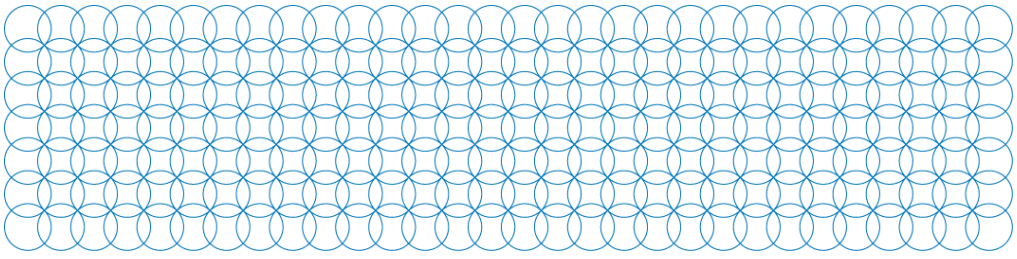
A Common European Sales Law for the European Union – A proposal for a Regulation from the European Commission

The Government Response



Ministry of JUSTICE

A Common European Sales Law for the European Union – A proposal for a Regulation from the European Commission

The Government Response

A joint publication produced by the Ministry of Justice, the Department for Business, Innovation & Skills, Scottish Government and the Department for Finance & Personnel Northern Ireland. It is also available on the Ministry of Justice website at www.justice.gov.uk

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Foreword

The Government supports the efforts of the European Commission to strengthen the functioning of the Single Market and to bring forward measures that drive growth in the European economy. We acknowledge that levels of cross-border trade should be higher and we have previously stated our ambition to *"unleash the competitive advantage of the single market"*[1].

The Government agrees with the objectives of boosting growth through enhanced cross-border trade, while reducing costs and complexity for businesses and consumers in the process. In particular the Government recognises the potential impact of the Digital Single Market.

Economic research estimates that the UK internet ecosystem is worth £82 billion a year, of which £45bn relates to e-commerce. The UK already has the highest level of e-commerce in Europe with 12% of the retail market already online (compared to 7.8% on average in the EU). It is argued that e-commerce could represent 15-20% of GDP growth by 2015[2].

However, while the responses to this Call for Evidence have demonstrated that there is broad support for the objective of increasing cross-border trade most UK stakeholders did not see the creation of an optional contract law, as a viable way of achieving that aim.

Domestically the UK is planning to modernise and simplify its consumer rights framework through a Consumer Bill of Rights and associated package of consumer law reforms. This package will implement the Consumer Rights Directive and will use common language and definitions to make it easier for businesses and consumers to understand their rights. The UK fully supports efforts to simplify consumer law. However, there is insufficient evidence to demonstrate that a new, optional, highly complex legal instrument focussed on contract law for cross-border sales can provide benefits to consumers or business. Nor is it clear that it will achieve the benefits to cross border trade and growth it presumes.

The Government is clear that we must provide practical and effective solutions to existing problems and that these solutions must be of real value to businesses, consumers and the Single Market. If we are to break down barriers to cross-border trade we must do so in a way that facilitates businesses to grow and develop. We must not add further layers of legal complexity but provide solutions that enable consumers to purchase and businesses to trade more freely across European borders with confidence.

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[1] Let's Choose Growth pamphlet: www.number10.gov.uk/wp-content/uploads/EU_growth.pdf

[2] Boston Consulting Group (September 2011) "Turning local: from Madrid to Moscow, the Internet is going native"

Executive Summary

1. The European Commission's proposed Regulation for a Common European Sales Law (CESL), published in November 2011, presents an alternative legal regime in the form of an optional instrument available to cross border business-to-consumer (B2C) and business-to-business (B2B) contracts covering goods and their related services. In B2B contracts it applies where at least one of the businesses is a small or medium enterprise (SME).

2. The Government published its Call for Evidence document on the European Commission's proposal for a Common European Sales Law on 28 February 2012. The period of public engagement closed on 21 May 2012. This document presents the findings to that exercise and the Government's response to them.

3. The Call for Evidence demonstrated that while there was broad support for the objective of increasing cross-border trade, most UK stakeholders did not see CESL as a viable way of achieving that aim. The legal and consumer sectors were particularly strong in their opposition. A minority of respondents, largely from small business organisations, expressed some support for the aims of the proposal. There was, however, no clear support from any sector for the proposal as currently drafted.

4. Issues raised by responses to the Call for Evidence provided a number of recurring themes in response to the questions posed:

    - Evidence of need: Respondents did not believe that sufficient need for the proposal had been demonstrated. They were unconvinced that contract law presented a significant enough barrier to warrant such a complex and wide ranging proposal. They believed other barriers were more significant and that these would not be resolved by this proposal. Many respondents were unconvinced that CESL was required or could achieve the results anticipated by the Commission.

    - Legal uncertainty: Respondents believed that the content of CESL would lead to significant legal uncertainty. There was felt to be a fundamental problem in creating a distinct law for the sale and supply of goods and services, separate from other contractual procedures. Respondents argued this would only lead to uncertainty and incoherence. Jurisprudence in the area would also take years and perhaps decades to establish, creating an additional burden on the UK's judicial system and on the Court of Justice of the European Union. This would lead to significant delays and expense in the resolution of disputes and interim uncertainty regarding the interpretation of the law.

- Confusion: Respondents believed that the introduction of a second regime of contract law would create confusion for both consumers and businesses. They argued that a new law was neither necessary nor practical and specifically noted the length and complexity of the CESL proposal. Many respondents believed that the implementation of further legislation in this area would make it harder, not easier, for businesses to agree contracts and for consumers to know their rights with certainty when purchasing across borders.

- Cost: Respondents believed that the costs of the proposal would outweigh the possible benefits. Representatives from business and legal professions were clear that CESL would have considerable cost implications for its initial implementation and for its continued application, whether it be for the costs of legal training, for the Court of Justice of the European Union or for litigants dealing with the more arduous disclosure requirements (for example Article 23) of CESL.

5. Respondents who were more in favour with the proposal, agreed with the principle of increasing and improving cross-border trade as a starting point. The potential benefits cited included the optionality of the instrument, the potential simplification of having a single set of contract law rules, and the potential to further harmonise consumer law. However, these respondents also had concerns about the proposal as currently drafted.

6. The Government has carefully considered the evidence provided in the responses to the Call for Evidence. In drawing conclusions from this evidence, we are concerned that there are fundamental flaws in both the principle and practical operation of CESL. Evidence indicates that it is most unlikely to produce the results the Commission claim. It is also clear that the proposal will be both time consuming and cumbersome to negotiate and implement, rather than providing a simple and practical solution to the immediate challenges presented to businesses, consumers and the growth of the Single Market.

7. The Government concludes that there are elements of CESL which do not provide sufficient clarity or legal certainty. The instrument is:

    - too complex,

    - incomplete in parts (some significant aspects of a contractual relationship are not covered),

    - unworkable for certain types of contract,

    - uncertain, both as to whether a contract is valid and as to the certainty of its terms; and

- unclear on its applicability, in particular how its provisions interact with other EU law.

8. The Government therefore concludes that it does not feel able to support the CESL proposal. The UK has, in the past, supported an ambitious approach to the harmonisation of consumer law to support the retail single market. We continue to think that this is more likely to deliver the Commission's aims than a new, voluntary contract law. We would therefore encourage the Commission to carry out a careful and specific review of the barriers to cross-border trade, considering the most appropriate solutions to them, before proceeding any further with negotiation of this proposal. The Government would be content to support the Commission in doing so.

Introduction

Background

9. The CESL proposal, published in October 2011[3], is the result of a long standing project for the European Commission. For over a decade experts and academics have been looking at the issue of European contract laws during which time a number of different approaches and proposals have been developed and considered.

10. In July 2010 the Commission published a Green Paper, *"Policy options for progress towards a European contract law for consumers and businesses"*[4] setting out a number of possible options to address the challenges presented by contract law to cross border trade. In response to this Green Paper the UK Government supported the proposal for a toolbox for legislators; a non-legislative proposal that would allow legislators to use a selection of common terms when drafting new law. This non-legislative option has not been taken forward despite support from a number of Member States and the agreement of the Justice and Home Affairs Council.

11. The Commission's current proposal for CESL attempts to resolve barriers to cross-border trade by introducing a new optional contract law. They suggest that these barriers are caused by the divergence of contract laws across the Member States which significantly hamper cross border trade, the smooth functioning of the Single Market and ultimately stifle potential growth within the European Union. The aim behind CESL is to provide *"a comprehensive set of uniform contract law rules covering the whole-life cycle of a contract, which would form part of the national law of each Member State as a 'second regime' of contract law."*[5] This proposed alternative regime would be available for cross-border B2C contracts and cross-border B2B contracts where at least one of the businesses is a Small or Medium Enterprise (SME)[6].

