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Practicing the Law of the World from New York

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Choosing New York Law as Governing Law for International Commercial Transactions

By Michael W. Galligan

Introduction

The state of New York encourages the choice of New York law as the governing law of international commercial transactions by permitting parties to a transaction where the consideration or obligation is not less than $250,000 to choose New York law "whether or not such contract, agreement or undertaking bears a reasonable relation" to New York state.[1] New York also encourages parties to international commercial transactions to use the courts of New York to adjudicate and resolve their disputes where the dispute arises from a contract, agreement or undertaking governed by New York law and where the consideration or obligation is not less than one million dollars.[2]

For most practitioners concerned with business, commercial and corporate law, the starting point of analysis for making a choice of law for an international commercial transaction is contract law. There are a number of salient differences in the approach to contract and commercial law in New York law (and other common law jurisdictions in general) on the one hand and civil law jurisdictions on the other hand. There are some less well known differences between New York law (and the common law of many other U.S. jurisdictions) and English law (and other exemplars of common law).

In addition, one must consider the impact of international treaties to which New York, as one of the United States of America, is bound and which therefore constitute part of New York law and the areas of commercial law relevant to the transaction. In the field of contract law, the most important of these treaties is the United Nations ("Vienna") Convention on the International Sale of Goods ("CISG"). The CISG actually constitutes the law of New York for international sales transactions where all of the parties have their places of business in one of the many countries that have become parties to the Convention (absent an agreement by the parties to "opt out" of the CISG rules under Article 6 of the Convention).[3]

In addition, in the twenty-first century, it is not enough to compare New York law with the law of other countries. There are a growing number of international formulations and "restatements" of law, particularly in the area of contract law, that have themselves become sources of law and that offer options to international businesses making choices about what law should govern their transactions. Chief among these are the UNIDROIT Principles of International Contract Law, the Principles of European Contract Law, the Draft Common Frame of Reference, and the OHADA Uniform Act on Contract Law.

Part I of this article—the longest—discusses key features of New York contract law and compares and contrasts New York's approach with those of English law, French law, German law, the provisions of the CISG (remembering, of course, that, for many international sales transactions, the CISG is itself the law of New York) and two of the most influential international contract restatements, the UNIDROIT Principles and the European Principles.[4] Part II features brief discussions of some distinctive features of New York commercial law. Part III consists of a short reflection on three points of distinction of New York procedural law that are very relevant to choices of substantive law. Part IV summarizes some of the conclusions of Parts I through III (particularly Part I) and offers some constructive proposals for revision or adjustment of New York law to promote a greater harmony between New York law and other sources of the international law of commercial contracts and to make New York law a more effective instrument for the promotion and support of international trade.

I. Contract Law

Common law and civil law all derive from Roman law (at least as articulated by the great legal scholar, Grotius, and his contemporaries) the basic legal principle that contracts must be fulfilled. But they differ in many important respects, including but not limited to (i) what types of contracts will be enforced, (ii) how contracts are to be construed and interpreted, (iii) whether and under what circumstances third parties can have rights under a contract, (iv) under what circumstances performance under a valid and binding contract can be excused or avoided, (v) when conditions on performance apply, and (vi) what remedies are available when obligations under a contract are breached.

A. What Constitutes an Enforceable Contract

Perhaps the most important practical difference between the civil and common law concerns the rules for determining what contracts are enforceable. Both systems doctrinally require an agreement, generally reflected in an offer and an acceptance. Thus, under Article 1101 of the French Civil Code, "[a] contract is an agreement by which one or more persons bind themselves, as to one or more other persons, to give, to do or not to do something." The consent of the party that binds itself, for French contract law purposes, is the key factor in establishing a contract—so long as, in addition, each party undertaking an obligation has legal capacity to do so, the contract has a "subject matter," and the contract has a valid "cause" or purpose.[5]

The UNIDROIT Principles of International Commercial Contract Law are not far removed from this view by providing under Article 2.1.1, 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." Under Article 2:101 of the Principles of European Contract Law, a contract is concluded if (i) the parties intend to be legally bound and (ii) they reach a sufficient agreement.

The common law has long required that an agreement, to be valid and enforceable, must reflect some exchange of value—which can consist of promises or performances—that constitutes "consideration." In the words of one court, "[w]ithout consideration there is no contract."[6] For a long time, to demonstrate the existence of consideration, it was thought necessary that one party must receive a benefit and the other party must suffer a detriment; today it seems to be acceptable if both parties benefit. It is also accepted that an exchange of promises that impose duties of some sort on each party itself constitutes valid consideration.

The classic example of the difference the consideration requirement can make has to do with gifts. In the civil law system, a promise to make a gift is generally enforceable, at least if it is in writing, even if the promise is gratuitous in nature.[7] Under English law, such a promise would not be enforceable unless made by deed or under seal.[8] Under New York law, by contrast, such a promise would not be enforceable in the absence of a demonstration of reasonable reliance on the promise and detriment by the promisee.[9]

It is important to be clear that the requirement of consideration is not a rule that consideration must be adequate or fair. The idea that the exchange must have been "bargained for," which has been adopted by courts in New York and in England, is largely intended to preclude the need for courts to delve into examinations of the fairness of contractual exchanges.[10]

Now, it may seem that, for the majority of contractual arrangements emerging from business negotiations and exchanges, the requirement of consideration should make little practical difference, since most commercial agreements are precisely the fruit of the give and take that we associate with bargaining and on which the requirement of consideration seems to be founded. After all, it has even been said that, in New York, "[r]ecitals of 'value received' are nearly conclusive evidence of consideration."[11] But in a number of situations, a lack of consideration under a strict application of the doctrine of consideration can make a difference between enforceability and non-enforceability: these include contract amendments, releases, and irrevocable assignments. New York has very helpfully provided statutory relief from the requirement of consideration for contract amendments and releases that are in writing under Section 5-1103 of the New York General Obligations Law. And Section 2-209(1) of the New York Uniform Commercial Code ("NY UCC") specifically exempts modifications to sales contracts from the consideration requirement. New York General Objections Law Section 5-1107 similarly exempts irrevocable assignments that are in writing from the consideration requirement. Finally, Section 5-1105 of the General Obligations Law actually disqualifies any attack on a promise that is in writing and is based on past consideration or prior obligation if the consideration is proved to have been given or performed and would have been valid consideration but for the time when it was given or performed. English law, by contrast, does not have a scheme of statutory relief in instances like this: a 1937 proposal for that purpose was never enacted. It is said that English courts have cut back the requirement of consideration in many of these circumstances by case law, but cases can always be distinguished. Thus, there is good reason to say that New York law confers more security and certainty on this important issue and thus also "levels the playing field" with civil law systems, for which consideration is not a factor.

In the final analysis, the important role that the doctrine of consideration plays in New York law has less to do with legal formalities and more with the way it contributes to what is sometimes called the "objective" orientation or perspective from which New York law approaches issues of contract law in general. Increasingly, in civil law the elements of subject matter and purpose, at least in the area of commercial contracts, seem to be adventitious and secondary in importance, with the main focus being on the "subjective" state of the parties—that is, whether, in the interchange of offer and acceptance, the parties have formed among themselves a mutual understanding or consent that constitutes an agreement. Thus, under French law, proof that an agreement was the result of mistake or fraud or duress would vitiate the consent that is critical to the existence of a contract and lead to the conclusion that no contract existed at all.[12] Under common law, proof of mistake, fraud or duress would make a contract voidable but, for example, in the case of fraud, the defrauded party usually has the option of having the contract rescinded or affirming the contract and suing for damages.[13]

This objective emphasis also evidences itself in another aspect of New York law: what a court may do to "save" a contract that is missing an important or essential term. A contract is missing an essential term if a basic component, such as price, is missing. On the one hand, an agreement by the parties to negotiate an essential term later on is generally not enforceable; a contract will not be enforced if the only way to fill in the gap is to wait for the parties to agree. But courts look for ways to interpret a contract to supply the missing term, especially if the parties have manifested an intent to be bound and there is evidence from commercial practice or usage in the area of business covered by the contract that would enable

a court to supply the missing term. Notice that the one thing a New York court would generally not do is to attempt to detect the intent of the parties by testimony as to the missing term: this will put a court in the position of having to determine the subjective intentions of the parties—something a common law court is generally loathe to do. But the court can and will, on its own initiative, seek to fill the term if it can make reasonable inferences from the objective evidence of the agreement and the customs and practices of the relevant area of business or commerce.

B. How Contracts Are to Be Construed and Interpreted

New York, like some other common law jurisdictions, requires some written evidence as an additional requirement for the enforcement of many contracts. These include contracts that, of their nature, take more than a year to perform, contracts for the sale of real property, agreements regarding the debt of another and promises to pay a debt discharged in bankruptcy, finder's fees and fees for services payable other than to attorneys, and real estate brokerage fee arrangements. In addition, New York Uniform Commercial Code Section 2-201(1) requires a writing in the case of contracts for the sale of goods in excess of Five Hundred Dollars. French law, while also requiring written evidence for contracts above a certain amount set by regulation, exempts commercial contracts from this requirement. English law, from which New York inherited the so-called "statute of frauds" (which is the origin of these writing requirements), has actually eliminated the requirement of a writing for all contracts except real estate contracts.

Agreements that are strictly oral in nature by necessity have a more subjective component, since there must be much more reliance on memory and mutual subjective understanding to prove the existence of a contract and to interpret it. In maintaining the requirement of at least some written evidence of a contract for enforcing a contract, the "statute of frauds" shifts the balance more in the direction of objective evidence that stands by itself apart from the memory of the parties. It should be noted that the writing that is required here is not necessarily what we would think of as a fully drawn agreement; in many cases a fairly minimum amount of written evidence is sufficient and, in a number of instances, partial or full performance of an obligation eliminates the need for the writing. Of course, it goes without saying that sophisticated international transactions will virtually always be reflected in a detailed written agreement anyway. Thus the importance of the writing requirement is important less for its practical relevance but for the way it tends to support the focus on an "objective" source for determining whether a contract exists and for determining its specific terms and obligations.

In the case of written agreements, however, New York law takes this objective orientation a step further by prohibiting, in the case of a dispute about the terms of an agreement, oral evidence of prior negotiations, representations and inconsistent understandings. Often known as the "parol evidence" rule, it might be better described as the "anti-extrinsic evidence rule." New York is said to have a "hard" parol evidence rule, as expressed in the "four corners" principle, under which a court must decide whether the terms of a contract are ambiguous on the basis of its analysis of the document itself and may only consider extrinsic evidence (written or oral) if it determines, as a matter of law and not of fact, that one or more of the contract terms are ambiguous. New York courts give even greater protection against extrinsic evidence regarding the terms of a contract if the parties have agreed to "merge" or "integrate" their agreement, extending the exclusion of oral evidence about so-called "collateral agreements," *i.e.*, agreements entered into at the same time as the agreement under judicial scrutiny. Such provisions are given almost complete deference by New York courts.[14]

The effect, if not the purpose, of the parol evidence rule and the merger rule is to clearly encourage parties to use agreements that fully set out the terms and obligations of the transactions and relationships. New York courts continue by and large to give effect to the "plain meaning" and "four corners" principles: a court's primary role is to give effect to the parties' intent as evidenced by the written contract. If that intent can be discerned from the plain meaning of the written agreement without recourse to any other document or representations (*i.e.*, "within the four corners" of the agreement), the court's interpretive task is to give effect to the terms of the agreement as thus disclosed.[15] Extrinsic evidence can be admitted to establish the meaning of ambiguous terms only if the court determines that the contract cannot be reasonably construed and interpreted based on the aforementioned principles. Notice that if an essential term of a contract is missing and the issue is not simply the meaning of an ambiguous term, two consequences can follow. One, the agreement may fail to qualify as a legal contract because there was no content to the agreement about which there could be meeting of the minds in the first place—the terms of the agreement would be simply too vague for there to have been an offer and acceptance that could be the basis for agreement. Two, the other possibility, at least in the case of contracts for the sale of goods (especially among business parties), is that courts can supply the missing term based on custom in the relevant industry or reasonable commercial practice in that area of business or the past practice of the parties themselves.[16]

It is often said that New York courts are not prone to substitute their judgment for the terms to which contracting parties have agreed and, indeed, this judicial restraint is one of the major reasons why contracts governed by New York law are said to be "certain" and sure to be confirmed according to their terms. As we can see from some

of the features of New York contract law just described, this is not just a matter of general philosophy but the fruit of the focus of New York law on the elements of bargaining and consideration in determining whether a contract exists at all, in the requirement of a writing for many types of contracts (especially those with longer duration or with more economic value at stake), and the strong deference to the written expression of contractual terms (thus limiting the ability of parties, whether deliberately or unwittingly, to try to amend their contracts by oral recollection and putting the court in a position of having to decide whether a written or oral version of the terms of a contract is more persuasive). This is all in marked contrast to the tendency in the civil law tradition to favor shorter and less exhaustive agreements and the willingness to rely on courts to fill in missing terms and to apply and even reshape contractual arrangements.

1. Excursus on the "Battle of the Forms"

A subsection of contract law that manifests some interesting differences between the law of New York and many other U.S. jurisdictions on the one hand and English law and most civil law jurisdictions on the other hand concerns how a contract is constituted and how it is construed in the often quick-fire world of the sale of goods, where contracts are often not negotiated or carefully drafted and where the terms of the contracts are determined by exchanges of offers and acceptances (with buyers and sellers on both sides of the offer-acceptance dichotomy) on standardized forms that include the buyer's or seller's preferred terms and conditions. These differences are especially relevant when acceptance of an offer is indicated not by an executory promise but by a performance—usually delivering goods or accepting goods and/or rendering payment.

The traditional common law approach is exemplified in the "last shot" rule: a seller who delivers a product in response to an offer to buy accompanied by variations from the terms of the offer can set the terms of the contract if the buyer accepts the goods because the variation in the seller's terms means that the seller has legally rejected the offer and substituted its own offer, which the buyer's acceptance of the goods confirms and ratifies. European law is generally consistent with this approach. For example, classical French jurisprudence would insist that there must be "an agreement of the parties on all the conditions of the contract."[17] The German Civil Code follows this principle when it provides, in Article 150(3), that "[a]n acceptance with amplifications, limitations or other alterations is deemed to be a refusal coupled with a new offer." Article 154 of the *Bürgerliches Gesetzbuch* ("BGB") provides that "So long as the parties have not agreed upon all points of a contract upon which agreement is essential, according to the declaration of even one party, the contract is, in case of doubt, not concluded." All of these approaches focus on "consent" as the key factor in determining if a contract exists—with the focus on searching for the "mirroring" of the subjective intentions of the parties.

The New York Uniform Commercial Code takes a very different approach by providing in Section 2-207(1) that "[a] definite and seasonable expression of acceptance or a written confirmation which is sent within a 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." Under this approach, acceptance of an offer to buy by delivery of the goods, even if the delivery is accompanied by different terms and conditions, represents an acceptance of the offer so that a contract has been established. This does not mean that the inconsistent terms included in the seller's document necessarily become part of the contract: "The additional terms are to be construed as proposals for additions to the contract."[18] But, as between merchants, "such terms become part of the contract" subject to certain exceptions, the most interesting of which is that "they materially alter it."[19] Thus, even terms that materially alter the contract do not necessarily invalidate the contract, but rather create an issue about the terms of the contract. In such cases, "the terms of the particular contract consist of these terms in which the writing of the parties agree, together with any supplemental terms incorporated under any other provisions of the Act."[20]

Section 2-207(2) of the New York Uniform Commercial Code provides no express guidance as to the criteria for determining whether an additional term materially alters the terms of an offer under Section 2-207(1), although Comment 4 to Section 207 suggests that the test of material alteration is whether the additional term would "result in surprise or hardship if incorporated without express awareness of the other party." It has been suggested that evidence that the offeror never objected to the addition of a term similar to that added by the offeree and accepted by the offeror in previous transactions between the parties establishes a "course of dealing" between them and therefore cannot arise to the requisite "surprise" needed to meet the materiality test.[21] Under NY UCC Section 1-205, "a course of dealing…is fairly to be regarded as establishing a common basis of understanding for interpreting [the] expressions and other conduct" of parties to a particular transaction. Reference to courses of dealing between contracting parties for establishing the terms of a contract seems to be blessed by NY UCC Section 2-207(3), according to which "[c]onduct by both parties" recognizing the existence of a contract can be sufficient to establish a contract, the terms of which agreement will consist of the writings of the parties…together with any supplementary terms incorporated under any other provisions of this Act," including presumably Section 1-205. However, it should be noted that NY UCC Section 2-207(3) usually applies when the parties have failed to establish a contract under Sections 207(1) and (2) and that

the terms proposed to be added by the offeree under Section 207(2) may not avail if the contract is established by conduct of the parties under Section 207(3) rather than by the exchange of express contractual terms under Sections 207(1) and (2).[22]

England has not passed any legislation similar to NY UCC Section 2-207. Lord Denning, in the much-discussed case of *Butler Machine Tool Co Ltd v. Ex-cell-O Corporation (England) Ltd.*,[23] proposed that "[t]he better way is to look at all the documents passing between the parties—and glean from them, or from the conduct of the parties, whether they have reached agreement on all material points." But it is unclear how widely this approach has been accepted in England. The rule of Uniform Commercial Code Section 2-207 makes more sense in a jurisprudential environment where the focus on the subjective intentions and meaning of the parties is less important than the outer or objective inferences that can be drawn from the conduct of the parties and where courts focus more on what a "reasonable person" might think the parties intended or meant. Ironically, by requiring that the terms to which the parties have agreed be supplemented by terms incorporated under other provisions of the Act, Section 2-207 seems to create an opportunity for New York courts to become involved in contract supplementation more familiar to civil law practice than to common law practice.

2. Excursus on "Plain Meaning"

It should be pointed out that adoption of the plain meaning rule does not mean that courts in either New York or England are bound to a purely literalist construction of contracts based on the dictionary meaning of the words. Lord Hoffman, in *Investors Compensation Scheme Ltd v. West Bromwich Building Society*,[24] set forth a so-called "modern" approach to contract construction that emphasizes not so much the meaning of words in dictionaries and grammars but rather what "the parties using those words against the relevant background would reasonably have been understood to mean." New York courts have emphasized the importance of the "purpose of the contract" and interpreting the terms of a contract consistently therewith.[25]

3. Excursus on "Entire Agreement" Clauses

Under New York law, the parol evidence rule does not by itself preclude evidence of collateral agreements or understandings. To preclude evidence of such other agreements and understandings, a contract must contain a provision that recites that it represents the sole and complete ("entire") expression of the parties' understanding, thus "integrating" or "merging" any other agreement or understandings into the contract.[26] The same option is available for purposes of contracts for the sale of goods, under Uniform Commercial Code Section 2-202. English law generally follows the same concept.[27] While the parol evidence and "merger" clauses were generally unique to the common law, the concept of precluding oral evidence in the case of agreements that contain an "entire agreement" clause has been accepted by the UNIDROIT Principles of International Commercial Contacts at Section 2.1.17 and by the Principles of European Contract Law at Section 2.05.

Notwithstanding the general acceptance of entire agreement clauses by New York law as well as English law, it appears that English courts are inclined to read these provisions more strictly, especially when issues of misrepresentations have been raised. The issue is whether such undertakings preclude evidence of pre-contractual representations. Thus, in *Thomas Witter Ltd v. TBP Industries Ltd*,[28] and *EA Grimstead & Son Ltd v. McGarrigan*,[29] the court held than an "entire agreement" clause did not exclude remedies for alleged pre-contractual understandings where the agreement incorporated in the contract contained an acknowledgement that the plaintiff party had not been induced to enter the contract by any representation or warranty other than the statements contained in the warranty schedule.[30] It has been suggested that, in England, taking into account the provisions of the Unfair Contract Terms Act 1977, any such non-reliance clause must distinguish between innocent and negligent misrepresentation, on the one hand, and fraudulent misrepresentation, on the other.[31] New York courts are more likely to bar fraudulent as well as non-fraudulent misrepresentation claims where the contract has a specific statement of nonreliance with regard to representations on which, under the clause, the parties have agreed they have not relied. The authority for this broader enforcement was set forth by the New York Court of Appeals in *Danann Realty v. Harris*,[32] and applied in *Grumman Allied Industries Inc., v. Rohr Industries*.[33]

C. The Role and Application of Good Faith Under New York Contract Law

New York law (and to a certain extent a number of other U.S. jurisdictions—though not all) stands in an interesting "middle" position between the civil law on the one hand and English law on the other hand when it comes to the doctrine of "good faith" in the law of contracts. Perhaps the most noted example of the legal requirement of good faith is to be found in Section 242 of the German Civil Code, which provides that all contractual obligations must be performed with "faith and trust" ("*Treu und Glauben*"). Article 1143(3) of the French Civil Code similarly provides that contracts must be carried out in "good faith" ("*bonne foi*"). Several articles of the Italian Code also impose a "good faith" requirement: Article 1375 requires that a "contract must be performed in good faith"; Article 1366 provides that a "contract must be interpreted in good faith"; and Article 1337 imposes obligations of "good faith and fair dealing" in debtor-creditor relations. The principle of good faith has become enshrined in efforts to harmonize European and international laws of contract. Thus, Article 1.106 of the Principle

of European Contract Law imposes an obligation of "good faith and fair dealing." The UNIDROIT Principles of International Contract Law impose a similar obligation. The Convention on Controls for the International Sale of Goods does not have an express provision imposing a duty of good faith in the performance of contracts, but it does provide that regard must be had for "promoting the observance of good faith in international trade" in the interpretation of the Convention.

New York courts were the first courts in the United States to introduce the implied covenant of good faith into contract law jurisprudence. In *New York Central Iron Works Co. v. United States Radiator Co.*,[34] a case involving a long-term requirements contract, the Court of Appeals declared that "[t]he obligation of good faith and fair dealing towards each other is an implied concept of this character." Another landmark case was *Wood v. Lucy*,[35] in which Justice Benjamin Cardozo, then sitting on the New York Court of Appeals, opined that the contract at issue was "instinct with an obligation, imperfectly expressed" of good faith performance. The duty of good faith was further strengthened under New York contract and commercial law when New York, in 1962, adopted the Uniform Commercial Code. Section 1-203 of the Uniform Commercial Code provides that "[e]very contract or duty within this Act imposes an obligation of good faith in its performance or enforcement." Section 2-103 of the Uniform Commercial Code defines good faith for purposes of the sale of good as "honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade."

New York continues to adhere to this principle.[36] For New York law, the duty to act in good faith under a contract is not generally separable from a duty to perform one's duties under the contract itself. Thus, a breach of a covenant of good faith is generally not seen as giving rise to an independent cause of action.[37] It is supposed to aid the interpretation and performance of the terms of the contract itself "by protecting the promise against breach of the reasonable expectations derived from an agreement of the parties."

In the early New York cases, such as *New York Central Iron Works*, the implied covenant was introduced to construe contracts in a manner that was commercially reasonable and fair without compromising New York law's adherence to the plain meaning and parol evidence rules.[38] As recently as 1995, the Court of Appeals suggested that, within the parameters of protecting the reasonable expectations of the parties, courts can read or imply into a contract "a promise that a reasonable person in the place of the promisee would justifiably believe was included within the contract."[39] But in an age where more and more contracts between commercial parties are written with the assistance of counsel, the need and inclination of New York courts to use the covenant for the purpose of essentially supplementing or revising contracts can be said to have waned. A few years before *Dalton*, the Court of Appeals had noted that "[f]reedom of contract prevails in an arms-length transaction between sophisticated parties and, in the absence of countervailing public policy concerns, these parties will not be relieved of the consequences of their bargain."[40] In *Reiss v. Financial Performance Corp.*,[41] the Court of Appeals declined to imply a contractual term to a contract for the purchase of stock warrants to deal with the contingency of a reverse stock split after the terms of the purchase were set. To the Court, the possibility of a stock split was reasonably foreseeable and the parties had to be assumed to have advisedly declined to address modifying the purchase price in the event of any such split. While this decision seems to run contrary to an earlier decision of the U.S. Court of Appeals for the Second Circuit in *Bank of China v. Chan*,[42] which suggested a more generous approach to implying terms not expressly addressed, the *Reiss* case seems to underscore the policy of New York law not to allow the covenant of good faith and fair dealing to become an excuse for commercially sophisticated parties not to carefully consider and address all foreseeable issues that could arise under the terms of their transactions.[43]

Thus, in many ways, the covenant of good faith, as between sophisticated commercial parties, tends to serve primarily as a "negative protection," *i.e.*, allowing the court to imply prohibitions on conduct that would undermine the performance of obligations of an agreement or deprive a party of the benefit of its bargain. "The covenant applies only where an implied promise is so interwoven with the contract as to be necessary for the effectuation of the purpose of the contract. For a violation of the covenant to occur, the defendant's action must directly violate an obligation which may be presumed to have been intended by the parties."[44] In such cases, at least one New York court has suggested that a separate claim for violation of the covenant of good faith might exist, even if there is no viable breach of contract claim, if a defendant has used its rights under the contract for its own gain or to deprive the plaintiff of benefits under the contract or to realize gains that the contract implicitly denied to the defendant.[45]

The reluctance of New York courts to apply the covenant of good faith and fair dealing to impose additional positive obligations on parties or to address contingencies the parties declined to address themselves contrasts with the more expansive view of the duty of good faith taken by civil law courts. For example, Section 242 of the German Civil Code, which imposes a duty of "trust and faith" ("*Treu und Glauben*") on contracting parties, was used very broadly by the German courts in the aftermath of the inflation after the First World War to relieve parties from the perceived loss of financial position that resulted from the massive devaluation of the German currency. Similar adjustments were made in cases arising after the conclusion of World War II. Implementation of this

provision in recent decades has been less dramatic but is still much more expansive than the New York approach. German courts are seen as having a broader ability to fill in gaps and to supply contractual provisions that will enable the transactions contemplated to be completed. According to a recent review of comparative perspectives on the notion of contractual good faith, Section 242 "notably permits the completion, limitation and concretization of existing agreements."[46]

French law has long been known for its insistence on the principle that contracts must be followed. The role of the principle of good faith has been said to be "moderating" and "a valve of commutative justice or of 'contractual solidarity.'"[47] The duty of good faith under French contract law is said to be "classically defined as the expression of the duty of loyalty by each co-contractor so as not to offend the confidence that gave rise to the contract [so that]…[t]he parties must act towards one another with loyalty, without fraud or malice." Expressed this way, the duty of good faith has led some legal scholars to conclude that the principle of good faith gives rise to a positive obligation of cooperation, and, at least in cases of "flagrant abuse," to imply obligations of information or security, in order to provide suitable remedies.

