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The Use of the UNIDROIT Principles as Neutral Law in Arbitration

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This article discusses the use of the UNIDROIT Principles of International Commercial Contracts in international commercial arbitration. Because the Principles are designed specifically for cross-border commercial transactions, the use of the Principles avoids many of the legal rules that would govern from otherwise applicable domestic law that do not reflect the expectations of parties in international trade.

Key Words : UNIDROIT Principles, Arbitration, Applicable Law, Neutral Law, CISG

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I. Introduction

We may start with the question of whether lawyers seriously consider the issue of the operative substantive law when drafting the documents for aninternational commercial transaction. It is common wisdom when lawyers discuss this to assert that the substantive law is always a major consideration. Yet, a study of actual transactional documents and the disputes that arise in international commercial transactions suggest otherwise.

This may be due to a large extent to where the question of the substantive law fits within the list of concerns that counsel must address. The first and primary concern is always the substantive obligations of the parties. The second consideration is the question of regulatory and administrative requirements, such as customs and government mandated standards of quality and performance. Having dealt with these issues, which are the heart of the transactions, the issues of dispute resolution (choice of court or arbitration clause) and substantive law (choice of law) are secondary concerns that lawyers often do not address or address perfunctorily. To the extent that the parties use form contracts that provide for dispute resolution or choice of substantive law, the problem may be exacerbated because of the veneer of thoughtful choice when there is probably no real choice actually being made for the particular transaction.

It may be argued that the underlying substantive law may not be of great importance because parties usually are able to contract for specific terms and contract around otherwise applicable rules in the underlying substantive law. This is, of course, true to an extent. However, this assumes that the parties are able an anticipate the potential problems at the time of contracting and provide for these contingencies, and therefore do not need to rely on the default rules of the underlying substantive law. This would seem to be a risk that a lawyer thoughtful enough to negotiate the substantive obligations and the rules to govern these obligations would not want to take.

With this background in mind, I would like to examine the reasons why and the methods by which parties in arbitration might choose the UNIDROIT Principles of International Commercial Contracts (“Principles”) as the substantive

law for transactions or the part of transactions that come within the scope of the Principles.

Ⅱ. UNIDROIT and the Principles

The Principles are the product of the International Institute for the Unification of Private Law ("UNIDROIT").UNIDROIT is an independent intergovernmental organization with its seat in Rome. The purpose of UNIDROIT is to study the needs and the methods for modernizing and harmonizing private law, particularly commercial law, at the international level. UNIDROIT was created in 1926 as an auxiliary organ of the League of Nations. Following the demise of the League of Nations, UNIDROIT was reestablished in 1940 on the basis of a multilateral agreement. This agreement is known as the UNIDROIT Statute, and the membership of UNIDROIT is restricted to states that have acceded to the statute. There are presently sixty-three member states including the Republic of Korea.

The UNDROIT Governing Council approved the project to draft the contract's Principles in 1971, but a working group was not set up until 1980. The first set of the Principles was approved in 1994. These are composed of a Preamble and 119 articles divided into seven chapters: "General Provisions" (Chapter 1); "Formation" (Chapter 2); "Validity" (Chapter 3); "Interpretation" (Chapter 4); "Content" (Chapter 5); "Performance" (Chapter 6); and "Non-Performance" (Chapter 7). Chapter 6 has two sections dealing with "Performance in General" and "Hardship," respectively, while Chapter 7 has four sections: one concerning "Non-Performance in General," one on the "Right to Performance," one on "Termination," and one on "Damages."

The second set of Principles was promulgated in 2004. The 2004 Principles do not replace the 1994 Principles but supplement them with new additional chapters on "Set off" (Chapter 8); "Assignment of Rights, Transfer of Obligations, Assignment of Contracts" (Chapter 9); and "Limitation Periods" (Chapter 10); as well as a new section 2 to Chapter 2 on the "Authority of Agents".[1]

1) The only substantive change made from the original 1994 text is an amendment to article

A third set of Principles was completed in 2010. The 2010 edition adds new sections on illegality, conditions, restitution in failed contracts, and plurality of obligors and obliges, and amends some of the sections in the general provisions, the grounds for avoidance, and termination. In addition, some reordering of the Principles have been made.