12. The Commission's Impact Assessment on the CESL acknowledges that there are a number of barriers to cross border trade[7]. They argue that by tackling the challenges presented by the divergent contract laws of the Member States they will see an increase in cross border trade through reduced transaction costs for traders and increasing choice for consumers.

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[3] COM(2011)635 final 11 October 2011
[4] COM(2010)348 final 1 July 2010
[5] Pg7 of doc.15432/11,k 13 October 2011, Communication from the Commission [http://ec.europa.eu/justice/newsroom/news/20111011_en.htm]
[6] Page 26, COM(2011)635 final
[7] Page 208, SEC(2011)1165 final

13. Initial EU level negotiations of the proposal commenced in November 2011. The UK has been clear that it remains to be convinced of the need for this CESL proposal.

The Call for Evidence Period

14. The Ministry of Justice, jointly with the Department for Business, Innovation and Skills, the Scottish Government and the Department of Finance and Personnel (Northern Ireland), published its Call for Evidence on CESL on 28 February 2012.

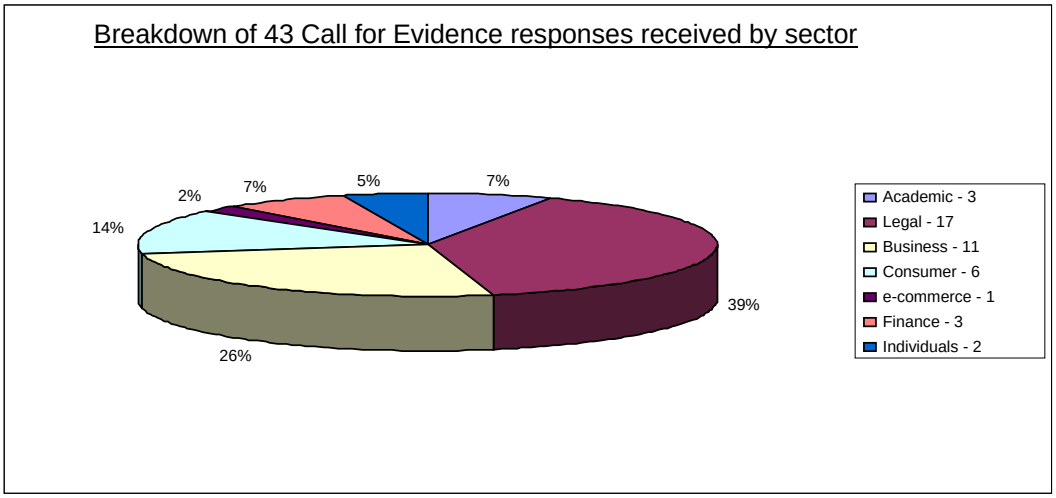
15. The Call for Evidence period was conducted between 28 February and 21 May 2012. The Call for Evidence was sent to a wide range of UK interest groups who had previously engaged with the Ministry of Justice on this issue. It was also made available to the public through the Ministry of Justice website.

16. The Call for Evidence sought views, and more specifically, evidence from UK interest groups affected by the proposal, particularly in terms of whether:

- the Commission's assessment of the barriers to cross-border trade were accurate,
- the principle of CESL was necessary and workable; and
- the proposal as drafted was something they could support.

17. In addition, a number of engagement forums were held. A public workshop was held on 8 May in London at which attendees were invited to share their views on the proposed Regulation. A similar event was held in Edinburgh by the Scottish Justice Department on 15 May 2012. The Ministry of Justice also engaged with its stakeholder Partner Group (representing key interests within Government) during this period to discuss the responses to the Call for Evidence questions.

18. Forty-three responses were received to the Call for Evidence from a wide spectrum of affected sectors, including the legal profession and representative organisations, businesses and consumers as well as the judiciary, academics and members of the public. The Government is extremely grateful to all those who took the time to contribute. A full list of respondents can be found at Annex A.



19. An analysis of the responses to the Call for Evidence has been undertaken and forms the basis of the Government's response outlined in this paper. Overall, the Government concludes that the majority of respondents were unconvinced that CESL would or could achieve the intended benefits to cross border trade and growth, as proposed by the Commission. Although a minority of respondents expressed support for the principle behind such an instrument, as they thought it had the potential to remove barriers to cross border trade, the majority were sceptical or displayed outright opposition to the proposal.

Technical Advisory Committee

20. The Ministry of Justice established a Technical Legal Advisory Committee, attended by a number of legal experts, who analysed the detail of CESL. This Committee was chaired by Lord Mance. Membership to the Committee reflected legal expertise (including cross border trade) in all aspects of the proposal from business and consumer sectors, and members of the judiciary with significant experience of consumer and commercial disputes.

21. The key findings of the Committee are incorporated in this response paper under Part II which analyses the Annex I to CESL.

Devolved Administrations

22. The UK consists of different legal jurisdictions. Domestic contract law is generally a devolved matter: responsibility rests with Devolved Administrations for Scotland and Northern Ireland, and with the UK Government for England and Wales. Responsibility for consumer policy is devolved for Northern Ireland, but reserved to the UK Government for England, Wales and Scotland.

Scotland

23. During the Call for Evidence period the Scottish Justice Department held an event on 15 May 2012 to give Scottish interests an opportunity to examine the issues which CESL raised, specifically for law and commerce in Scotland.

24. The event was attended by members of the legal community, academics, a representative from Scottish Development International and representatives from two consumer bodies. A representative from the Ministry of Justice also attended. The discussion revealed a desire for consistency and certainty in domestic and international contract law. Whilst the consumer organisations expressed some major concerns about the effectiveness of the proposal, there were others that showed more interested, seeing it as a laudable attempt to create standard laws to facilitate the future behaviours of businesses and consumers.

Northern Ireland

25. The Call for Evidence went out across Northern Ireland and specific comment was invited from members of the legal profession, the business community and organisations which deal with consumer protection.

26. While there was an understanding of the desire to facilitate cross-border transactions and enhance consumer choice, there was also concern that CESL would actually reduce the level of consumer protection, place additional burdens on advisory and enforcement bodies and create greater legal complexity, uncertainty and confusion for consumers. It was also suggested that businesses would have to invest more resources in training, customer care and legal advice.

PART I

The Commission's proposal: the Proposed Regulation

The Common European Sales Law

27. The Call for Evidence posed a series of targeted questions. Respondents were invited to provide their answers, supported by evidence wherever possible.

28. The first Part of the document, Part I, sought respondents' views on the principle, scope and content of the proposed Regulation for a Common European Sales Law (CESL). It also addressed the Impact Assessment presented by the Commission in support of its proposal.

29. Not all respondents dealt directly with the questions posed. Some provided a narrative response which covered the questions whilst others used the question and answer structure in the Call for Evidence document. It has been noted how many respondents answered each of the targeted questions specifically.

The principle of a Common European Sales Law

Q1. Do you support the principle of a Common European Sales Law as proposed by the Commission? Please give evidence and reasons for your answer.

30. **25 of 43 respondents** answered Question 1 directly.

31. Respondents from consumer groups, the legal profession and business organisations all expressed concerns over the principle of the proposal. Although respondents recognised the efforts of the Commission to improve the functioning of the single market, the majority were unconvinced by the specific proposal.

32. **20 respondents** to this question were explicitly opposed to the principle of CESL. The main reasons given for their opposition were:

a. **Evidence of need:** Respondents did not believe a sufficient need for the proposal had been demonstrated. They were unconvinced that contract law presented a significant enough barrier to warrant such a complex and wide ranging proposal. They believed other barriers were more significant and that these would not be resolved by this proposal. Many respondents were unconvinced that CESL was required or could achieve the results anticipated by the Commission.

b. **Legal uncertainty:** Respondents believed that the content of CESL would lead to significant legal uncertainty. There was felt to be a fundamental problem in creating a distinct law for the sale and supply of goods and services, separate from other contractual procedures. Respondents argued this would only lead to uncertainty and incoherence.

c. **Confusion:** Respondents believed that the introduction of a second regime of contract law would create confusion for both consumers and businesses. They argued that a new law was neither necessary in principle nor practical and specifically noted the length and complexity of CESL. Many respondents believed that the implementation of further legislation in this area would make it harder, not easier for businesses to agree contracts. For consumers it would pose difficulty in ascertaining and knowing their rights with certainty when purchasing across borders. The CESL would cut across UK Government attempts to simplify consumer law and communicate those rights clearly to consumers, through its proposed Consumer Bill of Rights.

d. **Cost:** Respondents believed that the costs of the proposal would outweigh the possible benefits. Representatives from business and legal professions were clear that CESL would have considerable cost implications. These would arise through its initial implementation and for its continued application, whether it be for the costs of legal training, for the Court of Justice of the European Union or for litigants dealing with the more arduous disclosure requirements in B2B contracts (outlined at Article 23) of CESL.