English law has, at least to date, steadfastly declined to adopt the principle of good faith into its contract law. English courts, it is said, have a reluctance to "generalize abstract principles" and a preference "to work with particular instances of duty which can be identified in particular cases."[48] Secondly, English judges have expressed concerns "about the lack of certainty in defining the duty of good faith in the context of the relationship between contracting parties"—particularly as this may apply to negotiations between parties before agreement is reached.[49] The discomfort about "abstract principles" seems, to this author, itself to be somewhat theoretical, as even the notions of consideration and agreement with which English courts are comfortable are themselves general principles that gather their meaning and application from particular cases. In the case of New York, it is clear that the principle of good faith has been handled very cautiously and with great discretion. It is not, except in some highly unusual situations, the basis of a cause of action or a claim separate from a claim of breach, and it has been used very sparingly to supply terms in existing contracts, especially in the case of written agreements between sophisticated commercial parties. At the same time, it places a certain "floor" as to the range of activities that parties to contracts may take in reference to the obligations they have undertaken. It recognizes that, while negotiations in certain contexts may indeed be adversarial at least in inception, many contracts, beyond those for discrete purchases of goods, entail longer relationships and therefore require a degree of mutual respect and cooperation that needs to be taken into account in determining the constraints that a party may need to place on its actions in order to perform its contractual obligations.

The principle of good faith has led to developments in two important areas of European law that New York law has been more hesitant to adopt: pre-contractual liability and adaptation of contracts for hardship or dramatic changes in economic circumstances.

1. Pre-Contractual Liability

A corollary of the rule that contracts must be observed would seem to be that no such duty arises until agreement has been reached. French law and German law have been more willing to find that certain remedies can be available for conduct that constitutes bad faith in pre-contractual negotiations. English law, by contrast, has been very reluctant to find any such liability. New York law admits the possibility of such liability in certain cases where parties have contractually bound themselves to conduct negotiations, but cabins any such liability very closely.

The concept of good faith and fair dealing in business negotiations received perhaps its best known formulation in the writings of the German nineteenth century legal scholar, Rudolph von Jhering. He argued that parties to pre-contractual negotiations have a duty of good faith, fair dealing, care and loyalty.[50] It has been suggested that this is consistent with the civil law's focus on the relationship between the parties (*i.e.*, their consent to be bound in duties to each other), as distinguished from the common law's stress on the bargain between them. Under French law, remedies for violation of duties inherent in pre-contractual negotiations arise under tort law, not contract law itself. Bases for liability can include "unjustified and abusive rupture of negotiations" as well as negotiation without serious intent to contract, failure to cooperate, misuse of information provided in confidence, entry into negotiations in order to prevent someone from entering into an agreement with another party, and failure to disclose essential and material facts. The chief factors that seem to increase the chance of a finding of liability are (i) the advanced stage of negotiations, (ii) the amount of work already undertaken, and (iii) the suddenness of the breaking off of negotiations.

Under German law, duties and liabilities with regard to pre-contractual liabilities are inferred from Section 242 of the Civil Code, so that the principle of good faith and fair dealing applies in the pre-contractual as well as the contractual stages. English law, by contrast, assumes that the relationship between the parties during negotiations, far from being one of mutual cooperation and loyalty, is intrinsically adversarial. Granted the assumed adversarial nature of the negotiation context, under English law, a party has the right to withdraw from negotiations at any time up to the point where a contract or agree-

ment has been reached. One exception to this approach is when there is an express agreement to renegotiate an agreement.[51]

The New York Court of Appeals, in *American Broadcasting Companies, Inc. v. Wolf*,[52] opened the door to possible pre-contractual liability for failure to negotiate in good faith in a case involving a contract between the famous sportscaster Warner Wolf and the American Broadcasting Company ("ABC"). The agreement between Wolf and ABC required that he "enter into good faith negotiations…for the extension of his agreement on mutually agreeable terms," and the Court of Appeals ordered Wolf to comply. But New York courts have been very careful not to extend this case beyond its facts. There can be an obligation only to negotiate in good faith when the parties use definite language indicating a present intent to be bound and "the subject of negotiations must be both specific and backed by ascertainable indications of intent regarding the anticipated outcome of the process."[53] Significantly, New York courts give great deference to stated intentions by the parties that they intended to execute their agreement in a written form. Thus, in *R.G. Group, Inc. v. Horn & Hardart Co.*,[54] the court stated that "when a party gives forthright, reasonable signals that it means to be bound only by a written agreement, courts should not frustrate that intent." An effort to try to find contractual liability in the absence of a concluded contract based on promissory reliance or estoppel was firmly rejected by the Federal Court of Appeals for the Second Circuit, per Judge Learned Hand, in *Baird v. Gamble Brothers*.[55] There, the court, applying New York law, declined to find a subcontractor accountable to the general contractor because the general contractor obtained a contract in reliance on the subcontractor's bid, which the subcontractor withdrew before the general contractor's offer was accepted by the contractor. Thus, while New York law may be slightly more open to enforcing express agreements to negotiate in good faith where a contract already exists or where sufficient terms have already been agreed to, New York law does not seem inclined to extend the duty of good faith and fair dealing in any significant way outside the contours of concluded contracts.

2. Notions of Impossibility, Impracticability and Hardship

One of the most salient issues of contract law—especially in the case of contracts that take a long time to perform—is whether circumstances could so dramatically change the obligations of the parties to each other so as to cause any of them to have a legal basis for suspending or terminating performance under the contract. In civil law systems, the adjudication of cases rests on concepts of *force majeure* and hardship, while in common law systems, the relevant concepts are impossibility of performance, frustration of contractual purpose, and commercial impracticality. In general, the concepts of *force majeure*, impossibility and frustration stand on one side of the more restrictive continuum while the concepts of commercial impracticality and hardship stand on the more expansive side.

Section 1148 of the French Civil Code enshrines the concept of *force majeure*. To grant relief from the duty to perform one's contract, one most show that performance has been rendered dischargeable by reason of some event that was unforeseeable, irresistible and external. An explanatory note to Section 1148 explains that the concept of *force majeure* "applies to events that make performance impossible, but not to those that make performance only more difficult."[56]

The Court of Appeals for the Second Circuit has explained the distinction between impossibility and frustration of purpose: "Impossibility may be equated with an inability to perform as promised due to intervening events such as an act of state or destruction of the subject matter of the contract…Frustration of purpose, on the other hand, focuses on events which materially affect the consideration received by one party for its performance."[57] In the case of frustration, "[b]oth parties can perform but, as a result of the unforeseeable events, performance by party X would no longer give party Y what induced him to make the bargain in the first place." In either case, the fact that performance has become more burdensome, difficult or expensive does not absolve a party from performing its obligations. As with cases of impossibility, discharge on the basis of frustration is "generally limited to instances where a virtually cataclysmic, wholly unforeseeable event has rendered the contract valueless to one party."[58]

Section 2-615(a) of the New York Uniform Commercial Code excuses delay in delivery or even non-delivery "if performance as agreed has been made impracticable by the occurrence of a contingency the non-occurrence of which was a basic assumption on which the contract was made or by compliance in good faith with any applicable foreign or domestic regulation or order whether or not it later proves to be invalid." As the Official Comment notes, "[i]ncreased cost alone does not excuse performance unless the rise in cost is due to some unforeseen contingency which alters the essential nature of the performance." English law and New York law seem here not to differ greatly: "Frustration is exceptional, and cannot be invoked lightly. If frustration is extended to cover the case where the fixed price becomes "so unfair to the contractor that he ought not to be held to his original price," then "there would be an untold range of contractual obligations rendered uncertain, and possibly unforseeable."[59]

Providing on the continuum to the most flexible of these concepts, "[h]ardship refers to performance being rendered more difficult, but not impossible, by an unforseeable change in circumstances beyond the parties' control."[60] Hardship makes its appearance in French law under the concept of *imprevision*, but French law does not

grant a remedy for hardship between private parties, but only to parties to contracts with government agencies. The Algerian and Egyptian Civil Codes have adopted provisions that, in cases of hardship, allow judges not to rescind a contract between private parties but to adjust the obligations of the parties. In 2002, Germany enacted a substantial revision of the relevant sections of its Civil Code regarding obligations, including a new Section 313, which addresses the "collapse of the foundation of a contract" ("*Wegfall der Geschaeftsgrundlage*"): "If circumstances at the basis of the contract formation have substantially changed and the parties would not have entered into the contract at all or with a different contents if they could have anticipated this change, a claim for an adjustment of the contractor can be made, provided that, given all circumstances of the individual case, especially the contractual or statutory risk distribution, one cannot be expected to continue with the contract as it is."

The UNIDROIT Principles of International Commercial Contracts and the Principles of European Contract Law are considered by some to have adopted rules that come close to reflecting the German perspective. Section 6.2.1 reiterates the basic principle that contracts must be performed subject to its provision on hardship. Hardship, under Article 6.2.2, is designated as occurring "where the concurrence of events fundamentally alters the equilibrium of the contract either because the cost of a party's performance has increased or because the value of the performance a party has received has diminished," provided that (i) the events occur or become known to the disadvantaged party after the contract has been concluded, (ii) the events could not have reasonably been taken into account by the disadvantaged parties at the time the contract was concluded, (iii) the events are beyond the control of the disadvantaged party and (iv) the risk of such events was not assumed by the disadvantaged party. In the case of such a qualifying occurrence of hardship, Article 6.2.3 allows the disadvantaged party to request renegotiations but does not excuse that party's non-performance. Upon failure to reach agreement, either party may resort to a court and, if the court finds that hardship has been established, it may, "if reasonable," terminate the contract on a date and on terms to be fixed or adapt the contract with a view "to restoring its equilibrium." Article 6.111 of the European Principles follows the UNIDROIT Principles, except that it also provides that "the court may award damages for the loss suffered through a party refusing to negotiate or breaking off negotiations contrary to good faith and fair dealing." Article 79 of the CISG provides a more limited form of "exemption" in the case of a party's failure to perform because of "an impediment beyond its control"; the exemption is available only for the period during which the impediment lasts and the party claiming the exemption must give the other party notice within a "reasonable time" after the impediment came to (or should have come to) the affected party's knowledge.

3. "*Force Majeure*" and Material Adverse Change Clauses

New York as well as English courts generally pride themselves on honoring the terms of the agreement the parties have agreed to, without substituting their own business judgment for that of the parties. General discomfort with granting relief based on change of circumstances and hardship can cause them to construe provisions that call for the renegotiation of contract terms in the event of an event of *force majeure* or material adverse change more narrowly than civil law courts, in part perhaps because of the general common law discomfort with enforcing "agreements to agree."[61]

In *IBP, Inc. Shareholders Litigation v. Tyson Foods, Inc.*,[62] the Delaware Court of Chancery applied New York law to adjudicate the effort of Tyson Foods to withdraw from its agreement to acquire IBP, Inc., based on a change of IBP's projected earnings after the "9/11" attacks. The Delaware Chancellor held that a New York court would incline toward a view that a buyer ought to have to make a strong showing to invoke a "material adverse change" exception to its obligation to close a very heavily negotiated merger agreement covering many details with great specificity and detail. Interestingly, the Chancellor acknowledged that the "Material Adverse Change" or "MAC" clause was very broadly drafted, most likely in an effort not to undercut the MAC clause by allowing it to be limited, under the doctrine of "*eiusdem generis*," to a list of specific circumstances. Still, the court concluded that the MAC clause "is best read as a backstop protecting the acquiror from the occurrence of unknown events that substantially threaten the overall earnings of the target in a durationally significant manner" and found that the change of earnings invoked by Tyson did not meet that test.[63] Other New York cases tend to support the preference for enforcing *force majeure* clauses only to specific types of occurrences expressly mentioned in the clause.[64]

Strict as New York law may seem to be, English law may be ever more restrictive. Thus, the UK Take Over Panel, in the *WIP/Tempus* case, declined to accept WPP's invocation of the MAC clause in its agreement to acquire Tempus, stating that a "material" change of circumstance "requires an adverse change of very considerable significance striking at the heart of the purpose of the transaction, *analogous…to something that would justify frustration of a legal contracts*." (Emphasis added.) This seems to be a very strict test indeed, which renders MAC clauses almost meaningless if the circumstances in which it is invoked falls short of frustration of purpose.[65]

D. The Principle Under New York Law of Fiduciary Loyalty Among Business Partners

A discussion of New York law on the issue of good faith cannot be complete without considering the very high standard of conduct New York law imposes on business partners in regard to each other. This standard

amounts to the duty of a fiduciary and was memorably articulated by Justice Benjamin Cardozo, then sitting as a Judge of the New York Court of Appeals, when he wrote: "Joint venturers, like co-partners, owe to one another, while the enterprise continues, the duty of the finest loyalty." Justice Cardozo elevated the relationship of those in business partnerships to "those bound by fiduciary ties," as if each partner were a trustee to the other. For trustees, Cardozo noted "the standard of behavior" is "[n]ot honesty alone but the punctilio of an honor the most sensitive."[66] Joint ventures and partnerships (whether formally structured as partnerships, corporations or limited liability companies) are all governed by agreements or contracts—and therefore the agreements that business partners make among themselves, and the standard for their implementation and interpretation, should be as much taken into account when weighing the merits of New York contract law as agreements to buy and sell goods and other relatively short-term transactions.

The law of England knows the duty of business partners to each other as *uberrimae fidei*; French and German law do not speak in this exact terminology but interpret the principle of good faith very fully to what French legal scholars increasingly recognize as "agreements of co-operation." Interestingly, many states of the United States have adopted a non-fiduciary, so-called "contractarian" approach to the mutual duties of business partners by adopting the Revised Uniform Partnership Act of 1994 ("RUPA"), which "[m]oves away for a reliance on this broad fiduciary duty to regulate partner conduct" and instead "limit[s] fiduciary duty to a duty of loyalty, which is further limited… to specific conduct instead of being a general concept tailored by courts to cover a broad array of impermissible conduct."[67] Significantly, unlike almost forty other states of the United States, New York has not adopted RUPA. Thus, the same judge whose dissenting appellate decision opinion in the *Reiss* case[68] (later adopted by the New York Court of Appeals) declined to adjust the terms of the warrant purchase agreement despite appeals to the principle of good faith firmly upheld the standards of utmost good faith and fiduciary loyalty in *Rickbell Information Services, Inc. et al. v. Jupiter Partners et al.*[69] There, Judge Saxe determined that fiduciary obligations could arise between parties to a joint venture even in the absence of an express agreement between them and that these obligations can impose limits on the parties' otherwise unfettered exercise of their contract rights.

In a perhaps further ironic turn, a Singapore legal scholar, in an article now posted on the website of the Singapore Academy of Law, suggests that the decision in *Rickbell* shows that New York courts cannot be counted on to strictly interpret and enforce contracts on their own terms.[70] There is a double confusion here. The fact that New York law holds business partners to a very high standard of mutual conduct does not mean that New York law has imposed the same high standard on what Justice Cardozo termed the "workaday world for those acting at arm's length," as the well documented aversion of New York courts to upset private contractual arrangements demonstrated in the *Reiss* case clearly attests.

E. Third-Party Beneficiaries

A corollary of the common law doctrine of consideration is the doctrine of contractual privity—the rule that says the benefits and detriments of a contract can only adhere to persons who are parties to that contract. As a consequence, common law (before changes made in New York and other states in the nineteenth century and changes in English law introduced in 1999), as a general proposition, did not permit persons who were not parties to a contract to enforce any rights or benefits conferred on them by the contract that required the performance of obligation in their regard. There were, of course, exceptions to this rule, in areas like trust law and insurance law, but at least in England the exclusion of third-party remedies was still strong until relatively recently. As discussed earlier, consideration is not a factor in constituting a valid contract under civil law and, at least under German law, third parties could more easily claim benefits and rights in respect of a contract to which they were not a party. BGB Section 328, for example, provides that "a contract may stipulate performance for the benefit of a third party, so that the third party acquires the right directly to demand performance." A third party may also, under German law, seek damages for failure of a party to perform its duty under the contract.[71] The French Civil Code does not contain provisions regarding third-party rights. On the other hand, as with most civil law systems, French law does not draw a rigid distinction between tort law and contract law in the style of the common law, and therefore tort remedies are more easily available with regard to contractual matters.

England overcame the traditional common law aversion to providing third parties the possibility of having rights under contracts by enacting "The Contracts (Rights of Third Parties) 1999." The Act provides that, subject to the provisions of the Act, "…a person who is not a party to a contract (a 'third party') may in his own right enforce a term of the contract if (a) the contract expressly provides that he may, or (b) subject to Section (2), the term purports to confer a benefit on him"; Section 2 provides that the provision just mentioned "does not apply if on a proper construction of the contract it appears that the parties did not intend the term to be enforceable by the third party."

New York law has been far less hostile to third-party beneficiaries. As far back as 1918, the New York Court of Appeals recognized that the doctrine of privity should be set aside in the case of contracts made for the benefit of a third party.[72] In 1985, the Court of Appeals adopted

the principles put forth in Section 302 of the Restatement (Second) of Contracts regarding third party beneficiaries. Under this test, a third-party beneficiary has the burden of demonstrating that (i) a valid and binding contract exists, (ii) it was an intended beneficiary of the contract, and (iii) the benefit to it is sufficiently immediate to indicate that the contracting parties intended to compensate the third party if it lost its benefit.[73] Under New York law, a third-party beneficiary takes no greater rights to enforce a contract than the actual parties would, "'its rights are subject to the same defenses as the rights of the promisee,'" and it is bound by the same limitations on liability that are provided for in the contract.[74] Anecdotally, this author understands that advisors often feel more comfortable with the longer tradition of respect for third-party beneficiary rights under New York law, where the courts are not bound by a statutory scheme in the mode of the 1999 English Act. Thus, for example, it is considered much easier and reliable to provide for the rights of purchasers in the structuring of American Depositary Receipts under New York law than it is under English law.

F. Performance Issues: Perfect Tender, Substantial Performance, *"Nachfrist"*

Under the law of New York (NY UCC Section 2-601(a)), subject to certain exceptions, "if the goods or the tender of delivery fail in any respect to conform to the contract, the buyer may (a) reject the whole; or (b) accept the whole; or (c) accept any commercial unit or units and reject the rest." Section 35 of the English Sale of Goods Act 1994 is to the same effect. Article CISG 52 does allow a buyer to reject goods "if the seller delivers the goods before the date fixed" or "if the seller delivers a quantity of goods greater than that provided for in the contract." But, upon delivery, CISG Article 49(1)(a) allows the buyer to avoid the contract once goods have been delivered *only* "if the failure by the seller to perform any of its obligations under the contract or this Convention amounts to a fundamental bread of contract."

Article 25 of the CISG defines a breach of contract as "fundamental" only if "it results in such detriment to the other party as substantially to deprive him of what he is entitled to expect under the contract…" CISG Advisory Council Opinion No. 5 advises that the following factors should be taken into account in determining whether a breach is "fundamental": (i) the terms of the contract; (ii) the purpose for which the goods are bought; and (iii) the possibility of repair or replacement. Article 7.3.1 of the UNIDROIT Rules adopts the same rules not just for contracts for the sale of goods but on a broader basis for when the failure of a party to perform an obligation under a contract amounts to a "fundamental non-performance," and sets forth a broader set of circumstances where non-performance can be "fundamental," including where the non-performance is "intentional or reckless" or where strict compliance is "of the essence" under the contract.

The CISG offsets the loss of the "perfect tender" rule for the buyer under Article 50 by allowing the buyer, under Article 50, "[if] the goods do not confirm with the contract and whether or not the price has already been paid…[to] reduce the price in the same proportion as the value that the goods actually delivered had at the time of the delivery bears to the value that conforming goods would have had at the same time." This is a remedy not available under New York law or English law. Under the CISG, the buyer has all the other remedies for damages provided by Articles 74-77 as well. The CISG makes it very important for the buyer to inspect goods received quickly and not to tarry in pursuing remedies. Article 38(1) requires the buyer to examine the goods within as short a period as is practicable under the circumstances and Article 39 requires that the buyer give notice to the seller of any non-conformity "within a reasonable time after he has discovered it or ought to have discovered it." Section 2-607(3)(a) of the New York Uniform Commercial Code is arguably less stringent when it provides that "[w]here a tender has been accepted, the buyer must within a reasonable time after he discovers or should have discovered any breach notify the seller of breach or be barred from remedy."

Under CISG Article 48, a seller may "remedy at his expense any failure to perform his obligations if he can do so without unreasonable delay and without causing the buyer unreasonable inconvenience or uncertainty of reimbursement by the seller of expenses advanced by the buyer." However, CISG Article 49, borrowing the German concept of "*Nachfrist*," gives the buyer a measure of self-help in the case of delay in the seller's performance. CISG Article 47 allows the buyer "to fix an additional period of time of reasonable length before performance by the seller of its obligations." If the seller fails to perform within the time set by the buyer, under CISG Article 49(1)(b), "the buyer may declare the contract avoided…if the seller does not deliver the goods within the additional period of time fixed by the buyer."

G. Passage of Title and Risk (Sale of Goods)

In a somewhat unusual confluence, English law as well as French law provide that, in the absence of agreement to the contrary, title to specific goods under a contract of sale passes upon the conclusion of the contract of sale.[75] New York's UCC Section 2-401(2) provides a presumptive rule that title passes "at the time and place at which the seller completes his performance with reference to the physical delivery of the goods." The CISG leaves the question of passage of title to be determined by local law.

It should be noted that passage of risk of loss does not necessarily follow passage of title. Thus, under English law, while title often passes on conclusion of the contract, passage of risk follows when the goods are transferred to the buyer.[76] On the other hand, under French law, where

title also passes on conclusion of the contract, passage of risk follows as soon as the buyer acquires title to the goods. Under NY UCC 2-509, in the case of a sale where shipment is required but not to a particular destination, risk of loss passes to the buyer when the goods are delivered to the carrier—as long as they are conforming. Where delivery must be made to a particular destination, risk passes when the goods are tendered at the specific place indicated. With regard to goods that are not delivered but stored, title passes when a negotiable bill of lading is delivered to the buyer. The provisions of CISG Article 67 on issues of passage of title are very similar to those of the NY UCC.[77]

Section 2-509(4) of the New York Uniform Commercial Code provides that the provisions of Section 2-509 dealing with the risk of loss in contracts for the sale of goods are "subject to contrary agreement of the parties."

The "International Commercial Terms" published by the International Chamber of Commerce, or so-called "Incoterms," provide a convenient menu of options denominated in three letter trade terms for allocating the costs and risks of transporting and delivering goods under contracts for the sale of goods and are equally useful whether the CISG or Article 2 of the New York Uniform Commercial Code applies to a particular transaction.[78] Significantly, Incoterms do not endeavor to regulate when title passes, but rather regulate only when risk of loss passes.

H. Remedies

In addition to the contrasting approaches the civil law and the common law traditions take to hardship and fundamental changes of circumstances, the civil law and the common law differ substantially, at least in theory, in several other matters related to remedies, including the basic criteria for determining liability for loss, the role of foreseeability in determining damages, the availability of specific performance and the availability of liquidated damages.

By way of introduction, under common law concepts, contracting parties are strictly liable for breach of contractual obligations whereas, under civil law, liability is generally based on fault.[79] Under New York law, "[w]hen a contract is breached, the non-breaching party may assert a claim to recover damages for the loss it suffered as a result of the breach."[80] Fault is simply not a relevant issue. English law is of the same view: "Non-performance and defective performance are not seen as 'wrongs' in the same sense that a tort is a wrong."[81]

For civil law, the issue of liability turns on whether the breach arose from the fault of the breaching party. Thus, Article 1147 of the French Civil Code provides that: "[t]he debtor is held…to the payment of damages, whether because of the non-performance of the obligation or because of the delay in performance, whenever he fails to show that the non-performance is due to a foreign cause, and further that there was no bad faith on his part at all." The introduction of the issue of good faith into the determination of liability essentially allows the breaching party to lessen or even avoid liability if it can be shown that he did everything reasonable to attempt to perform the breaching party's obligations. Article 254 of the German Civil Code establishes a general principle of contributory negligence in contract law as well as in tort law. French case law also allows set-off for the responsibility of the non-breaching party; on the other hand French law does not impose a duty to mitigate losses on the injured party.[82] Notwithstanding the prevailing fault-based regime of French law, it does, unlike common law, allow parties to provide for *obligations de resultat*, where liability can arise on a single demonstration that a promise was not performed.[83]

1. Consequential Damages

Under New York and English law, the major categories of contract damages are (i) general or compensatory, (ii) reliance damages, and (iii) consequential or indirect damages. Punitive damages are not allowed unless a claim can be made out in tort.

German law acknowledges the fundamental principle that damages should compensate for loss of profit or gain but the range of the loss, following the general tort-like analysis of the civil law even in the area of contracts, looks more to the damages that can be causally tied to the breach and, as for foreseeability, focuses more on the damages that could be foreseen at the time of breach rather than at the time the contract was formed.[84]

The notion of foreseeability, which became so prominent for the common law in the aftermath of the seminal English case of *Hadley v. Baxendale*,[85] may have actually been borrowed from Articles 1150-1151 of the French Civil Code. But under French law, in the case of deliberate non-performance, the focus narrows to the damage caused by the breach, even if the damage was not foreseeable.[86] Under the rule of *Hadley v. Baxendale*, a breaching party's liability includes not only loss that would ordinarily flow "in the normal course of things" from a breach at the time the contract was entered into but also loss that follows from breach due to special circumstances known to the parties at the time the contract was formed. The 2008 decision of the House of Lords in *The Achilleas*[87] appeared to require proof that the defendant expressly assumed the risk of loss that could be expected to arise in the ordinary course from a breach of the contract—a requirement that would not only significantly change English law but cause English law to differ from New York law. However, the 2010 decision of the High Court in *Sylvia Shipping*[88] appears to have limited *The Achilleas* case to its facts and declined to apply the assumption of responsibility test that *The Achilleas* seemed to introduce.[89]

Under New York law, under the *Hadley v. Baxendale* rule, general damages compensate the non-breaching party for economic loss because of the non-performance of a contractual obligation, but "special damages" compensate the non-breaching party for losses that could arise under special circumstances the parties contemplated at the time the contract was entered into. The analysis looks to whether there has been any conscious assumption to pay the claimed special damages and whether, by words or deeds, the defendant reasonably led the plaintiff to believe the defendant had assumed such liability.[90]

It should be noted that both the UNIDROIT Principles of International Commercial Contracts in Article 7.4.4 and the Principles of European Contract Law in Article 9.503 provide for damages that "reasonably" could have been foreseen at the time of the conclusion of the contract as being likely to result from non-performance. If by "reasonably" there is intended an objective test, "special damages" seem to be excluded. As with "entire agreement" clauses and MAC clauses, parties can limit their exposure to consequential special damages by careful drafting. New York law generally enforces such clauses if they are not "unconscionable" and NY UCC Section 2-719(3) applies the same principle to contracts for the sale of goods.[91] As with MAC clauses, specificity in the drafting of such clauses makes them more likely to be enforced. Thus, while the "demarcation between direct and consequential damages is a question of fact usually left for resolution at trial," in *Roneker v. Kenworth Truck Co.*[92] the court determined that the waivers in the contract at issue included a detailed listing of the consequential damages to be excluded that permitted the court to determine "as a matter of law" whether the trucker's damages were direct or consequential.[93] Drafting waivers under English law requires awareness that English courts have held that "consequential loss" is a synonym for "indirect loss" and therefore that a general waiver of "consequential losses" might not preclude damages that arise from, "special circumstances" under the second branch of the *Hadley v. Baxendale* test. Thus, if the parties intend to exclude "lost production, profits, business, revenue or the like," it is best that these be expressly referred to in the waiver clause.[94]

2. Specific Performance

Under New York law, "the proper measure of damages for money withheld is lost interest" and the plaintiff cannot claim consequential damages. European law recognizes the right of a creditor to require the performance of a contractual obligation by payment of money.[95] Under civil law, a party generally has a right to seek specific performance of a non-monetary obligation. Thus, Article 1184(2) of the French Civil Code provides that "[t]he party towards whom the undertaking has not been fulfilled has the chance whether to compel the other to fulfill the agreement when it is possible, or to request its avoidance with damages." While the common law makes specific performance an essentially discretionary remedy available in equity, specific performance is not available when a remedy at law (basically monetary damages) will suffice.[96] So far, English law has resisted a tendency to give the remedy of specific performance a broader application.[97] In reality, parties to contract disputes in the civil law jurisdictions resort to specific performance as a desired remedy in far fewer instances than the general doctrine might lead one to suppose. Specific performance is not available if it would be unreasonable, involves services or work of a personal character or depends on a personal relationship.[98] It has been found to be rarely applied, based on a detailed study of the use of the remedy in Denmark, Germany and France, in part due to a reluctance to incur the administrative costs of enforcement.[99]

3. Liquidated Damages

Civil law and common law countries also have different doctrinal points of departures regarding the enforceability of liquidated damage clauses. The French Civil Code was noteworthy for allowing penalty clauses—clauses that exact a very high cost for non-performance as a means of determining breach. This permissive attitude towards penalty clauses was consistent with the theory of the civil law, which sees contracts and torts as part of one overarching law of obligations, where the concept of fault applies to breach of contract as well as to tort injury. In the common law, penalty clauses have been seen as a form of punitive damages, which are generally not allowable as a remedy in contract because of the strict liability of contractual breach and the general irrelevance of issues of fault.

