The UNIDROIT Principles of International Commercial Contracts and their Applicability in the MERCOSUR Countries*

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Résumé

Ce texte est consacré à deux sujets principaux. D'une part, l'auteur fait un survol des systèmes de droit international privé des pays membres du MERCOSUR, et ce, plus spécifiquement en ce qui concerne le principe de l'autonomie de la volonté et les règles applicables aux contrats internationaux. D'autre part, il aborde la question de l'application des Principes dans les pays du MERCOSUR sous quatre aspects : l'incorporation des Principes à titre de dispositions contractuelles; l'application des Principes à titre de loi

Abstract

This paper deals with two basic topics. On the one hand, the author gives an overview of the international private law systems of those countries who are members of the MERCOSUR, and studies more specifically the principle of the autonomy of the will and the rules and regulations applicable to international contracts. On the other hand, he discusses four aspects of the applicability of the Principles in the MERCOSUR countries: the inclusion of the Principles as contract provisions; the application of the Principles as

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applicable au contrat; l'application des Principes à titre de moyen d'interprétation et de complément du droit domestique et l'utilisation des Principes à titre de moyen d'interprétation et de complément de la Convention de Vienne sur la vente internationale de marchandises.

legislation applicable to the contract; the application of Principles as interpretative tools and complements to the local legislation; the utilisation of the Principles as interpretative tools and complements to the Vienna Convention on the International Sale of Goods.

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Adopted in 1994, the *UNIDROIT Principles of International Commercial Contracts* have already been translated into fifteen languages, inspired several legal researches, and have deserved increasing consideration from the international community[1].

Established under the form of a restatement[2], the Principles are a non-legislative source of unification or harmonization of international commercial contracts law. Their authority as a source of law arises, on one hand, from the excellence of the work performed by the jurists involved in their elaboration, representatives of all modern legal traditions[3], and, on the other, from their increasing adoption in international contracts, arbitrations and judicial disputes, which all reflect the persuasive character of the Principles. From their publication in 1994 to now (November 2002), around 70 cases in which the Principles were applied both by judicial and arbitral tribunals have been listed, which demonstrates their progressive acceptance by the international legal community[4].

The Principles reflect the current tendency in international law towards the creation of rules, transnational in nature, specializing in international commercial transactions, which experience increasing *deterritorialization* and, therefore, *denationalization*. The

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1 INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW, *UNIDROIT Principles of International Commercial Contracts*, Rome, UNIDROIT, 1994 (hereinafter "Principles" or "UNIDROIT Principles"). For a general overview of the Principles, selected bibliography and jurisprudence, and of the uniformization work performed by the UNIDROIT, consult the following homepage: [http://www.unidroit.org].

2 Restatements represent an attempt of systematizing common law by means of quasi-codes of private source. According to BLACK's *Law Dictionary*, 6th ed., p. 1313 (1991), a restatement of law consists of « a series of volumes authored by the American Law Institute that tell what the law in a general area is, how it is changing, and what direction the authors (who are leading scholars in each field covered) think this change should take ».

3 For more information on legal traditions, see: H. Patrick GLENN, *Legal Traditions of the World: Sustainable Diversity in Law*, Oxford/New York, Oxford University Press, 2000.

4 The application of the Principles by arbitration and state courts has been recorded in the *Uniform Law Review/Revue de Droit Uniforme*, published by UNIDROIT. For a summary of the recorded cases, see: *Selected Case Law Relating to the UNIDROIT Principles of International Commercial Contracts* at the following electronic address: [http://www.unilex.info].

non-intergovernmental nature of the Principles helps to fill an important gap in the area of international commercial law, not covered by international conventions of uniform law, such as that of the *United Nations Convention on Contracts for the International Sale of Goods* (CISG, Vienna, 1980).

The main objective of the Principles is to provide the international trade agents with a set of uniform rules that govern the several aspects of a contractual transaction, such as: formation, validity, interpretation, performance and non-performance, along with special situations such as hardship and *force majeure*.

Since the Principles do not result from diplomatic compromise between representatives of different and autonomous legal orders, as it usually happens at the drafting works of international treaties, their development ultimately benefited from a higher degree of coherence and uniformity, since

> [they] *reflect concepts found in many, if not all, legal systems. Since however the Principles are intended to provide a system of rules especially tailored to the needs of international commercial transactions, they also embody what are perceived to be the best solutions, even if still not yet generally adopted.*
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> *The objective of the* UNIDROIT *Principles is to establish a balanced set of rules designed for use throughout the world irrespective of the legal traditions and the economic and political conditions of the countries in which they are to be applied. This goal is reflected both in their formal presentation and in the general policy underlying them.*[5]

Practically speaking, the Principles allow lawyers and other international trade agents to benefit from a set of rules permitting them to circumvent the existing barriers for an adequate knowledge of the national laws involved in the negotiation, execution and performance of an international contract. In the same vein, they increase the chances, for the contracting parties, of finding a satisfactory common denominator between the laws involved in their transaction.

For the international lawyer the Principles constitute a *lingua franca* of commercial contracts, due to their simplicity, clearness and objectivity, as well as their neutrality *vis-à-vis* any of the existing national legal systems. Their seductive power is compelling,

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5 Unidroit Principles, *supra*, note 1, Introduction, p. viii.

especially for those who in their daily work come across several national laws governing, often in a conflicting way, the multiple faces of an international contract. The Principles may also seduce judges and arbitrators who, faced with the application of the "generally accepted principles of international commercial law" to a dispute, can now refer to a systemic body of contractual norms that witness strong reputation and are easily identified in the international context.

In free-trade and common market zones, such as the MERCOSUR, the Principles can play a very important role in fostering and deepening the goals of economic integration. The importance of uniform contract law principles in an area which represents 50% of Latin America's GDP, a potential market of 210 million consumers, and experiences increasing internal and external trade figures, can hardly be fully stressed[6].

Though the Principles are still scarcely known in the South Cone of the Americas, they bear the potential to become, among us, a powerful instrument of voluntary harmonization of international contracts law, both in intra-MERCOSUR transactions and in those performed between MERCOSUR-domiciled parties with partners established in other countries. The use of uniform rules, specifically created for transnational commercial transactions may as well allow the parties, judges and arbitrators to circumvent the rigidity resulting from the "localization" of international contracts within a given national legal system, keeping the respective disputes away

6 The MERCOSUR is a process of economic integration among Argentina, Brazil, Paraguay and Uruguay established by the 1991 *Treaty of Asunción*, complemented by the 1994 *Treaty of Ouro Preto*. The MERCOSUR countries' global imports growth has averaged 20.5%, with total figures climbing to US $83,217 billion (1996) from US $32,140 billion (1991). Intra-MERCOSUR imports growth has averaged 26.9%, with figures climbing to US $17,092 billion (1996) from US $5,125 (1991), while extra-MERCOSUR imports growth has averaged 18.9%, with figures climbing to US $66,125 billion (1996), from US $27,016 billion (1991). Intra-MERCOSUR FOB exports have also grown by 334% to US $17,058 billion (1996), from US $5,102 billion (1991). For more on the economics of regional integration in Latin America, see: R. DEVLIN and R. FFRENCH-DAVIS, "Towards an Evaluation of Regional Integration in Latin America in the 1990s", (1999) 22 *The World Economy* 261.

from solutions often marked by unpredictability and arbitrary choice of the law applicable[7].

The analysis of the Principles' applicability in the MERCOSUR countries is not, however, a task without hurdles. The Portuguese and Spanish legal heritage that flourished in the South American colonies, impregnated with authoritarian ideas of State sovereignty, along with the absence of national rules allowing choice-of-law autonomy in contractual matters and our countries' scarce tradition in the use of arbitration as an alternative means of dispute resolution create, here and there, a number of obstacles for the effective application of the Principles in the MERCOSUR region[8].