The Principles are intended to enunciate rules that are common to most legal systems.[2] To the extent that the rules do not reflect these principles, they are designed to accommodate the special requirements of international trade.[3] The "black-letter rules" are accompanied by extensive and detailed comments, including illustrations, which form an integral part of the Principles.

The stated purposes of the Principles are enumerated in the preface:

They shall be applied when the parties have agreed that their contract be governed by them.

They may be applied when the parties have agreed that their contract be governed by general principles of law, the lex mercatoria or the like.

They may be applied when the parties have not chosen any law to govern their contract.

They may be used to interpret or supplement international uniform law instruments.

They may be used to interpret or supplement domestic law.

They may serve as a model for national and international legislators.

The Principles should be placed within the broad family of nonbindinglegal rules that are often referred to as "soft law".[4] These include model laws,[5]

2.8(2) on the effect of holidays occurring during or at the expiration of the period of time fixed by an offeror for acceptance. This section is now a new Article 1.12.

2) Bonell, M.J., (2005) An International Restatement of Contract Law: The UNIDROIT Principles of International Commercial Contracts, 3d. ed. at p. 46. The primary influences were codifications that had recently been drafted or amended. These include domestic legislation, such as American Uniform Commercial Code and Restatement 2d of Contracts, the Algerian Civil Code, the Dutch Civil Code, the Civil Code of Quebec, and the law of obligations of the German Civil Code. The CISG also was a major influence. *Ibid.* at pp. 48-49.

3) *Ibid.* at 46-47 and 50-52.

4) Defined by one commentator, "'soft law' is understood as referring in general to instruments

codifications of customs and usages,[6] and the promulgation of international trade terms.[7]

The official versions of the 2010 Principles have been published in English, French, German, Italian and Spanish. Unofficial versions have been published in Chinese, Greek, Hungarian, Japanese, Portuguese, Russian and Ukrainian. Versions of the 2004 Principles are also available inArabic, Korean, Romanian, and Vietnamese.

Ⅲ. The Principles and the CISG

To the extent that an international commercial transaction is concerned with the sale of goods, the governing law is often the United Nations Convention on Contracts for the International Sale of Goods (“CISG”),[8] and therefore any discussion of the Principles will logically start with a comparison of the Principles with the CISG. The Principles may work with the CISG in one of three ways: to supplant the CISG, to interpret the CISG and to supplement to CISG.

Although the CISG will apply by default to those transactions that come within its scope, the parties may freely choose to exclude the application of CISG.[9] When parties exclude the CISG, the operative substantive law in an international commercial contract will be the law either chosen by the parties with a choice of law clause or the law that will apply by the conflict of law rules of the jurisdiction that would otherwise governthe transaction absent the CISG. As will

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of normative nature with no legally binding force and which are applied only through voluntary acceptance”. Bonell, M.J., (2005) “Soft Law and Party Autonomy: The Case of the UNIDROIT Principles”, Loyola Law Review, Vol 51 p. 229.

5) See, e.g., UNCITRAL Model Law on International Commercial Arbitration (1985).

6) For example, the International Chamber of Commerce (ICC) has promulgated the Uniform Customs and Practice for Documentary Credits which set out the rules and principles that govern international letters of credit.

7) See, e.g., International Chamber of Commerce, Incoterms 2010.

8) Seventy-nine nations have ratified the CISG, including the Republic of Korea and the Republic of Korea's three largest trading partners- China, Japan and the United States. The forth largest trading partner with the Republic of Korea is the European Union, of which every major country except the United Kingdom has ratified the CISG as well.

9) CISG art. 6.

be discussed below, because the Principles may not be considered "law" as that law is understood under conflict of law rules, if the parties choose to exclude the CISG, the Principles will apply only if the parties expressly choose the Principles as the operative law in the agreement.[10)]

The Principles might also be used to interpret the CISG to the extent that the CISG already applies to the transaction. Because the Principles were written with a focus on international commercial contracts, an arbitral tribunal may on its own find both the principles as well as cases and arbitral awards interpreting the Principles as useful guides to interpret a transaction. This seems more of a theoretical than practical result, though, because, given the substantial case law and arbitral decisions interpreting the CISG already, it is unlikely that a tribunal would look beyond that body and independently choose the Principles to interpret the CISG. The parties could also actually specify that within a transaction governed by the CISG, that that the Principles are to be used to interpret the CISG.[11)]Even in this situation, though, it is unclear how a tribunal would use the Principles to interpret the CISG in the face of the current substantial volume of interpretation on the CISG.