But the two systems have moved closer toward each other. New York courts generally recognize and give effect to liquidated damage clauses when the damages represent reasonable estimates of the cost of breach, especially under circumstances where establishing the cost of breach may not be easy. They are enforceable as long as they are neither unconscionable nor contrary to public policy, but penalties for violations of contractual obligations are still not enforceable.[100] English law is of the same view, save for the fact that the courts are very reluctant to interfere with liquidated damage clauses as between sophisticated commercial parties.[101] On the civil law side, there has been a tendency to mitigate penalty clauses in some courts. The Council of Europe issued a "Resolution on Penalty Clauses" in 1971 with the aim of recommending a uniform application of penalty clauses under which "the penalty amount may be reduced by the courts if they are manifestly excessive, or if part of the main contractual obligation has been performed." Many countries have passed legislation consistent with the Resolution, including France and Germany.[102]

4. Early Termination of Contract

Perhaps the most fundamental remedy for breach to which a party to a contract can resort is unilateral termi-

nation of the contract and suspension of its obligations under the contract. All of the legal systems discussed here, as well as the international instruments, recognize the availability of this remedy if the defaulting party's breach is "substantial" or goes to the heart of the contract. The aggrieved party is given a choice between terminating the contract and seeking damages on one hand, or continuing with the contract on the other.[103] Section 1147 of the French Civil Code provides that non-performances of a contract "for no external reasons" is grounds for termination. Article 7.3.1 of the UNIDROIT Principles puts forth the most comprehensive list of circumstances where termination is justified: (i) the non-performance substantially deprives the aggrieved party of what it is entitled to expect unless the defaulting party did not foresee and could not reasonably have foreseen that result; (ii) strict performance of the obligation in question is "of issue" under the contract; (iii) the non-performance is intentional or reckless; and (iv) the non-performance gives the aggrieved party reason to believe that it cannot rely on the other party's future performance. Section 323 (1) of the German Civil Code requires that, in the case of a reciprocal contract, the aggrieved party may revoke the contract "if he has specified, without result, an additional period for performance or cure."

The fourth UNIDROIT criterion for establishing the "fundamental" or "material" nature of a breach justifying the remedy of termination, which looks to the likelihood of future performance, raises the issue of when the remedy of termination is available for anticipatory breach of contract. Under New York law, "where one party clearly and unequivocally repudiates his contractual obligations…prior to the time performance is required, the non-repudiating party may deem the contract breached and immediately sue for damages."[104] The same essential rule for "repudiatory breach" holds under English law[105] and under German law.[106] French law appears to be less open to the remedy of termination for anticipatory or repudiatory breach: Section 1186 of the Civil Code provides that when the performance of an obligation is due only on a certain event (i.e., a specific date), its performance cannot be claimed before the contract.

II. Commercial Law Topics

A. Negotiable Instruments

The law of negotiable instruments has two major sources. For the common law, the primary source is the English Bills of Exchange Act, which formed the background against which Articles 3 and 4 of the UCC were drafted. For the civil law, the two major sources of law are the Geneva Convention Uniform Law for Bills of Exchange and Promissory Notes and the Geneva Convention Uniform Law for Cheques. Perhaps the most striking difference between the two systems has to do with the effect of a fraudulent endorsement on a bill for the subsequent negotiation of the bill. Under the Geneva system, a holder acquiring an instrument in good faith and without gross negligence by an uninterrupted series of endorsements can be a good faith purchaser even though the instrument was lost or stolen and one of the signatures was forged. But under the New York Uniform Commercial Code and similar common law provisions, at least in regard to instruments made out to a payee, a thief can never be a holder (and therefore not a holder in due course) because an individual qualifies as a holder only by showing that the person is in possession of the instrument and that the order or promise on the bill "runs" to that person. Since, by definition, the instrument cannot be made to the order of a person who is not the payee, the thief cannot be a holder within the meaning of NY UCC Section 1-102(20) and therefore the thief cannot endorse the instrument to someone else within the meaning of NY UCC Section 3-302.[107]

The Geneva approach, it has been said, better reflects the interest of the law merchant in the free circulation and negotiability of instruments, while the New York and common law approach is more attentive to property law concerns. At least one commentator believes that the approach of the UCC is an instance where "better policies necessitated the law to prefer the protection of property, unless the dispossessed owner has been at some fault or in a position to avoid loss."[108]

B. Letters of Credit

Letters of credit are governed in New York by NY UCC Article 5. Perhaps the most fundamental characteristic of a letter of credit is that the issuing bank cannot withhold payment on the basis of breach by a party to the underlying transaction that gave rise to the issuance of the letter in the first place. This substantially diminishes the risks to issuing banks and makes banks more willing to support these payment mechanisms, on which so much of international trade depends. No set-offs or counterclaims are generally allowed and the bank cannot be impleaded in any action between the applicant for the letter and the beneficiary of the letter related to the underlying obligations as between the letter's applicant and its beneficiary.[109]

In general, some civil law jurisdictions, particularly in Latin America, are said to have difficulty in completely isolating the documentary commitment from the underlying transaction. The courts of England and New York have been very firm in upholding the "abstraction" of the letter of credit from other circumstances affecting the applicant or beneficiary. However, New York, following the lead of the Supreme Court of New York County in *Sztejn v. J. Henry Schroder Banking Corp et al.*,[110] has made an exception where a bank has received notice of actual fraud on the applicant by the beneficiary. There, the court distinguished between a breach of warranty and an intentional failure to deliver the goods, and denied a defendant's motion to dismiss the claim of the buyer to stop

the payment where there was credible evidence that the bill of lading had been falsified. Although recognizing an exception to the independent status of a letter of credit in principle, English courts have been very reluctant to give relief, while New York courts have continued to be more willing to issue temporary injunctions in cases where credible allegations of fraud have been raised. New York's UCC Section 5-109 provides guidance for certain situations under which an issuing bank should honor a demand for payment despite allegations of fraud, gives the bank discretion in other cases, and permits New York courts to issue injunctions stopping payment upon compliance with a detailed list of requirements.

C. Bills of Lading

In New York, bills of lading are governed by NY UCC Article 7. A salient issue with regard to bills of lading has been whether a carrier is responsible for misrepresentations by the ship's master. Under the leading (although very counter-intuitive) English case of *Grant v. Norway*,[111] a shipping company could not be held responsible for the master's misrepresentation about goods the master never received. The New York Court of Appeals, in *Bank of Batavia v. New York, Lake Erie & Western Railroad*,[112] became one of the first courts in the United States to dissent from the English view and find that a carrier was not estopped from liability on the bill when the carrier's freight agent issued a bill of lading without having received the goods. The Comments to UCC Section 7-507 provide that the carrier who issues a bill of lading is liable for the bill when the carrier's agent has received no goods.[113] The English Carriage of Goods By Sea Act 1992 effectively repeals the rule of *Grant v. Norway* as to transferable bills of lading, but not "straight bills of lading" and waybills made to specific consignees.[114]

D. Providing for Security Interests

Article 9 of the New York UCC provides a framework for secured lending. It contains provisions for creating and perfecting a security interest in personal property and enforcing it. New York's UCC Article 9 provides for liquid collateral, which means that a creditor may acquire a security interest in categories of property (including not only many categories of personal property but also some categories of real property). The lien can be "floating"—*i.e.*, apply to property that may exist in the future as well as property that exists at the time the security interest is established—a very important feature that facilitates security interests in accounts receivable and inventory that necessarily change over time. New York's UCC Article 9 provides a uniform filing system for perfecting security interests by providing that a secured party may register its security interest at a designated depositary and need not give individual notice to all actual or suspected creditors of the debtor. By providing for centralized registration of security interests, New York's UCC Article 9 also provides a more efficient and reliable system for prioritizing interests. Finally, NY UCC Article 9 provides for various forms of self-help in the event a security interest holder needs to execute against the collateral.[115]

The system of security interests is generally more limited under French law. French law does not recognize the concept of a "floating lien" as a way of acquiring a security interest in inventory. A security interest in accounts receivable would be limited to existing accounts. Under special legislation passed in 1981 ("*Loi Dailly*"), a lien may be placed on future accounts receivable but only if the debtor periodically provides information about them. The effect of the lien is that the secured lender actually takes title to the accounts receivable and can give notice to the obligors on the accounts to pay the secured lender directly. But there is considerable doubt as to whether creditors who are not French or European banks can avail themselves of the benefits of the *Loi Dailly*. German law technically recognizes floating liens, but requires that collateral be described with a degree of specificity that would be strange to New York requirements. In the case of inventory, security interests may be taken out only in inventory described and located at a specific place. There is no national system of registration in either France or Germany. Under both German and French law, executing on the collateral requires application to a court; in France, an insolvency administrator must be appointed, although it is easier to attain an order of attachment (*saisie-conservatoire*) against a borrower's assets or even an order of payment (*injunction de payer*).[116]

The English system of security interests bears more resemblance to the New York system. English law recognizes floating liens. However, English law makes a distinction between "fixed charges" and "floating charges." A fixed charge carries a higher priority against other claimants. But to enjoy this benefit, the secured lender must have a high degree of control over the collateral, which make this approach to security interests unattractive to borrowers. Floating charges leave the borrower in effective control of the assets, with the lien only becoming "fixed" upon an actual default. Floating charges are in turn divided into "equitable" and "legal" charges. But while England has a central registration system, "legal" charges over receivables—which have a higher degree of priority—only apply if account debtors have been given individual notice. Also, registering a security interest only satisfies the notice requirements for parties *likely to search*—so notice to specific creditors still remains preferable, even if not as absolutely necessary as in France or Germany. English law does give the holder of a lien over substantially all of a Borrower's assets and a form of self-help through a right to appoint an "administrative receiver" who answers to the secured lender and who can take control of the assets as long as an "ordinary receiver" has not been appointed by a court. The administrative receiver may apply to a court to sell an asset subject to a proper lien if the administrative receiver can show that superior recovery could be had.[117]

Of course, the ability of parties to stipulate what law would apply in a secured loan is limited by local laws protecting the debtor or the assets that will constitute collateral. But the benefits of NY UCC Article 9 can be achieved by creative planning, including organizing collateral in a way that would give it a situs in New York or making the debtor take on a form of legal personality or presence in New York that may give New York courts jurisdiction over it.

III. Considering the Interaction of Contract Law and Civil Procedure

The 2011 Report of the New York State Bar Association's Task Force on New York Law and International Matters focuses on issues that have been raised about the alleged length, complexity and cost of litigation in New York, as distinguished from other common law centers such as London and Singapore or civil law centers such as Paris or Frankfurt. The Task Force Report also explains the many ways in which parties can adjust or ameliorate these concerns by agreements to waive jury trials, shorten or limit pre-trial discovery, adjust the allocation of legal costs among the parties and so forth.

However, there is a larger issue, which has to do with the effectiveness of proceedings conducted under a given form of civil procedure to afford effective and equitable remedies and relief. This is critical because the evaluation of the procedural rules available in the jurisdiction where disputes would be resolved cannot be totally separated from the area of substantive law likely to govern any dispute likely to arise. Those who counsel clients about choosing governing laws and dispute resolution should consider whether the legal principles that may be most meaningful for the client can be effectively applied within the confines of the procedural rules that the forum of choice will employ.

A. Oral Contracts

Most jurisdictions other than New York do not require a writing to make a contract enforceable. However, an oral contract, by its very nature, has to be proved by evidence and, when there is no writing to confirm the obligations in question, testimony has to be given to prove the contract. In common law jurisdictions, oral testimony by witnesses is usually a key component in the proof because affidavits do not present opportunities for cross-examination and for the exploration of questions that the litigating parties or the judges themselves may think important to resolve the matter. In civil law jurisdictions, there is generally much greater dependence on written testimony: Having a witnesses testifying in support of a claim on direct examination—that is, giving the witness the opportunity to tell the story behind the claim to the judge in person—is generally not possible, since testimony is usually quite limited and is ordinarily based on questions posed by the judge. Attorneys often do not question the witness directly but rather present questions for the judge to ask.[118] Thus, a forum that entertains oral testimony almost necessarily has to be the better forum in which to prove an oral contract.

B. Fraudulent Conduct

As we have seen, New York law implies an obligation of good faith in matters of contract—applied perhaps in a somewhat more constrained way than in many civil law jurisdictions. And, as we have also seen, in several areas of commercial law, New York law tends to be more protective of parties that have been the victim of fraud than the law of civil law jurisdictions. Parties engaging in fraud, almost by definition, try to conceal facts or conditions they do not want others to see; they are certainly not going to volunteer them. Under the procedural rules of most civil law jurisdictions, parties do not have the right to ask for documents they cannot specifically identify and therefore the ability to review a party's entire record with regard to a transaction is not generally available.[119] By contrast, under the rules of procedure of New York, a party can obtain access to a range of documents without which it is unlikely the fraud could be discovered or proven. In situations that may involve significant sums of money and major commitments of resources and personnel, especially among parties who do not know each other and whose honesty and integrity have not been really tested, it stands to reason that there is a greater risk that fraudulent representations may be made, material facts not disclosed, or obligations not undertaken in good faith. Having the ability to obtain relief if any of these circumstances were to occur can be critical: thus, the possible need to prove fraud and to obtain relief from it has to be weighed against the supposed economies in cost and time associated with civil law forums and also common law jurisdictions such as England that do not usually permit pre-trial depositions.

C. Commercial Practice in Technical Specialties

Finally, one must consider the importance of expert testimony in the event it should be necessary to seek judicial remedies for breach of contractual obligations. Many areas of commerce involve highly specialized issues of technology, finance and commercial practice, about which even the most qualified jurist would need expert advice. Under the rule of civil procedure of most civil law countries, the court selects experts to advise it, sometimes after taking into account recommendations from the parties. This, of course, puts the expert chosen by the court—especially in cases that primarily turn on knowledge of practice and custom in highly technical areas of business or production—almost in the position of the court itself. Under New York law, the court does not generally choose a single expert, but rather the parties choose their own experts, with the court having the opportunity to hear the testimony and perspective of each side's expert. While it is easy to lampoon so-called "battles of the experts," in

many areas of commerce there can be substantial differences of professional opinion on technical issues that may be material to the disposition of a case. Depending on the nature of the science involved in a particular transaction, parties to joint ventures that are especially dependent on intellectual property may want to preserve their right to make a full presentation of their side on technical issues rather than risk that the entire case turns on a court's choice of an expert.[120]

IV. Summary and Proposals

Our survey has highlighted legal principles and rules within the domain of contract and commercial law, identified the approach of New York law to them, and compared and contrasted the New York approach with the laws of England, France, Germany, the CISG, and the UNIDROIT and European Principles of International Commercial Contract law.

This article has emphasized the so-called "objective" focus of New York law in the construction and enforcement of contractual obligations, highlighting the important place of the requirement of consideration and the parol evidence rule. New York law (and, to a large extent, English law) have adhered to these principles despite the weight of disfavor they receive in civil law systems and in the international restatements. The Task Force Report emphasizes the respect that New York courts give to the contractual arrangements of private parties and their reluctance to substitute their judgment for the choices made by such parties. It can be argued that the claim of New York to have such a high level of respect for the contractual autonomy of parties to commercial and corporate transactions derives from and is supported by the New York practice embodying contractual undertakings in detailed and comprehensive agreements, which may be of considerably greater length and detail than their civil law counterparts. Whether the noninterventionist predilections of New York courts is the cause of this custom of highly articulated contracts or whether private legal practice in commercial matters has encouraged this policy of New York law, the requirements of consideration and the parol evidence rule encourage commercial parties carefully to think through and address the issues that are most likely to arise in their relationship—rather than rely on the courts to solve their problems for them. *At the same time, I think it is at least worth considering whether, in the long-run, the stringency of the discipline that New York courts seem to expect of commercial parties should be more carefully calibrated to deal with the cross-cultural and cross-linguistic context of international commerce, at least in instances that I discuss below.*

A. Eliminating or Reducing the Applicability of the Statute of Frauds

New York, as we have seen, continues to require that certain obligations be embedded in writing in order to be enforceable, while England—the "mother" of the statute of frauds—has virtually eliminated this requirement, and most civil law jurisdictions, the CISG and the international restatements never adopted it. There are two provisions that deserve special comment: the requirement of a writing under the New York Uniform Commercial Code for transactions of more than Five Hundred Dollars and the requirement of a writing under the New York General Obligations Law for transactions that are not to be performed within one year. The Five-Hundred-Dollar limit appears to date back to 1962, when the New York first adopted the Uniform Commercial Code; the National Commissioners on Uniform State Laws have encouraged states to raise this limit to Five Thousand Dollars. This seems clearly advisable, at least in the case of contracts between merchants. The "more than one year" rule is not always easy to apply and, for an international lawyer not steeped in New York law and even for New York lawyers, it can be another trap for the unwary. It is not clear what purpose it really serves in today's context. *Eliminating—or at least reducing—the instances where a writing is a condition of a contract's enforceability (and at least raising the monetary limit for contracts for the sale of goods) would also introduce greater consistency between domestic New York law and the CISG and thus reduce mistakes about when the New York domestic rule or the CISG rule applies.*

B. Using Commercial Practice in the Construction of Contracts

As for construction of contracts, in the case of written contracts, as already noted, New York courts are loathe to admit extrinsic evidence about additional terms or even collateral terms when it appears the contract's essential terms can all be gleaned from "the four corners of the written agreement." But, at least in the absence of a merger or "entire agreement" clause, when an essential term is missing, there is a general trend in New York law, perhaps encouraged by the policies embedded in the New York Uniform Commercial Code, toward supplying the missing term from evidence of the party's conduct and general commercial practice in the relevant field of trade or business.[121] The tendency to use objective evidence to supply "missing terms" is consistent with the objective emphasis of New York contract law. *This tendency is also consistent with Articles 8 and 9 of the CISG and should be encouraged, among other reasons, to eliminate needless divergence between the New York law of domestic sales transaction and the New York's default law for most international transactions*. It is also consistent with the principles enshrined in the UNIDROIT and European Principles. As to "entire agreement" clauses, it is noteworthy that the UNIDROIT and European Principles, despite the strong civil law influence evident in both documents, have adopted the concept of excluding extrinsic evidence in the determination of contract terms where agreements contain "entire agreement" or merger clauses.

C. Return to a Modified Mirror Image Rule?

One of the innovations of Article 2 of the UCC was to reverse the "mirror image" rule, under which an acceptance of a purported offer does not constitute an effective acceptance if the acceptance is subject to the change of any terms proposed in the offer, but rather is viewed as a new offer proposed to the original offeror. The purpose of the UCC in reversing the traditional rule was said to be to "save contracts" and facilitate the flow of commerce. Be that as it may, the statute is recognized in many quarters as having been drafted in a confusing manner and, ironically, going against the general drift of New York law of encouraging parties to take responsibility for creating their contractual arrangements by not placing courts in the position of having to determine the material terms on which the parties could not agree. It is noteworthy that not only civil law jurisdictions continue to follow the "mirror image" rule as to essential or substantive terms but the international restatements do as well. Most importantly, Article 19 of the CISG maintains the "mirror-image" rule as to material terms of an offer. Thus, in the recent case of *Hanwha Corporation v. Cedar Petrochemicals, Inc.*,[122] where the litigants were businesses in New York and Korea, the CISG applied, with the result that no contract was formed because the parties could not agree on the substantive law that would replace the CISG! *Therefore, to avoid traps for the unwary (especially for New York parties to international transactions that are not the subject of fully negotiated executory contracts), adoption of the "mirror image" as to material terms, at least as between international merchants, seems advisable.*

D. Applying the Principle of Good Faith

The recognition by New York law of the implied obligation of "good faith" in the performance (if not the negotiation) of contracts places New York in a position closer to the civil law tradition than to the English common law version as well as the articulation of international contract law adopted by the international restatements. As we have noted, New York courts have applied the obligation in a very restrained fashion and New York law does not appear, at this time, to embrace the broad mandate of the UNIDROIT Principles that "[e]ach party must act in accordance with good faith and fair dealing in international trade," especially in pre-contractual negotiations. No doubt, New York's restrained approach enables it to continue to put itself forward as a jurisdiction that encourages parties to structure their own transactions and to determine for themselves the rules and conditions to which they want to be subject in carrying them out. Likewise, this restraint supports the position that New York courts are loathe to substitute their business judgment for the decisions private parties make about weighing and balancing the risks and rewards of their transactions—a position that, at least according to some recent research, helps to make New York law, among jurisdictions in the United States, a far more popular choice of law than the law of California, whose courts appear to apply common law contract rules in a manner more reminiscent of the German tradition and some features of the international restatements.[123]

But caution should be taken here because the studies and surveys that appear to favor New York's generally "formalist" and "non-contextualist" approach appear primarily to test the preferences of U.S. domestic private parties. Should it not be wondered if the sole value international businesses, merchants and traders look for in choosing a governing law—especially in the case of international businesses that may not have the resources to retain the most sophisticated cross-border counsel and advisors—is a completely formalist approach to contract construction, especially if a purely formalist approach can lead to a disproportionate allocation of risks that the parties may well not have contemplated? Does it always help New York law when a very learned commentator can say that "New York's tenderness for freedom of contract expresses itself, at times, in a seemingly atavistic pleasure in imposing the consequences of bad bargains?"[124]

In this context, let us revisit the *Reiss* case discussed above. There, the party exercising its warrants gained what the Court of Appeals admitted was a "windfall" when it became entitled to acquire the shares of stock after a five-to-one reverse stock split for the same price it had contracted to purchase the shares before the split. The court reasoned that the agreement had been entered into by experienced business parties and that the parties must have addressed the issue, notwithstanding the complete silence of the purchase agreement on the issue, because the company had issued warrants to other parties under agreements that did address the effect of a reverse split on an exercise of warrants. The court declined the company's invitation to imply a term or otherwise reform the contract on the basis that the contract was in writing, that the agreement was complete (at least in the sense that, in the court's opinion, no essential terms were missing), that there were no ambiguities as far as the writing was concerned, and therefore, under the parol evidence rule, the court was not permitted to find or add terms for the unaddressed contingency.

On the basis of these principles, the decision is very consistent with what one might expect of New York law. On the other hand, one wonders, as a general matter of policy, whether the parol evidence rule should operate to exclude consideration of gaps where, "within the four corners of the agreement," it is hard to say whether the failure to address a key issue was deliberate or not. Because the *Reiss* case did not involve businesses from different countries and also because sales of securities are excluded from the province of the CISG, the CISG did not apply. But in an analogous case among international par-

ties where the CISG would apply, the parol evidence rule would not apply and, under CISG Article 8, if the intent of the parties was not evident from their statements and conduct, a "reasonable person" standard would be applied, "due consideration" being given "to all relevant circumstances of the case, including the negotiations, any practices which the parties have established for themselves, usages and any subsequent conduct of the parties." It is not too far a distance between CISG Article 8 and Article 4.8 of the UNIDROIT Principles, which directs that "[w]here the parties to a contract have not agreed with respect to a term which is important for a determination of their rights and duties, a term which is appropriate in the circumstances shall be supplied."

Interestingly, the principle behind UNIDROIT Principle 4.8 was essentially adopted in *Reiss* by the majority opinion of the Appellate Division on the initial appeal by the warrant holders from the decision of the New York Supreme Court, which adjusted the terms of the warrants by holding that the failure of the warrants to address the contingencies of a split or a reverse split constituted an omission of an essential term of the warrant transaction. "[F]ormalistic literalism serves no function but to contravene the essence of proper contract interpretation, which, of course, is to enforce a contract in accordance with the true expectations of the parties in light of the circumstances existing at the time of the formation of the contract."[125] *This reasoning seems more consistent with the application of the principle of good faith and commercial reasonableness that we see in what appears to be a developing consensus of international commercial jurisprudence and it is one to which New York courts might well consider giving a more robust application.* (See Part IV(H) below for more details.)

E. Hardship and Commercial Impracticality; the Issue of Foreseeability

A related area that may be very relevant to a decision to choose New York law for an international transaction is how New York law deals with contracts whose economic balance has been fundamentally altered by major changes in economic, political or meteorological circumstances, especially macro-economic factors for which it may be very difficult for private parties to foresee or anticipate. Aside from the ameliorative rule of NY UCC 2-615 in cases involving the sale of goods, the doctrines of impossibility and frustration of purpose generally offer very little relief to a party for whom performance may have become extremely burdensome or ruinous because of the limited circumstances to which they apply.