We feel, however, that the winds of change, blown by the world globalization and political and economic liberalism, tend to foster a redefinition of the State monopoly on law creation and the administration of justice, opening new fields where the use of non-legislative sources, such as the Principles, can prove to be more adapted to the governance of transnational contracts.

The use of the Principles is possible in five different contexts: (a) when the parties choose to incorporate the Principles into the international contract; (b) when the parties agree to submit the contract to the "general principles of law", the *lex mercatoria* or to other similar formulas; (c) when it proves impossible to determine the relevant rule of the law applicable to the contract; (d) when an uniform law instrument needs to be interpreted or supplemented; and (e) when their norms are used as a model for the national and international legislators[9].

We can easily figure, thus, that the binding character of the Principles arises mainly from the autonomy of the contracting parties to choose the law applicable to their transaction, since their norms are not autonomously binding, as occurs in State and classic international legislations.

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7 Michael Joachim BONELL, "The UNIDROIT Principles and Transnational Law", (2000) 2 *Unif. L. Rev.* 216.

8 On the history of national codifications and their inspiring principles, see: Jürgen SAMTLEBEN, *Derecho Internacional Privado en América Latina*, Buenos Aires, ed. Depalma, 1983, vol. 1 – parte general, p. 3-7.

9 UNIDROIT Principles, *supra*, note 1, Preamble.

Bearing this in mind, our investigative effort, essentially pragmatic, shall aim at examining the applicability of the Principles in the MERCOSUR countries. To that end, we shall first consider, for each of the MERCOSUR member-countries, their rules of private international law on the choice-of-law autonomy and their respective arbitration laws (I). Subsequently, we shall approach the applicability of the Principles taking into account the various contexts in which they can be used (II) and, finally, as a closing chapter, we shall bring forward our conclusions (III).

I. Introductory Remarks: the MERCOSUR Countries' Private International Law Systems and the Rules Applicable to International Contracts, Choice-of-Law Autonomy and Arbitration

A. The UNIDROIT Principles and the Choice-of-Law Autonomy in Private International Law

The Principles, as seen above, address four basic purposes[10]:

a) Legislative model for the States that wish to enact modern laws on international trade contracts;

b) A drafting guide of international contracts;

c) Applicable law chosen by the parties in an international transaction; and

d) Normative reference for arbitrators or domestic judges in disputes involving international contracts.

Taking into account the Principles' transnational character, the effectiveness of their application arises most often from the parties' choice directed towards that purpose, which is expressed on the basis of the principle of choice-of-law autonomy, applicable in contractual matters.

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10 Michael Joachim BONELL, "The UNIDROIT Principles of International Commercial Contracts – General Presentation", in *The UNIDROIT Principles: A Common Law of Contracts for the Americas?*, Acts of the Inter-American Congress (November 1996), Valencia (Venezuela), UNIDROIT, 1998, p. 22-27.

From a substantive or material perspective, when the parties choose to incorporate the Principles into the international contract, directly or by mere reference, their rules become substantive contractual norms. Such norms shall rule the interpretation, content, performance and non-performance of the contract, according to the provisions and respective commentaries included in the Principles. We can distinguish, in this particular application of the Principles, the expression of the principle of contractual freedom, which allow the parties to self-regulate their private interests and constitutes an important legal pillar of trade, both domestic and international. It is noteworthy that, in the area of international trade, the parties' contractual freedom becomes even more important as trade flows become freer and more competition-oriented.

Contractual freedom finds limitations in some economic sectors where there exists no free and fair competition – such as in monopolized or oligopolized sectors, in which the public interest arises to prevent the rise of open markets[11]. The contractual freedom principle is also rejected in cases where mandatory rules, of both national, international or supranational nature exist, *e.g.,* to establish money exchange controls, restrictions to economic concentration or special clauses, and in those situations they shall always prevail upon the provisions contained in the Principles[12].

From a conflicts-of-laws perspective, when the parties to an international contract choose the Principles as the applicable law, both to interpret and govern their transaction, the grounds for such a choice derive from the choice-of-law principle established in private international law rules. Already five centuries old, the principle was first elaborated by the French jurist Charles Dumoulin, being subsequently adopted in Europe, by several doctrinal schools, before it spread to other continents[13].

Functioning as an international echo of the substantive principle of contractual freedom, the choice-of-law autonomy provides the agents of international trade with a practical and predictable

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11 UNIDROIT Principles, *supra*, note 1, art. 1.1 and respective comments.

12 *Id.*, art 1.4 and respective comments.

13 On this subject, see: Nadia de ARAÚJO, *Contratos Internacionais: Autonomia da Vontade, Mercosul e Convenções Internacionais,* 2ª ed., RJ, Renovar, 2000; Haroldo VALLADÃO, *Direito Internacional Privado,* 5ª ed., RJ, Freitas Bastos, 1980, v. 1, p. 111, at 361.

solution for the determination of the law governing their transactions. In cases where the Principles are chosen, the agreement will be governed by an organized set of rules that are fully instrumented to accommodate the specific needs of international trade[14].

Nonetheless, even in countries whose conflicts-of-laws rules traditionally embrace the choice-of-law autonomy principle, we can note, sometimes, a strong resistance in accepting the Principles as the law applicable to a contract. Such situation results from the restrictions imposed to the parties or national judges in most legal systems to accept the choice in favor of a non-legislative system, transnational in nature, such as the Principles. Generally speaking, those who support such prohibition argue that a contract cannot exist entirely disconnected from a national legal system; in other words, a « contract without law » cannot be valid.

In spite of the increasing transnational character of commercial transactions and the apocalyptical voices that announce the end of nation States, domestic laws remain as solid pillars for the application of international law, be it in the form of international conventions and treaties ratified by the world nations, or by means of the application of the domestic conflicts-of-laws rules. Along these lines an eminent Brazilian scholar once stated that:

> *When in Private International Law the parties' will chooses the applicable law, it is because another law, that of Private International Law, authorized it to proceed in such way, offering it such freedom.*[15]

The scholar's lesson is greatly pertinent when we bear in mind that the Latin American countries' legal systems, which make part of the Civil Law tradition, were formed on the basis of the Iberian Peninsula law, strongly centralizing and State-oriented[16].

It is not surprising that the choice-of-law autonomy in contractual matters, nowadays widely accepted by most European and North-American legal systems, still finds resistance in the South-American countries, whose conflict rules derive from XIXth

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14 Friedrich K. JUENGER, "The *Lex Mercatoria* and Private International Law", (2000) 1 *Unif. L. Rev.* 179.

15 H. VALLADÃO, *op. cit.*, note 13, p. 363.

16 Alfredo BUZAID, "Juízo Arbitral", (1959) 181 *Revista Forense* 453.

century legal doctrines and suffer from the rigidity and strong influence of the territorialism principle[17].

Because the Principles constitute a body of non-legislative provisions, their adoption shall depend, to a great extent, on the degree of contractual freedom the parties are entitled to, either to determine substantially the contents of their transaction, or to choose the law applicable to their agreement. As to the former, the MERCOSUR countries' domestic legislations do not prevent, in principle, the parties from incorporating the Principles into their contract, provided that the imperative norms and the forum's public order are respected. As to the latter, however, the acceptance of the Principles as the applicable law reveals a greater deal of complexity. Therefore, we propose a brief analysis of the conflict rules currently applicable in the MERCOSUR context.