In the case where the CISG is the applicable law, the third possible, and most likely, use of the Principles is to supplement the CISG. This could occur either by express party agreement[12)] or by an arbitral tribunal that determines that the Principles reflect the understandings of the transacting parties. Given the relatively narrow scope of the CISG,[13)] the Principles could easily be used as a

10) Recently UNIDROIT published a series of Model Clauses for the use of the Principles. http://www.unidroit.org/english/principles/modelclauses/modelclauses-2013.pdf. The Model Clauses specifically provide for choosing the Principles as the Governing Law. The suggested language for designating the Principles the governing body of law is: "This contract shall be governed by the UNIDROIT Principles of International Commercial Contracts (2010)" or "This contract is governed by the UNDROIT Principles of International Commercial Contracts (2010) and, with respect to issued not covered by such Principles, by the law of [State X]. Whether this language would meet the requirements of a valid choice of law clause could be in doubt under some legal systems, and is discussed *supra.*

11) The UNIDROIT Model Clauses for the use of the Principles suggests that following language: "This contract shall be governed by the United Nations Convention on Contracts for the International Sale of Goods (CISG) interpreted and supplemented by the UNIDROIT Principles of International Commercial Contracts (2010)." Ibid. at 17.

12) Ibid.

13) See, e.g., Henry D. Gabriel, The CISG: Raising the Fear of Nothing, 9 Vindobona J. Int'l

source of law for questions not answered by the CISG.[14] This includes set-off rights, assignment of rights and transfer of duties, third party rights, illegality, conditions, and plurality of obligors and obligees.

Ⅳ. Are the Principles Law?

A significant question is whether the Principles constitute "law" as that is understood under the rules of private international law because the Principles have not been adopted as positive law by any jurisdiction. This raises the possibility that the parties' choice of the Principles under a choice of lawprovision may not be considered a valid choice of law.[15] Although one might assume an arbitral tribunal may give the parties more latitude on this than a court might, this is still a concern that with careful lawyering can be avoided.

By choosing the Principles as "terms" to the agreement as opposed to the actual choice of the underlying substantive law, the parties should not create a legal question of what is 'law" for the tribunal. Acknowledging this potential problem,[16] UNIDROIT has provided a model clause to insert in the agreement

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Com. L. & Arb. 219, 219 (2005).

14) It is worth noting that UNCITRAL itself has already accepted the UNIDROIT Principles as the proper source of law in those areas where the scope of the CISG does not extent. See e.g., Report of the United Nations Commission on International Trade Law, fortieth session (25 June - 12 July 2007), UN Doc. A/67/17 (Part I), para. 213:

> '[The UNIDROIT Principles] shall be applied when the parties have agreed that their contract be governed by them,
> 'They may be applied when parties have agreed that their contract be governed by general principles of law, the lex mercatoria or the like, . . . [and] when the parties have not chosen any law to govern their contract,
> 'They may be used to interpret or supplement international uniform law instruments, . . . [and] to interpret or supplement domestic law,
> 'They may serve as a model for national and international legislators.'

15) Thus, for example, the American Uniform Commercial Code requires, for purposes of choice of law, that the parties choose the law of a country that bears a reasonable relationship to the transaction. Uniform Commercial Code § 1-103(a). This has been interpreted as requiring an enacted law of the jurisdiction, and thereby may exclude the Principles as a choice of law.

16) "Parties choosing the UNIDROIT Principles as the rules of law governing their contract or the rules of law applicable to the substance of the dispute are well advised to combine such a choice-of-law clause with an arbitration agreement. Domestic courts are bound by

to provide for the Principles to be terms of the agreement.[17)]

V. When Will The Principles Be Used in Arbitration

The Principles can apply in an arbitration in one of fourcircumstances.[18)] First, the parties may expressly choose the application of the Principles as a choice of law or as incorporated terms in the agreement.[19)]

Second, an arbitral tribunal may choose the Principles as the appropriate law in the absence of a choice of law provision. In the absence of a choice of law provision, a courtwould normally apply its conflict of laws rules, which would almost inevitably result in the application of a domestic law and not soft law

the rules of private international law of the forum, which traditionally and still predominantly limit the parties' freedom of choice to domestic laws, so that a purported choice of non-state rules such as the UNIDROIT Principles will be considered not as a choice of law but, rather, as an agreement to incorporate them into the contract." Model Clauses for the Use of the UNIDROIT Principles of International Commercial Contracts, (2013), p.4.