33. **5 respondents** expressed support for the principle behind CESL though all who expressed support provided areas where amendment or improvement would be required. The main reasons given in support were:

a. **Optionality.** Those finding favour with the principle of CESL did so on the basis that it would be optional, and therefore they felt *"could do no harm"*. It would add to the possible legal options for businesses to use in cross border trade. Business organisations were clear that the proposal would have to be optional to achieve any interest.

b. **Simplicity.** Some respondents agreed with the principle of a single EU-wide set of contract law rules as opposed to tackling as many as 27 different laws when carrying out cross-border trade. This was certainly the view expressed by two business respondents.

c. **Consumer law harmonisation.** Some business and academic respondents believed that the principle of CESL could present a possible solution to the failure to secure maximum harmonisation of consumer law in the recently finalised Consumer Rights Directive. Business respondents noted that the proposal could allow businesses to circumnavigate the mandatory consumer law rules of the Rome I Regulation set out in Article 6 (2), which they felt presented a barrier to businesses selling to consumers in multiple Member States.

Q2. Do you see any major strengths, weaknesses, opportunities or threats associated with the proposal? If so, what are they and who do they affect?

34. **25 of 43 respondents** answered Question 2 directly.

35. **20 respondents** expressed mostly serious concern about the weaknesses of the proposal in their responses. Comments relating to weaknesses and threats considerably outweighed those identifying strengths and opportunities.

36. Key weaknesses and threats, identified by respondents and as noted in response to Question 1, were legal uncertainty, cost and confusion. One consumer representative believed the proposal was an inappropriate way to address the challenges to cross border trade and expressed *"real concerns that the EU legislative process was not appropriate for an instrument of this type."* The specific legal weaknesses and concerns with the proposal are addressed in Part II of this Government Response.

37. Some respondents also presented the possible threat to consumer rights and the treatment of digital content as weaknesses.

a. **Consumer rights:** Respondents from consumer organisations argued that an insufficient level of consumer rights protection was provided and further feared that this level was likely to be compromised further during the negotiation of the proposal.

b. **Treatment of digital content:** Whilst the inclusion of digital content was welcomed by a number of respondents due to the current lack of clarity of the law, some thought that CESL, as an optional instrument, was not the right method to address this. Some also felt that the treatment of digital content in the proposal was not appropriate and required a more bespoke approach. Others argued for a consolidated approach towards digital content that considered consumer rights for digital content alongside other areas, such as copyright law, data privacy, payment methods and online security.

38. **5 respondents** (from academic and business backgrounds) saw mostly strengths and opportunities in the proposal. Views varied between respondents in this respect with the same issues identified as both a strength and weakness by different respondents.

39. Key strengths and opportunities identified were, as noted above in answer to Question 1, the proposed optional nature of the proposal, the possibility of a single law being applicable in all Member States and the chance to further harmonise consumer laws.

Q3. The proposed Common European Sales Law is an optional instrument. Is it, as drafted, something you would choose to use or advise others to use? Please outline the nature of your interest in the Common European Sales and give reasons for your answer.

40. **24 of 43 respondents** answered Question 3 directly.

41. **19 respondents** said that they would not use, or advise others to use, CESL. Respondents believed it would add greater complexity and legal uncertainty to the process of cross-border sales. The proposal was described by legal respondents as "an unwelcome initiative" and "potentially counter-productive to the objective which it was apparently seeking to achieve."

42. As in Questions 1 and 2 the same reasons were given for the lack of support for the use of CESL.

a. **Legal representatives.** The majority of legal respondents said that they would not use, or recommend the use of CESL. Cost, confusion and lack of certainty were all given as reasons in support of this position.

b. **Consumer organisations** unanimously opposed the use of CESL. They argued that it did not represent a genuine choice for the consumer and as such they would not recommend its use. They observed that a new proposal would not in itself resolve consumer confusion on the process of cross-border trade.

c. **Business organisations** indicated areas where changes would need to be made to improve the likelihood that businesses would consider using CESL. In particular, respondents suggested that a customer's journey, the online process for a consumer purchasing an item, would be lengthened and complicated by having to specifically agree to CESL. This would need to be made significantly clearer.

43. **5 respondents** indicated that they would be inclined to use the proposal or advise others to do so. In doing so, however, all indicated areas where changes would need to be made before they would consider using it. The most positive aspect of the proposal was its optionality, which respondents believed could enable a business to target sales in more Member States than they were presently inclined to do, and equally choose a national law where it suited better.

The scope of the Common European Sales Law

Q4(a). What are your views on the proposed scope of the draft Regulation, including: the kind of transactions it can be used for sale of goods or digital content?

44. **21 of 43 respondents** answered Question 4(a) directly. They provided a range of perspectives on the scope. Most did not believe that the proposed scope of the Regulation was right, with 13 respondents openly opposed to its present scope.

45. It was apparent that views on the scope were mixed with a few respondents feeling additional aspects ought to be included, for example service contracts. Others however were keen for it to be narrowed, or believed it to be unworkable as drafted. The scope of the Regulation was felt to be too broad and was more likely to magnify problems. It tried to cover several types of contract but did not sufficiently address the needs of any of them. While there was some support for the inclusion of digital content within the scope of CESL, some thought that an optional instrument was not the right vehicle while others thought that digital content had not been dealt with appropriately in the Regulation (see Q9).

46. The main points made by respondents were:

a. **Interface with other legislation:** respondents noted the potential overlap with other Commission initiatives such as the Consumer Rights Directive which has not yet come in to force. Legal representatives noted that CESL would need to be supplemented with national laws as important issues, such as the passing of title, were not dealt with by the draft Regulation. This they felt would lead to additional cost and complication.

b. **Inclusion of digital content:** A number of respondents were pleased to see that digital content had been considered but were unsatisfied by the result. Business respondents noted that the current position between consumer rights and digital content was unclear. It was noted that digital content had been added to the draft proposal late in the drafting process. Respondents disagreed with the use of an optional instrument and argued for a consolidated approach towards digital content. They questioned whether inclusion of digital content in CESL would deliver the benefits suggested. A few respondents thought that a separate digital directive might be a better way of dealing with digital content than the CESL.

c. **Treatment of specific sectors:** Respondents from specific sectors were broadly pleased that their own areas had not been included in the Regulation, for example consumer credit. The focus of concern centred on whether or not certain types of contract, e.g. construction contracts, were within scope, and what "mixed purpose contract" defined in Article 6 actually covers. This would cause confusion for customers and result in significant levels of legal uncertainty.

Q4(b). What are your views on the proposed scope of the draft Regulation, including: the availability for distance, off-premises and on-premises contracts?

47. **11 of 43 respondents** answered Question 4(b) directly. All respondents to this question recognised that the greatest potential for the proposal lay in distance (online) contracts and the majority felt that if this proposal was taken forward it should specifically be limited to online, cross-border trade.

48. Respondents identified a number of practical difficulties with the scope available for distance (internet), off-premises (telephone, mail order and door-step selling) and on-premises (shops) contracts:

a. **Online contracts:** Small business organisations recognised that it may be easier for those implementing and using CESL to only apply it to online cross-border trade. However they were also concerned that this would create a difficult separation between online and off-line trade. A business respondent was clear that the proposal should only apply to online trade describing it as *"unnecessary and illogical for off-premises contracts."* On balance, the majority of business respondents felt that on-line was the most practical application for any prospective instrument.

b. **Practical implications:** Respondents felt the broad scope of the proposal was impractical, particularly in its awkward application to telephone sales and in terms of providing the other party with pre-contractual information. In practice this would be time-consuming and cumbersome for both the trader and consumer. The implications for the validity of the contract, if a form remained unsigned, was unclear. Nor was the Regulation felt suitable for off-premises contracts as consumers could become increasingly vulnerable to aggressive selling practices (and there would be no adequate safeguards for mis-selling). This could have the effect of limiting Member States ability to effectively target problem selling (such as aggressive doorstep selling). Consumer protection could therefore be significantly reduced in this area.

c. **Confusion of multiple regimes:** Many respondents highlighted the difficulties of operating different regimes for domestic and cross-border trade for off-premises and on-premises sales. Confusion could increase if a retailer were operating different contractual rules for domestic consumers on and offline from those in other Member States. This would undoubtedly result in increased costs for businesses because they would be operating two legal regimes in parallel. It may therefore be better if the Regulation were only applicable to online distance selling.

Q4(c). What are your views on the proposed scope of the draft Regulation, including: the limitation of the draft Regulation to cross-border contracts?

49. **16 of 43 respondents** answered Question 4(c) directly. A significant majority of the total respondents sought to ensure the proposal was not extended beyond consideration of cross-border contracts. The lack of a sufficient evidence base was the main reason for this argument, as well a lack of practical experience of the Consumer Rights Directive, which has not yet been implemented.