We shall see that, as a rule, these legal systems resist to accept the party autonomy to choose the law applicable to a commercial transaction, which means denying validity to the choice-of-law freedom principle at the international contractual level. Similarly to the MERCOSUR countries' domestic legislation, the international conventions in force in the region also render anachronistic allegiance to rigid connecting factors and to the old-fashioned territorialism principle.

We can easily perceive that such attitude represents a considerable cost for the international commercial transactions executed among parties domiciled in the MERCOSUR, as well as between MERCOSUR and foreign partners. In the same vein, it prevents the improvement of legal mechanisms that could most certainly foster both the regional integration process and that of hemispheric integration, since it keeps the huge gap that currently exists between the South Cone legislations and those which, in contractual matters, privilege the party autonomy and stimulate the adoption of uniform rules, of both legislative and non-legislative

17 Jürgen SAMTLEBEN, "Teixeira de Freitas e a autonomia da vontade no direito internacional privado latino-americano", (1985) 22, 85 *Revista de Informação Legislativa* 257-276.

character, assuring stability and safety for international trade transactions.

1. Argentina, Paraguay and Uruguay

a. International Law

i. Montevideo Treaties, 1889/1940

These three countries are parties to the Montevideo Treaties, first signed in 1889/1890 and later revised in 1939/1940, which establish common conflict rules regarding international contracts (Art. 36 to 43).

Influenced by Savigny's theory, the *International Civil Law Treaty* (Montevideo, 1940) established that the international contracts' centre of gravity is the place of its performance *(lex executionis*)[18]. As a result, Article 37 of the 1940 Montevideo Treaty states that the *lex executionis* governs all fundamental aspects of the contract, such as its: a) existence; b) nature; c) validity; d) effects; e) consequences; and f) performance. When it becomes impossible to determine the place where the contract is to be performed, the subsidiary connection factor set forth by Article 40 of the Treaty, which is the place of conclusion of the contract – *lex celebrationis,* is then applicable.

At the international level, therefore, party autonomy is not accepted with respect to the choice of the applicable law to international contracts. As a result, the legislator and the national judge are the only entities capable of determining the *lex contractus*, not the parties themselves. Rigid connecting factors are adopted with respect to contracts, which very often appear to be merely accidental and unimportant for an adequate determination of the applicable law.

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18 The private international law theory formulated by Savigny, which privileged the *domicile* as the fundamental connecting factor, to the detriment of *nationality* defended by Mancini, enjoyed wide acceptation in Latin-American countries, which reached political independence in early XIXth century and whose populations included important contingents of European immigrants. According to Savigny the *domicile* of the contract was the place of its performance.

ii. UN Convention on Contracts for the International Sale of Goods – Vienna, 1980

Argentina and Uruguay are parties to the Vienna Convention, which establishes uniform law provisions on international contracts of sale of goods for more than 60 countries, including France, United States, Canada, Germany and Japan[19]. As a matter of fact, the Convention only regulates the formation of the contract and the rights and obligations of both the seller and the purchaser. The matters not falling under the Convention rules are governed by the general principles on which the Convention is based and, by lack thereof, by the law applicable by virtue of the conflict rules in force in the forum.

Under Article 1 of the 1980 Vienna Convention, the uniform contractual law applies when the contracting parties are domiciled on the territory of the Convention member-States, or else, when the conflict rules applicable to the contract determine the application of the law of one of the Convention's signatory State. However, according to its Article 6 the parties to the contract can themselves refuse the application, wholly or in part, of the uniform conventional law stipulated in the 1980 Vienna Convention.

In the present context, as shall be seen hereafter, the Principles can be used, in the cases where the 1980 Vienna Convention is applicable, to interpret and integrate the uniform law stipulated therein.

b. Domestic Law

i. Argentina

– *Civil Code*, 1869

The Argentine private international law rules that govern conflicts in contractual matters are established in Articles 1,205 to 1,216 of the country's *Civil Code*. In cases where the agreement does not bear a connection with Argentina, the applicable law is that of the place of conclusion *(lex celebrationis)*, as stated in Article 1,205

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19 Chile, a MERCOSUR associated member, is also a party to the 1980 Vienna Convention. For more information, including jurisprudence, please refer to the following homepage of the Pace University School of Law: [http://cisgw3.law.pace.edu].

of the *Civil Code*. On the other hand, when the contract is executed abroad but its place of performance is situated in the Argentine territory, it is then governed by the territorial law, that is, by the Argentine law *(lex executionis),* according to Article 1,209 of the *Civil Code*.

Though the Argentine rules of private international law neither distinguish themselves by their clarity, nor expressly mention the party autonomy principle, eminent Argentine jurists such as Goldschmidt and Boggiano support the acceptation of the latter principle[20].

Argentine courts, however, reject it massively, except for rare exceptions[21]. In that sense, a decision often mentioned is the case *Feramérico* v. *Lital S.A.,* in which the parties' autonomy to choose the law applicable to the contract was, more clearly, acknowledged by the Supreme Court[22].

– Arbitration

The Argentine *Federal Code of Civil and Commercial Procedure*, along with the provincial codes, govern domestic arbitration. At international level, Argentina is a party to the 1958 *UN Convention on the Recognition and Enforcement of Foreign Arbitral Awards* (New York Convention), the 1975 *Inter-American Convention on International Commercial Arbitration* (Panama Convention) and the 1979 *Inter-American Convention on the Extraterritorial Validity of Foreign Judgements and Arbitral Awards* (Montevideo Convention)[23].

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20 Didier OPPERTI BADÁN, "El tratamiento juridico de los contratos comerciales internacionales en el continente americano", in *The UNIDROIT Principles: A Common Law of Contracts for the Americas?, op. cit.*, note 10, p. 35. According to the author, Goldschmidt grounds the autonomy on a consuetudinary norm, originated in Articles 1,143 and 1,197 of the Argentine *Civil Code*. Boggiano accepts the autonomy based on Articles 19 and 31 of the Argentine Constitution.

21 Cecilia FRESNERO, *La autonomia de la voluntad en la contratación internacional,* Montevideo, Fundación de Cultura Universitaria, 1991, p. 49, in N. de ARAÚJO, *op. cit.*, note 13, p. 73.

22 *Id.*

23 For a panorama of arbitration in the Mercosul countries, see: Adriana Noemi PUCCI, *Arbitragem Comercial nos Países do Mercosul,* SP, LTr, 1997. In this excellent work the author does not examine, however, the question of the law applicable to the arbitration in the respective countries.

Similarly to its private international law rules, Argentine domestic arbitration law does not openly admit the party autonomy principle in the choice of the law applicable to the dispute.

ii. Uruguay

– *Civil Code*, 1868 – Law 10,084/41

Article 2,399 of the Uruguayan *Civil Code* states that contractual obligations are governed, with respect to their existence, nature, validity and effects, by the law of the place where they must be performed *(lex executionis)*. Furthermore, the Code refers to the interpretation rules set forth in the Montevideo *Civil Law Treaty* (1889/1940).

According to eminent legal authorities, conflicts solution in contractual matters must always consider the application of a given State law. Moreover, there exists strong reticence in accepting the party autonomy principle in the choice of the law applicable to an international transaction[24]. Even the rule set forth in Article 2,403 of the *Civil Code*, which permits the parties to express their will within the limits imposed by the applicable law, is construed in a restrictive manner. In other words, the international contract is subject to the law and to the judge of the State in which the obligation is to be performed (Art. 2,399 and 2,401 of the *Civil Code*). Whether such State is Uruguay or any other, the parties cannot modify such rules of legislative and judicial competence because the relevant law prevents them from doing so (Art. 2,403)[25].

The main consequence that arises from such restrictive perspective is that, in practice, Uruguayan case-law also positions itself in the sense of forbidding the parties to choose the law applicable to the international transaction[26].