17) "The UNIDROIT Principles of International Commercial Contracts (2010) are incorporated in this contract to the extent that they are not inconsistent with the other terms of the contract." Ibid. at 14.

18) Although not of direct relevance to arbitration, it is worth noting that he Principles have been and will likely continue to be the basis of legislation. For example, in the preparation of the new Civil Code of the Russian Federation – theUNIDROIT Principles have been chosen as one of the sources of inspiration even before the publicationof their first edition in 1994. In the following years the UNIDROIT Principles were chosen as a model for the new Civil Codes of Estonia and of Lithuania, both of which entered into force in 2001. Other significant examples are the proposals for the reform of the rules on interpretation of legal acts published in 1996 by the Scottish Law Commission and the proposal for the reform of the general rules on commercial contracts in the Spanish Commercial Code published by the *Comisión General de Codifición* in 2004. The German legislature, in preparing the reform of the law of obligations of the German Civil Code (BGB) which entered into force in 2002, took into account, thougheventually only to a limited extent, the UNIDROIT Principles. Most recently, the French reform of thelaw on limitation periods in private law relationships of 2008 was inspired by the provisions onlimitation periods in the UNIDROIT Principles. The Chinese Contract Law of 1999, widelyinspired not only by the CISG but also by the UNIDROIT Principles and the projects for the modernization and harmonization of contract law in Mongolia, Vietnam and Georgia.

19) The difference between the Principles applying by a choice of law provision or by incorporation into the agreement, and the reasons why parties would choose one or the other is discussed below.

such as the Principles. Arbitral tribunals, however, have greater flexibility in choosing the appropriate law, and to the extent that the tribunal concluded that the Principles reasonably reflect party expectations, a tribunal may choose the Principles as appropriate to the transaction.[20]

A third situation is when the parties have designated that the agreement be interpreted by "general principles of law" or "general principles of international commercial law", the "lex mercatoria" or similar language.[21] Although the choice of a tribunal to apply the Principles as general principles of international commercial law is quite sensible, as I will discuss below, I do not think it normally is a sound idea for parties to leave the choice of law this vague.

A fourth situation is where the Principles might be used is as a basis to interpret an agreement that is otherwise subject to domestic law. Although this has been lauded by academics as a means to reflect common expectations of parties to an international commercial transaction,[22]it is unikely that a tribunal that is charged with intepreting domestic law will see its mandate as going beyond that an using extrensic law as an interpretive aid.

Ⅵ. The Principles as Neutral Law

Having the power to choose the Principles does not address the question of why parties might make this choice. Specifically, the question is what do the Principles offer that would not be available in the otherwise applicable law. Here, I would like to outline what I believe are some of the possible benefits.

20) This has been the case in several ICC Arbitration awards. See e.g., ICC International Court of Arbitration 9771 (http://www.unilex.info/case.cfm?id=1060) (2001); ICC International Court of Arbitration 11601 (http://www.unilex.info/case.cfm?id=1421) (2002); ICC International Court of Arbitration 12698 (http://www.unilex.info/case.cfm?id=1396) (2004); ICC International Court of Arbitration 12193 (http://www.unilex.info/case.cfm?id=1365) (2004).

21) See e.g., Award of International Arbitration Court at the Chamber of Commerce and Industry of the Russian Federation (http://www.unilex.info/case.cfm?id=857) (2002).

22) See e.g., A.S. Komorov, "Remarks about the Application of the UNIDROIT Principles of International Commercial Contracts in International Commercial Arbitration", in Institute of International Business Law and Practice, UNIDROIT Principles for International Commercial Contracts: A New Le Mercatoria? ICC Publication No. 490/1 (1995), p. 155 *et. seq.*; A. Boggiano, "La Convention interamericaine sur la loi applicable aux contracts internationaux et Principes d'UNIDROIT", (1996 Uniform L. Rev. 226).

a. Knowing the Law In Advance

As I mentioned earlier, often what is perceived by counsel as more important is not what the substantive law is that will govern the transaction, but knowing what this law is in advance. With this knowledge, counsel knows what default rules need to be contracted around.