50. **10 of 16 direct respondents believed that CESL should be limited to cross-border sales only**, and were not in favour of extending it to domestic contracts. Respondents argued there was no need to extend the proposal to domestic contracts as national law currently dealt sufficiently with such trade and was an area that should be left to Member States to deal with. Any extension to domestic contracts was felt to be a matter for national Government to address. There was some support for restricting the Regulation to cross-border sales for now but to consider, at a later stage subject to a review of whether the instrument worked in practice, whether its extension was feasible.

51. **6 of 16 direct respondents believed that CESL should be available for domestic use**. An optional instrument on contract law would have the benefit of enabling businesses to offer one set of terms and conditions for all sales for both domestic and cross-border trade rather than two separate regimes. It could have the advantage of decreasing costs and uncertainty and resolve the issue of a consumer's residence for internet sale purposes.

Q4(d) What are your views on the proposed scope of the draft Regulation, including: the requirement that at least one party to a business-to-business contract must be an SME?

52. **16 of 43 respondents** responded directly to this question. All of those felt that the requirement that at least one party to a B2B contract must be an SME was impractical, unworkable or undesirable. A number of those that did not respond to this question directly made the same points in their narrative responses. There was no support for limiting this proposal to SMEs.

53. Overall, the main concern centred on the practical problems resulting from applying the SME test. It was unclear how this would work in practice, particularly in the case where the status of an SME changed during the course of a contract. There was considerable opposition to this aspect of the proposal.

54. In addition, a number of respondents considered that CESL was inappropriate in B2B transactions as it would interfere with the freedom to contract, which is the freedom of individuals and corporations to form contracts without Government restrictions. These respondents considered that B2B contracts should be removed from the scope of the instrument as the Commission had not demonstrated a need to resolve problems in this area.

Q5. The proposed Regulation purports to be a "stand alone" code of contract law rules. Does the proposal achieve this objective? Is there anything currently excluded that ought to be brought in to scope or is there anything that ought to be removed?

55. **22 of 43 respondents** responded directly to Question 5. All 22 respondents believed that the proposed Regulation did not achieve its objective of being a "stand alone" code of contract law.

56. Respondents stated that the proposal did not cover all aspects of a contractual relationship. Some were concerned that it may not cover sufficient areas to be a real alternative to national law and that it would be necessary to have recourse to both CESL and national law. Others commented that some issues may arise in the context of disputes which are not covered by CESL.

57. Responses, generally those critical of the proposal more widely, argued that businesses would still have to take advice on other, non contractual, aspects of the law for each Member State into which they intended to expand, for example, advertising, labelling and tax - all matters of regulation under the local law of the Member State in question. These of course are matters that no contractual code could include but nevertheless businesses will continue to need legal advice on these areas. Respondents were clear that the Commission were not accurate in presenting this proposal as a "stand alone" code.

58. Regardless of their views on the proposal more generally, all respondents identified relevant and potentially important areas which were not covered by CESL. Many responses referred to Recital 27 of the Regulation, which sets out a list of areas not covered by the Regulation. These specific areas will be governed by existing national law.

59. Those areas of law not covered by CESL and of most concern to respondents included: transfer of ownership, which could become extremely important in cases of cross border bankruptcy, illegality and capacity. These are important issues. A key element of consumer confidence in shopping across borders relates to confidence in the receipt of goods paid for, and so the rules on transfer of ownership in sales situations matter when a trader goes bankrupt before the item is received. Equally, illegality and capacity, although areas which are sensitive in the individual legal cultures of Member States, are important because each goes to the heart of the validity of a sales contract.

60. The role of the Rome I Regulation (which governs the choice of law applying to the contract) also featured in several responses. Some respondents expressed concern about how Rome I and CESL would interact. Some thought that using national laws under Rome I to fill in the gaps in CESL was likely to be complex and might not be possible without amending Rome I itself.

61. Despite the majority of responses identifying at least some of these gaps, very few respondents offered a view on whether they should be included or whether there were other areas currently covered that should be removed.

The Content of the Common European Sales Law

BUSINESS-TO-BUSINESS

Q6. Will the proposal, as drafted, provide benefits for businesses, particularly SMEs, wishing to sell to consumers in other Member States? Please give reasons for your answer.

62. **23 of 43 respondents** responded directly to Question 6.

63. **8 respondents** believed that the proposal would provide benefits for businesses, whilst the majority (15 respondents) believed it would not.

64. There was a mixed response to this question in all sectors, but the majority of respondents thought that the costs to businesses would outweigh the benefits identified. Some respondents who were positive about the benefits of CESL for businesses also recognised that there were changes they would like to see made to the proposal.

65. The main benefits identified by those who thought the proposal would be good for businesses were:

- **Solution to problems with Rome I.** Several respondents thought that one of the main benefits for businesses would be the resolution of problems with minimum harmonisation in consumer law.

- **A single set of contract law rules.** Most respondents thought that a single set of contract law rules would be of some benefit to business, in terms of certainty and reduced costs for legal advice in each Member State. Whilst some responses recognised that other barriers to cross border trade exist, it was also considered that addressing contract law divergence was, at least, a start.

- **An air of legitimacy or trust.** A number of responses suggested that CESL could become a set of rules that consumers would become familiar with. This may help extend an air of legitimacy to companies, particularly start-ups and SMEs, helping them to gain the trust of consumers thereby increasing their sales.

66. Respondents who did not believe that the CESL would provide benefits for business, or that the costs associated with the proposal outweighed any benefits, made the following main points:

- **Contract law is not the main barrier to cross-border trade.** Many respondents questioned the size of the impact a common sales law would have in reality, since there were many other barriers which would still exist and which played a larger part in a company's decision not to expand across borders. Other barriers identified included language, variations in taxation and VAT rates, differing technical and labelling requirements and logistical issues. It was also important to note that many barriers to international trade relate to a firm's capacity and capabilities.

- **CESL does not cover all aspects of sales law.** Several respondents raised this as one of the main problems with CESL, arguing that as a number of areas were not covered by it, traders would still need to be aware of, or take legal advice on the laws in each Member State. Some felt that this undermined the aim of the proposal to reduce costs for businesses and only served in adding a further layer of complexity.

- **An additional, optional regime adds another layer of complexity and uncertainty.** Many responses made it clear that businesses value certainty, but in contrast to those who thought that CESL would simplify divergent contract laws by providing a single set of rules, the majority of respondents who addressed this question thought that it would create more confusion and uncertainty. Some argued that the optionality of CESL would mean that businesses would have to spend money on advice in order to determine which regime was more beneficial to their business. This advice would have to be ongoing to keep up as case law developed, which would be a significant cost burden for businesses.

BUSINESS TO CONSUMER

Q7. Does the proposal, as drafted, provide an appropriate level of consumer protection – is set too low or too high? Are there any particular changes you would like to see made?

67. **22 of 43 respondents** responded directly to Question 7.

68. **17 respondents** thought that the level of consumer protection provided by CESL was inappropriate.

69. **5 respondents** viewed the level of consumer protection as appropriate. These respondents thought the provisions generally provided a high level of consumer protection whilst striking an appropriate balance between the interests of consumers and businesses.

70. Amongst the respondents who thought the level inappropriate there was a split between those that thought the level of consumer protection was too high and those who thought it too low. Slightly more respondents were of the view that CESL did not provide a high enough level of consumer protection whilst a number of business respondents commented that the level of protection was disproportionately high and would impose unreasonable burdens on business. This would make using CESL unattractive for businesses. A small number of those who thought the level to be inappropriate commented that the grounds of protection provided to consumers were inconsistent. Many of the respondents who thought that the level of protection was inappropriate also commented that the provisions were complex and would lead to confusion and uncertainty.

71. One particular area of concern for respondents who found the level of protection inappropriate (both those who thought it too high and those who thought it too low) were the provisions relating to consumer remedies for non-conformity. Concerns here centred on the 10 year termination period for non-conformity (which was regarded as too long) and the uncertainties and reduction in consumer protection created by the provisions on payment for use when goods do not conform. Those respondents who thought that the level of protection was too low were also concerned that the proposed two year limitation period was too short and the non-availability of damages for inconvenience or distress would disadvantage consumers.

72. Many respondents commented that they would like the detail of the provisions to be amended during negotiations to address their concerns. Some consumer organisation respondents stated that they were concerned that the level of protection provided would be reduced during negotiations to address business concerns. Some business respondents commented that although they thought the current provisions provided an appropriate level of consumer protection they would not like to see that level increased further during negotiations.

Q8. What do you believe will be the impact on UK consumers if the Common European Sales Law is available for cross-border business-to-consumer contracts?

73. **30 of 43 respondents** responded directly to Question 8.

74. **21 respondents** thought that the impact would be negative and 9 thought it would be positive.