However, in a relatively recent judicial decision (decision nr. 81, of 06.11.97), the *Tribunal de Apelaciones en lo Civil de 6° Turno* stated that the law applicable to a maritime transportation contract (Brussels Convention of 1924 – Cognizance), chosen by the parties, was valid by virtue of Article 2,399 of the *Civil Code*. According to

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24 D. OPPERTI BADÁN, *loc. cit.*, note 20, 68.
25 *Id.*, 37.
26 C. FRESNERO, *loc. cit.*, note 21, 78.

this ruling, the law applicable to the international contract is the *lex executionis* and, in the particular case, Turkish law was applicable *(lex executionis)* because Turkey was the place where the contract was performed and had ratified the Brussels Convention, chosen by the parties as the law applicable to the contract[27].

Despite the promising tone of this decision, we must bear in mind that it dealt with the indirect admission of the party autonomy principle, since the law applicable according to Article 2,399 of the Uruguayan *Civil Code* (Turkish Law) was the conventional law (Brussels Convention, ratified by Turkey), chosen by the parties and validated by the rule held in Article 2,403 of the Uruguayan *Civil Code*.

– Arbitration

Domestic arbitration is governed in Uruguay by the *General Procedure Code of the Oriental Republic of Uruguay* ("C.G.P."). At international level, the country is bound to the 1958 New York *Convention on the Recognition and Enforcement of Foreign Arbitral Awards*, the 1975 *Inter-American Convention on International Commercial Arbitration* and to the 1979 *Inter-American Convention on the Extraterritorial Validity of Foreign Judgements and Arbitral Awards*[28].

Although Article 490 C.G.P. mentions the parties' freedom to agree upon the arbitration procedural rules, no other arbitration rule allows the parties to choose the law applicable to the matter submitted to arbitration.

iii. Paraguay

– *Civil Code*, 1985

Before 1986, the Argentine *Civil Code* was applied in Paraguay for civil matters. The country's new Code contains private international law provisions that govern obligations, though superficially. For example, Article 23 of the Code embraces the *locus regit actum* rule to govern the agreement's formal aspects, while Article 17 states that rights deriving from contractual obligations

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27 (2000) 2 *Unif. L. Rev.* 359 and 360.
28 A.N. PUCCI, *op. cit.*, note 23, p. 29 and 30.

are presumed to be situated in the place where the obligation must be performed (*lex executionis*).

Article 297 of the *Civil Code* deals with contracts in general, and indicates the *lex executionis* as applicable to obligations to be performed within the national territory, even if executed in a foreign country. According to some jurists, the party autonomy principle, though absent from the Code's provisions, can be found through the joint interpretation of Articles 297 and 669 of the *Civil Code*, which govern freedom of contract[29].

However, as the Argentine tradition, still influent in the Paraguayan doctrine and jurisprudence, doesn't embrace the party autonomy principle and, on the other hand, the Montevideo Treaty is still in force in Paraguay, the prevailing conclusion is that the rule applicable to international transactions contracts remains the *lex executionis*[30].

– Arbitration

Paraguay authorizes arbitration as an alternative means of dispute resolution in its own Constitution (Art. 248). Domestic arbitration is governed by the *Code of Civil Procedure*, Articles 774 to 835. At international level, the country is a party to the 1975 *Inter-American Convention on International Commercial Arbitration* and the 1979 *Inter-American Convention on the Extraterritorial Validity of Foreign Judgements and Arbitral Awards*. As it was the case with Brazil until recently, Paraguay is not a party to the 1958 *UN Convention on the Recognition and Enforcement of Foreign Arbitral Awards*.

The country is also a party to the 1965 *Convention on the Settlement of Investment Disputes between States and Nationals of other States* (ICSID Convention). This international convention clearly allows the parties to choose the law applicable to the merit of the dispute submitted to arbitration. However, such permission is limited to arbitrations governed by the ICSID Convention.

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29 Daniel HARGAIN and Gabriel MIHALI, *Contratación Mercantil Internacional en el MERCOSUR*, Montevideo, Julio Cesar Faria, 1993, p. 72 and 73, in N. de ARAÚJO, *op. cit.* note 13, p. 79.

30 N. de ARAÚJO, *op. cit.*, note 13, p. 80.

Influenced by the 1985 *UNCITRAL Model Law on International Commercial Arbitration*, a new arbitration law has been recently approved by the National Congress. Its Article 32 expressly allows the parties bound by an arbitration agreement to choose the law applicable to the merits of the dispute, in line with other modern arbitration laws[31]. However, if literally interpreted, the Article 32 provision limits the choice of law to a State law rule, excluding thus the applicability of the Principles.

Therefore, in Paraguay, it is uncertain whether the Principles are applicable to disputes submitted to arbitration.

2. Brazil

a. International Law

Brazil is a party to the *Bustamante Code* (Havana, 1928)[32], which deals in its Articles 164 to 186 with international obligations and contracts. Resulting from the compromise of several schools of legal thought prevailing at the time of its conclusion, the *Bustamante Code* failed to adopt precise connecting factors, sometimes using territorial law, sometimes personal law, sometimes the *lex celebrationis,* and sometimes the *lex executionis.* Nowhere in the Code there is mention to the party autonomy principle, which explains the absence of doctrinal consensus on its admission in contracts signed between parties domiciled in the Code's signatory States[33].

b. Domestic Law

i. Introductory Law to the Civil Code, 1942

Concerning conflict of laws rules, Brazilian domestic law is anachronistic, since it still adopts rigid criteria for the determination of the law applicable to international contracts and rejects the party autonomy principle. According to Article 9 of the

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31 Luis A. BREUER, "Paraguay como Centro de Arbitraje Internacional. Objetivo de una Nueva Ley de Arbitraje", (2001) *Rev. Jurídica La Ley Paraguaya* 515-521.

32 The Private International Law Convention of the American States (*Bustamante Code*) was enacted in Brazil in 1929 through Decree nr. 18,871. On the subject, see: J. SAMTLEBEN, *op. cit.*, note 8.

33 N. de ARAUJO, *op. cit.*, note 13, p. 160-164.

Introductory Law to the Civil Code ("LICC"), the law applicable to international transactions is the *law of the place of conclusion of the contract.* When the contract is concluded by mail, fax or other such means, the governing law is then the *law of residence of the offeror.*

Under the previous regime, which prevailed from 1916 to 1942, the Brazilian conflict rules favored the party autonomy to choose the governing law of contractual obligations, "since the obligations originated from the [parties] will, dominion of the individual will, and their option for a determined law should be respected"[34].

The current Brazilian conflicts-of-laws system, from our point of view, doesn't admit the party autonomy principle in the choice of the law applicable to international contracts. Such opinion is also that of the majority doctrine and case-law[35].

In line with the 1994 *Inter-American Convention on the Law Applicable to International Contracts* (Mexico Convention), Article 11 of Bill nr. 4.905/95 substantially revises the conflict rules applicable in contractual matters, widely admitting the choice, by the parties, of the law applicable to the contract. In the absence of express or tacit choice by the parties, the applicable law is that of the country with which the contract bears the most significant relationship. Unexplainably, a few years ago the Bill was withdrawn from the Congress, "considering the need for reexamination of the matter", which until today hasn't occurred.

A notable absence in Bill nr. 4,905/95 was the permission to apply, where pertinent, the rules and principles of international commercial law, as well as the generally accepted commercial usages and practices, which constitute non-legislative law, of

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34 Clóvis BEVILAQUA, *Código Civil Comentado*, v. 1, 12ª ed., RJ, Livraria Francisco Alves, 1959, p. 110; in N. de ARAÚJO, *op. cit.*, note 13, p. 96.