With that in mind, it may appear that there is no particular advantage to any specific default rules of contract, be it a domestic law or the Principles, as wise counsel will simply draft the agreement with the necessary alterations to avoid any default rules that do not reflect the parties intent.[23] But this is not necessarily so. For in any international commercial transaction, one runs the risk of uncertainty as to whatsubstantive law will govern under applicable conflict of laws rules unless the agreement has a specific choice of law clause.

Because, for purposes of this article, we are assuming the parties have already chosen arbitration as the dispute resolution mechanism, one can assume counsel is thoughtfully working through the agreement. Choosing arbitration is a statement of control. Arbitration allows party choice in many ways that a judicial proceeding does not, such as the choice of who will decide the dispute and under what terms the dispute will be resolved. It is unlikely and unwise that, having exercised this level of control, the parties would leave open the question of what law applies, and hence an arbitration clause should also provide an appropriate choice of law provision.

A thoughtful choice of law clause should focus on the what rules will govern absent a specific negotiated term to the contrary: in other words, what default rules will govern. It is to this question that knowing the law in advance is important, for parties should have certainty not only to knowing what rules need to be contracted around, but also what rules will govern absent a specific negotiated term. As is discussed below, it is here that the UNIDROIT Principles may provide a better choice than an otherwise applicable law.

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23) I am assuming some level of cooperation and agreement between the parties. If one party has the bargaining position to impose its terms irrespective of the wishes of the other party, that party will be less concerned with the intent of both parties, and more concerned with that party's own respective self-interest.

b. Mandatory Rules

Underlying the Principles is a broad recognition of freedom of contract and party autonomy.[24] Whether this is a broader mandate than that which would be provided under other possible applicable law, this is somewhat restricted as the Principles are constrained, as is other law, by mandatory rules that limit party choice under the governing law of the jurisdiction.[25]

Moreover, even absent the express provision in the Principles that limit the application of the rules by otherwise applicable mandatory rules, the mandatory rules would inevitably govern over the Principles as rules of freedom of contract do not generally provide for the exclusion of mandatory rules.

To the extent that the parties may wish to provide some leeway in the application of the mandatory law that the Principles will be subject to, it is worth noting that although in a judicial proceeding the agreement is generally governed by the 'lex fori"; the place where the court sits, in an international commercialarbitration, the law is often governed by the 'lex arbitri"; the law of the place of the arbitration as determined by the parties. Thus, with thoughtful planning, parties can maximize the effectiveness of the Principles by minimizing the mandatory rules that would otherwise govern the agreement by choosing the "lex arbitri" most favorable to the transaction.[26]

c. Reasons for Choosing the Principles as the Applicable Law

ⅰ. Balancing Party Expectations in International Commercial Law

For hundreds of years it has been recognized that international commercial

24) UNIDROIT Principles art. 1.1 "The parties are free to enter into a contract and to determine its content."

25) UNIDROIT Principles art. 1.4 "Nothing in these Principles shall restrict the application of mandatory rules, whether of national, international or supranational origin, which are applicable in accordance with the relevant rules of private international law."

26) Although beyond the scope of the discussion of this article, it should be noted that the very mandatory rules that the parties seek to avoid may be applicable if one of the parties seek to enforce the arbitral award in the jurisdiction in which the parties had sought to avoid by choosing another jurisdiction as the lex arbitri.

contracts have been driven by an implicit "lex mercatoria"; an international commercial law, that is based on the practices and expectations of parties in international trade. These practices have evolved from the practical experience of businesses that reflect how international trade is conducted. Moreover, these business practices tend to be universal, and thus not grounded in any particular domestic law. It is often the case that business parties in international commercial transactions have these expectations in mind whether explicit or implicit.[27]

In addition, in contemporary international trade, a substantial number of trading partners will be from disparate legal systems. This provides transactions with widely varying standards of contract formalities, performance requirements and remedial structures.[28]

The Principles are intended to address both of these concerns. First, the Principles are drafted to addressthe particular needs of international commercial transactions. Moreover, the Principles are meant to be universal,[29] and therefore avoid the particular requirements of what may be an unknown foreign legal system.

ii. Avoid Legal Parochialism

Most domestic law will be based broadly on either the Common Law or the Civil Law. While both legal families provide ample latitude to craft contractual agreements, counsel who are used to practicing in one of the traditions may be uncomfortable working in the other legal family, much less another domestic law

27) It is worth noting that in many jurisdictions, there are separate laws to govern domestic and international arbitrations. This is in recognition that the expectations of the parties are different depending on whether the transaction is domestic or international.