75. Those who thought the impact would be positive pointed to the potential for CESL to increase the choice of goods available (through cross-border offers) as well as the possibly of lower prices for UK consumers. It was also suggested that CESL would make it easier to provide advice to consumers on cross-border shopping.

76. Conversely a number of respondents thought that the impact on UK consumers would be negative, suggesting that CESL may in fact deter consumers and lower confidence in shopping across borders. One respondent stated that as UK consumers generally have a wide choice of goods available at reasonable prices there is unlikely to be a significant increase in B2C cross-border trade as a result of the Regulation.

77. The main reasons given by respondents who thought that the CESL would have a negative impact were:

- confusion, complexity and uncertainty for consumers;
- a reduction in consumer protection as consumers would no longer benefit from the protection provided by Article 6(2), Rome I; and
- consumers would not have a choice as to whether to contract under CESL or national law as the choice of law would be determined by the business.

78. Other concerns included the potential to increase burdens on advice and enforcement agencies as they would need to understand, provide advice on and enforce both national law and CESL provisions. A number of consumer organisations were concerned that CESL would ultimately be used in domestic contracts (either through an extension of scope or because it would be impossible to prevent in practice) which would undermine domestic consumer protections.

79. A small number of respondents thought that any impact on consumers would be minimal as it would depend on the extent to which businesses would use CESL. In addition, as consumers tend not to read terms and conditions before entering into a contract, it is unlikely that they would be in a position to conclude whether CESL offered them a better prospect than their own national contract law (in terms of protections, remedies etc).

DIGITAL CONTENT

Q9. Do you support the approach taken towards digital content in the Common European Sales Law, including the use of a specific digital content category, the scope of digital content covered and the application of rights and remedies that are identical to those for goods? Please give reasons.

80. **16 of 43 respondents** responded directly to Question 9.

81. **8 respondents** by and large supported the approach taken towards digital content in CESL. Although these respondents agreed to the approach taken, the majority thought that an optional instrument was not the right instrument by which to do this.

82. Key strengths and opportunities identified:

- **Classification/definition of digital content**. Respondents thought that the introduction of a digital content category, with a broad definition, would help address the current uncertainty as to the classification of digital content as either a good or a service.

- **Clarification of rights and remedies for digital content.** Respondents noted that this was an unclear and uncertain area of the law. The steps taken to clarify the position for digital content, particularly the rights and remedies available to consumers, was welcomed.

- **Rights and Remedies akin to those available for goods.** Some respondents commented that they supported the CESL approach of applying rights and remedies for digital content similar to those available for goods.

- **A tool/foundation for further legislation**: Some respondents felt that although the proposals may be of limited use as an optional instrument, they could form the basis for further European legislation in future.

83. **8 respondents** disagreed with the approach taken towards digital content in CESL.

84. Key weaknesses and threats identified:

a. **Optional nature of the instrument.** Respondents felt that such an important area of the law should not be addressed in an optional instrument. They doubted whether businesses would opt to use CESL as it would provide stronger rights for consumers than current legislation. Two respondents suggested that a stand alone directive on digital content would be better.

b. **Piecemeal approach.** Respondents argued that addressing consumer rights and digital content required a consolidated approach and that CESL failed to deliver this. These respondents asked that consumer rights in relation to digital content be considered alongside other areas, such as copyright law, data privacy, payment methods, online security etc.

c. **Not appropriate for digital content.** Many respondents felt that CESL did not adequately address the unique nature of digital content. Some respondents thought that a sales law was not a suitable vehicle for digital content contracts because they frequently involve the granting of an intellectual property license rather than rights equivalent to ownership.

d. **Legal uncertainty.** Respondents were unclear as to how some proposals would apply and how they would work in practice. One respondent raised concern around the proposed 'related services' category and what this included. Another thought that a separate category for digital content would sit unhappily with definitions elsewhere in the EU acquis, e.g. in the VAT Directive, where e-books are defined as a service.

Impact Assessment

Background

85. The Government's view was that the introduction of CESL could potentially have a significant effect on various groups in the UK. As a result, the Call for Evidence exercise sought to identify, and where possible quantify, what the economic impact might be and how the UK might be affected overall. It was considered that the potential impact of CESL could be huge as it could attract widespread use. In cross-border contracts alone, it could cover contracts worth billions. UK trade with the EU is currently worth approximately £28.9billion; EU imports amount to some £17.1 billion, with UK exports to the EU amounting to a further £11.8 billion[8].

86. Even if the proposal were limited to cross-border consumer contracts the impact could be significant, particularly if businesses elected to use the new instrument. In 2011 approximately 64% of UK adults (40 million people) bought goods or services online[9]. Collectively they spent around £50 billion on goods and travel. UK consumers tend to spend more on domestic online purchases (1,093 Euro over the last 12 months) but less on cross-border purchases (664 Euro) than the average EU online shopper (939 Euro and 693 Euros)[10] The European Commission estimates that for Europe as a whole about 9.5% of on-line consumer sales are cross-border purchases[11].

Assessment of impact

Q10. What, in your view, would be the impact of the Common European Sales Law? We are interested to hear from all affected sectors; consumers, business, advisory groups and the legal sector.

87. **35 of 43 respondents** commented directly on Question 10.

[8] HMRC EU Overseas Trade Statistics – July 2012
[9] Office of National Statistics – Briefing Note – Internet usage in households by individuals – How the UK compares with the rest of the EU – 18 April 2012
[10] Statistics extracted from Consumer Market Study on the functioning of e-commerce and internet marketing and selling techniques in the retail of goods – Civic Consulting – Sept 2011
[11] SEC(2011)1165 final

88. **4 respondents** believed CESL would have a positive impact, the main reasons given were as follows:

- it would **facilitate cross-border trade and reduce certain costs** for businesses, particularly the costs associated with obtaining legal advice on the rules applicable to trading in foreign markets. One respondent suggests that 76% of businesses could achieve cost savings using a single European contract law, savings estimated in the range between 5,000-30,000 Euros [per business].

- it would **enable online retailers to target more markets**; and

- it would have the benefit of **attracting new work for law firms** through the need for legal advice and services although in terms of growth in this area it was not quantifiable.

89. **31 respondents** believed CESL would have a negative impact, the main reasons given were as follows:

- it could **create significant legal uncertainty** which would **increase the need for businesses to seek legal advice**, thereby incurring transaction costs. The costs of seeking this advice could be passed on to consumers in terms of the cost of the goods they procure. The costs associated with this were not quantifiable.

- the **training costs** (both one off and ongoing) that would be **incurred by practitioners, the judiciary, businesses and advice** services. There is doubt that the impact of these costs has been sufficiently taken into account by the Commission. It was suggested by one respondent that the cost of training per lawyer is likely to equate to Euro 2500 rather than the Euro 1400 estimated by the Commission;

- the **optional nature of the instrument** was **unlikely to aid or encourage real growth**. It was cumbersome to use, was likely to be of limited use to businesses or consumers, with the negative impacts seeming to far outweigh any benefits. It was also suggested that this could lead to a decrease in competition. Costs here were not quantifiable.

- could lead to the **fragmentation of consumer protection.** The impact here was likely to accrue costs because of the uncertainty being created.

- the problems and **delays resulting from any expansion of the Court of Justice of the EU** in introducing a new legal system and the costs associated with this. This was not readily quantifiable.

Q11. Do you believe it would provide the benefits identified in the Commission's Impact Assessment?

90. **35 of 43 respondents** responded directly to Question 11.

91. **4 respondents** believed CESL would have the positive benefit presumed by the Commission, the main reasons given in support of this view were:

- **trading under a single law** would prove more useful **as** well as being beneficial to the Single Market. It was suggested by one respondent that if the statistics provided by the Commission realised even a fraction of that estimated then there was a strong case for supporting the instrument; and

- **the potential to boost online cross border trade.** It was suggested that the operation of a single contract law across borders would improve trade in this area as it would overcome one of the barriers to trade. This was not quantified.

92. **31** respondents answering this question directly were of the view that CESL would not provide the benefits identified in the Commission's Impact Assessment. The main reasons given were as follows:

a. **contract law was not felt to be the main barrier to trade**. Other factors such as tax, delivery, language were felt to be more problematic. Some respondents stated that the case for need for an optional instrument had been overstressed and the evidence provided in support did not appear to deliver the benefits suggested in the Commission's Impact Assessment.

b. the **reduction in costs was likely to be significantly less** than presumed by the Commission. Some respondents felt that it was unlikely that costs would reduce. Nor was it felt that burdens on traders would decrease. Indeed, some respondents felt the introduction of CESL would increase/attract costs through the need to litigate and this would only succeed in hampering growth. These points were unquantifiable.

c. there are **a number of methodological inefficiencies.** Assumptions had been made that CESL would be used and that all cross border trade would be additional trade. In addition a number of aspects had not been taken into account in terms of costs, for example communication costs, information and compliance costs, legal operation costs and training costs. Nor were the costs associated with the need to continue to investigate foreign laws, obtain translations etc. This would affect the cost savings presumed by the Commission.

d. it would be **more prudent to raise awareness of how to trade across borders**. This would be of more benefit to both traders and consumers and could be achieved in a more cost-effective manner. The introduction of CESL will not ensure uniformity of the rules that will apply nor will it necessarily create choice, reduce procedures or create stronger rules on consumer protection.