35 See, for all: N. de ARAÚJO, *op. cit.*, note 13.

international source, considered in Article 10 of the Mexico Convention.

ii. Arbitration

At international level, Brazil is a party to the 1975 Inter-American Convention on International Commercial Arbitration and to the 1979 Inter-American Convention on the Extraterritorial Validity of Foreign Judgements and Arbitral Awards.

Four decades late, Brazil has recently given an important step to join the international arbitration community with the ratification of the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, which binds the country since September 2002.

So as to compensate the legislative leniency in the modernization of Brazilian private international law rules, the 1996 *Arbitration Law* (Law nr. 9,307/96) has opened the doors for the adoption, in Brazil, of the party autonomy principle in conflictual matters.

In disputes submitted to arbitration, Article 2 of the *Arbitration Law* allows the parties to freely choose the rules applicable to the merits of the dispute. Furthermore, this rule allows the dispute to be resolved under the general principles of law, the *lex mercatoria* and the international trade rules.

This is a true revolution in Brazilian private international law, since the *Arbitration Law* recognizes both the validity and effectiveness of the parties' choice-of-law not only in relation to the rules of a State legal system, but also to those that constitute non-legislative law, such as the Principles[36].

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36 On this subject, see: Nadia de ARAÚJO, "A nova Lei de Arbitragem brasileira e os Princípios Uniformes dos Contratos Comerciais Internacionais elaborados pelo UNIDROIT", in Paulo B. CASELLA (ed.), *Arbitragem – lei brasileira e praxe internacional*, 2ª ed., LTr, 1999, p. 133-162.

B. *De lege ferenda*

1. The 1994 Inter-American Convention on the Law Applicable to International Contracts (Mexico Convention)

Regarding international contracts, we must celebrate the 1994 *Inter-American Convention on the Law Applicable to International Contracts* (Mexico Convention), in force since December 15, 1996 in Mexico and Venezuela, the only countries that have ratified it so far[37]. In addition to those countries, the Mexico Convention was signed by Bolivia, Brazil and Uruguay.

The 1994 Mexico Convention is a modern instrument of uniform conflict rules applicable to international contracts, and represents a remarkable evolution in comparison with similar instruments, such as the 1980 Rome Convention on the Law Applicable to Contractual Obligations.

The 1994 Mexico Convention allows the parties to an international contract to choose, either expressly or tacitly, the law applicable to their transaction (Art. 7). Subsidiarily, it determines that the contract, in the absence of choice of the applicable law, shall be governed by the law of the State with which it bears the most significant relationship (Art. 9), the general principles of international commercial law accepted by international organisms being taken into account in such determination[38].

Besides, Article 10 of the 1994 Mexico Convention authorizes, when pertinent, the application of norms, usages and principles of international commercial law, as well as generally accepted commercial usages and practices, with the purpose of assuring the needs of justice and equity in the resolution of a particular case.

However, doctrinal authorities haven't yet reached consensus on the parties' freedom to choose, based on the Convention, a set

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37 Organization of American States – information dated of November 2002 obtained on the following website: [www.oas.org].

38 On the Mexico Convention, see: N. de ARAÚJO, *op. cit.*, note 13, p. 165-188, and cited bibliography; see also: F. K. JUENGER, "Contract Choice of Law in the Americas", in *The UNIDROIT Principles: A Common Law of Contracts for the Americas?, op. cit.*, note 10, p. 77.

of non-legislative provisions to rule the contract – such as the Principles –, case in which we would have a "denationalized contract". Article 17 of the 1994 Mexico Convention states that the expression "law" must be understood as the law validly accepted in a State, with the exception of the norms regarding conflicts of laws. Thus, the applicability of non-legislative sources such as the Principles shall take place only subsidiarily, with the purpose of supplementing the applicable national law or interpreting it under the light of the international context.

The adoption of the 1994 Mexico Convention by the MERCOSUR countries would undoubtedly have the advantage of harmonizing the contractual conflict rules in the region. In addition, it would clearly and safely admit the principle of party autonomy in the choice of the law applicable to the contract, as well as the application of generally accepted international trade law principles.

2. Arbitration – Autonomous Regulation in the MERCOSUR

At MERCOSUR level, its member-countries signed in Buenos Aires (1998) two uniform arbitration conventions, which, however, haven't yet entered into force. The first is the 1998 *MERCOSUR Agreement on International Commercial Arbitration*, concluded between the member-countries, and the second is the 1998 *Agreement on International Commercial Arbitration* signed between MERCOSUR, Bolivia and Chile[39].

These instruments constitute true international arbitration conventions, which establish uniform arbitration rules and principles for the signatory countries. When the 1998 MERCOSUR Agreements enter into force, the region will benefit from a consolidated international arbitration regime, favoring certainty and stability for the trade exchanges taking place within the region and abroad[40].

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39 The mentioned Arbitration Agreements were approved by the Council of the Common Market by means of decisions 3/98 and 4/98, respectively.

40 On the Arbitration Agreements in the Mercosul, see: Maria Blanca NOODT TAQUELA, *Arbitraje Internacional en el MERCOSUR*, Buenos Aires, Ed. Ciudad Argentina, 1999.

Argentina is the only country that approved the Agreements so far[41]. Although Brazil has already obtained from its national Congress the legislative approval for both Agreements, it deemed suitable to suspend the deposit of the respective ratification instruments because of considerations on a potential conflict between Article 10 of the Agreements and Article 2 of the domestic Arbitration Law[42]. By virtue of the Brazilian position, which now asks for a revision of the Agreements provisions by the MERCOSUR authorities, we can expect a certain delay in their implementation by the other signatory countries.

The pending controversy deals precisely with the principle of party autonomy. Article 10 of both Agreements has the following language:

Article 10

Law applicable to the dispute by the arbitral tribunal

The parties may choose the law that shall be applied to resolve the dispute based on private international law rules and principles, as well as on international trade law. Where the parties have no agreement on this matter, the arbitrators shall decide pursuant to the same sources.

The Brazilian authorities consider that Article 10 of the 1998 MERCOSUR Agreements limits the scope of application of Article 2 of its domestic *Arbitration Law*, and therefore base their revision request on the fact that the problem should be resolved before the incorporation of the Agreements into the domestic legal system. Article 2 of the Brazilian *Arbitration Law* bears the following language:

Article 2

The arbitration may be based on law or equity, at the parties' discretion.

§ 1° The parties may freely choose the rules of law that shall be applied in the arbitration, provided that there is no violation of good moral standards and public order.

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41 Law 25,223, of 11.24.99 (Official Gazette of May 1, 2000). The respective ratification instrument was deposited on March 30, 2000.

42 The first Agreement was approved by Legislative Decree nr. 165/2000 and the second by Legislative Decree nr. 483/2001.

§ 2° The parties may also agree that the arbitration takes place on the basis of the general principles of law, on the usages and customs, and rules of international trade.

Article 10 of the 1998 MERCOSUR Arbitration Agreements states that the parties can choose the law applicable to the dispute *based on private international law* rules and principles, as well as on *international trade law.* This provision actually embraces the principle of party autonomy in relation to contractual obligations and does not prevent the parties from choosing a non-legislative system, such as the Principles, to rule their dispute. Therefore, in our opinion Article 10 of the Agreements does not conflict with Article 2 of the Brazilian *Arbitration Law*, for the former allows the choice of the Principles to rule the substance of the dispute submitted to arbitration.