28) A primes example of this is Principles art.2.1.1, which provides that a "contract may be concluded either by the acceptance of an offer or by conduct of the parties that is sufficient to show agreement." The import of this provision is clear: if the parties have begun or completed performance or made substantial preparations for performance, a contract will be assumed. In other words, when the parties act as if they have a contract, formalities of formation are not necessary.

29) Of course, one of the potential drawbacks of a universal set of rules is the inability to be too specific on some points. For example, the Principles do not attempt to define "commercial". Any attempt would have to result in failure as the domestic standards that delineate between commercial and consumer are too varied to accommodate.

within the same legal family.[30] The Principles avoid this problem to a substantial extent by having been drafted to be independent of, rather than to work in conjunction with, any particular domestic law or legal tradition.[31] Moreover, the Principles assume an international, and not a domestic, transaction, and therefore are designed to reflect the expectations of international commercial contracts.

It is worth noting that the unified rules of contracts contained in the Principles avoids a specific problem that could arise if one of the parties is unfamiliar with the intricacies of a specific jurisdiction's law of contracts in a Common Law jurisdiction. Specifically, it is typical for the rules of contract in a common law jurisdiction to be a combination of both statutory and case law. This creates a potential trap to anyone unfamiliar the law of a particular jurisdiction.[32] Conversely, by choosing the Principles, there is a unified body of rules and interpretations.

The Principles also avoid some specific legal concepts and terms that are

30) There is a natural tendency to prefer one's own domestic law, if for no other reason than familiarity. This should not necessarily be determinative. For instance, as pointed out by the President of the International Court of Arbitration of the Russian Federation,

> [a] reason which may militate in favor of the wide use of the Unidroit Principles is the fact that Russian lawyers and business people do not seem to be as reluctant as their foreign counterparts to contemplate references to the Principles in place of the application of their domestic law on the ground that the former would not confer on them the advantages which parties to foreign trade contracts usually expect from the application of their own domestic law, namely the well-known and detailed regulation of business transactions to which they are accustomed."

(A. KOMAROV, "The UNIDROIT Principles of International Commercial Contracts: A Russian View", 1996 Uniform L. Rev. 247, 250).

31) See F. FERRARI, "Universal and Regional Sales Law: Can They Coexist?", 8 Unif. L. Rev. / Rev. dr. unif. (2003), 177; G. PARRA-ARANGUREN, "Conflict of Law Aspects of the UNIDROIT
Principles of International Commercial Contracts", 69 Tulane Law Review (1995), 1239; A.M. GARRO, "Reconciliation of Legal Traditions in the U.N. Convention on Contracts for the International Sale of Goods", 23 International Lawyer (1989), 443, 480-83.

32) This can be particularly daunting in a federal system. Thus for example, , to speak of an American law of commercial contracts is somewhat misleading because commercial law is for the most part state, and not federal law, there are fifty separate state (and several district and territory) laws that govern commercial transactions, each with its own contract and commercial law. The same problem exists in Canada and Australia.

specific to certain legal families or domestic laws. Thus, for example, in the formation provisions, the Principles eschew concepts such as “consideration” and “cause”and focus instead on the process of contract formation. Likewise, the Principles avoid terms such as “warranty” whose meanings are not consistent even among Common Law jurisdictions, much less between Common Law and Civil Law jurisdictions.

iii. Freedom of Contract/Party Autonomy

Consistent with the general expectations of international commercial contracts, the Principles embody a strong policy favoring freedom of contract and party autonomy.[33)]The concepts of freedom of contract and party autonomy are the hallmarks of contract law, and thus it might be thought that thestatement of these bedrock concepts in the Principles adds nothing that would not be assumed in an otherwise applicable domestic law.[34)] This may not be the case, however, in some developing economies where there is not a strong tradition of enforceable contract rights, particularly where contract and property rights are subject to some level of government regulation and interference.

