoff, 1973. Goldštajn, A.: The New Law Merchant, Journal of Business Law, 1961. Langen, E.: Transnational Commercial Law, Leiden, 1973. Rodríguez López A.M.: Lex Mercatoria and Harmonization of Contract Law in the EU, DJOF Publishing, 2003. Rozehnalová, N., Transnacionální právo mezinárodního obchodu, Brno, 1994. Rozehnalová, N.: Lex mercatoria - teorie či fikce, Právník, 11, 1998. Schmitthoff, C.M., The Law of International Trade, its Growth, Formulation and Operation, in: The Sources of the Law of International Trade, London, 1964. Schmitthoff, C.: M., Nature and Evolution of the Transnational Law of Commercial Transaction, in: The Transnational Law of International Commercial Transaction, 1982. Teubner, G.: Global Law without a State, Dartmouth, 1997.

[5] There is no ideal solution built on universal basis agreed for example in an international contract.

[6] See the definition of Section 1 of Act No. 97/1963 Coll. on Private and Procedural International Law (hereinafter referred to as PILA): *The purpose of this Act is to determine, which legal system is to be applied to civil, family, labour and other similar relationships with an international element, to regulate the status of foreigners as well as to determine the procedure of Czech judicial bodies when regulating and deciding on these relationships and thereby contribute to international cooperation.*

[7] See for example Kučera, Z.: Mezinárodní právo soukromé, Brno: Doplněk, 2004, P. 17 – 26.

[8] In foreign literature see for example: Geeroms, S., Foreign Law in Civil Litigation, Oxford, 2003. Hausmann, R., Pleading and Proof of Foreign Law– a Comparative Analysis, the European Legal Forum, 1- 2008.

[9] Private International Law Act – Draft from November 2008, art. 24.

[10] See for example v. Bar, Ch., Mankowski, P, Internationales Privatrecht, München, 2003, p. 75 et seq . Boele-Woelki, K., Principles and Private International Law, ULR, 1996, p. 652 et seq. Lando, O., Conflict-of-Law- Rules for Arbitrators, Festrichrift Zweigert, 1981. p.157 et seq. . Lando, O., The Lex Mercatoria in International Commercial Arbitration, ICLQ,

1985, p. 747 et seq. López Rodríguez, A.M. Lex Mercatoria and Harmonization of Contract Law in the EU, Copenhagen, 2003. In Czech literature see for example: Kučera, Z. op.cit. 7, p. 206 et seq. Rozehnalová, N., Střelec, K, Zásady mezinárodních smluv UNIDROIT, lex mercatoria a odvaha k aplikaci, Časopis pro právní vědu a praxi, 2004, č. 1, s. 45 a násl. Salač, J. Nástin vývoje a význam, Právník, 1998, p. 498 et seq.

[11] The Rome Convention on the law applicable to contractual obligations (1980).

[12] COM(2002) 654 final 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.

[13] COM(2005) 650 final 2005/0261 (COD) Proposal for a Regulation of the European Parliament and the Council on the law applicable to contractual obligations (Rome I).

[14] Preamble, Article 14: If the Community adopts the rules of contractual obligations including the standard terms of contract by means of a suitable legal tool, such tool may determined that the contracting parties are allowed to apply these rules.

[15] Here the objective is to determine the legal system and only subsequently to regulate the conduct of the parties to a private legal relationship, or directly to regulate the conduct of subjects of a private legal relationship.

[16] Audit, B., The Vienna Sales Convention and the Lex Mercatoria, in: Thomas E. Carbonneau ed, *Lex Mercatoria and Arbitration*,., Juris Publishing 1998, pp. 173-194.