The party autonomy principle, which is central in modern conflicts-of-laws systems, is hardly applied by national judges in Brazil. However, the language of Article 2, paragraph 1 of the Arbitration Law undoubtedly validates the choice-of-law made by the parties and its effectiveness in arbitration proceedings. In turn, Article 2, § 2 of the *Arbitration Law* bears substantially the same meaning of Article 10 of the MERCOSUR Arbitration Agreements. Therefore, there is only an apparent conflict between those provisions, and no contradiction arises on that point between the 1998 MERCOSUR Arbitration Agreements and the Brazilian *Arbitration Law*. Most possibly the question should be resolved by means of a simple interpretative declaration of the 1998 MERCOSUR Arbitration Agreements.

II. The Applicability of the UNIDROIT Principles in the MERCOSUR Countries

We can easily note the lack of general acceptation of the party autonomy principle, in contractual matters, among the MERCOSUR countries. The most likely outcome in cases submitted to the judicial courts is a clear refusal of the parties' choice of the law applicable to the contract. The only exception to such rule occurs when the case is submitted to arbitration. We can therefore draw the conclusion that the application of the Principles in the region, as it depends on the acceptance of the party autonomy principle, faces the consequences of the legislative diversity within the

MERCOSUR, which also raises solid obstacles to harmonizing the law of international contracts within the region.

We shall examine, hereafter, for each MERCOSUR country the most current practical situations in which the UNIDROIT Principles may be used, both by arbitrators and national judges. For each of the topics, we will seek for the actual chances of using the Principles in the region.

A. Incorporation of the Principles as Substantive Contractual Provisions – Material Autonomy

In such situations the contracting parties opt to incorporate the Principles, wholly or in part, into the contract. They can also incorporate the Principles by reference, as an integral part of the contract, by means of a specific clause. Thus, the application of the Principles derives from the parties' freedom of contract that expresses their ability to set the contents of their agreement. Sometimes, when the legal context is hostile to the parties' choice of the law applicable to the contract, the use of material autonomy can represent an efficient alternative to the uncertainty resulting from the fact that the parties don't know whether the relevant legal system validates their choice of the applicable law.

As it often occurs in the context of self-regulation of private interests, the freedom of contract principle shall be restrained by the limitations imposed by some of the national law rules under the light of which the contract is examined, especially those of public order and mandatory nature. Such situations are foreseen in Article 1.4 of the Principles, which establishes a self-limitation to its scope of application by stating that mandatory rules of both national, international or supranational origin which are applicable in accordance with the relevant rules of private international law must prevail over the Principles.

From that perspective, there seems to exist no obstacle for the application of the Principles neither in the MERCOSUR countries, nor in other Latin American countries. As stated by an eminent Argentine jurist who collaborated with the UNIDROIT workgroup that created the Principles, there are few differences between the Principles and the Latin American countries' contract laws. As with the Principles, the contractual law of those countries have adopted

the values of freedom of contract (*autonomy of will*) and of the binding nature of the contracts (*pacta sunt servanda*)[43].

In Argentina, for instance, material autonomy is based on Article 1,137 (principle of freedom of contract) and Article 1,197 (*pacta sunt servanda).* Along those lines, the Argentine Supreme Court recognized, in the case *Government of Peru* v. *Sifar,* the validity of the F.O.B. clause agreed by the contracting parties. At first sight, the judgment could be interpreted as the acceptance of the choice, made by the contracting parties, of a norm integrating the so-called *lex mercatoria.* However, in the particular case, the Supreme Court recognized the material autonomy of the parties, relating to the freedom of contract and to set the contents of the agreement, as the rule in question had been incorporated into the contract by the parties themselves. Therefore, the court didn't deal with the party autonomy principle at private international law level, which would ultimately have resulted in submitting the agreement to the rules of a non-State legal system[44].

Within the MERCOSUR the incorporation of the Principles into a contractual agreement can represent an efficient alternative to their choice as the law applicable to the contract. We must, however, take into account the fact that in those situations the functioning of the Principles shall take place in the context of and in accordance with the relevant rules of a given national legal system.

B. The Principles as the Law Governing the Contract

The Principles can be chosen by the parties as the law governing the contract, in which case no national laws may be applicable to the agreement. The application of the Principles as the governing law can also result from the circumstances that involved the agreement's conclusion and performance, in which case the choice of the Principles as the law applicable is incumbent on the arbitrators or the judge to whom the case is submitted.

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43 Alejandro GARRO, "Unification and harmonization of private law in Latin America", 40 *Am. J. Comp. L.* 609 (1992). For an excellent analysis of the values shared between the Principles and the new *Civil Code of Quebec* (Canada), see: Paul-André CRÉPEAU, with the collaboration of Élise M. CHARPENTIER, *Les Principes d'UNIDROIT et le* Code civil du Québec *: valeurs partagées?,* Scarborough, Carswell, 1998.

44 N. de ARAUJO, *op. cit.*, note 13, p. 73.

During the four-year period (May 1994 – December 1998) that followed their edition, the Principles were used in at least 23 arbitral awards submitted to the International Court of Arbitration of the International Chamber of Commerce ("ICC")[45]. One-third of the cases indicated the Principles as the governing law of the international contract *(lex contractus)*. The majority of these cases were resolved under *de jure* arbitration, which excludes *ex æquo et bono* decisions, and the choice of the Principles as the governing law was made on the basis of former Article 13 of the ICC Arbitration Rules, whose current equivalent is Article 17:

> **Article 17**
>
> *Applicable Rules of Law*
>
> 1. *The parties shall be free to agree upon the rules of law to be applied by the Arbitral Tribunal to the merits of the dispute. In the absence of any such agreement, the Arbitral Tribunal shall apply the rules of law which it determines to be appropriate.*
>
> *2. In all cases, the Arbitration Tribunal shall take account of the provisions of the contract and the relevant trade usages.*
>
> [...]

This was the case, for instance, in an arbitration proceeding held in 1996 by the National and International Arbitration Court of Milan (Italy). The dispute involved an Italian company and an American agent, bound by an agency contract for distribution of furniture. The Italian party had terminated the contract based on the non-performance of obligations by the agent, who had failed to reach the expected results. The agent, on the other hand, argued that termination of the agreement was illegal and claimed damages for the incurred losses. At the outset of the arbitration proceedings the parties agreed that the Principles were the proper law of the contract, and their application would be "*tempered by the recourse to equity*". In order to resolve the dispute, the sole arbitrator thus applied several Principles provisions, such as Articles 1.3, 4.1, 4.2,

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45 Fabrizio MARRELLA and Fabien GÉLINAS, "Les Principes d'UNIDROIT relatifs aux contrats du commerce international dans l'arbitrage de la CCI", (1999) 10, n° 2 *Bulletin de la Cour internationale d'arbitrage de la CCI* 26-122. For a comparison of figures, on January 1, 1995, there were 801 cases submitted to the International Court of Arbitration of the International Chamber of Commerce, 855 cases on January 1, 1996 and 935 on January 1, 1997 ((1998) 9, n° 1 *Bulletin de la Cour internationale d'arbitrage de la CCI*).

7.3.1, 7.3.5, 7.4.1 and 7.4.2, 7.4.3 and 7.4.4, as well as 7.4.9. and 7.4.13, without reference to any other legal system[46].

On another occasion the arbitral tribunal verified the absence of choice, by the parties, of the law applicable to the dispute. By a further analysis of the circumstances involving the conclusion of the contract, the tribunal determined that the only certitude regarding the contracting parties' intention was that each party intended to exclude the application of the other party's national law to the agreement. As a result, the arbitrators, based on the former Article 13 of the ICC Rules of Arbitration, decided to apply the Principles as the law governing the contract[47].