By choosing the Principles as the substantive law of the agreement the parties signal to an arbitral tribunal the fact that they intend the broadest latitude in their allocation of their rights and duties. This includes the right of the parties to specify with particularity the basis for performance and non-performance,the standards for default as well as the structure of remedies and damages upon non-performance.

iv. Favoring Contract Validity

Through various provisions, the Principles provide a strong preference for contract validity.[35)]Therefore, by choosing the Principles, the parties signify their

33) In effect, the Principles support a free market economy. See, M.J. BONELL, AN INTERNATIONAL RESTATEMENT OF CONTRACT LAW: the UNIDROIT Principles of International Commercial Contracts, 3d. ed. (2005). at p. 88.

34) For purposes of an international contract for the sale of goods, the concepts of party autonomy and freedom of contract are well embedded in the CISG.

35) Principles ch.3. sec. 2 .

intent to maintain the agreement irrespective of some technical legal impediments.

Significantly this includes the absence of any requirements of "consideration" or "cause' as a predicate to formation. This avoids technical arguments against contract formation after the performance of the agreement has begun.

Reflecting actual business practice, the Principles also provide for the possibility of open terms: "If the parties intend to conclude a contract, the fact that they intentionally leave a term to be agreed upon in further negotiations or to be determined by a third person does not prevent the contract from coming into existence."[36]

A particularly important set of provisions, especially for arbitration, are the provisions providing for hardship.[37]By providing the arbitral tribunal the power to adapt the contract or to require the parties to renegotiate the contract, the Principles encourage the maintenance of the agreement irrespective of changed circumstances that might otherwise force a contract termination. Likewise, in the case of "gross disparity" the Principles provide for adaptation to allow the contract to continue under more reasonable terms as opposed to an avoidance of the agreement.[38]

Another important provision in the Principles that encourages the continuation of agreements when there has been a breach is the right of the defaulting party to cure the defect.[39] Because minor breaches are common in major internationalcommercial transactions, this provision prevents the non-defaulting party from avoiding an agreement for minor but curable problems.

Another aspect of the Principles that favors contract validity and continuance is the standard for termination. Although under some domestic laws a minor breach may give the non-breaching party the right to terminate the agreement,[40] under the Principles, a non-breaching party can terminate the agreement and suspend its performance onlywhen the breach constitutes a "fundamental non-

36) Principles art. 2.1.14.
37) Principles arts. 6.2.1, 6.2.2, 6.2.3.
38) Principles art. 3.10.
39) Principles art. 7.1.4.
40) See e.g., the American Uniform Commercial Code § 2-601.

performance".[41] This higher standard of non-performance for termination provides a means to continue the agreement when there is a minor breach.

v. Policy Favoring Trade Usage

Another important aspect of the Principles, and consistent with international practice,[42] is their encouragement of the trade usages as terms to the agreement. Thus the parties are bound not only to "[a]ny usage to which they have agreed and … any practices which they have established between themselves,"[43] but also "a usage that is widely known to and regularly observed in international trade by parties in the particular trade concerned, except where the application of such a usage would be unreasonable."[44] It is important to note that this standard provides an objective basis for trades usages; in other words, not what the parties actually knew, but what a party in that business should have known in international trade. This provides an objective standard that avoids one party being subject to the subjective understanding of the other party who might come from another country where the usages are not the sam e.[45]

It is important to note that trade usage under the principles includes both usages that define basic contract rules as well as the underlying substantive obligations. For example, evidence of trade usage may be used to show basic contract rules regarding formation[46] and the time and order of performance.[47] It may also be used to show the substantive obligations such as the quality of the contracted goods or services.

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41) Principles art. 7.3.1. This, of course, is the default rule, and under the Principles the parties are free to set any good faith standard for non-performance that will constitute a breach.

42) CISG art. 9.

43) Principles art. 1.9(1).

44) Principles art. 1.9(2).

45) Obviously, if both parties have the same subjective understanding, the parties " had reason to know" what the other party understood. In other word, the Principles to not supplant a subjective standard with an objective standard; the objective standard subsumes the subjective standard.