Q12. Do you have any views on changes that could be made to the proposal to increase its potential benefits for the UK?

93. **23 of 43 respondents** answered Question 12 directly.

94. It is apparent from the responses received that there is not a coherent position on how best the proposal can be amended to increase its benefits to the UK. Those in favour and opposed to the proposal took opposing views on the same issues, particularly on scope where some felt the benefits would be increased by a wider scope, though a much larger number felt it would be improved by a narrower scope.

95. There were some common themes emerging in response to this question, which included the need to:

- **clarify the applicability/effect of Rome I**, particularly Article 6(2);
- **resolve the different levels of consumer protection**. One respondent suggested that the consumer protection provisions be superimposed into national law. Another suggested that consumer provisions should be tailored to sit more easily alongside the Consumer Rights Directive.
- **alter the scope**; a small number felt a wider scope would be beneficial but the majority believed a narrower scope was required. Variations of this were suggested:
  - it should be limited to cross-border online transactions or apply to digital content only matters in B2C contracts;
  - Small and Medium Enterprises (SMEs) should be able to contract with other SMEs as this could assist in their growth; and
  - it should be restricted to B2C contracts; B2B contracts should be removed from scope and;

- those who felt the scope could in fact be wider suggested that in future the proposal could be extended to include **provisions on mixed used contracts, capacity/validity, advertising and product liability**.

- **increase certainty for contracting parties**. Apart from the general uncertainty surrounding a number of the provisions, full consideration appeared not to have been given to the fact that parties to a contract may have their disputes settled in courts where their counterparties are living. Nor had consideration been given to the fact that legal advice on national law would still be required. In addition, the proposed database of decisions failed to take into account that decisions of one Member State would not be binding on another. The impact here had not been assessed.

- **clarifying the responsibility for interpretation of CESL.** Further assessment was also needed on the impact on the Court of Justice of the EU. The limited number of cases predicted by the Commission seemed implausible.

96. Some respondents also suggested **returning to the idea of a non-binding toolbox** of definitions and principles of contract rather than a legislative measure. One respondent also suggested it may be better to **develop best practice codes which set a world standard** for specific areas of industry.

Government Response to Part I

97. The Government is particularly grateful to respondents to this Call for Evidence for their detailed and constructive responses. It notes that there is not a unified response to the questions of principle, scope and content for CESL. This reflects the challenge facing the European Commission and Member States in the negotiation of this proposal.

98. The Government strongly encourages the Commission to reconsider the current basis for and scope of this proposal, which seems highly unlikely to deliver its aims. Whilst a small minority of respondents expressed some interest in the proposal, 31 of 43 respondents believed that the proposal could not achieve its intended outcomes and that its impact would in fact be negative.

99. The responses to the questions regarding the scope of the proposal in particular demonstrate that there are considerably mixed opinions across, and within, different sectors as to what is the most appropriate scope for this proposal. It is however clear that the majority of respondents do not believe that the present scope of the proposal is right.

100. Respondents were clear, and the Government agrees, that there is insufficient evidence of need for the Commons European Sales Law proposal as presently drafted. It again encourages the Commission to reflect upon how it is seeking to achieve its objectives of increased cross-border trade and growth, objectives which the UK Government strongly supports.

101. The Government agrees with the significant majority of respondents who were clear that the proposal should remain restricted to cross-border contracts, if indeed the proposal is to proceed. The Government has no ambition to amend the arrangements for domestic law in this area beyond what it is already contemplating in its proposed Consumer Bill of Rights and would not support an extension of CESL to domestic contracts.

102. The Government acknowledges the current lack of clarity in the law in relation to consumer rights for digital content but agrees with the majority of respondents that an optional CESL is not the right instrument by which to address this. The Government has put forward proposals to clarify consumer rights for digital content in the UK in its Consultation on the Supply of Goods, Services and Digital Content, published on 13 July and open until 5 October.

PART II

Assessing the Commission's Proposal: Annex I

Legal Assessment

103. The European Commission claim that their proposal does not aim to replace existing national laws, but would act as an alternative optional regime to the existing contract law regimes in each Member State. The Government's Call for Evidence sought views on the likely impact of the provisions, particularly in terms of whether they were likely to deliver the benefits presumed for consumers, businesses and other sectors.

104. Respondents from a wide range of sectors have provided views and evidence on:

- whether the provisions provide sufficient legal certainty and clarity;
- whether it is clear as to which provisions are mandatory or not; and
- whether the provisions strike the right balance between fairness and certainty.

105. Opinion was also invited on whether any specific provisions were problematic. This is discussed further at paragraph 120.

106. The engagement and level of interest in responding to Question 13 has been significant, as has the level of information and detail provided.

Q13 (a) Do you feel the provisions provide sufficient clarity and legal certainty? If not, why not, and how could the provisions be improved in this regard?

107. **35 respondents** commented on this question in total.

108. **2 respondents believed** that CESL **did provide sufficient clarity and legal certainty**. One respondent commented that uncertainty was unavoidable in any new law and that this in itself should not pose significant concerns. Uncertainty currently existed for business exposed

109. **33 respondents believed** that CESL **did not provide sufficient clarity or legal certainty.** Most respondents expressed concern about the over-complicated nature of the Regulation, the lack of legal certainty resulting from a number of the provisions, its interaction with other EU law as well as national law, the risks associated with using CESL, the likelihood of increased costs in terms of the need to seek legal advice, delays in litigation etc. One respondent suggested that CESL, rather than resolve barriers to trade, was likely to create new barriers.

110. In terms of the Regulation and the Annex, focus from respondents centred mainly on CESL:

- **not being a complete code of contract law.** A number of respondents commented that not all aspects of contractual relationships were covered (for example, capacity, illegality, intellectual property laws and whether contractual and non-contractual liability could be pursued in tandem).

- its **possible extension** from cross-border sales **to domestic sales.** A number of respondents expressed concern about this possibility. This was felt to be a matter for national Governments to decide.

- it was **unworkable for certain types of sales contract**, for example telephone sales;

- its **interaction with other laws** (specifically Rome I, national laws and the consumer acquis);

- **the lack of certainty on whether a contract is valid or not** and which law applies to the choice. For example, what would happen if no choice of applicable law was made?

- **the difficulty in assessing whether certain types of contracts are covered.** For example, it is difficult to ascertain what contracts are excluded by Article 6, dealing with “mixed purpose” contracts. Equally, it will not be easy to determine whether a business is an SME or not (particularly given the definition in Article 7 of the Regulation);

- **the difficulty in the application of good faith and fair** dealing and the uncertainty stemming from its interaction with other provisions.

- **undermining consumer protections,** particularly in terms of the right to terminate, damages for distress and inconvenience and the potential to undermine a Member State's ability to tackle particular abuses such as aggressive selling tactics; and

- **the uncertainty posed by a number of provisions in terms of how they will apply in practice**, for example, various provisions seem to enable a court to effectively rewrite the contract; and the fact that contract terms may be implied or derived from certain pre-contractual statements etc.

Q13 (b) Is it sufficiently clear whether a provision is or is not mandatory?

111. **17 of 43 respondents** answered Question 13(b) directly.

112. **4 respondents** believed it was clear which provisions were mandatory, albeit that one respondent commented that navigation of the instrument could be made easier. Another respondent commented that as the provisions would be used by legal professionals their mandatory nature or otherwise could easily be followed.

113. **13 respondents** stated that it was not clear which provisions were mandatory and which were not. The main reasons given in support of this view were:

- it was **unclear whether provisions could be deviated from/excluded** and whether they applied to both B2B and B2C contracts or not. Greater clarity was needed on the structure;

- **the number of provisions which parties** can choose to **exclude should be kept to a minimum;** and

- **the mandatory nature** was ambiguous from a consumer perspective.

Q13 (c) Do you feel that the provisions strike an appropriate balance between considerations of "fairness" when things go wrong, and providing sufficient certainty to contracting parties that what they have agreed will be upheld? If not, how could the provisions be improved?

114. **25 of 43 respondents** responded directly to Question 13(c).