As we shall see hereafter, the effectiveness of the Principles in the MERCOSUR countries is closely connected to their application by arbitrators, rather than domestic judges. This, however, is not a situation particular to the MERCOSUR countries but rather a consequence of the fact that the Principles constitute a body of non-national rules, persuasive in nature, whose binding effects derive chiefly from the will of the parties. Given the Principles' non-legislative nature, domestic judges resist to their application. Therefore, the official comments to the preamble of the Principles recommend to combine the choice of the Principles with an arbitration agreement, so as to ensure their effectiveness.

In addition to applying the Principles as a result of the express choice by the contracting parties, they can also be used in the context of the *lex mercatoria.* In that case, the application of the Principles occurs where the parties or arbitrators refer to one of the following clauses:

- "general principles of law"
- "usages and customs of international trade"
- "*lex mercatoria*"
- "general international trade law principles"

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46 01.12.1996 – *Camera Arbitrale Nazionale ed Internazionale di Milano*, case A-1795/51, in [www.unilex.info] – UNIDROIT Principles – cases (by date).

47 F. MARRELLA and F. GÉLINAS, *op. cit.*, note 45, p. 30.

In the context of an ICC arbitration, for instance, the issue consisted in determining the law applicable to related contracts concluded between a non-European State and a UK company. The contracts contained no express choice of law clause but mentioned, here and there, the expression "natural justice". The plaintiff argued that the parties had intended to apply the "general principles of law" to their transaction, while the defendant, pursuant to the indirect method set forth in the former article 13 of the ICC Rules of Arbitration, argued that UK substantive law was applicable, since it was the "most closely connected" with the case and related to the place of residence of the obligor of the characteristic performance[48].

By using the direct method to determine the applicable law, the arbitral tribunal decided to apply the "general principles of law", and inferred from the parties' intention the existence of a negative choice, so as to exclude the application of any specific national law. The arbitral tribunal concluded that "the reasonable intention of the parties regarding the substantive law applicable to the contracts was to have all of them governed by general legal rules and Principles in matter of international contractual obligations such as those arising out of the contracts which, though not necessarily enshrined in any specific national legal system, are specially adapted to the needs of international transactions and enjoy wide international consensus". The tribunal also held that such "general principles" were primarily reflected in the Principles, which should therefore govern the dispute with respect to all matters falling within their scope[49].

In such disputes, more frequently submitted to arbitral tribunals than to national courts, the Principles are applied as *jus commune,* generally accepted in the international community. However, it must be underlined that some of the Principles' provisions do not enjoy wide international consensus, as is the case for the hardship clause, laid down in its Articles 6.2.1 and 6.2.3[50].

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48 00.06.1995 – ICC International Court of Arbitration, case 7110, in [www.unilex.info] – UNIDROIT Principles – cases (by date).

49 *Id.*

50 *Hardship* is generally defined as the situation in which the occurrence of reasonably unexpected events determines a fundamental modification in the balance of the obligations agreed by the contracting parties. The Principles authorize, in those situations, the disadvantaged party to request renegotia-

For example, in a 1997 ICC arbitration case, the tribunal faced the plaintiff's argument that the Principles' hardship provisions should apply, on the grounds that they represented veritable trade usages under Article VII of the 1961 Geneva Convention on International Arbitration and former Article 13(5) of the ICC Rules of Arbitration and Conciliation, despite the existence of a choice of law clause in favour of Spanish law. The tribunal decided to reject the application of the Principles, on the grounds that the Principles are applicable only where there is express choice made by the parties or in situations where the contract refers to "general principles of law", *lex mercatoria* or the like. Furthermore, the tribunal held that the Principles' provisions on hardship did not correspond to the current practice of international trade[51].

Despite the resistance of Argentine conflicts rules and case-law to accept party autonomy in international contractual matters, this country bears the honor to be the first in the MERCOSUR region to experience the application of the Principles, precisely in the context of the *lex mercatoria.*

The Principles were applied in the context of an *ad hoc* arbitration held in 1997 in Buenos Aires to resolve a dispute between the shareholders of an Argentinean company and those of a Chilean company. The parties had signed an agreement that stipulated the purchase of 85% of the Argentinean company by the Chilean company. After the conclusion of the contract, the purchaser discovered that the seller had dissimulated its liabilities and decided to suspend the payment of the remainder of the purchase price. The sellers, then, initiated the arbitration proceedings asking for full payment. The purchaser in turn asked the tribunal to confirm avoidance of the contract, to award damages or, subsidiarily, to reduce the price of the deal in proportion to the hidden debts discovered[52].

The contract had no choice of law clause and the arbitral tribunal was authorized to decide as *amiable compositeur.* Though

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tions. Upon failure to reach a new agreement within a reasonable time either party may resort to the court.

51 00.07.1997 – ICC International Court of Arbitration, case 8873, in [www.unilex.info] – UNIDROIT Principles – cases (by date).

52 [1998] 1 *Unif. L. Rev.* 179-181. 10.12.1997 – *Ad Hoc* Arbitration, Buenos Aires, in [www.unilex.info] – UNIDROIT Principles – cases (by date).

the parties had founded their respective pleadings on substantive provisions of the Argentine law, the tribunal decided to apply the Principles, on the grounds that they constitute "the usages of international trade reflecting the solutions of different legal systems and of international commercial practice" and, thus, according to Article 28(4) of the UNCITRAL *Model Law on International Commercial Arbitration*, they must prevail upon any domestic law[53].

The arbitral tribunal considered the Principles as the law applicable to the transaction, rejecting the application of any specific domestic or international law. As a result, it applied to the particular case the Principles provisions regarding notice of avoidance (Art. 3.14), confirmation (Article 3.12) and the *contra preferentem rule* (Art. 4.6).

Had the same issue been raised before a domestic judge, most likely there would have been no application of a non-legislative system to interpret and govern the contract. In fact as public officials domestic judges are bound to apply the law of their respective national State, or, if the case may be, that of a foreign State, according to the forum's rules of conflicts. Very seldomly domestic judges have been allowed to consider "contracts without law" or "denationalized" transactions.

For the comfort of true internationalists, an outstanding exception came from a North-American judicial court, specifically the U.S. District Court, S.D. California that confirmed a 1997 ICC award under the light of the 1958 New York *Convention on the Recognition and Enforcement of Foreign Arbitration Awards*. The court considered that the application of the Principles, even if not resulting from the parties' choice, carries no violation to Article V(1)(c) of the Convention. This last rule prevents recognition and enforcement of foreign arbitral awards that have exceeded the terms of the submission to arbitration. The Ministry of Defense and Support for the Armed Forces of the Islamic Republic of Iran, which had requested the award confirmation, eventually won the case against U.S.-based Cubic Defense Systems, Inc.[54].

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53 *Id.*

54 07.12.1998 – United States District Court, S.D., nr. 98-1165-B, in [www.unilex.info] – UNIDROIT Principles – cases (by date).

In Brazil, Article 2 of the *Arbitration Law* widely allows the party autonomy principle in the choice of the law applicable to the dispute. It also allows the parties to choose general principles of law, usages and customs or international trade to govern the arbitration. Thus, in spite of the rigidity of Article 9 of the LICC (conflicts of laws rules) and the absence of other rules authorizing domestic judges to apply the Principles, the Brazilian legal system widely allows for their application in the context of arbitrations, both domestic and international.

In Paraguay and Uruguay, although their respective legal systems do not accept the party autonomy principle neither to choose the law applicable to contracts nor to the dispute submitted to arbitration, it shall be possible for the contracting parties to indirectly express their will in that sense. The parties may submit their actual or future disputes to arbitration and agree upon the adoption of arbitration rules such as those laid down by the ICC or the UNCITRAL, which allow the choice of the law applicable to the arbitration.