As noted above, CISG Article 79, which represents New York contract law for a very substantial portion of international sales transactions involving New York parties, provides a limited form of "exemption" in the case of a party's failure to perform because of "an impediment beyond its control" for the period of time during which the impediment applies, where the party claiming the exemption could not reasonably be expected to have taken the impediment into account at the time their contract was entered into or to have overcome it. The drafters of the UNIDROIT and European principles have developed what appears to be a careful and cabined rule for a broader range of circumstances by providing, as provided in Article 6.1.1.1 of the European Principles, that "where the concurrence of events fundamentally alters the equilibrium of the contract either because the cost of a party's performance has increased or because the value of the performance a party has received has diminished," the aggrieved party may request renegotiation of the transaction and, if the negotiations fail, judicial relief, which may include termination of the contract or its reform. *It may be advisable to consider whether such a provision dealing with hardship and commercial impracticability would make a prudent addition to New York's common law or even the General Obligations Law.*

The crux of hardship cases, as even the language of the UNIDROIT and European Principles demonstrate, is the definition of foreseeability. It has been recently observed, in reference to NY UCC Section 2-615, that "… despite the implication that the test should be whether the event was unforeseen by the parties at the time of contracting, courts have frequently required that the event be unforeseeable or outside of the realm of logical possibility."[126] *Thus, as valuable as adding provisions to New York law dealing with hardship or commercial impractability on a wider scale than UCC Section 2-615 may be, even more valuable would be judicial or statutory guidance as to what contingencies may be considered reasonable to think the parties should have contemplated themselves and those that are not.* Certain circumstances may be simply too unlikely or, even if predictable, too difficult to measure or to meaningfully analyze, or the efforts to account for them too speculative and burdensome to penalize the parties for not having resolved them contractually.

F. Limiting Perfect Tender Rule

One of the major divergences between New York law on the one hand and the CISG and the laws of many other jurisdictions on the other hand concerns the right of a buyer to reject goods that do not completely conform to the requirements of the contract, even if they substantially conform thereto. In a number of cases, the New York UCC limits the application of the rule—perhaps most importantly by excluding its application to installment sales but also by making rejection of the product subject to the UCC's requirement of good faith as well as to trade usage and prior or current courses of dealing.[127] The adoption of the substantial performance standard under the CISG derives from the view that the distances and expenses of transporting of goods in international commerce makes a perfect tender rule less sensible and therefore the substan-

tial performance rule better reflects the likely expectations of parties in international trade. Putting New York law in conformity with the CISG on this topic eliminates another possible area of confusion and mistake, especially when parties may not be sure whether the NY UCC or the CISG applies or, worse—as one suspects is still often the case—not even aware that there is an issue and a difference here. *Consideration, therefore, should be given as to whether NY UCC Section 2-601 should be modified so that the perfect tender rule, under New York law, would not apply to international merchants (leaving it in place for consumers and domestic merchants).*

G. Integrating New York Law Standards for Commercial Transactions and Business Collaboration

We have considered that New York applies the principle of good faith in a relatively sparing way, at least among sophisticated commercial parties, but imposes a very strict duty of fiduciary among business partners. The distinction between "contracts of exchange" and "contracts of co-operation" is well-known in contemporary French jurisprudence and seemingly reflected in New York law's restrained application of the "good faith" standard for commercial trade and it is much more generous application of the "fiduciary duty" standard for business collaboration seems to reflect this distinction very sharply. But one may well ask, especially in the context of international commercial transactions and relationships, whether this distinction should not be tempered. Contractual relations span a spectrum of commitments of time, financial resources, proprietary technology and human energy. There are many types of contract relationships that do not invoke the long-term commitments of a joint venture or business partnership but involve more resources and more mutual dependence than the purchase and sale of fungible products of manufacture, agriculture or mining. *New York courts could use the New York legal principles of good faith and business loyalty to effect a compelling "bridge" between the hyper-literalist philosophy of some common law contract jurisprudence and the overly malleable and unpredictable contextual tendencies of at least some branches of the civil law tradition.*

Much litigation around the issue of "good faith" turns on the question of what terms are essential to a contract, without which the contract, even if valid, cannot be said to be complete, and whether the courts should supply or imply any such missing terms. It could be helpful if New York courts—or perhaps even the New York legislature—were to identify the terms that, for New York law purposes, are essential for a range of basic forms of commercial contracts. The typical trio of price, term and product may be sufficient for most contracts for the sale of goods but the sale of goods should not necessarily be the sole model or paradigm for the great variety of contracts that are necessary for commerce—domestic or international—especially those for which the stakes in the allocation of risk of loss are especially high. "Entire agreement" or "merger" clauses could still bar any implication of missing terms, but otherwise, in the absence of an express provision allocating the relevant risks, New York courts would be permitted to supply a missing term in order to prevent extreme or even absurd outcomes. Whatever the merits of the Court of Appeals' decision in *Reiss*, on its particular facts, its seems to me that Judge Friedman's method, in his decision for the Appellate Division, of inferring additional "essential terms" relevant to the type of contract at issue, represents, for the long run, a more nuanced, insightful and creative way of developing New York law on these issues. This could provide the courts a way to give precise and significant meaning to the implied covenant of good faith without compromising the dedication of New York jurisprudence to the enforcement of contracts in accordance with their express terms.

H. Dealing with Passage of Risk; Damages

New York's correlation of delivery and passage of risk seems sensible, consistent with the CISG and also more or less consistent with the part of the civil law tradition based in German law, while, in this area, the English and French rules seem more difficult to apply and even counter-intuitive. The general approach of New York law to damages also seems consistent with the approach of the CISG, which focuses, like New York law, primarily on loss and less on fault. In this, the international restatements, particularly the UNIDROIT Principles, focus on "harm" in a way that still suggests a strong role for fault, which at the one and the same time, makes expectations of relief less certain (because willfulness or negligence may have to be established) and also liable to a broader scope of claims (even for emotional damages under the UNIDROIT Principles).[128] *In dealing with contract provisions excluding or limiting consequential damages, as with entire agreement clauses and hardship provisions, drafting must be especially careful and complete*. Notwithstanding the general deference by New York courts to the "private ordering" for which parties provide in their agreements, it appears New York courts (as common law courts in general) tend to interpret provisions that limit remedies under New York law (such as consequential damage exclusions) or that provide relief where New York law might not ordinarily provide it (such as allowing for hardship or providing a remedy of specific performance) or that limit liability (such as "entire agreement" clauses seeking to exclude relief for misrepresentation) by applying a very strict standard of specificity and comprehensiveness in such areas where common law courts are generally loathe to tread. Providing a detailed map for navigating the rights and obligations of contracting parties in such uncharted legal waters is clearly the best way to win the adherence and support of New York courts.

Endnotes

1. NY General Obligations Law Section 5-1401 (“NY GOL”).
2. *Id*. §5-1402. *See* Final Report of the New York State Bar Association’s Task Force on New York Law in International Matters, Section II(A)(1)(e) (25 June 2011).
3. Pursuant to the Declaration made by the United States at the time it deposited its ratification of the CISG, the Convention is applied in the United States to contracts of sale under which all contracting parties have their businesses in countries that have ratified the Convention but not to contracts where the law of a U.S. jurisdiction would apply by application of principles of conflicts of laws. See Appendix B hereto: *Sample Governing Law and Choice of Form Clauses*, Part I, n. 3.
4. More space could allow for consideration of other national laws. But English law has been the “fount of law” for most common law jurisdictions, and French law and German law have had a pervasive influence on the law of most civil law jurisdictions—whether in Europe, Latin America or Asia. Nor should one overlook the important influence of the CISG on the shape of national laws, perhaps most notably in the case of China.
5. See French Civil Code, Article 1108.
6. Glen Banks, New York Contract Law §2:27 (2006), *citing Express Industries v. Elsevier Sciences, Ltd.*, 927 F. Supp. 2d 688, 703 (S.D.N.Y. 1996).
7. See Vranken, European Civil Law §532.
8. John Cartwright, Contract Law: An Introduction to the English Law of Contract for the Civil Lawyer 114-116 (2007).
9. *See* G. Banks, note 6 *supra*, §4:26.
10. *Id*. §§2.29 and 6.27. Note that the important role that the principle of good faith plays in the German tradition and, to an important extent, also in the French tradition, even in pre-contractual negotiations, makes it somewhat more likely that civilian courts will become involved in assessing and adjusting the terms of contracts than New York or English courts would be inclined to do. *See generally* Richard Zimmerman and Simon Whitaker, Good Faith in European Contract Law.
11. Miller, *Bargaining on the Red-Eye: New Light on Contract Theory* at 55, *available at* http://papers.ssrn.com/ sol3/papers.cfm?abstract_id=1129805.
12. *See generally* Martin Vranken, Fundamentals of European Civil Law, §§508-525; and Jan Dalhuisen, 2 Transnational Comparative, Commercial, Financial and Trade Law §1.4.2 (4th ed.).
13. G. Banks, note 6 *supra*, §12:4.
14. *See* Miller, note 11 *supra*, at 40.
15. G. Banks, note 6 *supra*, §§9:3-9:4.
16. *Id*. §§2:19-2:21.
17. Vergne, *The “Battle of the Forms” under the 1980 United Nations Convention on Contracts for the International Sale of Goods*, *available at* http://www.cisg.law.pace.edu/cisg/biblio/vergne.html *citing* Cass. Civ. lère, 17 juillet 1967, Bull. Civ. III, 29.
18. NY UCC §2-207(2).
19. *Id*. §2-207(2)(b).
20. *Id*. §2-207(3).
21. *Isn’t 60 Some Years of Litigation Enough?*, 48 The Uniform Commercial Law Letter 7 (March 2014).
22. *See Coastal & Native Plant Specialties, Inc. v. Engineered Textile Products, Inc. v. Occidental Chemical Corporation*, 139 F. Supp. 2d 1326 (N.D. Fla. 2001) (applying New York law).
23. [1979] 1 WLR 401 (CA). The case is discussed in J. Cartwright, note 8 *supra*, at 96.
24. [1985] AC 191, 201, discussed in J. Cartwright, note 8 *supra*, at 186-188.
25. G. Banks, note 6 *supra*, §9:5 *citing Cromwell Towers Redevelopment Co. v. City of Yonkers*, 41 N.Y.2d 1, 6 (1976): “Where the document makes clear the parties’ overall intentions, the construction that would effectuate the plain purpose and object of the agreement should be given to the particular language at issue.” *See also id*., §9:6, *citing Kass v. Kass*, 91 N.Y.2d 554, 567 (1998). “In interpreting contract terms,” the New York Court of Appeals has stated, “the court considers the matter from the perspective of the ordinary business person making an ordinary business contract,” *Michaels v. City of Buffalo*, 85 N.Y.2d 754, 757 (1995), “keyed to the level of business sophistication and acumen of the particular parties.” *Uribe v. Merchants Bank of New York*, 91 N.Y.2d 336 (1983). *See* G. Banks, note 6 *supra*, §§9:6-9:7.
26. G. Banks, note 6 *supra*, §8:18.
27. J. Cartwright, note 8 *supra*, at 184.
28. [1996] 2 All ER 573.
29. [1999] WL 852482.
30. Jones Day, *Some Differences in Law and Practice Between U.K. and U.S. Stock Purchase Agreements*, 16 April 2007.
31. Kamya and Thompson (Steptoe & Johnson LLP), *Entire Agreement Clauses—Are You Adequately Protected?* (October 2010).
32. 184 N.Y.2d 599 (1959).
33. 748 F.2d 729 (2d Cir. 1984).
34. 174 N.Y. 331 (1903).
35. 222 N.Y. 88 (1917).
36. *See, e.g.*, *Dalton v. Educ. Testing Serv.*, 87 N.Y.2d 384, 389 (N.Y. 1995) (covenant of good faith and fair dealing in the course of contractual performance is implicit in all contracts).
37. G. Banks, note 6 *supra* §11:16. *See also* Official Comment to NY UCC 2-103.
38. *See* Harold Dubroff, *Implied Covenant of Good Faith in Contract*, *available at* http://www.stjohns.edu/ academics/graduate/law/journals/lawreview/issues/80_2/Dubroff.stj.
39. G. Banks, note 6 *supra*, §11:17, *citing 511 West 232nd Owners Co. v. Jennifer Realty Co.*, 98 N.Y.2d 144 (2002), *quoting Dalton v. Educational Testing Service*, 87 N.Y.2d 384, 389 (1995).
40. G. Banks, note 6 *supra*, §6:23, *citing Oppenheimer & Co. Inc. v. Oppenheim, Appel, Dixon & Co.*, 86 N.Y.2d 685,695 (1991).
41. 97 N.Y.2d 195 (2001).
42. 937 F.2d 780 (2d Cir. 1991).
43. *See* G. Banks, note 6 *supra*, §11:20, *citing Gillman v. Chase Manhattan Bank, N.A.*, 73 N.Y.2d 1 (1988) (implied covenant cannot be used to interpret away rights expressly given to parties under a contract).
44. G. Banks, note 6 *supra*, §11:17, *citing Thyroff v. Nationwide Mut. Ins. Co.*, 460 F.3d 400, 407, *certified question accepted*, 7 N.Y.3d 837, 824 (2006).
45. Howard Hunter, Modern Law of Contracts §8:8 (2011), *discussing Gross v. Empire Healthchoice Assurance, Inc.*, 126 Misc. 3d 112(A) (Sup. Ct. N.Y. Cty. 2007).
46. See section on German law in Squire Sanders, *The Notion of Contractual Good Faith: Perspectives from Comparative Law*, *available at* http://larevue.ssd.com/The-Notion-of-Contractual-Good-Faith-Perspectives-from-Comparative-Law_a1010.html.
47. *Id*.

48. J. Cartwright, note 8 *supra*, at 59.

49. *Id*. at 60.

50. *See* Polkinghorne & Korman, *Paris Energy Series No. 3*, *available at* http://www.whitecase.com/files/ Publication/04a3da7b-fef6-40ee-88a0-8340c02c68a3/Presentation/PublicationAttachment/7d60a026-379c-42ce-8c0c-889a36bb7ea4/article_ParisEnergySeries%20_Disputes_No3.pdf.

51. J. Cartwright, note 8 *supra*, at 69.

52. 52 N.Y.2d 394 (1981).

53. Miller, note 11 *supra*.

54. 751 F.2d 69 (2d Cir. 1984).

55. 64 F.2d 344 (2d Cir. 1933).

56. Polkinghorne and Kirkman, *The Paris Energy Series No. 4*, *available at* http://www.whitecase.com/files/ Publication/83c9518e-90da-48b1-8ec3-3b6b3d8dbee4/Presentation/Publication Attachment/f260d894-23ee-4728-8471-3c6bdbe29c2f/The_Paris_Energy_Series_No_4.pdf.

57. *U.S. v. General Douglas MacArthur Senior Village, Inc.*, 508 F.2d 377, 381 (2d Cir. 1974).

58. G. Banks, note 6 *supra*, §20:18.

59. J. Cartwright, note 8 *supra*, at 241, *citing Davis Contractors Ltd v. Fareham UDC*, [1956] AC 696 (HL) 729.

60. Polkinghorne and Kirkman, note 56 *supra*.

61. *Id*., at 8.

62. No. CIV.A.18373.2001 WL (Westlaw) 675330 (Del. Ch. 18 June 2011).

63. *See* Kirsten Birkett, PLC, *Untying the Knot: Material Adverse Change Clauses, available at* http://corporate. practicallaw.com/6-101-6634.

64. G. Banks, note 6 *supra*, §20.14, *citing Kel Kim Corp. v. Central Markets, Inc.*, 70 N.Y.2d 900 (1987); and *Phillips Puerto Rico Core, Inc. v. Tradax Petroleum Ltd.*, 1984 WL 677 (S.D.N.Y. 1984), *aff'd*, 782 F.2d 314 (2d Cir. 1985).

65. *See* Kirsten Birkett, note 63 *supra*; Suhrud Mehta (Milbank), *Material Adverse Change Clauses in Adverse Markets*, *available at* http://www.milbank.com/images/content/7/8/783/Material_Adverse_Change_Clauses_Mehta .pdf.

66. *Meinhard v. Salmon*, 249 NY 458, 463-464 (1928).

67. Franke, *Resisting the Contractarian Insurgency: The Uniform Trust Code, Fiduciary Duty, and Good Faith in Contract*, 36 ACTEC L.J. 517, 539 (Winter 2010).

68. Judge Friedman, writing for the majority, determined that, for a stock warrant purchase agreement, a provision dealing with the effect of stock splits and reverse stock splits was an "essential term" which the court should supply. *Marvin M. Reiss et al. v. Financial Performance Corporation*, 279 A.D.2d 13 (1st Dep't 2000).

69. 309 A.D.2d 288, 298-302 (1st Dep't 2003).

70. *See* Yeo Ting Min, *A Note on Differences in English Law, New York Law, and Singapore Law*, *available at* http://linklibrary.smu.edu.sg/sol_research/365.

71. Keilhack, *Third Party Rights: A Comparison of English and German Law with Respect to the UNIDROIT Principles on International Commercial Contracts*, Section B(II), *available at* http://www.grin.com/en/e-book/22898/third-party-rights-a-comparison-of-english-and-german-law-with-respect#inside.

72. G. Banks, note 6 *supra*, §8:6, *citing Seaver v. Ransom*, 224 N.Y. 233 (1918).

73. *Id*. §8:6, *citing Fourth Ocean Putnam Corp. v. Interstate Wrecking Co., Inc.*, 66 N.Y.2d 38 (1985); and *State of California Public Employees' Retirement System v. Sherman & Sterling*, 95 N.Y.2d 427 (2000).

74. *Id*. §8:7.

75. Sale of Goods Act 1979 §61(1); French Civil Code Art. 1583.

76. Sale of Goods Act (1979), §20(1).

77. *See* Tetley, *Sale of Goods—The Passing of Title and Risk—A Resume*, *available at* http://www.international privatelaw.com/files/Property_and_Risk.pdf.

78. Incoterms 2010, published by the International Chamber of Commerce, became effective as of 1 January 2011. *See* http://www.iccwbo.org/products-and-services/trade_facilitation/incoterms-2010.

79. *See* The Restatement 2d of Contract Law §260(2).

80. G. Banks, note 6 *supra*, §22:1.

81. J. Cartwright, note 8 *supra*, at 271.

82. Cafaggi, *Creditor's Fault: In Search of a Comparative Frame*, text accompanying footnotes 9 and 23, *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1551825.

83. Pejovic, *Civil Law and Common Law: Two Different Paths Leading to the Same Goal*, 32 Victoria U. of Wellington L. Rev. 817-841 (2001), *available at* http://trove.n/a.gov.au/version/167133.811.

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85. (1854) 9 Ex. 341.

86. J. Cartwright, note 8 *supra*, at 267.

87. [2008] UKHL 48.

88. [2010] EWHC 542.

89. Howell and Rogers, *Remoteness of Damages under English Law: Hadley v. Baxendale Remains the Standard Test*, Fulbright & Jaworski, 14 July 2010, *available at* http://www.fulbright.com/index.cfm?fuseaction=publications .detail&pub_id=4566&site_id=494&detail=yes *See also* G. Banks, note 6 *supra*, §22:18.

90. G. Banks, note 6 *supra*, §22:18, *citing Globecon Group LLC v. Hartford Ins. Co.*, 2006 WL 29413 (2d. Cir. 2006).

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92. 944 F.Supp. 179 (W.D.N.Y. 1996).

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104. *American List Corp. v. U.S. News & World Report*, 75 N.Y.2d 38 (1989).

105. *See SK Shipping (5) Pte Ltd. V. Petroexport Ltd.* [2009].

106. BGB §323(4).

107. *See generally*, Chan-Hung Chung, *A Holder in Due Course of Commercial Paper Under the UCC and a Good Faith Purchaser of Bills and Checks Under the Geneva Uniform Law*, 18 Korean J. Comp. L. 1 (1990).

108. Geva, *Forged Check Indorsement Losses under the UCC: The Role of Policy in the Emergence of Law Merchant from Common Law*, 45 Wayne L. Rev. 1733 (2000).

109. Roberto Luis Frias Garcia, *The Autonomy Principle of Letters of Credit*, 3 Mexican L. Rev. 68, 74-75 (2010).

110. 31 N.Y.S.2d, 631-34 (Sup. Ct. N.Y. Cty., 1941).

111. 10 C.B. 665, 138 Eng. Rep. 263 (C.B. 1851.)

112. 106 N.Y. 195 (1887).

113. *See also* Murray, *History and Development of the Bill of Lading*, 37 U. Miami L. Rev. 689 (1983).

114. *See* Indira Carr, International Trade Law 175-176 (4th ed. 2010).

115. *See* McGuire Woods, *Security Interests in Accounts Receivable and Inventory in Common Law and Civil Law Jurisdictions*, *available at* http://www.mcguirewoods.com/news-resources/publications/financial_services/banking 03.pdf.

116. *See generally id*.

117. *See generally id*.

118. *See* Pejovic, note 83 *supra*, Section IV(E).

119. *See id.* Section IV(C).

120. This is not to gainsay the importance of the Recommendation of the Litigation Subcommittee of the Task Force on New York Law and International Matters regarding the adoption of special chambers within the Commercial Division of the New York Supreme Court that could apply a variety of rules of procedure, including those of London or Paris. As the Task Force Report emphasizes, New York courts are very familiar with applying the substantive law of other countries, in accordance with the governing law clauses of the contracts that may come before them. Having the ability to apply diverse procedural rules would enhance the international character of the New York courts and allow parties the greatest flexibility and autonomy in making choices that may combine what contracting parties may see as the best advantages of one system for governing law and another system for civil procedure.

121. *See* G. Banks, note 6 *supra*, §2:18-2:22.

122. 09 Civ. 10559 (S.D.N.Y. 01/18/11) (Hellerstein, J.).

123. *See* Eisenberg and Miller, *The Flight to New York, An Empirical Study of Choice of Law and Choice of Forum Clauses in Publicly-Held Companies' Contracts*, 30 Cardozo L. Rev. 1475 (2009); Miller, note 11 *supra*.

124. Miller, note 11 *supra*, Section II, at 2.

125. *Reiss et al. v. Financial Performance Corporation*, 279 A.D.2d 13 (1st Dep't 2000), *rev'd*, 97 N.Y.2d 195 (2001).

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Appendix A

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Appendix B

Sample New York Governing Law and Choice of Forum Clauses Adapted from the Sample Clauses of the NYSBA Task Force on New York Law and International Matters[1]

Part I: Sample New York Governing Law Clauses

Dispute resolution agreements and clauses are found across a wide section of transactional contracts—from complex merger documents to royalty agreements, oil exploration contracts and joint venture agreements.

At its best, the drafting of a dispute resolution clause is the convergence of the business lawyer's negotiating skills and ability to foresee difficulties for the lawyer's client and the arbitration/litigation lawyers' insights about what clauses work best in what types of agreements and circumstances.

At its worst, drafting is a haphazard, last-minute guessing exercise by transaction lawyers at the eleventh hour of a deal's closing—which down the road can cost the client significantly in terms of outcome and costs.

Assuming the parties wish to submit any disputes to the New York courts, and provided the parties want their contract to be governed by New York, the provisions in this and the next two parts may be considered for adaptation to the circumstances of a particular international agreement.

A. Governing Law—General Contract

This Agreement shall be governed by and construed in accordance with the laws of the State of New York, without regard to conflicts or choice of law rules that would result in the application of the substantive laws of any other jurisdiction.

B. Governing Law for Contracts for International Sale of Goods[2]

(1) Contract for International Sale of Goods Where Application of CISG is Desired and All Parties Have Their Place of Business in Jurisdictions That Are Parties to the Convention:

This Agreement shall be governed by and construed in accordance with the laws of the State of New York, without regard to any conflicts of law rules that may cause the substantive law of another jurisdiction to apply, it being assumed for all purposes of this Agreement that the 1980 United Nations Convention on Contracts for the International Sale of Goods is an integral part of the law of contracts of the State of New York with regard to international sales transactions governed by the said Convention.

(2) Contract for International Sale of Goods Where Application of CISG is Desired but One or More Parties Have Places of Business in Jurisdictions That Are Not Parties to the CISG:[3]

This Agreement shall be governed by and construed in accordance with the laws of the State of New York, without regard to any conflicts of law rules that may cause the substantive law of another jurisdiction to apply, it being assumed for all purposes of this Agreement that the 1980 United Nations Convention on Contracts for the International Sale of Goods (the "Convention") is incorporated as an integral part of the law of contracts of the State of New York with regard to international sales transactions governed by the Convention, without regard to whether (or to what extent) any jurisdiction in which any party to this Agreement has its place of business or otherwise has authority to resolve a dispute hereunder has ratified or acceded to the Convention or made any declaration under Article 95 thereof.

(3) Contract of International Sale of Goods Where Application of the CISG Is Not Desired:

First Alternative:

This Agreement shall be governed by and construed in accordance with the laws of the State of New York, without regard to any conflicts of law rules that may cause the substantive law of another jurisdiction to apply and without application of the 1980 United Nation Convention on Contracts for the International Sale of Goods (the "Convention") as if none of the jurisdictions in which parties to this Agreement have their places of business are parties to the Convention.

Second Alternative:

This Agreement shall be governed by and construed in accordance with the laws of the State of New York, without regard to any conflicts of law rules that may cause the substantive law of another jurisdiction to apply, provided, however, that the parties hereto agree that the provisions of the 1980 United Nations Convention on Contracts for the International Sale of Goods are excluded in their entirety.

C. Governing Law for Trusts and Wills[4]

First Alternative (Trusts):

I hereby direct, pursuant to Section 7-1-10 of the New York Estates, Powers & Trusts Law, that the law of the State of New York shall apply to the validity, effect and interpretation of all provisions of this Agreement in so far as they govern property located in New York State as well as property located outside of New York State.

Second Alternative (Wills):

I direct that this Will be submitted for, and I request that this Will be admitted to, original probate in the State of New York and I hereby elect, pursuant to Section 3-5.1(h) of the Estates, Powers and Trusts Law of the State of New York, that the formal validity, interpretation and effect of this Will with respect to all property of mine situated in New York as well as all property of mine situated anywhere else outside of New York State shall be governed by the laws of the State of New York and that my estate shall be governed by and under said laws.

Part II: Sample New York Dispute Resolution Clauses (Submission to Jurisdiction and Governance of Proceedings)

A. General Submission to the New York Courts

The parties agree that the New York Supreme Court (__________ County) and the United States District Court for the ____________ District of New York shall be the exclusive forums for the resolution of any dispute, claim or controversy arising out of or relating to this Agreement, or the breach, termination, enforcement, termination or validity thereof, submit irrevocably to the exclusive jurisdiction of the said Courts and irrevocably waive any objections thereto based on lack of personal or subject matter jurisdiction, improper venue, or the doctrine of forum non conveniens.

B. Submission to New York Supreme Court, Commercial Division, Waiver of Right to Remove to Federal Courts

The parties agree that the New York Supreme Court (__________ County), Commercial Division, shall be the exclusive forum for the resolution of any dispute, claim or controversy arising out of or relating to this Agreement, or the breach, termination, enforcement, termination or validity thereof, submit irrevocably to the exclusive jurisdiction of the New York Supreme Court (__________ County) Commercial Division, and irrevocably waive any objections thereto based on lack of personal or subject matter jurisdiction, improper venue or the doctrine of forum non conveniens, as well as any right to seek to remove any such proceedings to the Federal courts of the United States of America, whether based on diversity of the parties, Federal subject matter jurisdiction or any other basis.[5]

C. Optional Additional Clauses

Having included the provisions of paragraphs A or B above, the parties may wish to add some or all of the following:

(1) *Service of Process*:

The parties agree that service of process shall be complete if timely, made by delivery a copy of same upon _________________, whose address is ______________________, _______________, New York.