115. **6 respondents believed** the right balance had been struck between fairness and certainty. One academic respondent from academia argued that provisions reflecting the value of "fairness" were not only relevant when things go wrong but helped to put them right. Contracting parties want to operate in a culture where the expectation is that they will behave fairly and reasonably. This culture can be reinforced by appropriate legal rules. Another respondent, although agreeing that an appropriate balance had been struck between fairness and certainty believed that the terms of CESL may not be easy for a consumer to understand and suggested plainer language be used. Comment was also made that many SMEs are risk adverse and it was highly likely that many would want to have the protection offered by the mandatory rules in CESL, particularly where terms that were not negotiated were unfair. CESL would achieve this aim.

116. **19 respondents** disagreed that balance had been achieved between fairness and certainty. The main reasons given were:

- **the concept of good faith and fair dealing.** A number of respondents comment that:
  - there was no clear definition of good faith and fair dealing; and
  - it would become burdensome to business because businesses could not predict their contractual obligations nor those of the other party.
- **fairness seems to have been prioritised over certainty.** This may be appropriate in B2C matters but not in B2B. Freedom of contract is fundamental in B2B contracts. Article 2 is at odds with the nature of commercial contracts whereby parties effectively apportion risk in the event of breach.
- **Consumer protection levels are too high in some areas where as some are insufficient.** Some respondents were concerned about the extended periods during which a consumer might have a right to reject. Others were concerned about the allowance for use provisions and the effect of the novel imposition of a duty of good faith on a consumer.

Q13 (d) Are there any provisions that give rise to particular concerns, and why?

117. **31 of 43 respondents** answered Question 13(d) directly. Respondents provided a wide range of provisions that raised particular concern and would require further attention and consideration.

118. **1 respondent** did not believe there were any provisions which posed significant concern, the main reason being that CESL was not designed to solve every problem associated with cross-border trading. Language issues, for example, would still be problematic. CESL nevertheless offered a step in the right direction.

119. **30 respondents** believed there were provisions that gave rise to concern. These areas can broadly be grouped as follows:

General concerns

120. Underpinning many of the responses was a concern that the proposal does not meet the needs of the various sectors it covers. The proposal attempts to apply the approach of existing EU consumer protection law to commercial situations and the sale of digital content. As one legal respondent put it,

> "*B2B contract law is fundamentally different from B2C law. B2C contract law is primarily a matter of regulation….B2B law is primarily concerned with freedom of contract."*

The application of the duty of good faith

121. Article 2 is of general application and has two specific effects. Firstly, breach may limit the ability of the party to rely on rights, remedies and defences which he or she otherwise would have. Secondly, breach of Article 2 is in itself an independent basis of liability regardless of the other provisions of the contract.

122. Respondents raised considerable concerns about this provision, in particular that:

    a. it is uncertain and unpredictable in its effect, given the width of the concept. Little guidance is, however, given on how it should apply. This is likely to lead to divergent interpretations in 27 Member States and one respondent at least thought that it would be impossible for the Court of Justice of the EU to comprehensively define it so as to control that divergence;

b. despite the assertion of the principle of freedom of contract in Article 1, Article 2 undermines the contractual agreement of the parties, making reliance upon what has been agreed and the remedies they otherwise have unpredictable;

c. it imports considerable scope for argument between the parties about whether each acted in good faith, which benefits neither.

An imbalanced approach to addressing specific abuses

123. Some respondents expressed concerns regarding the treatment of mistake and fraud (Articles 48 and 49), which were felt to impose insufficient obligations on a party to protect his or her own interests, and unnecessarily wide duties on the other party to do so on his/her behalf. A number of respondents were particularly concerned about Article 51. This provision would relieve a party of his or her contractual obligations where he or she had "urgent needs", was "improvident" or "ignorant". English law protects a party against "unconscionable bargains" but the proposal goes much further. Respondents were anxious that Article 51 unfairly disadvantages a party who is knowledgeable, or well advised. One business respondent indicated that the provision invites judicial control of a "fair price", something that not even existing unfair terms control does, and makes *"a significant inroad into the basic commercial principle that a vendor is entitled to demand the best price which is supported by the demand for his product".* It was suggested that the provision was entirely unsuitable for B2B transactions, and should be treated with extreme caution for consumer contracts.

The difficulty in working out when the proposal applies

124. Respondents also raised the difficulty of establishing when the proposal would apply to a specific case. There were a number of circumstances that could lead to an apparently invalid choice of CESL, for example, misapplying Article 4 (cross border requirement) or Article 6 (mixed purpose contracts) on the facts of the case, or the complexity and impracticability of trying to establish whether one of two businesses is an SME so that CESL can be used (Article 7). Equally, the agreement to use CESL could itself lead to an invalid choice, for example the difficulty of applying the provisions of Articles 8 and 9 to a consumer contract made by telephone.

125. Finally, some respondents had concerns about the relationship between the Rome I instrument and the CESL, in particular in the absence of any amendment to Rome I in the light of the CESL. A particular problem was raised by two respondents. If the availability of CESL enables parties to opt out of national rules which are mandatory in national law, did that then in fact strip the national rules of their mandatory nature, because they could actually be avoided by choosing CESL?

Business to consumer contracts

126. Particular issues identified by respondents included a reduction of consumer protection compared to UK laws:

    a. Consumer's right to reject. Article 114 was seen as a reduction of consumer protection compared to UK laws, under which the consumer has an absolute right to reject. Under the proposal, that right to reject is lost for minor non-conformity.

    b. Good faith duties imposed on consumers. The imposition of the good faith duties on consumers in Article 2 is novel. There was concern that this could be abused by unscrupulous traders to delay resolution and to deter consumers from obtaining a remedy, for example by disputing allowance for use.

    c. The proposal does not permit damages to be awarded for distress or disappointment.

127. Businesses could be disadvantaged by the apparently extensive period of time for rejection (Article 119), whilst extended arguments over the application of the good faith principle (Article 2), the time for rejection and the allowance for use were not likely to benefit either party.

Business to business contracts

128. In addition to concern about the suitability of the duty of good faith to the essentially competitive nature of commercial contract negotiation, there were other significant concerns about whether the proposal was suitable for commercial contracts.

129. Freedom of contract is undermined. A commercial contract is a means by which parties apportion risk, making the consequences of breach predictable. Article 1 states the principle of freedom of contract, but this is heavily undermined by various provisions which restrict the ability of the parties to rely on the agreed terms, and which give the court wide powers to rewrite their bargain.

130. Concerns raised by respondents included that:

    a. where the parties' standard terms conflict, only those common in substance form part of the contract, leading to potential gaps and imbalances in the content of the contract, which is then likely to be quite different to what either party anticipated (Article 39);

    b. the interpretation provisions of chapter 6 and the "content" provisions of chapter 7 raise uncertainty by providing too little emphasis on what has been agreed in writing and allowing too much exploration of the circumstances surrounding conclusion of the contract;

c. Article 70 excludes “not individually negotiated terms” which have not been brought sufficiently to the attention of the other party, regardless of whether they are substantively unfair;

d. Article 89 effectively allows the court to rewrite the parties’ bargain in the event of a change of circumstances, and the requirement to renegotiate the bargain in such an event is unlikely to appeal to businesses, especially when an urgent solution may be required.

131. The uncertainty that these and other provisions raise regarding the ability of parties to rely on their contract terms was considered likely to lead to the court effectively deciding for them what their bargain was with the benefit of hindsight. Such uncertainty was also likely to increase the costs of litigation.

132. Some respondents were particularly concerned about the treatment of standard terms in the proposal. Standard terms can be very commercially efficient. They are often industry standard terms, negotiated by trade bodies, and well understood. This makes them predictable and reliable. The proposal seems to assume that they are automatically problematic, with harsh consequences (for example the rule in Article 70).

Technical Legal Advisory Committee

133. The Technical Legal Advisory Committee, chaired by Lord Mance, is a non-Statutory Committee established to provide technical legal advice to Ministry of Justice officials on the content of the proposed European Community Regulation for a Common European Sales Law. The Committee met four times between February and May 2012 and carried out a detailed examination of the legal content of the proposed Regulation with a view to identifying areas of difficulty. It was not the remit of the Committee to provide a view on the merits of the policy underpinning the proposal as a whole nor the Government’s policy response. It should be noted that the Committee primarily commented on the proposal from the point of view of English law rather than other UK laws.