46) Principles, arts. 2.1.6(3) and 2.1.7.

47) Principles arts. 6.1.1 and 6.1.4.

vi. Realistic Treatment of Form Contracts

An anomaly in contract law is the treatment of conflicting form contracts. In the case of inconsistent forms (such as a purchase order and an invoice), rules have evolved based on the twin assumptions that parties must actually agree upon the terms of the contract as well as assumption that a form with inconsistent terms to a prior form is a counter offer.[48] Thus, many legal systems will treat the last form as the final counter offer with performance being deemed acceptance. What this effectively does is artificially treat the terms on the final form as binding on both parties when it is clear that the party whose form is not the final form did not really agree to the terms of the final form.

The Principles embody a significant variation from this formation rule for standard term contracts. "Standard terms are provisions which are prepared in advance for general and repeated use by one party and which are actually used without negotiation with the other party."[49] In the case of standard terms, "[w]here both parties use standard terms and reach agreement except on those terms, a contract is concluded on the basis of the agreed terms and of any standard terms which are common in substance unless one party clearly indicates in advance, or later and without undue delay informs the other party, that it does not intend to be bound by such a contract."[50] Thus, when the parties use standard terms, the conflicting terms cancel each other out and do not become part of the agreement. If the terms cancel out so much of the agreement that there is no basis for finding a contract, the agreement fails for lack of assent. In this regard, the Principles set out rules that reflect those terms that the parties have actually agreed upon, and by doing so, limit agreements to those terms that have in fact been agreed to by the parties.

vii. Broad Requirements of Good Faith

The Principles embody a broad concept of good faith: "Each party must act in accordance with good faith and fair dealing in international trade."[51]This

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48) This is the basic rule of the CISG. See CISG art. 19.
49) Principles art. 2.19(2).
50) Principlesart. 2.22.

seemingly innocuous statement provides a basis to avoid local concepts of good faith, and instead emphasize that the focus is on international norms of behavior.

Unlike some common law jurisdictions where good faith is required only in the performance of the contract,[52] the obligation of good faith in the Principles cover all aspects of the transaction including the negotiations and formation.

Ⅶ. Possible Shortcomings with the Use of the Principles

A present shortcoming of the Principles that has to be appreciated is the current lack of definitive interpretations of its provisions. There have only been 142 published court decisions indexed in the UNILEX database[53] that involve the Principles,[54]and a substantial number of these decisions only mention the Principles in passing without analysis. There are less than 200 reported arbitral decisions in the UNILEX data base as well.[55]For this reason, unlike many domestic laws as well as the CISG, there is not a substantial body of cases interpreting the Principles to allow the comfort of a definite meaning for many of the provisions. Moreover, as mentioned above,[56]in order to draft the Principles as universal rules of international commercial transactions, a level of specificity had to be avoided. Without this level of generality, consensus would not have been possible.

In some areas of international commercial law, certainty of the law and the enforcement of the specific rules is a necessity. Because international

51) Principles art. 1.7.

52) See e.g., American Uniform Commercial Code § 1-304: “Every contract or duty within the Uniform Commercial Code imposes an obligation of good faith in its performance and enforcement.”

53) The UNILEX database is edited by UNDROIT, and it is currently the best resource for a comprehensive list and analysis of all published court cases and arbitral decisions that deal with the Principles.

54) This number is current as of July 8, 2013. See UNILEX Database, http://www.unilex.info/dynasite.cfm?dssid=2377&dsmid=13619&x=1.

55) Ibid.

56) Endnote 29, supra.

conventions and domestic laws are binding, they have the advantage of instant uniformity and enforceability. To the extent that parties have some concern about the enforceability of the Principles, either by choice of law or by incorporation into the agreement, the Principles, as with any soft law instrument raises the concern about its enforceability.

Ⅷ. Conclusion

The norms and expectations in international commercial contracts are not necessarily reflected in domestic contract law. The UNIDROIT Principles of International Commercial Contracts were drafted to reflect these expectations. The Principles also provide the widest latitude of freedom of contract to allow parties to craft agreements with as much flexibility as is necessary. Widely viewed as balanced and neutral, the Principles provide a very rational choice of law for international commercial contracts.

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