(2) *Jury Trials:*

The parties to this Agreement hereby irrevocably waive the right to trial by jury.

(3) *Damages:*

In any action arising out of or related to this Agreement, the parties irrevocably waive the right to recover punitive or exemplary damages and stipulate hereby that the court shall not be empowered to award any such damages.

(4) *Discovery:*

In any action arising out of or related to this Agreement, the parties waive the right to discovery as follows:

(i) There shall be no interrogatories or requests to admit;

(ii) ***First Alternative:***

There shall be no discovery depositions except as shall be authorized by the Court upon a showing of good cause shown and, in the event such depositions are permitted by the court, there shall be no more than _______ (__) depositions per side, with no deposition to exceed ______ (__) hours in length;

Second Alternative:

There shall be no pre-trial depositions except (1) depositions of witnesses for whom there is a reasonable basis to believe they will not be able to testify at trial or for whose testimony there may be otherwise a compelling need to preserve and (2) depositions of such witnesses whose pre-trial testimony any Court seized with responsibility for adjudicating a dispute hereunder shall determine is necessary in order to avoid mani-

fest injustice or a significant waste of Court resources.[6]

(iii) Documents requested by the parties shall be limited to those relevant to a claim or defense in the action and shall be restricted in terms of time frame, subject matter and persons or entities to which the requests pertain and shall not include broad phrases such as "all documents directly or indirectly related to…"

(5) Enforcement of Judgments:

The parties agree that a final judgment against it in any action, suit or proceeding taken in any Court to whose jurisdiction the parties have entrusted the resolution of any dispute shall be conclusive and may be enforced in any jurisdiction in the world by suit on the judgment, a certified copy of which judgment shall be conclusive evidence thereof, or by any other means provided by law.

D. E-Disclosure

Given the special considerations that may be required with respect to any request by a party for electronic records, the parties may wish to tailor the following provisions to the circumstances of the action:

In any action arising out of or relating to this Agreement:

(i) There shall be production of electronic documents only from sources used in the ordinary course of business. Absent a showing of compelling need, no such documents are required to be produced from backup servers, tapes or other media.

(ii) Absent a showing of compelling need, the production of electronic documents shall normally be made on the basis of generally available technology in a searchable format which is usable by the party receiving the e-documents and convenient and economical for the producing party. Absent a showing of compelling need, the parties need not produce metadata, with the exception of header fields for email correspondence.

(iii) The description of custodians from whom electronic documents may be collected shall be narrowly tailored to include only those individuals whose electronic documents may reasonably be expected to contain evidence that is material to the dispute.

(iv) Where the costs and burdens of e-discovery are disproportionate to the nature of the dispute or to the amount in controversy, or to the relevance of the materials requested, the parties consent and stipulate that the court shall either deny such requests or order disclosure on condition that the requesting party advance the reasonable cost of production to the other side, subject to the allocation of costs in the final judgment.

Part III: Sample New York Arbitration and ADR Clauses

International agreements most frequently contain arbitration clauses for the resolution of disputes since parties generally wish to avoid the risk of litigating in the courts of an unfamiliar jurisdiction. Arbitral institutions offer "standard" arbitration clauses for inclusion in such contracts, but the better practice is to adapt arbitration clauses to the particular circumstances of the business relationship reflected in the overall agreement. The following provisions are a starting point for the adaptation process.

A. Simple Agreement—Arbitration

Any and all disputes, controversies and claims arising out of or relating to this Agreement, including the formation, interpretation, breach or termination thereof, and also including whether the claims asserted are arbitrable, and any transactions pursuant thereto, shall be finally determined by arbitration in accordance with the [insert institutional arbitration rules]. The Tribunal shall consist of [one/three] arbitrator[s]. The place of the arbitration shall be New York, New York. The language of the arbitral proceeding, including the parties' written submissions, shall be English. Judgment upon the award rendered by the arbitrator[s] may be entered in any court having jurisdiction thereof.

B. Additional Provisions—More Complex Arbitration Agreement

(1) Enforcement of Awards:

Without limiting the foregoing, the parties to this Agreement agree that any Award rendered by arbitration may be entered in the Courts of the State of New York, and the said parties hereby submit to the non-exclusive jurisdiction of the said Courts in any proceeding for the recognition and enforcement of the Award and hereby designate ________________, whose address is ______________, __________, New York, as each such party's agent for purposes of service of process in connection with any such proceeding.

(2) Allocation of Costs and Fees:

In any arbitration arising out of or related to this Agreement, the arbitrators may [shall] include in their award an allocation to the prevailing party of

all or part of such costs and expenses, including arbitrators' fees, attorneys' fees and expert witness fees and disbursements, as the arbitrators shall deem reasonable.

(3) *Punitive Damages*:

In any arbitration arising out of or related to this Agreement, the arbitrators are not empowered to award punitive or exemplary damages, and each party hereby waives any right to seek or recover punitive or exemplary damages with respect to any dispute resolved by arbitration.

(4) *Disclosure—Exchange of Evidence*:

The parties shall be entitled to reasonable production of relevant and material, non-privileged documents carried out expeditiously. If the parties are unable to agree on such production, the arbitral tribunal shall have the power, upon application of any party, to make all appropriate orders for production of relevant and material, non-privileged documents by any party. There shall be no other form of disclosure or discovery, including pre-hearing depositions upon oral examination [nor shall there by any disclosure or discovery requests to any third parties].

(5) *E-Discovery*:

(i) There shall be production of electronic documents only from sources used in the ordinary courses of business. Absent a showing of compelling need, no such documents are required to be produced from backup servers, tapes or other media.

(ii) Absent a showing of compelling need, the production of electronic documents shall normally be made on the basis of generally available technology in a searchable format which is usable by the party receiving the e-documents and convenient and economical for the producing party. Absent a showing of compelling need, the parties shall not produce metadata, with the exception of a header fields for email correspondence.

(iii) The description of custodians from whom electronic documents may be collected shall be narrowly tailored to include only those individuals whose electronic documents may reasonably be expected to contain evidence that is material to the dispute.

(iv) Where the costs and burdens of e-discovery are disproportionate to the nature of the dispute or to the amount in controversy, or to the relevance of the materials requested, the arbitrator will either deny such requests or order disclosure on condition that the requesting party advance the reasonable cost of production to the other side, subject to the allocation of costs in the final award.

(6) *Confidentiality*:

The parties and the arbitrator(s) shall use only for the purposes of the arbitration and keep confidential all awards in the arbitration, together with all arbitral proceedings, all materials in the proceedings created for the purpose of the arbitration and all other documents produced by another party in the proceedings not otherwise in the public domain, save and to the extent that disclosure may be required of a party or arbitrator by legal duty, to protect or pursue a legal right or to enforce or challenge an award in legal proceedings before a court or other judicial authority.

(7) *Provisional Measure—Interim Relief*:

The arbitrator(s) shall be empowered to grant injunctive relief, including restraining orders and orders for specific performance, in addition to monetary damages. Nothing in this Agreement shall prevent either party from seeking provisional measures, including, but not limited to, pre-award attachments and injunctive relief, from any court of competent jurisdiction and any such request shall not be deemed incompatible with the agreement to arbitrate or a waiver of the right to arbitrate.

(8) *Time Limits*:

Notwithstanding any provision to the contrary in the Rules otherwise applicable to any arbitration arising out of or related to this Agreement, the parties shall complete all necessary steps in any arbitration, including the hearing on the merits, within [12] months of the commencement of the proceeding. The arbitrator(s) shall render a final award within [30] days of the close of the hearings. The arbitrators may determine that the interest of justice or the complexities of the arbitration requires that these time limits be extended.

(9) *Multi-Step or Phased Dispute Resolution, Including Negotiation, Mediation and Arbitration*:

The parties shall promptly attempt to resolve amicably by negotiation between party representatives, with authority to settle the dispute, any dispute arising out of or related to this Agreement, including the existence, validity, termination or breach thereof. If the dispute has not been resolved within [30] calendar days after any party requested in writing negotiation under this provision, then the parties shall promptly proceed to mediation as described below.

The parties shall promptly attempt to resolve amicably by mediation any dispute, not resolved by negotiations described above, arising out of or related to this Agreement, including the existence, validity, termination or breach thereof, under the [designated] Mediation Rules in New York, New York. If the dispute has not been resolved within [60] calendar days after any party requested in writing mediation under this provision, then the parties shall promptly proceed to arbitration as described below.

All communications during the negotiation and mediation described above shall be treated as made in the course of compromise and settlement negotiations for purposes of any applicable rules of evidence and any additional confidentiality and professional secrecy protections provided by applicable law.

(10) *Reasoned Awards*:

Any Award hereunder shall be in writing and shall set forth the reasons for supporting the Award in writing.[7]

(11) *Scope of Arbitrators' Authority*

The arbitrators shall be empowered to sit as "*amiable compositeurs*" and shall [not] be bound to apply strictly the law that would otherwise govern the resolution of any dispute hereunder.[8]

Endnotes

1. This set of sample clauses substantially replicates but expands on the clauses contained in Exhibits C and D to the Report of the NYSBA Task Force on New York Law and International Matters issued on 25 June 2011. Modifications, additions and annotations are by Michael W. Galligan, Partner, Phillips Nizer LLP. The additions include sample clauses for contracts for the international sale of goods and also for trust agreements and wills; additional clauses for choice of New York courts as a forum for dispute resolution and limitation of discovery, and some additional clauses for choice of arbitral procedures. For an excellent overview and additional sample clauses, see Pollack, *Drafting an International Contract: Jurisdiction and Arbitration Clauses*, First Annual Fundamentals of International Practice at 183-199 (NYSBA CLE Dept., 2009).
2. For helpful guidance, see Drago and Zoccolillo, *Be Explicit: Drafting Choice of Law Clauses in International Sale of Goods Contracts*, The Metropolitan Corporate Counsel at 9 (May 2002).
3. NY UCC § 1-105 provides, under certain circumstances, that parties to a sales transaction may apply the law of a state or nation other than New York. It is unclear to what extent this provision precludes a New York court from applying a choice of law provision electing the rules of an international treaty such as the UN Convention on the International Sale of Goods, especially where a party to a transaction has its place of business in a jurisdiction that is not a party to the Convention and the Convention, pursuant to the U.S. Declaration under Article 95 of the Convention, would not otherwise apply. Parties who nonetheless wish the Convention to apply may consider adopting this clause, but may also be well advised to elect to have disputes be governed by arbitration rather than by litigation. Please note that, pursuant to NY UCC § 1-105(2), if the Convention were to serve as governing judicial law strictly by private choice, it could not supplant the applicability of NY UCC § 2-402 (rights of creditors against sold goods).

   To ensure that this clause would be respected and applied in a judicial proceeding before a New York court, it would be best if NY UCC Section 1-1.05 were to be amended to provide that parties to contracts for the sale of goods with "reasonable connections" to both New York and other domestic and national jurisdictions may elect not only that their contracts be governed by the laws of the other relevant states or nations but by the 1980 Convention on the International Sale of Goods ("CISG").

   New York law, as a state of the United States, pursuant to the Supremacy Clause of the U.S. Constitution, must incorporate the law of any treaty to which the United States is a party. When the United States ratified the CISG, it entered a Declaration, as allowed by Article 95 of the Convention, to the effect that the Convention would only be applied by the United States to contracts of sale under which all contract parties had their businesses in countries that had ratified the Convention, even if the conflicts laws of another relevant jurisdiction not itself a party to the Convention should determine that the law of a state of the United States like New York should apply. Thus, in the case of a contract of sale between a French seller and a U.S. buyer located in New York, a New York court will apply the Convention rules because both France and the United States are parties to the Convention. But, in the case of a contract of sale between a UK seller and a New York buyer, it appears that, pursuant to NY UCC Section 1-105, a New York court is not required—and may not even be permitted—to apply the Convention rules, even if the parties have expressly agreed that the law of New York *incorporating the Convention rules* should apply, because the UK is not a party to the Convention.

   It would be well if the United States withdrew its Declaration under Article 95 of the CISG (ironically introduced into the Convention at the behest of certain "command-economy" states that have now converted to market economies), in order to effect a more stable and consistent set of rules for the international sale of goods throughout the world. (Singapore, one of the few market economy states other than the United States to make a similar Declaration, is said to be about to withdraw its Declaration). But in the meantime, an amendment to the New York UCC would be very helpful.
4. For some background, see *Buying USA: Minimizing US Transfer Taxes on US property Interests of Non-US Persons*, STEP**USA** at 11-15 (June 2007).
5. On the ability of parties to waive the right of removal to federal courts, see *Excell, Inc. v. Sterling Boiler & Mechanical, Inc.*, 106 F.3d 318 (10th Cir. 1997); *Archdiocese of Milwaukee v. Underwriters at Lloyd's*, 955 F. Supp. 2d. 1066 (E.D.Wis., 1997).
6. This sample clause aims to replicate to a reasonable extent the approach that courts in England might take to pre-trial depositions. See Cohen, *Voyages of Discovery: Obtaining Orders for Discovery in England in Support of Proceedings in the U.S.*, Volume 220, N.J. Lawyer at 52-55 (Feb. 2003).
7. Compare with Article 1471 of the Code of Civil Procedure of France.
8. Compare with Article 1474 of the Code of Civil Procedure of France.

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Please Contact Tiffany Bardwell at tbardwell@nysba.org with Any Questions

U.S. Competition Rules for Distribution

By Andre R. Jaglom

I. Introduction

The countries of the Association of Southeast Asian Nations (ASEAN) (Vietnam, Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore and Thailand) agreed to adopt competition laws by 2015. Half of them have; half have yet to do so. The laws in place, and those that can be anticipated, vary in some important respects from the rules applicable in the U.S., Europe and Latin America, and can significantly affect the way companies distributing goods to these nations structure their relationships.

This article summarizes the key competition rules in the United States governing vertical restraints,[1] to provide a benchmark for comparison with the rules in other regions and those that the ASEAN nations may develop.

II. Important Legal Issues

A. Resale Price Maintenance (Supplier Control of Reseller's Pricing)

Federal law in the United States judges resale price maintenance ("RPM") under the rule of reason,[2] and usually permits it, ever since the U.S. Supreme Court's 2007 decision in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*[3] *Leegin* overruled the previously applicable rule that vertical agreements "to maintain prices and stifle competition" were *per se* illegal, which had governed RPM for nearly a century, since *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, decided in 1911.

But there are circumstances discussed by the Supreme Court where such restrictions could be found unlawful even under *Leegin*. The Supreme Court identified various scenarios involving RPM programs which "may have anticompetitive effects":

- An RPM program may facilitate horizontal price-fixing by suppliers, either by helping identify price-cutting suppliers if the reduced price shows up at retail, or by discouraging suppliers from cutting prices, because they will not benefit from increased sales if retail prices do not increase.[4]
- An RPM program may facilitate horizontal price-fixing by resellers, where the RPM program is originated by a group of dealers and then foisted upon their supplier as an enforcement mechanism. The supplier then is at risk of becoming part of a horizontal, *per se* unlawful, price-fixing conspiracy among its customers.[5]
- A reseller with market power may call for an RPM program from its supplier to reduce competition from more efficient, discounting competitors.[6]
- A supplier with market power may use RPM to give resellers an incentive not to sell the products of the supplier's smaller rivals and new market entrants.[7]
- Consequently, the Supreme Court suggested in *Leegin* several factors relevant to the rule of reason inquiry of an RPM program:
  - *The number of suppliers using RPM in the industry*. The more manufacturers who use RPM, the more likely that it could facilitate a supplier or dealer cartel.[8]
  - *The source of the restraint*. If dealers are "the impetus for a vertical price restraint, there is a greater likelihood the restraint facilitates a [dealer] cartel or supports a dominant, inefficient [dealer]."[9]
  - *Whether a supplier or reseller has market power*.[10]

In considering whether to approve a proposed RPM program, counsel needs to review all the facts and determine whether any of these factors are present, or if there are other indications that the proposed program will have anticompetitive effects rather than enhancing interbrand competition. On the flip side, counsel needs to consider the extent to which the use of RPM in the particular circumstances will foster intrabrand competition by enabling or encouraging dealers to offer more services to consumers and by giving consumers greater choice of purchasing the product (but not the brand) from higher price-higher service dealers, low price-low service dealers or dealers offering a middle ground.

Moreover, individual states within the U.S. have their own state antitrust laws, and not all follow the new federal rule. Thirteen states have antitrust statutes that explicitly bar RPM programs or render them unenforceable, and other states are expressly not bound to follow federal precedent in interpreting their state antitrust laws.[11] As a consequence, at least some state attorneys general are likely to continue to address RPM schemes under state law using the *per se* rule.

For example, in March 2008, the State of New York filed an antitrust complaint against Herman Miller, Inc. in connection with the company's resale price-fixing.[12] "Although filed post-*Leegin*, in keeping with the New York Attorney General's *per se* stance, the complaint pled only

per se violations of Section 1 of the Sherman Act and the New York, Illinois, and Michigan antitrust statutes."[13] Herman Miller settled for $750,000 and agreed to a court order that prohibits it from agreeing on retail prices with its retailers, from passing on retail prices among its retailers, and from coercing its retailers to agree on a retail price. Additionally, Herman Miller must notify retailers of their right to set their own prices.[14]

In the end, a patchwork of states accepting or rejecting the *Leegin* approach in enforcing the individual state's antitrust law appears to be developing.[15] Consequently, counsel must carefully examine each relevant state's treatment of RPM, especially as state law continues to develop, before implementing any RPM Program.

Businesses should be hesitant to adopt RPM programs in this environment, notwithstanding the widely held, but erroneous, belief that the Supreme Court made resale price-fixing lawful in *Leegin*. If an RPM program is to be implemented, counsel needs to review all the facts and determine whether any of the factors described by the Supreme Court in *Leegin* are present, or if there are other indications that the proposed program will have anticompetitive effects rather than enhancing interbrand competition. In addition, a careful analysis needs to be made of the applicable state laws in each state in which the firm does business, to avoid state enforcement and private actions under state antitrust laws.[16]

B. Alternative Pricing Constraints

It is perfectly lawful in the U.S. for a supplier to suggest resale prices, so long as there is no enforcement mechanism and the customer remains truly free to set its own prices. In addition, a supplier may establish a *unilateral* policy against sales below the supplier's stated resale price levels and *unilaterally* choose not to do business with those that do not follow that policy, because it is only *agreements* on resale pricing that may be *per se* unlawful. This concept was recognized long ago in the U.S. Supreme Court decision of *United States v. Colgate & Co.*,[17] but care must be taken not to take steps that would convert such a unilateral policy into an agreement. Thus, when a manufacturer's actions go beyond mere announcement of a policy and it employs other means to obtain adherence to its resale prices, an RPM agreement can be created.[18] *Colgate* policies can be notoriously difficult to administer, because it is in a salesperson's DNA to try to persuade a customer to adhere to the policy rather than to cut off the customer (with the resulting loss of sales to the salesperson), but such efforts at persuasion can be enough to take the seller out of the *Colgate* safe harbor and into a potentially unlawful RPM situation.

Minimum advertised price ("MAP") policies that control the prices a supplier advertises, but not the actual sales price, are also generally permitted, although the issue of what constitutes an advertised price for online sales can have almost metaphysical dimensions. In order to avoid classification as RPM, the MAP policy must not control the actual resale price, but only the advertised price. The closer to the point of sale that advertising is controlled, the greater the risk. Thus, in the bricks-and-mortar world, policies restricting advertising in broadcast and print media are more likely to be permitted; restrictions on in-store signage would be riskier, and restrictions on actual price tags and labels on merchandise are most likely to be deemed to be restrictions on actual, rather than advertised, prices. Online, sellers have most often restricted banner ads and the price shown when an item is displayed, while restrictions on the price shown once a consumer places an item in his or her shopping cart carry a greater risk, which explains why some items are displayed with the legend "Place item in cart for lower price." Cooperative advertising programs that condition reimbursement of all or a portion of the cost of an advertisement on compliance with a supplier's MAP policy are judged under the rule of reason, but are not free from risk.[19]

C. Exclusive Territories and Customer Allocation

Ever since the decision of the U.S. Supreme Court in *Continental T.V., Inc. v. GTE Sylvania Inc.*,[20] non-price vertical restraints, such as exclusive territories, have been judged by the rule of reason in the U.S. and are generally permitted, in the absence of market power. Customer allocation by competitors, however, is a horizontal arrangement rather than a vertical one and is *per se* illegal.[21] It is thus critical that the impetus for exclusive territories comes from the supplier in a vertical arrangement and not from dealers or distributors making a horizontal allocation of territories.

It is worth noting that a system of exclusive territorial distributorships contains two aspects: a promise by the supplier not to permit others to sell into a distributor's territory or to do so itself; and a promise by the distributor not to transship the products outside its territory. Both aspects are judged under the rule of reason in the U.S. and will be permitted, absent market power. [22]

Where the restriction is based on types of customers as opposed to geographic location, the result is no different.[23]

The references to market power above arise because many U.S. cases have applied a so-called "market power screen" in rule of reason cases, and uphold non-price vertical restraints whenever the defendant lacks market power. For example, the U.S. Court of Appeals for the Seventh Circuit put it as follows in *Valley Liquors, Inc. v. Renfield Importers, Ltd:*[24]

> A threshold inquiry in any Rule of Reason case is whether the defendant had market power, that is, the "power to raise prices significantly above the competitive

level without losing all of one's business." [citations omitted].... Only if [a plaintiff] can allege facts that give rise to an inference that [the defendant] had sufficient market power to control liquor prices must we proceed to the first step of the Rule of Reason analysis, which is to balance the effect, the vertical restraint has on intrabrand and interbrand competition.

D. Additional Restrictions

1. Restrictions on active or passive selling out of assigned territory

U.S. antitrust law does not make a distinction between active and passive selling, and it is generally permissible for a supplier to prohibit all out-of-territory sales by a distributor, both active and passive, in the absence of market power. The general rule judging non-price vertical restraints under the rule of reason is applicable.

2. Restrictions on Internet sales

Restrictions on online sales are viewed as a non-price vertical restraint like exclusive territories, and so are judged by the rule of reason and generally permitted, in the absence of market power. Courts have upheld prohibitions on mail order and telephone sales under the rule of reason,[25] and an absolute prohibition on Internet sales should be judged no differently. Lesser restrictions on online sales would be similarly upheld.

3. Restrictions on parallel (grey market) imports

Parallel importing is not generally viewed as an antitrust issue. For trademarked goods, however, importation of goods bearing the trademark, even if genuine, can be blocked through the U.S. Customs and Border Patrol Service, provided the non-U.S. manufacturer is not affiliated with the U.S. trademark owner, under § 526(a) of the Tariff Act,[26] which prohibits the importation of a product manufactured abroad "that bears a trademark owned by a citizen of…the United States and…registered in the U.S. Patent and Trademark Office." In addition, where the parallel imported goods are materially different from the U.S. goods in quality, features, warranty or the like, it may be possible to take action on a theory of trademark infringement where customer confusion is likely to result.[27]

There is much less ability to restrict gray market importation under a copyright theory. The Supreme Court held in 2013, in *Kirtsaeng v. John Wiley & Sons, Inc.*,[28] that a copyright owner cannot exercise any control over a copyrighted work after its first sale, even if that first sale occurs abroad. Moreover, reliance on an insubstantial element of a product protected by copyright to attempt to block parallel imports may be held to be copyright misuse, which blocks enforcement of the copyright.[29]

4. Restrictions on sales of competing products

In the absence of market power, a supplier generally is free to restrict a distributor's sales of competing products,[30] although some state laws limit this ability.[31] Restrictions that extend beyond the term of a distribution agreement are disfavored in some states, and restrictions on competing products generally must be "ancillary" to the contract and in furtherance of its lawful purposes,[32] as well as reasonable as to the products restricted, geographic scope and duration.[33] Where a supplier provides a turnkey operation, as in a classic franchise, such post-term restrictions may be more broadly permitted, particularly if they are short in duration and restrict a limited geographic area.[34]

However, where exclusive dealing requirements are so broad as to foreclose a substantial portion of the market, they may be found unlawful.[35]

Endnotes

1. "Vertical" refers to relationships between buyers and sellers, and "vertical restraints" are those agreed on by suppliers and their customers. In contrast, "horizontal" relationships are those between competitors at the same level of distribution, and "horizontal restraints" are those agreed upon by competitors. Horizontal conduct and its legal implications are beyond the scope of this article.
2. Under the rule of reason, the court weighs the anticompetitive effects of a restraint (often on intrabrand competition between resellers of the supplier's brand) against the procompetitive effects (often on interbrand competition between the supplier's brand and those of competing suppliers), and if the latter outweigh the former, the restraint will be found lawful. *See Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1977); *Graphic Products Distributors Inc. v. Itek Corporation*, 717 F.2d 1560 (11th Cir. 1983). In contrast, restraints that are *per se* unlawful will be found illegal regardless of the procompetitive justifications that may be offered in their defense. *See, e.g., United States v. Socony-Vacuum Oil Co.,* 310 U.S. 150 (1940).
3. 551 U.S. 877 (2007).
4. *Id.* at 892.
5. *Id.* at 893.
6. *Id.*
7. *Id.*
8. *Id.* at 897.
9. *Id.* at 897-98.
10. *Id.* at 898. ("If a retailer lacks market power, manufactures likely can sell their goods through rival retailers…[a]nd if a manufacturer lacks market power, there is less likelihood it can use the practice to keep competitors away from distribution outlets.")
11. *See* Duncan and Guernsey, *Waiting for the Other Shoe to Drop: Will State Courts Follow "Leegin"?*, 27 FRANCHISE L.J. 173, 174 (Winter 2008), *available at* http://www2.mnbar.org/sections/antitrust/Duncan-Guernsey.pdf; Lindsay, *Resale Price Maintenance and the World After "Leegin,"* 22 ANTITRUST 32 (No. 1, Fall 2007) (ABA), *available at* http://www.dorsey.com/files/upload/antitrust_lindsay_fall07.pdf. Examples of state statutes prohibiting RPM include California (Cal. Bus. & Prof. Code § 16720(e)), Kansas (Kan. Stat. Ann. § 50-112), Maryland (Md Code Ann., Com. Law § 11-204(b)), and New York (N.Y. Gen Bus. Law § 369-a).

12. *State of New York et al. v. Herman Miller, Inc.*, No. 08-CV-02977 (S.D.N.Y. 21 March 2008).

13. *FTC Approves Resale Price Maintenance Agreements under Rule of Reason But State AGs Appear Undeterred*, Morgan Lewis antitrust lawflash (14 May 2008). *See also* New York State Attorney General, Antitrust Bureau Feature release, *available at* http://www.oag.state.ny.us/bureaus/antitrust/feature.html.