134. The main concerns expressed by the Committee were as follows:

General concerns

a. **Duty of good faith and fair dealing**. Article 2 was felt to be a difficult provision as the concept of good faith and fair dealing was largely unknown in English law, particularly in B2B transactions. It did not therefore sit easily with the competitive nature of contractual negotiation. The Committee acknowledged that it was less of a concern in B2C contracts where the concept was more known in the existing acquis, although the imposition of a good faith duty on the consumer was novel, potentially open to abuse, and it was unclear how this might operate in practice. Article 2(2) posed a major concern because it introduced a free standing entitlement to damages, or stripped a party of rights, remedies and defences that he or she would otherwise be entitled to, based on the vague notion of good faith. The concept was novel, ill-defined and liable to abuse. It was unclear what this provision meant and what effects it would have on the application of other provisions within CESL.

b. **Interpretation provisions.** There appeared to be too little emphasis in Chapters 6 and 7 on what has been agreed in writing in terms of the parties' contractual obligations to assure certainty. There was too much focus on identifying the parties' obligations under the contract from extraneous circumstances and pre-contractual statements.

c. **Termination provisions.** These were felt to be complex and unclear. In particular, the extended right to reject for faulty goods would cause great uncertainty for traders, whilst consumers would not necessarily appreciate the allowance for use provisions which could lead to protracted disputes between them and the trader.

d. The provision on **unfair exploitation** (Article 51) provided too wide a basis for a party to avoid a contract by reference to "ignorance", "improvidence" and "urgent needs".

e. **Article 70** provides for "not individually negotiated terms" to be excluded without reference to their substantive unfairness if insufficient attempts have been made to draw attention to them.

Business to business contracts

f. **Trader's standard terms.** There was significant uncertainty surrounding the extent to which standard terms could be relied upon if CESL were used as the basis under which to contract. Where the parties' standard terms were in conflict, those common in substance between them would form part of the contract, whilst all other terms not common would be excluded. This could potentially lead to considerable gaps or an imbalance in contract terms. The terms could also be affected by the rules on merger clauses, the ready importation of pre-contractual statements as terms, usages and practices which can trump standard terms and the signature of the parties not being decisive in respect of incorporation of terms. The duty to raise awareness of standard terms was also extremely onerous, much more so than under current UK law.

g. **Unfair terms control in B2B contracts**. Article 86 relies on concepts of good faith and fair dealing and good commercial practice that are uncertain in their application. No protection is given to "individually negotiated terms".

h. **Change of circumstances.** In addition, the obligation on the parties to renegotiate a contract where there had been an exceptional change of circumstances raised significant uncertainty in that a court could rewrite the contract if the parties could not agree. This might be an entirely inappropriate approach in commercial cases where a predictable solution is often required urgently.

i. **Complexity in identifying the availability and agreement to use CESL.** The sheer complexity of applying CESL (particularly the way it was drafted in terms of its scope and structure) was likely to drive up trader costs and deter traders from using it. Traders would struggle to run separate legal regimes for cross border cases compared to domestic ones. Identifying whether CESL was available to contract under was also problematic. The Regulation was complex and had the potential to raise disputes and anomalies in the identification of what was a cross border contract, whether the other party was an SME or not, and whether the contract was mixed purpose. In addition, even if the parties agreed that CESL could be used, the agreement provisions were unworkable in practice.

Consumer contracts

j. It would be important that **consumer protections** were not reduced from their current level during the negotiations. The inclusion of the allowance for use provisions, the loss of the absolute right to reject, and the absence of damages for distress and loss of enjoyment represented a lower level of protection over English law.

k. **Unfair terms controls** in chapter 8 do not cover the core terms in consumer contracts (in particular the "main subject matter" of the contract, Article 80), and only cover the "not individually negotiated" terms (Article 83).

l. The Committee were **unconvinced that the consumer has a true choice** as to whether to contract under CESL or not, and did not feel that the (very cumbersome) provisions of Article 9 of the Regulation could provide properly informed choice. Moreover, a combination of these provisions and some specific provisions contained in Annex I, import significant uncertainty about the point in time that the sales contract would be subject to the provisions of the Sales Law.

Digital content

m. This was an area which was considered to be very significant. However, it **requires a bespoke approach** drawing on existing legal approaches but specifically tailor made to the particular problems which arise in this area. In particular, intellectual property considerations would be central to effective regulation of this area. An optional instrument covering such a topic was felt to be inappropriate.

Government response to Part II

100. The Government concludes that there are substantial elements of CESL which do not provide sufficient clarity or legal certainty. The instrument is:

- too complex,
- incomplete in parts (some significant aspects of a contractual relationship are not covered),
- unworkable for certain types of contract,
- uncertain, both as to whether a contract is valid or not and as to the certainty of its terms; and
- unclear on its applicability, in particular how its provisions interact with other EU law.

101. In other aspects the provisions are contradictory, for example by stating that a fundamental principle is freedom of contract but then including provisions that undermine that freedom in significant ways (by too readily including pre-contractual negotiations as terms, requiring renegotiation where there is a change in circumstances etc). The benefits claimed for its advertised simplicity are therefore unlikely to materialise.

102. The Government does not agree that an appropriate level of balance has been struck between fairness and certainty. The concept of good faith and fair dealing is problematic, particularly in terms of its relationship with the other provisions within the proposal. Fairness seems to have been prioritised over certainty and although this may be appropriate, within proper boundaries in B2C cases it does not follow in B2B contracts. Freedom of contract is a fundamental aspect in B2B contracts. The concept applied under the Regulation is at odds with commercial practice, interfering with a business being able to manage their risk with any certainty. In B2C contracts, the imposition of a wide ranging duty of good faith on consumers is equally likely to be abused or lead to protracted disputes.

103. A fundamental problem is the all-encompassing nature of the Regulation. It is too broad and does not serve in resolving the specific problems that B2B, B2C and digital sectors may have. It is difficult to see how a B2C aquis, which CESL creates, will work for B2B, particularly when the ethos here is contractual freedom. Consumer contracts are normally a matter of regulation. Businesses on the other hand rely on freedom to contract as it enables them to assess their risk in terms of the deal they are undertaking, its predictability and the obligations they have. A wide ranging and ill defined concept of good faith is inappropriate in B2B situations. In addition, CESL is ill-suited to some of the methods of sale covered. The Government views CESL as unworkable in some situations, notably in telephone sales.

104. Businesses need certainty in their contracts but CESL undermines this. There is doubt surrounding a number of its provisions, as well as doubt about its interaction with other EU laws and confusion surrounding the mechanics for its use. Added to this is the uncertainty regarding its applicability and when and whether it applies to certain contracts (e.g. if a contract was found to be mixed purpose or one party was wrongly identified as an SME etc). Definitions of "SME", "mixed purpose contract" and "cross border" will prove difficult to apply with confidence. This makes the instrument less certain and more open to litigation. This uncertainty has not been assessed nor properly taken into account by the Commission.

Conclusion

105. The Government concludes that CESL, as an overall proposal, is not well tailored to the wide scope of sectors and types of contracts it intends to cover. Although it aims to address the problems that contract law is presumed to cause in trading across borders, it presumes that each sector has the same problems when this is not necessarily the case. As a result, CESL strikes an inappropriate balance between certainty and fairness and does so without proper consideration that what may be appropriate in the consumer acquis may well be inappropriate in the B2B arena. The result is an unbalanced proposal which is overly complex, introduces confusion and legal uncertainty and is unclear on how it interacts with other relevant EU laws. As a result, the Government severely doubts the overall benefits and cost savings presumed by the Commission and believes a closer examination of the more significant problems hampering cross-border trade for various sectors needs to be examined separately. The UK Government stands ready to assist the Commission on this front.

106. The Government is particularly grateful to those respondents who took the time to consider the technical, legal implications of CESL and provided constructive and detailed responses. It is clear from these responses that there are aspects of the proposal that will require further detailed consideration. The Government would also specifically like to thank those who took time to participate in the Technical Legal Advisory Committee and will continue to utilise their advice and expertise in the future consideration of this proposal.

Full list of respondents to the Call for Evidence

Alistair McFadzean

Allen and Overy LLP

The Association of Her Majesty's District Judges

Bar Council of England and Wales

The Booksellers' Association

British Bankers Association (BBA)

British Exporters Association

British Retail Consortium

British Vehicle Rental and Licensing Association (BVRLA)

Citizens Advice Scotland

The City of London Law Society

The City of London Corporation

Clifford Chance LLP

COMBAR – The Commercial Bar Association

Commercial Court Users Committee

Consumer Credit Association (UK)

Consumer Council, Northern Ireland

Consumer Focus

Direct Marketing Association (UK) Limited

Dr Lorna Gillies, University of Leicester

Faculty of Advocates, Edinburgh

Federation of Small Businesses

The Grain and Feed Trade Association

Herbert Smith LLP

Home Retail Group

Ince & Co LLP

Interactive Media in Retail Group (IMRG)

Investment and Life Assurance Group

James Petts

Law Society of England and Wales

Law Society of Northern Ireland

Law Society of Scotland

National Franchised Dealers Association (NFDA)

Odeaya Uziahu-Santcroos

Office of Fair Trading

Professor Eric Clive, Edinburgh University

Professor Hugh Beale, University of Warwick

The Publishers Association

Scottish Court Service

Technology and Construction Solicitors Association

UK European Consumer Centre

Vodafone

Which?

Produced by the Ministry of Justice

Alternative format versions of this report are available on request from Jean.McMahon@justice.gsi.gov.uk