14. Other examples: In March 2010, the New York Attorney General filed a state court action against Tempur-Pedic, a memory-foam mattress supplier, under a state law making resale price agreements unenforceable. *New York v. Tempur-Pedic Int'l, Inc.*, No. 400837/10 (Sup.Ct. N.Y. Co. filed 29 Mar. 2010). In February 2010 the California Attorney General filed a complaint and stipulated final judgment against DermaQuest, Inc., alleging an RPM agreement to constitute a *per se* violation of state antitrust and unfair competition law. *California v. DermaQuest, Inc.*, Case No. RG10497526 (Super. Ct. Calif. Alameda Co., Complaint filed 5 Feb. 2010, Proposed Final Judgment including Permanent Injunction filed 23 Feb. 2010). DermaQuest agreed to notify all its customers with whom it had RPM agreements disavowing those agreements, and not to enter RPM agreements in the future. It also paid $120,000 in civil penalties and attorneys' fees.

15. In addition to the New York and California cases discussed above, for example, the Kansas Supreme Court held in 2012 that Leegin's vertical price fixing was *per se* illegal. *O'Brien v. Leegin Creative Products, Inc.*, 2012 WL 1563976 (Kan. Sup. Ct. 4 May 2012), but the Kansas legislature is considering legislation to overturn that decision. Maryland passed a statute in response to *Leegin* making minimum resale price maintenance unlawful. Md Code Ann., Com. Law §11-204(b). Other states have followed *Leegin. See, e.g., Van Hoose v. Gravois*, 70 So. 3d 1017, 1023 (La. Ct. App. 2011). For a table listing the state of affairs in each State, see Lindsay, *Overview of State RPM*, 12 Antitrust Source (No. 4, April 2013) (http://www.americanbar.org/content/dam/aba/publishing/antitrust_source/apr13_lindsay_chart.authcheckdam.pdf).

16. While the focus of this article is on compliance with U.S. law, it is worth noting that the rules of other jurisdictions vary widely, and are developing. A 2012 Chinese court decision is in substantial accord with *Leegin. Johnson & Johnson*, Shanghai no.1 People's Court, *reported in Chinese Legal Daily*, 18 May 2012, as discussed in *Resale Price Maintenance – are China and America singing the same tune?*, *available at* www.Lexology.com/library/detail.aspx?g=0eec010b-38ba-47cb-800c-f7ed76553d59. Similarly, Canada repealed its *per se* rule against resale price maintenance in 2009, when it drastically overhauled its Competition Act, R.S.C. 1985, c.C-34. RPM has effectively been decriminalized, subject only to injunctive relief, not damages, and is presumptively legal unless challenged and shown to have an adverse effect on competition. Even then, several statutory affirmative defenses are available. There have been no private challenges to, or enforcement proceedings against, resale price maintenance since the new regime was adopted.

    In contrast, Europe still treats resale price maintenance as a "hard core restriction," except in certain narrow circumstances. European Commission Guidelines on Vertical Restraints, OJ 2010 C130/1 ¶223 (April 2010).

17. 250 U.S. 300, 307 (1919).

18. *United States v. Parke, Davis & Co.*, 362 U.S. 29, 45-46 (1960).

19. *In the Matter of Sony Music Entertainment, Inc.*, (FTC) File No. 971-0070 (10 May 2000), involved charges by the Federal Trade Commission that MAP programs were unlawful under the rule of reason. Five leading U.S. music companies each settled the FTC's charges that the defendants tried to eliminate discounting by conditioning cooperative advertising payments on advertising of CD prices at or above the supplier's MAP price – not only for broadcast and print advertising, but also for signs inside retail stores, and included advertising funded entirely by the retailer and not part of the co-op program.

20. 433 U.S. 36 (1977).

21. *See CDC Tech., Inc. v. IDEXX Labs, Inc.*, 186 F.3d 74, 80-81 (2d Cir. 1999) (unlike horizontal agreements between competitors, vertical exclusive distributorships are presumptively legal).

22. *See International Logistics Group, Ltd. v. Chrysler Corporation,* 884 F.2d 904 (6th Cir. 1989), *cert. denied*, 494 U.S. 1066 (1990) (summary judgment for defendant who terminated distributor who bought for export and then sold to domestic dealers); *Bruce Drug, Inc. v. Hollister Inc.*, 688 F.2d 853, 859-860 (1st Cir. 1982) (manufacturer's termination of transshipping dealer was justified where reasons included "controlling the distribution of its products in foreign markets" where a variety of factors had "the overall effect of promoting vigorous interbrand competition.").

23. *Matrix Essentials, Inc. v. Emporium Drug Mart, Inc.,* 1993-1 Trade Cas. (CCH) ¶ 70,196 (5th Cir. 1993) (upholding requirement that distributor sell only to hair-styling salons, not to retail stores; *Tripoli Co., Inc. v. Wella Corp.,* 425 F.2d 932, 936 (3d Cir. 1970) (upholding restriction on distributors reselling product intended for professional use to retail end users).

24. 822 F.2d 656, 666 (7th Cir.), *cert. denied*, 484 U.S. 977 (1987).

25. *H.L. Hayden Co. of New York, Inc. v. Siemens Med. Sys., Inc.*, 879 F.2d 1005, 1014 (2d Cir. 1989); *National Marine Elec. Distribs., Inc. v. Raytheon Co.*, 778 F.2d 190 (4th Cir. 1985); *O.S.C. Corp. v. Apple Computer, Inc.*, 792 F.2d 1464, 1468 (9th Cir. 1986).

26. 19 U.S.C. § 1526.

27. *See, e.g., Original Appalachian Artworks, Inc. v. Granada Electronics, Inc.*, 816 F.2d 68 (2d Cir. 1987); *Dial Corp. v. Manghnani Inv. Corp.*, 659 F. Supp. 1230 (D.Conn. 1987).

28. 133 S. Ct. 1351 (2013).

29. *Costco Wholesale Corp. v. Omega S.A.*, 2011 U.S. Dist. LEXIS 155893 (E.D. Cal. 9 Nov. 2011).

30. *See, e.g., Roland Machinery Co. v. Dresser Industries, Inc.,* 749 F.2d 380, 395 (7th Cir. 1984) (restriction on competing products eliminates divided loyalties and free riding); *In re Super Premium Ice Cream Distribution Antitrust Litigation,* 691 F.Supp. 1262 (N.D. Cal. 1988) (exclusive dealing prevents free riding, promotes distributor commitment), *aff'd sub nom. Häagen-Dazs Co., Inc. v. Double Rainbow Gourmet Ice Cream, Inc.*, 895 F.2d 1417 (9th Cir. 1990); *Joyce Beverages, Inc. v. Royal Crown Cola Co.,* 555 F. Supp. 271, 276 (S.D.N.Y. 1983) (restriction on competing products encourages distributor loyalty, incentive to make supplier's brand succeed).

31. *See, e.g., Cottman Transmission Sys., Inc. v. Melody*, 851 F. Supp. 660 (E.D.Pa. 1994) (Calif. law); *Scott v. Snelling and Snelling, Inc.*, 732 F. Supp. 1034 (N.D. Cal. 1990).

32. *See United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 282 (6th Cir. 1898), *modified and aff'd*, 175 U.S. 211 (1899) ("[N]o conventional restraint of trade can be enforced unless the covenant embodying it is merely ancillary to the main purpose of a lawful contract, and necessary to protect the covenantee in the enjoyment of the legitimate fruits of the contract, or to protect him from the dangers of an unjust use of those fruits by the other party").

33. A case in New York held that a one-year non-compete clause was unreasonable in duration as applied to an editor for a technology information publication, because of the speed at which the Internet industry moves. In that context, the court held, one year is "several generations, if not an eternity." *Earth Web, Inc. v. Schlack*, 71 F. Supp. 2d 299, 316 (S.D.N.Y. 1999).

34. *See*, *e.g.*, *Wilkinson v. Manpower, Inc.*, 531 F.2d 712 (5th Cir. 1976) (in a six-county area; for two years); *Meineke Discount Muffler Shops, Inc. v. Bleier*, Civ. Act. No. H-80-2495 (S.D. Tex. 1981) (twenty-five-mile radius of former shop; for one year); *Shakie's, Inc. v. White*, No. 77-106, slip op. (E.D. Mo. 1977) (within thirty miles of the franchised location; for one year); *Snelling & Snelling, Inc. v. Dupay Enters., Inc.*, 125 Ariz. 362, 609 P.2d 1063 (1980) (within thirty-five miles of franchised location; for three years).

35. *Standard Oil Co. v. United States*, 337 U.S. 293 (1949) (foreclosure of 6.7% of market was presumptively unlawful where competitors also used exclusive dealing); *United States v. Dentsply Int'l Inc.*, 399 F.3d 181 (3d Cir. 2005) (foreclosed competitors from the most important distributors); *Interface Group v. Mass. Port Authority*, 816 F.2d 9, 11 (1st Cir. 1987) ("Exclusive dealing arrangements may sometimes be found unreasonable under the antitrust laws because they may place enough outlets, or sources of supply, in the hands of a single firm (or small group of firms) to make it difficult for a new, potentially competing firms to penetrate the market."); *Twin City Sportservice, Inc. v. Charles O. Finley & Co.*, 676 F.2d 1291 (9th Cir.), *cert. denied*, 459 U.S. 1009 (1982) (long-term foreclosure of 24% of market was unlawful). *But see Jefferson Parish Hospital District No. 2 v. Hyde*, 466 U.S. 2, 45 (1984) ("Exclusive dealing is an unreasonable restraint on trade only when a significant fraction of buyers or sellers are frozen out of a market by the exclusive deal." An exclusive arrangement with a hospital with a 30% market share was upheld.) (O'Connor, J. concurring), *overruled on other grounds* by *Illinois Tool Works Inc. v. Independent Ink, Inc.*, 547 U.S. 28 (2006); *Satellite Television & Associated Resources, Inc. v. Contractual Cablevision, Inc.*, 714 F.2d 351 (4th Cir. 1983), *cert. denied*, 465 U.S. 1027 (1984) (foreclosure of 8% of households lawful); *Beltone Electronics Corp.*, 100 F.T.C. 68 (1982) (upholding exclusive dealing arrangements covering 16% of the hearing aid market pursuant to a rule of reason analysis); *Sewell Plastics, Inc. v. The Coca-Cola Co.*, 720 F. Supp. 1196 (W.D.N.C. 1989) (exclusive contracts foreclosed for 40% of the market, there was still adequate competition, so no "undue" foreclosure of market was found).

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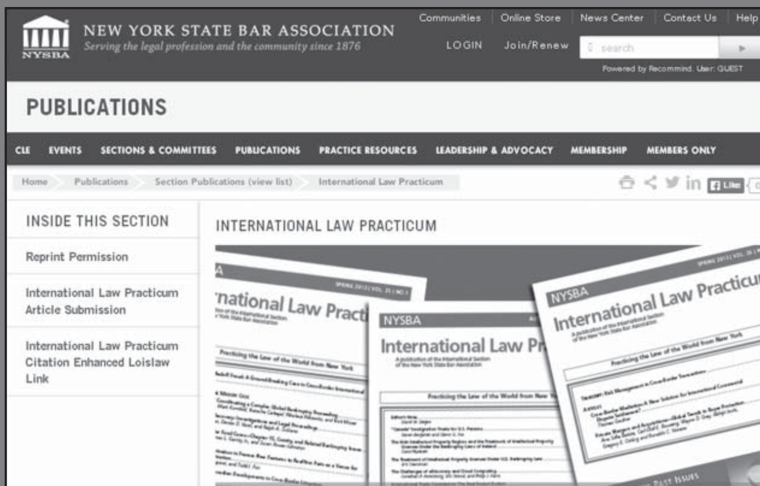

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NEW YORK STATE BAR ASSOCIATION

Snapshot of Competition Laws in ASEAN and China

By Franz Hepp de Sevelinges

I. The ASEAN Approach to Competition Law Harmonization

A. Generally

The Association of Southeast Asian Nations (ASEAN) was established on 8 August 1967 under the ASEAN declaration in order to promote social and economic development through the cooperation of the Southeast Asian countries.[1] In addition, the ASEAN member states agreed to the "Initiative for ASEAN Integration" (IAI) in 2000 as an important step toward narrowing unequal development, with the objectives of relieving the development gap and accelerating the economic integration of the newer members of ASEAN, namely, Cambodia, Lao PDR, Myanmar, and Vietnam. In 2007, the member states mutually agreed to the Declaration on the ASEAN Economic Community Blueprint, setting out a solid time frame for all ASEAN members to jointly complete integration of an ASEAN economic community by 2015. The Blueprint urges the member countries to develop competition law and policy to promote business competition and enhance the liberalization and integration of the ASEAN economy. This was followed by the adoption of the ASEAN Competition Policy Guidelines, which promote using competition law and policy to construct a competitive ASEAN economic liberalization and integration.[2]

By the action plans in the Blueprint, the ASEAN leaders agreed to set up the ASEAN Experts Group on Competition (AEGC) as a regional forum facilitating exchange of information, experience, and cooperation on competition policy in the region.

In the past decades many member countries of ASEAN have liberalized and deregulated their economies and privatized state assets to create a competitive market economy potentially attracting foreign investors. Singapore is an example of an economy that has created the conditions to attract international investments by liberalizing and deregulating its economy well ahead of other ASEAN neighbors. It has been followed by Malaysia, Thailand, Indonesia and the Philippines, and more recently by Vietnam with its Doi Moi economic renovation program initiated in 1988. The other countries, with the exception of Brunei, are poor economies and late starters in the economic development process. Brunei is one of the richest countries in the world, but has not developed a formal market economy because of the abundance of petroleum dollars. Although Laos had initiated reforms by introducing the New Economic Mechanism in 1986, it remains one of the poorest countries in the world. Cambodia and Myanmar have begun economic reconstruction as a result of coming out of war and isolation, respectively.

However, even though some members have a full systematic set of competition laws that regulates all types of anticompetitive conduct, the members' governments often only loosely enforce the laws. An important point to note is that, while the broad principles of competition law across jurisdictions may be similar, competition law is not identical across all ASEAN countries. Differences exist in terms of coverage, interpretation and enforcement of the law, reflecting the varying political and socio-economic climates and goals of the respective ASEAN member countries. These differences in nuances may mean that an activity which does not amount to a violation in one country could possibly violate the competition law of another country.[3] More time may be needed for ASEAN to have a systematic harmonization of competition law, since in order to have a "strong" competition law at a regional level, the member countries need strong domestic enforcement first.[4]

It is anticipated that the lack of a main institution which plays a role in developing competition law and policy in ASEAN will create an ineffective development of competition law and policy in ASEAN. Since the ASEAN Experts Group on Competition (AEGC) is just a consultative forum, it may well not play the role of a main institution enforcing competition rules and investigating the anticompetitive restriction and conducts across ASEAN.[5] This is different from the European Commission, which has the power to enforce regional competition rules and the power to stimulate regional movement to open market competition. The lack of a main competition agency in ASEAN is highlighted when anticompetitive restrictions and anticipated conduct are on a cross-border basis, since the purely consultative forum and domestic competition agencies would have only limited power to deal with such regional anticompetitive conduct.[6]

The AEGC and the guidelines do not address anticompetitive restrictions and conduct by state enterprises of ASEAN members, ignoring that state enterprises are main economic players which have state support and have a potential to restrict market access in the ASEAN region.[7] The failure to address issues related to state monopoly enterprises in ASEAN of course creates difficulties in building market competition and could be an impediment to constructing ASEAN economic liberalization and integration.[8]

B. Status Quo of Competition Laws in ASEAN

There are comprehensive competition laws and competition authorities in place in Indonesia, Singapore, Thailand and Vietnam. Malaysia's competition law and competition authority have started operating in 2012. Bru-

nei Darussalam, Cambodia, Lao PDR and Myanmar are currently drafting competition laws. The Philippines established a competition authority to begin implementing competition-related laws using a sectorial approach: A draft competition law establishing an Office for Competition is before the legislature.

1. Malaysia

The Malaysian Competition Act was passed by the Malaysian Parliament in April 2010 and came into force in January 2012. It prohibits anti-competitive activities and abuses of dominance, but it does not regulate mergers and acquisitions. It applies to any commercial activity—both activity within Malaysia and activity outside Malaysia that has an effect on competition in any market in Malaysia. However, commercial activity regulated under the Communications and Multimedia Act 1998 and the Energy Commission Act 2001 are not subject to the Malaysian Competition Act.

2. Thailand

The Trade Competition Act 1999 (Thai Competition Act) is the principal legislation that governs anti-competitive agreements, abuse of dominance, mergers and other unfair trade practices in Thailand. The Thai Competition Act co-exists with several sectorial laws that regulate competition in certain industries. The Trade Competition Commission (TCC), which is a part of the Ministry of Commerce, is the main regulator responsible for enforcing the Thai Competition Act. The TCC and the sectorial regulatory authorities may have concurrent or overlapping powers regarding anti-competitive conduct, mergers and monopolies. The relevant statutes or regulations are not always clear as to which authority will be the enforcing authority in the case of an overlap.

The Thai Competition Act is explicit on prohibiting vertical agreements that result in a monopoly. Such vertical agreements are prohibited and are declared *per se* illegal by Section 26 of the Thai Competition Act. Section 27 of the Act also prohibits vertical mergers that fix geographical areas in which each business operator may distribute or restrict the distribution of goods or services, or fix customers to whom each business operator may sell goods or provide services to the exclusion of other business operators from competing in the distribution of such goods or services or appointing or entrusting any person as a sole distributor of the same goods or services. Also prohibited are vertical agreements among upstream and downstream enterprises, such as agreements between vendors, manufacturers and retailers, and resale price maintenance agreements.[9]

Section 30 of the Thai Competition Act defines a dominant position as an enterprise with a market share of more than seventy-five percent and empowers the TCC to direct the enterprise with a dominant position to suspend, cease or vary its market share.

3. Vietnam

The Law on Competition (Vietnam Competition Act), which came into force in July 2005, is the main legislation that governs competition law in Vietnam. The two agencies in charge of regulating competition are the Vietnam Competition Administration Department (VCAD), which falls under the Ministry of Industry and Trade, and the Vietnam Competition Council (VCC). The Vietnam Competition Act co-exists with a number of sectorial laws that regulate competition in certain industries. Thus, in addition to the VCC and VCAD, the designated sectorial regulators also have concurrent jurisdiction in regulating certain sectors.

The Competition Act does not explicitly refer to vertical agreements, but states that all anti-competitive agreements are automatically null and void or illegal *per se*. These include tying, exclusive dealing, and/or territorial restraints. However, exemptions can be obtained for the development of scientific research, increasing production and distribution efficiency, increasing capacity of small and medium enterprises, increasing the international competitiveness of domestic firms, and increasing the quality of goods and services.[10]

Restrictive agreements are categorized into two categories: (1) those which are prohibited in all cases (Category 1 Agreements); and (2) those which are prohibited if the parties have a combined market share of thirty percent or more (Category 2 Agreements). Category 1 Agreements are those preventing or excluding other enterprises from participating in the market, or collusion in order for one or more parties to win a tender for the supply of goods and services.

Category 2 Agreements are price-fixing agreements, sharing of customer markets or sources of supply of goods, restraining or controlling the quantity or volume or goods produced, purchased or sold, agreements restraining technical or technological developments, and agreements imposing other enterprises conditions which are not related in a direct way with the subject matter of the contract.

It is important to note that there are no exemptions for Category 1 Agreements. In regard to Category 2 Agreements, an exception can be sought for a definite period of time if the agreement can be shown to fulfill certain criteria (e.g., rationalizes an organizational structure, increases business efficiency, promotes technical progress or improves the quality of goods etc.). The following conducts are prohibited if an enterprise holds a dominant position: selling goods by providing services below total prime costs of the goods aimed at excluding competitors; fixing an unreasonable selling or purchasing price or fixing a minimum re-selling price for goods or services, thereby causing loss to customers; restraining production or distribution of goods and services that limits the market or impedes it.[11]

In Vietnam dominance has been defined. Article 12 of the Competition Act of Vietnam states that "an enterprise or a group of enterprises acting together which have a market share in the relevant market above 50% shall be considered as having a dominant position in the market."

4. Indonesia

Law No. 5 of 1999 on the Prohibition of Monopoly and Unfair Business Competition Practices (Indonesian Competition Act) entered into force in 2000. The national competition agency known as Komisi Pengawas Persaingan Usaha (KPPU) regulates competition law in Indonesia. The Indonesian Competition Act applies to any individual or entity engaging in business or commercial activities.

The Competition Act prohibits price-fixing agreements between competing business actors and agreements for price discrimination without qualification. Competing business actors are prohibited from agreeing to fix prices below the market prices if the agreement may cause unfair competition. Likewise, minimum resale price maintenance is prohibited if it may cause unfair competition.

Competing business actors are prohibited from agreeing to allocate territories or customers for products if this agreement may cause monopolistic practices and/or unfair competition. This includes vertical and horizontal allocations.

In Indonesia, according to Article 25 of the Competition Act, an entrepreneur is said to be in a dominant position if it owns fifty percent or more of the market share of one type of certain goods or services. Alternatively a group of entrepreneurs are said to be in a dominant position if they own seventy-five percent or more of the market share.

5. Singapore

The Competition Act (Singapore Competition Act) is the main legislation that regulates competition law in Singapore. The Act prohibits anticompetitive agreements, decisions and practices, the abuse of dominant position, and mergers and acquisitions that substantially lessen competition. The Competition Commission of Singapore (CCS) is the main competition law regulator in Singapore and is a statutory board under the Ministry of Trade and Industry. The CCS has also released thirteen sets of guidelines, which provide useful explanations as to how the CCS interprets, administers and enforces the Singapore Competition Act. It is useful to note that, although the CCS is the only regulator which administers and enforces the Singapore Competition Act, sectorial laws are administered and enforced by sectorial regulators.

In the case of Singapore, there are no market share thresholds for defining dominance under the Singapore Competition Act. This is because the Singapore Competition Commission is of the view that high market share alone might not be a reliable guide to market power. According to the CCS "high market shares are…not necessarily an indication that competition in the market is not effective."[12] Although holding a dominant position is not illegal *per se*, Section 47 of the Singapore Competition Act empowers the Competition Commission to hear cases of abuses of dominant position. This is unlike the German model, which singles out dominant firms for special treatment, and does not allow them any exemptions from abuse of dominant position.

6. Cambodia

There is no generic competition law in force in Cambodia. The telecommunications sector and the banking industry are regulated by the National Information Communications Technology Development Authority and the National Bank of Cambodia, respectively.

7. Lao PDR

Lao PDR does not have a generic competition law, but competition is regulated by Decree 15/PMO on Trade Competition (Lao Decree). The Lao Decree generally applies to the sale of goods and services in business activities by business persons or business entities. It is important to note that the Lao Decree does not make a distinction between national and foreign business persons.

The Lao Decree prohibits specific restrictive business practices such as mergers and acquisition leading to monopolization, elimination of other business entities, collusions and arrangements, and cartels with foreign business persons. The Trade Competition Commission (TCC) within the Ministry of Industry and Commerce is to be responsible for the enforcement of competition law. However, the TCC has not yet been established.

8. Myanmar

There is no generic competition law in Myanmar.

9. Philippines

The Philippines does not have a generic competition law. However, the main sources of competition-related provisions in the Philippines are: (i) article XII of the 1987 Constitution; (ii) article 186 of the Revised Penal Code (Act No. 3815); (iii) article 28 of the New Civil Code (R.A. No 386); and (iv) the Act to Prohibit Monopolies and Combinations in Restraint of Trade (Act No 3247).

Since competition law is currently implemented at the sectorial level, enforcement of competition law/statutes is vested with different government agencies. Some of the enforcement agencies are industry-specific.

10. Brunei Darussalam

Brunei Darussalam does not have generic legislation regulating competition, law but it does implement competition policy on a sectorial basis. Thus, competi-

tion-related provisions have been implemented in the telecommunications sector under the Authority for Info-communications Technology Industry of Brunei Darussalam Order 2001 (the AITI Order) and the Telecommunications Order 2001. Both the AITI Order and the Telecommunications Order apply to all commercial entities that have obtained a license to operate as a service or infrastructure provider in the telecommunications industry.

II. China: Competition Rules for Distribution

A. The PRC Anti-Monopoly Law

After thirteen years of drafting and deliberation, the PRC Anti-Monopoly Law ("AML") was adopted on 30 August 2007 amid the country's continued economic reforms and the transformation from a planned economy into one that is market based. The AML is an attempt to codify the then-existing body of competition-related laws and regulations, which had been promulgated piece by piece over the years. It applies throughout the PRC with the exception of the two Special Administrative Regions of Hong Kong and Macau.[13] The AML is largely modeled on the competition law of the European Union. Its enforcement authorities frequently look to EU competition law to compare the approach taken by the European Commission and are clearly influenced by EU precedents. The AML includes prohibitions on monopoly agreements and abuse of dominant market position, as well as merger control notifications and review procedures.

In addition to the AML itself, implementing rules and published guidelines play a crucial role in the application of the AML.

In the AML's first four years, enforcement actions were mainly focused on merger notifications.[14] China has a merger notification regime similar to that utilized in the European Union and the U.S. With the concept of fair competition winning more support in the administration and the general public, and with the competition agencies and Chinese courts enhancing their competition-review capacities, an increasing number of high profile cases alleging cartels and vertical anti-competitive agreements have emerged in recent months.

A breach of the AML can result in fine of up to ten percent of a company`s annual revenues, confiscation of illegal gains, and private damage actions in the courts.[15]

It is important to note that, contrary to other jurisdictions, restrictions on pricing, resale price maintenance, exclusive supply arrangements, retailer fees are controlled, to a greater or lesser extent, by other laws as well: Contract Law of the PRC (1999); Anti-Unfair-Competition Law (1993); Price Law (1998); and the Criminal Law (1997).

B. Enforcement Structure

The AML introduced two new regulatory agencies: (i) The Anti-Monopoly Committee under the State Council, which is responsible for developing competition policy, conducting market investigations, publishing guidelines, and coordinating the competition administrative enforcement work; and (ii) the Anti-Monopoly Enforcement Authority designated by the State Council ("AMEA"), which is responsible for the enforcement of the AML. The enforcement powers of AMEA are divided between three agencies: National Development and Reform Commission ("NDRC") and the State Administration for Industry and Commerce ("SAIC") (which enforce the price and non-price-related rules of the AML, respectively) and the Ministry of Commerce ("MOFCOM") (which enforces the merger control regime).

C. Anti-Competitive Agreements

Monopoly Agreements are defined in Article 13 AML as agreements, decisions or other concerted behavior that eliminate or restrict competition. Articles 13 and 14 provide a list of monopoly agreements between competing undertakings that are automatically presumed to be illegal, such as price-fixing agreements or arrangements limiting production or sales volumes, dividing sales or procurement markets, restricting the purchase of new technology or new products, or involving resale price maintenance.

As with the EU and U.S. regimes, exception from the prohibition is available: Article 15 AML allows undertakings to rebut the anti-competitive presumption. In order to benefit from the exemption, the undertakings must show all of the following:

> The agreement in fact had a qualifying purpose, such as to upgrade technology or research and development, improve product quality, reduce costs, improve efficiency, enhance competitiveness of small and medium sized enterprises, or maintain public welfare or to be for the purpose of international trade and foreign economic cooperation.
>
> The agreement will not substantially restrict competition in the relevant market. Consumers will receive a fair share of the resulting benefits.

D. Enforcement Actions

To date, most of the enforcement actions have been carried out at the local level. The SAIC and NDRC have delegated their enforcement powers to their local departments (the "local AIC" and the "local price authority," respectively) to carry out investigations of anti-competitive conduct. These investigations are often concluded with the relevant undertaking offering to take corrective mea-

sures (without imposing a fine), and may not be reported by the press.

E. Specific Competition Rules in China

1. Resale Price Maintenance

Resale Price Maintenance (RPM) occurs when sellers restrict prices at which buyers may resell products to downstream customers. RPM restrains intra-brand competition among rival distributors of the same brand, and can weaken inter-brand competition by stabilizing prices within a multi-brand market. While RPM is illegal *per se* under antitrust rules in many jurisdictions, the lawfulness of RPM in other jurisdictions depends on the actual anti-competitive and pro-competitive effects in each specific case. Article 14 AML expressly bars business operators from "entering into the following monopoly agreements with their trading partners: (1) fixing the price of commodities for resale to third parties…" However, it is not clear whether the AML views RPM as hardcore or *per se* violations, since the AML provides a set of exemptions for RPM.[16] Exemption examples include technological improvement, research and development, efficiency enhancement, and public interest. Given these exemptions, it is likely that China will view RPM in a manner similar to that of the United States by applying a U.S.-style benefits-and-harm test (the U.S. "Rule of Reason").

In recent months, there have been a number of high profile enforcement actions against RPM in China. Despite this increased level of enforcement activity, the position of RPM under China's AML is uncertain.

(a) *Rainbow v. Johnson & Johnson Medical*

Johnson & Johnson Medical (China) Ltd (J&J) was sued by its former distributor, Beijing Ruibang Yonghe Technology and Co., Ltd. ("Rainbow"), alleging resale price restrictions on J&J sutures distributed by Rainbow. The issue in dispute is whether J&J set a minimum resale price in the distribution contract with Rainbow. Rainbow had been a business partner with J&J for fifteen years as its distributor of staplers and suturing products. According to the distribution contract, J&J authorized Rainbow to sell its product to hospitals in specific districts in Beijing with a minimum resale price. However, J&J discovered that Rainbow acquired distributorship in an unauthorized district by bidding at a price that was below the minimum resale price set by J&J. Consequently, J&J withheld Rainbow's deposit, terminated its distributorship in several hospitals and eventually terminated supply entirely. In 2010, Rainbow filed a lawsuit against J&J in Shanghai No. 1 Intermediate People's Court ("Shanghai No. 1 Intermediate Court"). Rainbow alleged that J&J conducted RPM, which breached Article 14(2) of the AML and asked to be compensated for its losses of RMB 14.4 million. On 18 May 2012, Shanghai No. 1 Intermediate Court ruled against Rainbow, finding that the plaintiff failed to prove that the RPM agreement had restrained or excluded competition. On 1 August 2013, Shanghai Higher Court, which went through three hearings (the first hearing in public, while the other two in private), made a final judgment, reversing the judgment of the lower court. The Shanghai Higher Court ordered J&J, the appellee, to compensate Rainbow for the appellant's losses of RMB 530,000 within ten days after the judgment became effective. Other charges against J&J were dismissed. The Shanghai Higher Court was of the view that, to find a horizontal agreement under Article 13 of the AML as a monopolistic agreement, a precondition is that the agreement shall have the effect of eliminating or restricting competition. Generally speaking, compared to vertical monopolistic agreement, the anti-competitive effect of a horizontal monopolistic agreement is much more significant, since it eliminates or restricts competition directly. Since elimination or restriction of competition is a necessary element even for horizontal agreements (which are more harmful), to prove a vertical monopolistic agreement, the effect of elimination or restriction of competition must also be proved.

(b) *Moutai and Wuliangye*

Two Chinese premium liquor distillers (Moutai and Wuliangye) were investigated by China's antitrust regulator in 2012 and 2013, respectively, shortly after they penalized some of their distributors for selling under their minimum retail price. Upon investigation, both companies announced that they had withdrawn the penalties and would reorganize their sales practices to comply with the AML. In February 2013, two provincial competition regulators (in the province where the manufacturers were located) issued fines of ¥247 million (approx. €31 million) and ¥220 million (approx. €28 million), figures that represented one percent of their annual sales of the products in question. In one of the announcements, the regulator stated that the RPM restricted or eliminated competition. Because the regulator issued such fines with a finding that the RPM restricted or eliminated competition, this suggests a reluctance to consider RPM to be an automatic violation, or one that need not include a determination that competition was distorted, restricted or eliminated.

(c) Other cases and legislation

According to 2012 media reports, Daimler's China joint venture, Beijing Benz, was investigated by China's competition regulator for imposing minimum resale price requirements on its dealers. Daimler's policy on resale pricing is said to have included a "price management and increase project" as well as a "regional sales management strategy." Price restrictions included standardizing price quotations provided in relation to telephone inquiries, prohibiting discount advertising and imposing minimum retail prices. In particular, Beijing Benz restricted the retail price of eleven models of Mercedes Benz C and E class sedans in March 2011. The dealers were also allegedly

forbidden to advertise or to sell directly or indirectly outside their appointed territory.

Although no official announcement was made on this investigation, a series of news media reports indicated that the automaker revised its dealership contracts and structurally reformed its Chinese distribution practices by eliminating the retail pricing restrictions.

According to sources, China has been forming an expert group to draft guidelines on vertical agreements and available exemptions and defenses. These guidelines may provide more clarity on how China will evaluate the legality of RPM. However, before such guidelines become available, Chinese regulators and courts will continue to assess allegations of RPM on a case-by-case basis.

2. Alternative Pricing Constraints

Suggested pricing is in compliance with the AML—so long as it remains a suggestion. Article 14 of China's Price Law requires that undertakings must not "work collaboratively to control market prices to the detriment of the lawful rights of other undertakings or consumers." Consequently mandatory pricing violates the AML.

Minimum Advertised Price Policies are not regulated under PRC law, but seem permissible so long as they are not mandatory for the final price.

3. Exclusive Territories and Customer Allocation

China imposes restrictions on both dominant distributors in respect to exclusive distribution and dominant suppliers in respect of territorial restrictions: Unless there is an applicable justification, a dominant supplier is prohibited from imposing "unreasonable restrictions on the territory of the sales."[17] In some circumstances dominance is presumed to exist when an undertaking has a market share as low as ten percent. If a supplier is dominant, it is unclear in Chinese law or practice what comprises sufficient justification. In determining under the SAIC Regulations what comprises sufficient justification for a territorial restriction, SAIC is required to consider whether the practice is conducted on the basis of ordinary operating activities and ordinary interests, and how the territorial restriction will affect economic efficiency, public interests and development of the economy.[18] Unfortunately there is neither case law nor further guidance from the SAIC on this issue.

The same ambiguity exists in regard to customer restrictions: According to SAIC Regulation 54 a dominant supplier/distributor must not impose "additional unreasonable restrictions on…customers targeted." [19]

4. Restrictions on Active or Passive Selling Out of Assigned Territory

There is no distinction between active and passive selling out of the assigned territory in China and it is generally possible to restrict sales out of the assigned territory, unless it is imposed by a dominant supplier who "unreasonably restricts the territory of sales." In order to evaluate such "unreasonable" restriction, SAIC has to consider whether the practice of territorial restriction is conducted on the basis of ordinary operating activities.

5. Restrictions on Internet Sales

Restrictions on internet sales are treated like assigned territories and are so analyzed by SAIC as to whether it unreasonably restricts the territory of sales.

6. Restrictions on Parallel (Gray Market) Imports

Whether parallel importing of trademarked products constitutes a trademark infringement is not specifically addressed in the PRC laws and regulations. There are two prevailing opinions regarding parallel importing: Some scholars argue that such imports do not constitute trademark infringements, based on the "Exhaustion of Rights Doctrine," while others believe that evidence of trademark infringements can be established in parallel import based on the local nature of intellectual property rights.

Chinese case law does support a brand owner`s ability to rely on trademark law to stop parallel imports. In 1999 the Guangzhou Intermediate Court held that trademark rights were infringed when "Lux" soap was imported from Thailand into China without the brand owner`s consent.[20]

In the *Michelin* case (2009),[21] the Court held that goods could not be imported because they had not obtained the 3C certification[22] and, as a result, the importation constituted an infringement of plaintiff's registered trademark rights by causing a prejudice to Michelin. The plaintiff, the French Michelin Group, found in the Chinese market that defendant was selling its "MICHELIN" branded tires manufactured in Japan, but did not obtain China's 3C safety certification. The plaintiff claimed that tires, important parts of a vehicle, were directly related to personal safety, and different materials, designs, process and structure were applied to manufacturers of tires according to different regional environments and road conditions. These products did not go through China's 3C compulsory safety certification, so that safety risks existed. In the event that the plaintiff's trademark registered in China were used on these products, the plaintiff's interests and the trademark's reputation would be severely affected once problems arose. Thus, the defendant's acts infringed the plaintiff's exclusive right to use of its registered trademark.

Experts read the *Michelin* case to indicate that parallel importation could be permissible if an importer had obtained the 3C certifications. Importers of parallel goods may find it difficult to get certifications for parallel products, since authorities could be reluctant to issue such certifications to importers who are not in a position to

provide requisite information. This is how China often handles controversial IP issues: While the law in China might indicate that importation of parallel goods is permissible, a number of hurdles (both practical and policy based) may prevent the importation of parallel goods into China.

7. Restrictions on Sales of Competing Products

Unless there is a justification, a dominant distributor is prohibited from requiring a supplier not to deal with the distributor's competitors.[23] In the absence of such dominant position of the distributor such restrictions seem permissible.

Endnotes

1. ASEAN, Asean Overview (http://www.aseansec.org/about_ASEAN.html.
2. ASEAN Regional Guidelines on Competition Policy (ASEAN, 2010).
3. Phanomkwan Devahastin Na Ayudhaya, *ASEAN Harmonization of International Competition Law: What is the Most Efficient Option?*, in 2 Int'l J. Bus., Econ. and L. 2 (2013).
4. *Id.*
5. Wisuttisak and Binh, *ASEAN Competition Law and Policy: Toward Trade Liberalization and Regional Market Integration*, 2012 ICIDR at 15.
6. Sokol, *Monopolists without Borders: The Institutional Challenge of International Antitrust in a Global Gilded Age*, 4 Berkeley Bus. L.J. 37 (2007), *available at* http://scholarship.law.ufl.edu/facultypub/67.
7. Forsyth, King and Rodolfo, *Open Skys in ASEAN*, 12 J. Air Transport Management 143 (2006).
8. Wisuttisak and Binh, note 5 *supra*, 2012 ICIDR at 16.
9. Sivalingam, *Competition Policy and Law in ASEAN*, 51 Singapore Econ. Rev. 241 (2006).
10. *Id.*
11. Articles 8 and 9 of the Vietnam Law on Competition.
12. Competition Commission of Singapore, 2005:5.
13. Hong Kong is currently proposing to adopt cross-sector competition laws.
14. The widely reported prohibition of Coca-Cola's acquisition of Chinese fruit juice maker Huiyuan was a high profile example of such merger enforcement in 2009.
15. Art. 46-50 AML.
16. The exemption under Art. 15 of the AML applies to all types of horizontal and vertical agreements, not just to RPM restrictions.
17. Art. 5 (1) SAIC Regulations.
18. Art. 8 SAIC Regulation.
19. SAIC Regulation No. 54 - Regulations on Prohibiting the Abuse of a Dominant Market Position.
20. In this instance, the court held that evidence provided by the defendant was insufficient to prove that the goods it imported were licensed to be manufactured by the trademark owner; therefore, the court determined that the defendant had committed trademark infringement, but failed to touch upon the issue as to whether the parallel importation had constituted infringement.
21. *Michelin Group v. Tan Guoqiang and Ou Can,* ChangZhongMinSan ChuZi, Case No.0073 (2009).
22. "3C" is regulated under the Mandatory Certificating system in China. Tire products are included in the "Catalog for First Batch of Products subject to Mandatory Product Certification."
23. SAIC Order 54/2010, article 5 (3).

Admitted to the bars of Berlin (Germany) and Paris (France) the author focuses on the negotiation and documentation of corporate and commercial transactions, with a particular emphasis on cross-border mergers and acquisitions, domestic and international joint ventures, commercial contracts, intellectual property, real estate transactions and arbitration. He has advised numerous clients in the automotive, aviation, chemical, energy and retail sectors. He has significant personal international experience, having lived and worked for extended periods in Germany, France, the U.S., Hungary, Vietnam and China.

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Commentary: U.S.-China Trade Relations—Litigation in the WTO Since 2001

By Stuart S. Malawer

I. Introduction

The World Trade Organization (WTO) dispute resolution system is widely used and is a litigation-oriented process. It is at the core of global trade relations today. Both the United States and China have been aggressive users of the system. Each country has shown a willingness to address contentious issues, which has been to the benefit of both countries. As newer trade issues arise, this process will be indispensable in keeping U.S.-China trade relations on a stable course.

My approach is to examine litigation data provided by the WTO and the United States Trade Representative (USTR) concerning the WTO dispute resolution system's inception, the activity of the Bush and Obama administrations in regard to trade disputes, and China's record in the WTO. A series of charts with short explanatory passages helps illustrate this story.

This is not a jurisprudential study, but rather one assessing empirical litigation data in order to disclose implications for American trade policy and the international trade system as they relate to China's role in the global trading system.[1]

The conclusions are straightforward. The dispute resolution system is widely used by many developed and developing countries. The U.S. has been the most active in the WTO's dispute resolution system. The focus of the U.S. has increasingly been on China, and Chinese litigation has been primarily focused on the U.S. Further, the pace of WTO litigation among all countries has picked up.

This review of U.S.-China litigation is of the competitions that reflect trade flows and frictions, which are addressed successfully in a rules-based system rather than as a narrative of a deadly winner-take-all conflict. Such legal conflicts and their resolution are the way that the system was intended to work by its architects, principally the U.S.

My general conclusion is that, whereas the U.S. and China are competitors, they have channeled their major trade disputes into an international diplomatic and adjudicatory mechanism that demonstrates cooperation and management. This approach is beneficial to both parties politically and to U.S.-China trade relations and global governance.

II. Background

The WTO negotiates and adjudicates global trade rules. The dispute resolution system is at the heart of the WTO today; it is the judicial system of the WTO and of the global trading system.

The WTO and its dispute resolution system are the successor to the older, much weaker GATT system and came into existence in 1995. For the first time in history, there is now a multilateral system that resolves trade disputes with binding decisions enforceable by sanctions. There is nothing else like it in the international economic arena today.

The basis of the dispute resolution system is the WTO's "Dispute Settlement Understanding" (DSU), one of the multilateral agreements that came to force in 1995. It establishes compulsory jurisdiction, binding decisions, and trade sanctions to enforce those decisions. The dispute resolution system applies all the rules found in the whole range of WTO trade agreements relating to agriculture, intellectual property, subsidies, services, investment measures, and merchandise trade, among others.

The United States has filed various actions against China concerning what it considers improper export subsidies and failure to enforce intellectual property rights. On the other hand, China has filed actions against the United States for its imposition of antidumping duties and safeguard tariffs. A large number of trade cases before the WTO involve "trade remedy legislation" authorizing dumping, subsidies, and safeguard measures.[2] Indeed, the dumping and subsidies codes are the most litigated substantive agreements. The dispute resolution system is widely used by many states, but most WTO litigation involves that between the United States and the European Union (EU). However, the most politicized and high-profile litigation involves the United States and China.

The actual dispute resolution process combines traditional negotiations and litigation and is relatively simple and quick. From start to finish, this entire process generally takes twelve to fifteen months. States file a request for consultation that involves confidential diplomatic negotiations between the parties. If consultation does not result in a settlement, the complaining party may request the establishment of a panel to hear the case. This is where the litigation takes place. However, the majority of cases requesting consultation are resolved without ever going through the full litigation process.

Panel members are trade experts selected by the WTO and then chosen by the parties. The cases are decided by the panelists, not juries—a seeming adaptation of the civil-law approach to litigation. While precedent, a common-law notion, is not specifically provided for in the Dispute Resolution Understanding, it is in fact often utilized in panel and Appellate Body decisions. For a very long time, these proceedings were closed and did not allow amicus briefs, but this has now changed somewhat.

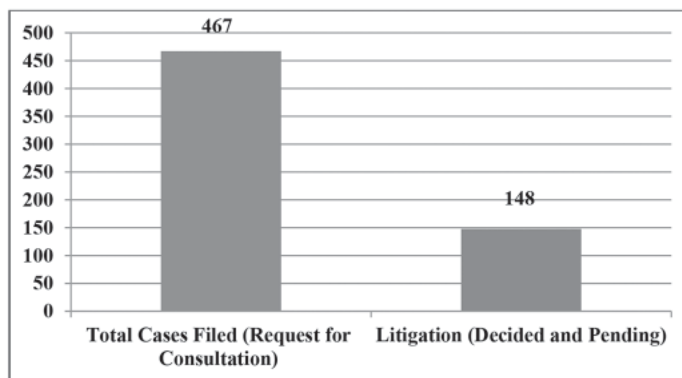
Parties may appeal the decision of the panel to the Appellate Body, which is composed of members selected by the WTO. Determinations by both the panel and Appellate Body are required to be adopted by the Dispute Settlement Body, essentially the entire membership of the WTO. In reality this adoption has proven to be automatic. When a decision is finalized, the losing party is required to bring its offending measure into compliance with the decision (technically, a recommendation), which allows it to formulate the specifics of the losing party's compliance to remove the offending restriction.

If there is a failure to comply after a reasonable time, the complaining party may request authorization to impose sanctions on the losing state. Most often, these sanctions are tariff surcharges on imports from the responding state until the offending measure is removed. Requests for sanctions have been very rare, and even when authorized, they have not always been imposed. Generally, states are no longer allowed to unilaterally impose trade sanctions on others unless authorized by the WTO. By and large, only multilateral trade sanctions as authorized by the WTO are lawful under global trade law today.

III. The WTO Dispute Resolution System

At the outset of any discussion of WTO litigation, it is important to note that only approximately one-third of cases filed go through the entire WTO litigation system. (It is a bit higher for cases involving the U.S.) The first stage in the litigation process is to file a request for consultation. This stage involves confidential diplomatic negotiations. Often, cases are dropped at this stage, even when there may not have been an agreement to remove contested restrictions. Only after negotiations are unsuccessful can the parties request for a panel to be formed. The chart below covers 1 January 1995 through 30 September 2013. Of the 467 cases filed (request for consultations), only 148 have led to litigation (some are still pending). Sanctions were authorized in only seven cases and sanctions were not actually implemented in any of them.

Chart 1. WTO Cases (Merits) Filed and Litigated from 1 January 1995–30 September 2013



Data Source: *2013 Annual Report of the DSB (1 Nov. 2013)—Overview of State of Play of WTO Cases by the Secretariat* is appended to the DSB Report WT/DSB/61/Add.1.

The WTO dispute resolution system has been widely utilized by both developed and developing countries. Developing countries have filed over one-third of the requests for consultation. For example, in 2012 Latin American countries alone filed nine of the twenty-seven requests for consultation.[3] A 2013 WTO report concluded that "developing countries participated strongly in the dispute settlement system, both as complainants and respondents."[4] A recent study sponsored by the WTO of litigation data observes, "The first conclusion that one can draw from the data is that these distinctions between common, code law and pluralism are not significant for explaining different members' level of litigiousness."[5]

A. The U.S. in the Dispute Resolution System

The U.S. has been extremely active in the WTO litigation process. In fact, it has been the most active member. The U.S. was brought before the WTO approximately fifty percent more often than it brought cases. As the complainant, it brought a total of ninety-nine cases. (This includes nine compliance cases that were brought after the original case in order to secure compliance.) It was a respondent in a total of one hundred forty cases. (This includes sixteen compliance cases.) Of the ninety original cases it brought, forty-two were fully litigated, resulting in thirty-eight wins and just four losses. Of the 124 original cases brought against the U.S., it lost fifty but won a relatively high number of seventeen. In total, the U.S. won just about as many cases as it lost (fifty-five wins and fifty-four losses). A significantly higher number of cases went on to the full litigation process when the U.S. was the respondent rather than when it was the complainant.

Chart 2. U.S. as Complainant 1995–2012 (Merits)[6]

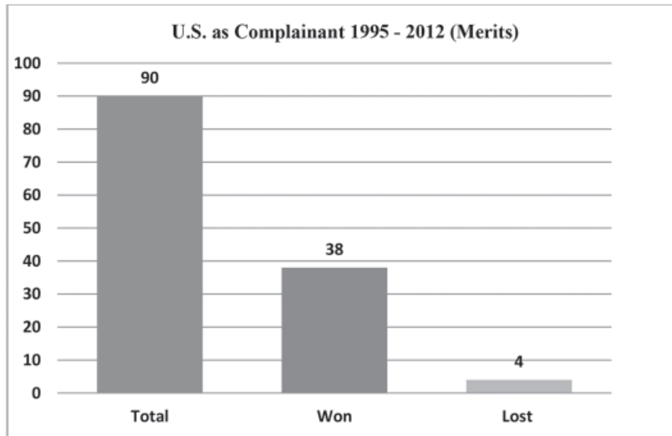


Chart 3. U.S. as Respondent 1995–2012 (Merits)

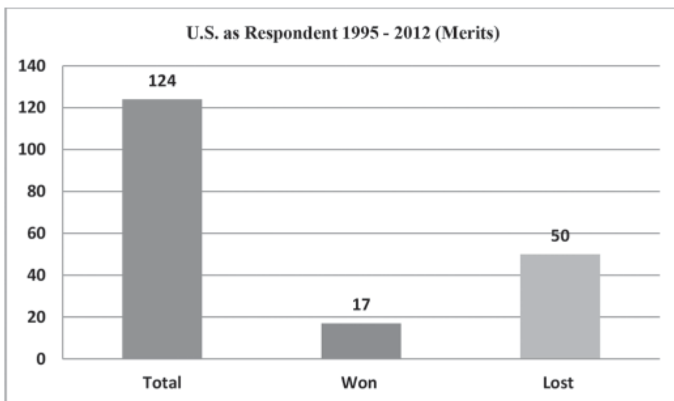


Chart 4. U.S. as Complainant and Respondent 1995–2012 in Total Cases (Merits and Compliance)

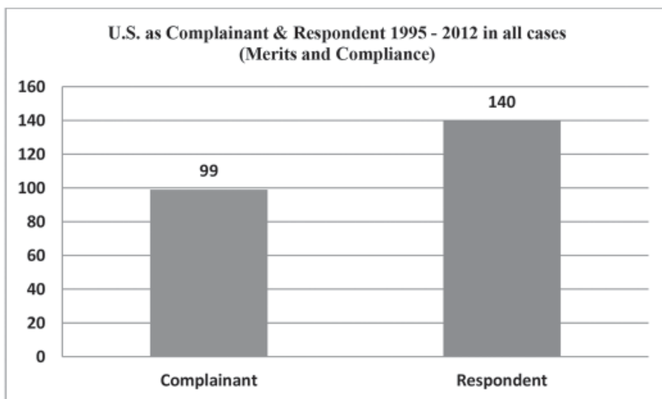
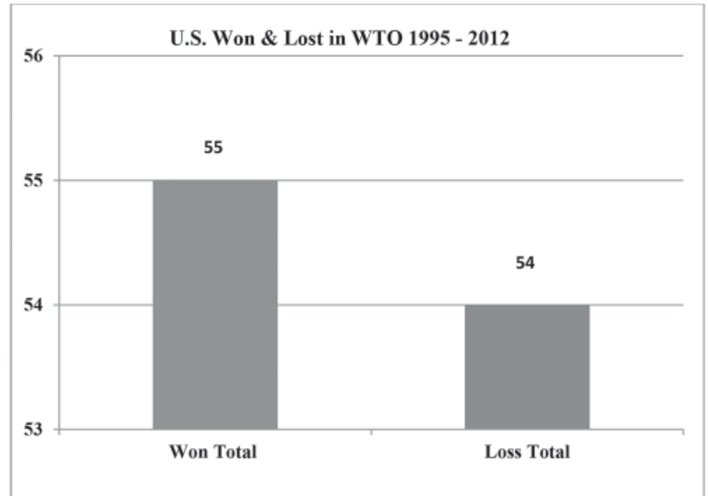


Chart 5. Total U.S. Won/Lost as Complainant and Respondent 1995–2012 (Merits)



Data Source for Charts 2–5 USTR, *Snapshot of U.S. Cases in the WTO* (8 August 2012), http://www.ustr.gov/sites/default/files/Snapshot%20Aug8.fin_.pdf.

B. Bush and Obama Administrations in the Dispute Resolution System

During the last presidential election, President Obama made much of his record for bringing legal actions against China and his aggressive use of the WTO legal process as a means of enforcing global trade obligations.

President Clinton actually brought a far larger number of cases before the WTO than did either President Bush or President Obama. Over eight years, President Clinton brought sixty-nine cases, whereas President Bush brought twenty-four cases. In five years, President Obama brought only thirteen cases. China was not a member of the WTO during President Clinton's administration. This decrease in number of cases brought subsequent to the Clinton years may well indicate that the United States is more satisfied today that trade obligations are being observed than in the earlier years of the WTO, as well as the possibility that the WTO has clarified many complex trade obligations.

Comparing President Bush's eight years and President Obama's first four years or so, it is clear that President Obama has been more aggressive than his predecessor. President Obama brought eight cases in four years compared to President Bush's seven cases in eight years. President Obama was much more focused on China in WTO litigation than was President Bush. President Bush brought a total of twenty-four cases; only seven were directed against China. President Obama has brought thirteen cases; eight of them were against China. Therefore, it is fair to conclude that President Obama has been very aggressive against China.

**Chart 6. Clinton, Bush, and Obama—
Total WTO Cases Brought (1993–Feb. 2014)**

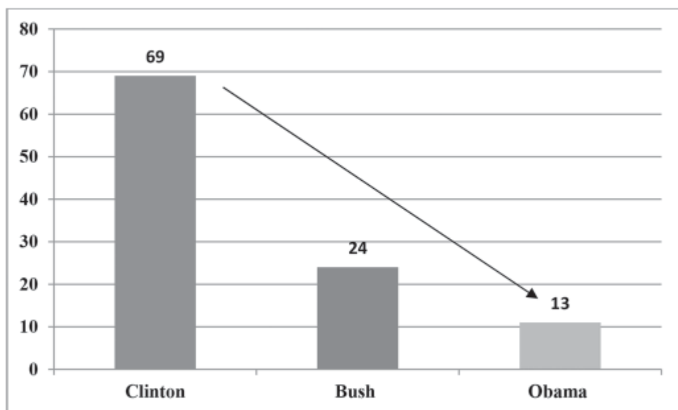


**Chart 7. U.S. Cases Against China—
Bush and Obama (2001–Feb. 2014)**

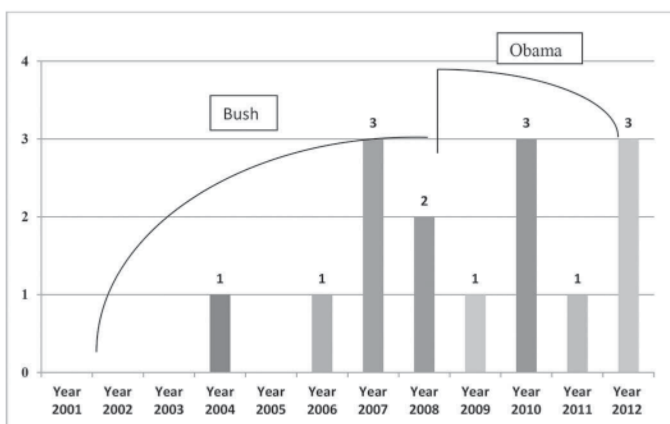
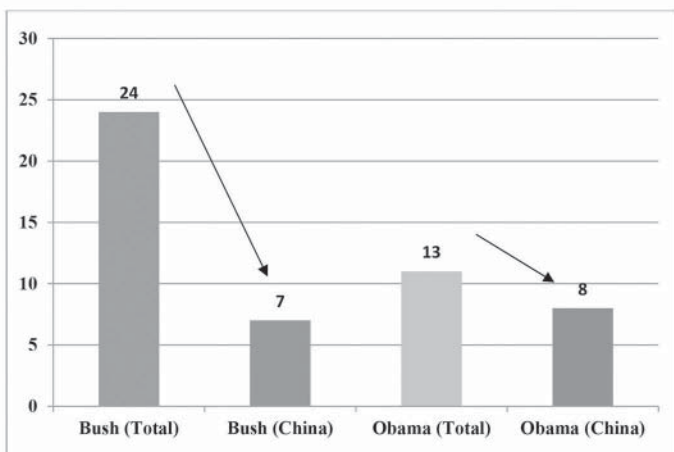


**Chart 8. Total Cases and China Cases
by Bush and Obama (2001–Feb. 2014)**



Data Source for Charts 6-8: WTO website, *Disputes from Countries/Territories* (10 Feb. 2014), http://www.wto.org/english/tratop_e/dispu_e/dispu_by_country_e.htm.

C. China in the Dispute Resolution System

Almost immediately after its accession to the WTO in 2001, China became extremely knowledgeable in the WTO litigation process. In fact, China filed a case against the U.S. before the U.S. filed its onslaught of cases against China.[7] China and the U.S. have been major adversaries in the WTO's litigation process, but China's litigation has also involved other member states, such as the EU and Japan.

China has brought fourteen actions against WTO members. It brought nine cases against the U.S. and three against the EU. However, China has been brought before the WTO more often than it has brought cases. China has been a respondent in thirty-one cases. The U.S. brought fifteen cases, whereas the EU brought seven. Further, nine other cases have been filed, including those by Mexico and Japan. It should be noted that most of the cases brought against China were parallel actions to those filed by the U.S., although some were totally independent. Parallel actions are those that by-and-large mimic U.S. arguments and legal issues. They merely involve different countries with their own fact-specific situations.

Of the twelve cases brought by China and concerning the U.S., five have been decided. The others are pending. China won three, and the U.S. prevailed in two. These cases almost exclusively involved dumping and safeguard issues. In the fifteen actions brought by the U.S. against China, the U.S. won all of the seven decided cases. The other cases are pending or inactive. The cases won by the U.S. involved, among other issues, intellectual property rights, dumping, and export controls. Therefore, in the twelve decided cases involving the U.S. and China, the U.S. won a total of nine cases, whereas China won three.[8]

One of the highest profile trade issues, the valuation of the yuan, has not been submitted by the Obama administration to the WTO, despite significant demands from Congress and the public to do so. In my opinion, both the Bush and the Obama administrations understand that the WTO agreements were never intended to cover this type of currency-exchange issue. Similarly, no cases have been filed by China against the U.S. concerning U.S. restrictions on Chinese direct investment in the U.S. when based upon claims of national security. The WTO provides architecture for global trade relations. The WTO's central mandate is trade, not finance or investment.

Chart 9. China as a Complainant and Respondent (2001–Feb. 2014)

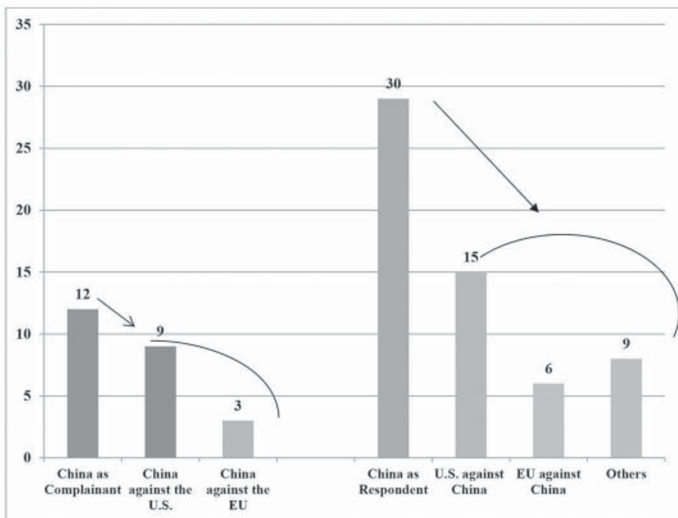
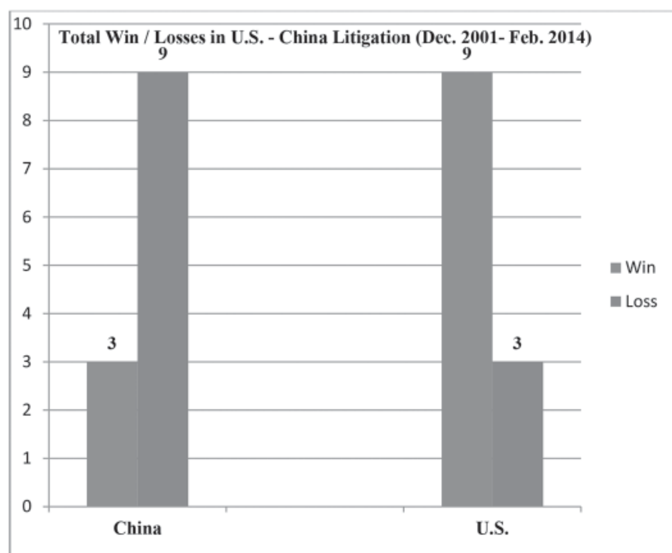


Chart 10. Wins in U.S.-China Litigation (2001–Feb. 2014)

Chart 11. Total Wins/Losses in U.S.-China Litigation



Data Source for Charts 9–11: WTO website, *Disputes from Countries/Territories* (10 Feb. 2014), http://www.wto.org/english/tratop_e/dispu_e/dispu_by_country_e.htm.

D. Observations

The Obama administration has not filed a new case against China since the 2012 election. In contrast, both the EU[9] and Japan[10] have filed actions against China. Moreover, China has filed recent actions against the EU[11] and the United States.[12]

Some observers argue that constant litigation is corrosive to the international trading system. For example, one commentator laments the fact that "more and more of the work of trade relations has shifted away from negotiations and towards litigation and arbitration."[13] Another argues, "The Obama administration has put enforcement of trade agreements at the heart of the approach toward China…But winning in the courtroom is often only the start of the battle."[14]

However, others have taken more nuanced approaches. In fact, an earlier skeptic recently stated, "In fact, the situation is more complex, and less worrying, than it might appear…[A] heartening amount of the litigation has actually been aimed at preventing arbitrary trade restrictions in the future…Much is aimed at obtaining rulings preventing others using 'trade defense' instruments, such as antidumping and countervailing duties, as a politicized tool of arbitrary retaliation."[15]

I view U.S.-China litigation in the WTO as validating the strength and critical importance of the WTO and its dispute resolution system. China is now the second-largest economy in the world. It is expected that disputes increase with trade flows. The strength of the international system is not in the absence of disputes, but in the way that they are resolved. The failure of the WTO to conclude a more robust agreement at the conclusion of the 2013 Bali Ministerial and the general failure of the Doha round of negotiations to formulate newer trade rules only highlight the growth and immense historical significance of the dispute resolution system.

An examination of the cases involving China shows that trade disputes that arise between it and the United States are submitted to the WTO and are resolved, either by diplomatic negotiations in the consultation stage or in the litigation phase. No enforcement actions by either country asking for sanctions have been filed under Article 22 of the Dispute Settlement Understanding. The primary focus of China's litigation in the WTO has been the U.S. Nevertheless, China is paying an increasing amount of attention to the EU and other countries.[16] China's use of the dispute resolution system and observance of the WTO's recommendations are beneficial developments in promoting a rules-based global trading system. This history of China's participation in the WTO's dispute resolution system shows a growing acceptance of global trade rules by China. This represents an understanding that, to benefit from the global trading system, China needs to follow the rules of the road.[17]

Chart 12. Summary of China's WTO Litigation (2001–2014)

CHINA'S WTO LITIGATION (2001–2014)

[12 as Complainant; 31 as Respondent]

As of 10 February 2014

CHINA AS COMPLAINANT					
Respondent	**Subject Matter of Case**	**Status**	**DS No.**	**Win**	
				China	**U.S.**
U.S.	U.S. Safeguard Measures on Steel Imports from China	AB (2003)	252	X	
U.S.	Dumping and Subsidies—Paper Imports from China	Consul. 2007	368	///	
U.S.	Dumping and Subsidies—Certain Products from China	AB 2011	379		X
U.S.	§ 727 (2009 Act) Denial of Poultry Imports from China	Panel 2120	392	X	
U.S.	§ 421 (1974 Act) Safeguard—Tire Imports from China	AB 2011	399		X
U.S.	Dumping—Shrimp and Diamond Sawblades	Panel 2012	422	X	
U.S.	Subsidies—Various Products	Consultation 2012	437	///	
U.S.	Dumping—Various Products	Consultation 2012	449	///	
U.S.	Dumping—Procedures (Steel)	Consultation 2013	471	///	
	[Non- U.S. Respondents]				
				China	**EU**
EC	Dumping—Iron & Steel Fastners from China	AB 2011	397	X	
EU	Dumping—Footwear Imports from China	Panel 2011	405	X	
EU	Subsidy —Reusable Energy Sector (3 Respondents)	Consultation 2012	452	///	
CHINA AS RESPONDENT					
Complainant	**Subject Matter of Case**	**Status**	**DS No.**	**Win**	
				China	**U.S.**
U.S.	VAT on Integrated Circuits	MAS (2005)	309	///	
U.S.	Measures on Import of Auto Parts*	AB (2008)	340		X
U.S.	Taxes and Refunds to China Firms*	Panel—MAS (2007)	358	///	
U.S.	Protection of IPR	Panel (2009)	362		X
U.S.	Distribution of Audiovisual and Entertainment Prod.	AB (2009)	363		X
U.S.	Financial Information Services and Suppliers*	Consult.—MAS (2008)	373	///	
U.S.	Grants and Loans (Subsidies)*	Consult. since 2008	387	///	

Respondent	Subject Matter of Case	Status	DS No.	Win	
				China	U.S.
U.S.	China's Raw Material Restraints*	AB 2012	394		X
U.S.	Restrictions on Credit Card & Elect. Payments	Panel 2012	413		X
U.S.	Dumping/Subsidies Duties on Steel from U.S.	AB 2012	414		X
U.S.	Subsidies on Wind Power Equipment	Consult. since 2010	419	///	
U.S.	Restrictions on Broiler Products	Panel pending 2012	427		X
U.S.	Export Restrictions on Rare Earth Metals*	Consult. filed 2012	431	///	
U.S.	Dumping and Subsidies on U.S. Auto Imports	Consult. filed 2012	440	///	
U.S.	Subsidies on Autos and Auto Parts	Consult. filed 2012	450	///	
[Non-U.S. Complainants] --- *Often Parallel Cases with the U.S.* ---					
				China	Other
EC	Measures on Import of Auto Parts*	AB (2008)	339		X
Canada	Measures on Import of Auto Parts*	AB (2008)	342		X
Mexico	Taxes and Refunds to China Firms*	Panel—MAS (2008)	359	///	
EC	Financial Information Services and Suppliers*	Consult.—MAS (2008)	372	///	
Canada	Financial Information Services and Suppliers*	Consult.—MAS (2008)	378	///	
Mexico	Grants and Loans (Subsidies)*	Consult. since 2008	388	///	
Guatemala	Grants and Loans (Subsidies)*	Consult. since 2009	390	///	
EC	Raw Material Export Restraints*	AB 2012	395		X
Mexico	Raw Material Export Restraints*	AB 2012	398		X
EC	Iron and Steel Fasteners from EU (Dumping)	Consult. since 2010	407	///	
EU	Dumping Duties on X-Ray from EU	Panel since 2012	425		X
EU	Export Restrictions on Rare Earth Metals*	Consultation 2012	432	///	
Japan	Export Restrictions on Rare Earth Metals*	Consultation 2012	433	///	
Mexico	Subsidies on Apparel and Textile	Consultation 2012	451	///	
Japan	Chinese A/D Duties on Steel	Consultation 2012	454	///	
Europe	Chinese A/D Duties on Steel	Consultation 2013	460	///	
* Parallel Cases with other Complainants					

Data Source: WTO website, *Disputes from Countries/Territories* (10 Feb. 2014) http://www.wto.org/english/tratop_e/dispu_e/dispu_by_country_e.htm.

IV. Conclusion

An analysis of all WTO cases filed in 2012 in *The WTO Annual Report for 2013* shows that the U.S. filed five cases (requests for consultation), whereas China and Japan filed three each.[18] The main targets of all litigation were China (seven), the U.S. (six), and the EU (three).[19] The report concluded, "In sum, WTO dispute settlement activity increased markedly in 2012. It is clear that WTO members, both developed and developing, continue to have a high degree of confidence in the WTO dispute-settlement mechanism to resolve their disputes in a fair and efficient manner. It is also evident that members are confident that the system is capable of adjudicating a wide variety of disputes covering significant questions and complex issues."[20]

It is worthwhile to note the recent observation by Pascal Lamy, then Director General of the WTO.[21] He argued that "trade frictions are a statistical proportion of trade volumes," whereas "trade disputes are a statistical proportion of trade frictions." He brushed off concerns about the increasing number of trade disputes between the U.S. and China. He contended that the WTO mechanism takes the heat out of disputes by utilizing a process that is rules-based, predictable, and respected.[22]

Lamy warned in a subsequent presentation that geopolitics is back at the trade table.[23] He noted that the value chains are multilateralizing and that trade governance needs to meet this challenge. Lamy argued that China would benefit from taking a more active role in global governance in trade and related issues: "China's economic take-off benefited from a stable external environment. Its sustainability depends on a well-functioning global trading system. As a key stakeholder, China should take a more proactive role in international economic governance...."[24]

While inheriting a complex trade situation,[25] the Obama administration has clearly put trade at the heart of its second-term agenda.[26] This policy includes negotiating the Trans-Pacific Partnership (TPP) and the Trans-Atlantic Trade and Investment Partnership (TTIP). The future of these negotiations is dependent on Congress's authorization of "fast track" authority for President Obama.[27] Nevertheless, the core of the administration's trade policy is its insistence on greater trade enforcement by U.S. trade agencies and the WTO, particularly with China. What is the point of negotiating rules if they will not be enforced? Secretary of State John Kerry succinctly stated, "Foreign policy is economic policy."[28]

The 2013 Report to Congress on China's WTO Compliance by the United States Trade Representative (USTR) stated clearly the central position of WTO litigation in U.S.-China trade relations: "When trade frictions have arisen, the United States has preferred to pursue dialogue with China to resolve them. However, when dialogue with China has not led to the resolution of key trade issues, the United States has not hesitated to invoke the WTO's dispute settlement mechanism." [29] While the "U.S.-China Strategic and Economic Dialogue" (S&ED) was established by President Obama in order to discuss diplomatically a broad range of issues, the report continues that "the United States has placed a strong emphasis on the need for China to adhere to WTO rules, holding China fully accountable as a mature participant in, and a major beneficiary of, the WTO's global trading system.... Unquestionably, China's incomplete adoption of the rule of law has exacerbated this situation."[30] Indeed, the report outlines a large number of issues that might very well eventually find their way to the dispute resolution system. The report outlines a policy that is continuing under USTR Michael Froman, a former member of the National Security Council,[31] and under the new United States Ambassador to China, Max Baucus, former chairman of the Senate Finance Committee. USTR Froman recently stated in the 2014 Trade Agenda Report to Congress, "A robust international trading system offers the greatest economic benefits when all trading partners abide by their commitments and play by the same rules.… It is for this reason that President Obama has placed trade enforcement on a par with opening markets for U.S. exports.… As a top priority…we will continue to hold China accountable to its WTO obligations to ensure that U.S. producers and workers have a level playing field to compete in a wide range of industries."[32]

At least in terms of adjudicating trade disputes and governing existing and emerging trade issues, the WTO has proven itself well beyond the grandest dreams of the early architects of the dispute resolution system. The new Director-General of the WTO, Roberto Azevêdo, appropriately noted in one of his first speeches that "The dispute settlement mechanism is under heavy demand. This is yet another sign of the importance of the WTO system in uncertain times."[33] A recent book sponsored by the WTO makes the point that international economic law and global trade rules enhance a country's ability to participate in the global economy and helps strengthen the domestic rule of law.[34]

Newer trade issues are emerging swiftly in this rapidly globalizing trading system.[35] A recent WTO panel on "Defining the Future Trade Issues" released its report in 2013.[36] It enumerated nine issues, including competition policy, international investment, currencies, labor, climate change, corruption,[37] and coherence of international economic rules. Some of these issues have been around for a while, and some have become much more pressing.

To this list, I would add the issue of cyber-espionage for commercial and economic gain as a new front in global trade wars. The Obama administration has sug-

gested[38] that trade tools should be used to combat cyber-espionage for commercial gain, which would possibly involve WTO litigation.[39] Of course, recent disclosures that the National Security Agency (NSA) has discussed with the Australian intelligence agency Australia's snooping on Indonesia's communications with its American legal counsel, involved with its WTO actions against the United States, complicates this policy proposal by the Obama administration.[40]

In addition to this newer issue of commercial cyber-espionage, I would add two additional issues: foreign direct investment and taxation. Growing foreign investment by Chinese companies has raised questions of national security.[41] Tax avoidance has become the scourge of many countries and international organizations who have targeted it as economic development and national budgets come under increasing pressure because of global economic problems.[42] These areas could certainly benefit from greater multilateral-based solutions through the WTO, perhaps leading to trade agreements relating to direct investment (TRDI) and to international taxation (TRIT). These areas may even be subject to future litigation in the WTO under existing rules.

Challenges remain and are expected to continue. Those relating to the most important bilateral trade relations in the world today between the U.S. and China are set to grow as trade develops even more. Global transactions in a multijurisdictional world need a mechanism to resolve a wide range of business, trade, and economic issues.[43] In an increasingly interconnected trading system, and a less hierarchical political system, cooperation through diplomacy and adjudication is preferable to outright power-politics confrontation.

Each country has shown that it is willing to work with the other to apply the rules of global trade, which will need to continue as new disputes arise and even newer trade issues evolve. It is in the national interest of China to conform to the global rules and to be proactive in developing them. This approach should be at the core of Chinese foreign-policy decision-making in the 21st century. It is to the advantage of both the U.S. and China that they look toward the future together to build a peaceful, international rules-based system.

Endnotes

1. A new study released by the WTO and written by Professor Craig VanGrasstek presents, in part, a statistical assessment of WTO litigation relying upon data compiled by the WTO. See Chapter 7 – "Dispute Settlement" in C. VanGrasstek, The Future and History of the WTO (2013).
2. 2013 Appellate Body, Annual Report 13 (Chart 2) (March 2014), *available at* http://www.wto.org/english/ news_e/news14_e/ ab_14mar14_e.htm.
3. 2013 WTO Annual Report of the World Trade Organization 82 (WTO 2013), *available at* http://www.wto.org/.english /res_e/ booksp_e/anrep_e/anrep13_e .pdf.
4. *Id*.
5. C. VanGrasstek, note 1 *supra*.
6. Over forty cases did not make it out of the consultation stage. The USTR considered that twenty-nine of them were resolved to the U.S.'s satisfaction without completing litigation. The remainder were either dropped or inactive. *Snapshot of US Cases in the WTO* (8 August 2012), *available at* http://www.ustr.gov/sites/default/ files/Snapshot% 20Aug8.fin_.pdf.
7. DS 252, *China v. US (US Safeguard Measures on China Steel Imports)* (26 March 2002).
8. The two panel reports were released in March 2014 and are not included. The cases won or lost by the United States or China: DS 431, *Exportation of Rare Earths*, WTO News (26 March 2014); DS 449, *U.S. Measures on Chinese Products*, WTO News (27 March 2014). The panel in *Rare Earths* upheld the U.S. challenge to China's export restrictions. The panel in *Measures on Chinese Products* issued a split-decision: It denied China's challenge to the 2012 U.S. legislation authorizing countervailing duties on imports from non-market economies, but upheld China's challenge to "double remedies" when anti-dumping duties are also applied.
9. DS 460, *EU v. China (China A/D Duties on EU Steel Imports)* (13 June 2013). The EU and China have settled the "solar case" after mutually threatening WTO filings. This has raised issues concerning the common or external trade powers of the EU. *Frustrated and Outflanked*, Financial Times (31 July 2013).
10. DS 454, *Japan v. China (China A/D Duties on Japan Steel Imports)* (24 May 2013).
11. DS 452, *China v. EU (European Subsidies in Renewable Energy Sector)* (5 Nov. 2012).
12. DS 471, *China v. US* (*A/D Methodology on Steel into US)* (3 December 2013).
13. Beattie, *How Lawsuits Are Coming to Dictate the Terms of Trade*, Financial Times (20 February 2007).
14. Schneider, *At WTO, US Racks up Wins against China, But the Benefit Is Less than Certain*, Washington Post (9 August 2012).
15. Beattie, *Decommission the Weapons of Trade Warfare*, Financial Times (8 August 2012).
16. Yap and Shangguan, *China Ups Ante in Trade Spat with E.U.*, Wall Street Journal (5 June 2013) (involving solar panels and wine subsidies).
17. Former USTR and former World Bank President Robert Zoellick recently stated, "Twenty years ago Zhu Rongil, China's former premier, shrewdly used negotiation over his country's accession to the World Trade Organization to open its domestic markets … and gave China a greater stake in global trade." Zoellick, *International Treaties Can Once Again Help China Advance*, Financial Times (10 March 2014). China's trade policy is now not just to join the global trading system but to help write the rules for 21st century global commerce. Donnan, *China Craves Invitation to join Global Trade Club*, Financial Times (3 April 2014).
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19. *Id*.
20. *Id*. at 89.
21. Politi, *Lamy Dismisses Rise in U.S.-China Disputes*, Financial Times (1 October 2012).
22. *Id*.
23. Lamy, *Putting Geopolitics Back at the Trade Table*, WTO News (29 January 2013).
24. Lamy, *China Should Be More Active in Global Economic Governance*, WTO News (24 March 2013).

25. Schneider, *Inheriting a Complex Trade Agenda*, Washington Post (22 June 2013).
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30. *Id*.
31. Goldfarb, *More Obama Appointments: Froman for Trade Representative*, Washington Post (13 May 2013).
32. 2014 Trade Policy Agenda and 2013 Annual Report 9 (USTR 2014), *available at* http://www.ustr.gov/sites/ default/ files/201420Trade%20Policy%20Agenda%20and%202013%20 Annual%20Report.pdf.
33. *Azevêdo Launches "Rolling Set of Meetings" Aimed at Delivering Success in Bali*, WTO News (9 September 2013).
34. M. Jansen, M. Jallab and M. Smeets, *Connecting to Global Markets* 4 (WTO 2014).
35. Korea filed a new action against the U.S. in the WTO over its antidumping and subsidies measures concerning imports from Korea that utilize "*zeroing*." This methodology has long been contested in many actions against the U.S. in the WTO. The U.S. has almost always been found to have violated the WTO's rules for imposition of antidumping duties based upon zeroing. *Korea Files Dispute (Washing Machines)*, WTO News (29 August 2013).
36. *The Future of Trade: The Challenges of Convergence* (WTO Panel Report to the Director-General) (24 April 2013).
37. USDOJ and SEC, *A Resource Guide to the U.S. Foreign Corrupt Practices Act* (November 2012).
38. "The Administration will utilize trade policy tools to increase international enforcement against secret theft to minimize unfair competition against US companies." *Administration Strategy on Mitigating the Theft of US Trade Secrets* 4 (White House) (February 2013). "Finally, we need China to engage with us in a constructive direct dialogue to establish norms of behavior in cyberspace." *Remarks by Tom Donilon to the Asia Society - The US and Asia-Pacific in 2013* (White House) (11 March 2013).
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41. Herzstein, *The Dangers behind the Smithfield Deal*, Washington Post (1 June 2013). The U.S. and China have agreed to restart negotiations over a new bilateral investment treaty during the annual strategic economic dialogue talks. This could lead to international rules governing direct investment into both China and the U.S. and alleviating tensions in this area. *U.S., China to Pursue Investment Treaty*, Wall Street Journal (12 July 2013).
42. Houlder, *Nations on Defensive as Anger Grows over Tax Avoidance*, Financial Times (29 April 2013).
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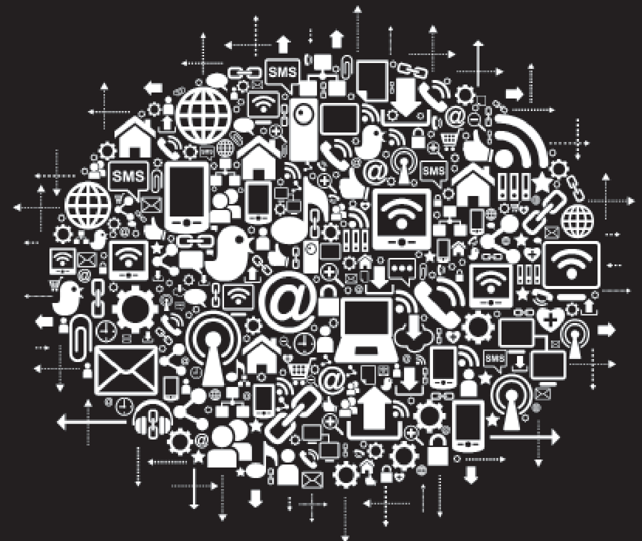

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