A foreign illustration of such situation comes from an arbitral award delivered in 1997 by the International Arbitration Court of the Chamber of Commerce and Industry of the Russian Federation. The case concerned a sales contract concluded between a Russian trade organisation and a Hong Kong company where the parties had made no choice as to the law applicable to the contract. However, when the dispute arose, they agreed to choose the Principles as the applicable law concerning issues not expressly regulated in the contract. The tribunal then applied a number of Principles provisions to resolve the dispute, deciding, for example, that the Russian party had the right to terminate the contract (Art. 7.3.1) and that the restitution of the goods already delivered should occur (Art. 7.3.6)[55].

If and when the 1998 MERCOSUR Agreements on International Commercial Arbitration become enforceable in all countries of the region, the obstacles relating to the choice of law in arbitrations

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55 Case cited by Michael Joachim BONELL, *An International Restatement of Contract Law*, 2nd ed., p. 252 and 253 (1997). 20.01.1997 – International Arbitration Court of the Chamber of Commerce and Industry of the Russian Federation, case 116, in [www.unilex.info] – UNIDROIT Principles – cases (by date).

shall be completely removed by reason of the provision set forth in its Article 10[56].

With respect to domestic courts, these very obstacles can be greatly removed if the MERCOSUR countries decide to ratify the 1994 *Inter-American Convention on the Law Applicable to International Contracts* (Mexico Convention), whose Article 10 allows for the application of the Principles provisions[57].

C. The Principles as a Means of Interpreting and Supplementing the Applicable Domestic Law

Given their intrinsically transnational character, the Principles may help arbitrators and judges to interpret and supplement the domestic law applicable under the relevant law applicable according to private international law rules. Very often the domestic law provisions, enacted to govern basically the country's domestic transactions, show no ability to deal with transnational matters. In many instances, the domestic law has no specific rules that consider the international aspects of a given transaction.

In those situations, the Principles can fill the blanks of the applicable domestic law, delivering "international color" to the relevant rules of the domestic law. In the previously mentioned ICC arbitral awards research, 9 out of 23 arbitrations used the Principles with the purpose of construing or supplementing the applicable domestic law, being apparently successful in such mission[58].

In such situations the use of the Principles corresponds to a modern comparative legal approach, by means of which the results obtained with the application of domestic law are compared with those reached by the use of a transnational rule. When such results converge, the exercise of comparison allows international arbitrators to affirm that the decision based on domestic law is in conformity with the generally accepted principles of international contracts law. According to the leading doctrine in this field, there occurs an "international test" of the domestic law, which can be very

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56 See *supra*, chapter II.
57 *Id.*
58 F. MARRELLA and F. GÉLINAS, *op. cit.*, note 45, p. 31.

helpful for the arbitrators given the growing internationalization of contracts and litigation proceedings[59].

This is, for example, the result reached by the arbitral tribunal in a dispute between an American supplier of telecommunication systems (claimant) and a Middle Eastern manufacturer of telecommunications cables (defendant). Under a pre-bid agreement the parties undertook to negotiate in good faith the supply of cables and the service agreements in the event the American company won a bid for the implementation of a telecommunications project in Saudi Arabia[60].

The American company's bid was successful but nevertheless it terminated the preliminary agreement with the Middle Eastern cable manufacturer, arguing that the parties were unable to reach a permanent agreement by means of good faith negotiations. As there was no voluntary choice of the law applicable to the dispute, the claimant invoked the application of Saudi law (*lex executionis*), of English law (*situs of arbitration*) or of the State of Georgia (*the location of the principal negotiations*). The defendant, in turn, invoked the application of the laws of the States of New York or New Jersey and asked the court to apply the Principles.

With a view to preserve the parties' undertaking to negotiate in good faith a permanent agreement, the tribunal chose the New York law, whose rules enforce this kind of undertaking, to govern the dispute. It also referred to the Principles, stating that international arbitrators can call upon the general principles of law where the case involves competing systems of law whose connecting factors do not sufficiently attract the contract. Therefore the tribunal declared that the Principles were a useful legal source for establishing general international commercial contracts rules, underlining that the application of the Principles led to the same conclusion as that resulting from the application of New York law, that is, the enforceability of the undertaking to negotiate in good faith[61].

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59 *Id.*

60 Cited in *White & Case International Dispute Resolution*, v.10, March 1997, p. 3. 04.09.1996 – ICC International Court of Arbitration, case 8540, in [www.unilex.info] – UNIDROIT Principles – cases (by date).

61 *Id.*

Another ICC arbitration case concerned a dispute over a contract of distributorship signed by parties domiciled in Switzerland, Singapore and Belgium, where the main issue referred to the regulation of repurchase of the inventories, following the contract termination by agreement of the parties. Even though the parties had indicated the Swiss law as applicable to the contract, the arbitral tribunal, when deciding on the exchange rate to be chosen for the payment of the repurchase in local currency, referred to Article 6.1.9(3) of the Principles. It intended, thus, to validate internationally the solution given by the domestic law (Swiss law) applicable in the particular case[62].

Finally, a very interesting ICC arbitral award rendered in Colombia also applied the Principles to a contract governed by the *Colombian Commercial Code*, so as to demonstrate that the solution found under domestic law corresponded to modern international commercial law[63].

In Argentina, as well as in other MERCOSUR countries, the Principles can be a helpful instrument to interpret and supplement the domestic law (of the forum or of a foreign State) applicable to the international contract. The Argentine legal doctrine supports such application, according to the distinguished opinion of Antonio Boggiano, judge of the Argentine Supreme Court, who says that:

> [t]*he Principles of the* UNIDROIT *can be used to interpret, supplement and apply the national law chosen by the parties or applicable by virtue of the rules of conflicts of laws: the rules of the applicable national law may reveal themselves as very rigid or of little conformity with the international contracts* [...].[64]

It seems reasonable to recommend the supplementary application of the Principles in arbitrations taking place in the MERCOSUR region, since the region's arbitration rules generally show the

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62 Cited by K.P. BERGER, "The *Lex Mercatoria* and the UNIDROIT Principles of International Commercial Contracts", (1997) 28 *Law and Policy in International Business* 982. 00.07.1995 – ICC International Court of Arbitration, case 8240, in [www.unilex.info] – UNIDROIT Principles – cases (by date).

63 00.12.2000 – ICC International Court of Arbitration, case 10346, in [www.unilex.info] – UNIDROIT Principles – cases (by date).

64 Antonio BOGGIANO, "La Convention interaméricaine sur la loi applicable aux contrats internationaux et les Principes d'UNIDROIT", (1996) *Unif. L. Rev.* 226. This opinion is also supported by Michael Joachim Bonell and other eminent authors, *cf.*: M.J. BONELL, *loc. cit.*, note 7, p. 212 and 213.

needed flexibility for such application. However, in the practice of judicial litigation, given the scarce international vocation of the MERCOSUR domestic and international legislations and the little creativity of case-law in matter of international contracts, we think that hardly any situation may arise in which, over and above the applicable national law, the judge will be led to perform the "international test" with the aid of the Principles.

However, should the MERCOSUR countries ratify the 1994 *Inter-American Convention on the Law Applicable to International Contracts* (Mexico Convention), the creative and effective use of the Principles shall be assured by force of its Article 10, below:

> **Article 10**
>
> *In addition to the provisions of the foregoing articles, the guidelines, customs, and principles of international commercial law as well as commercial usage and practices generally accepted shall apply in order to discharge the requirements of justice and equity in the particular case.*

At judicial level, for instance, the Principles were applied by an Australian court in 1997. The Federal Court, when applying the domestic law in a suit filed by an American company (Hughes Aircraft Systems International) against an Australian government agency (Airservices Australia), grounded on the violation of the principles of good faith and fair dealing in matters of bidding procedures, decided to refer to the Principles to confirm its understanding under the light of international law. It thus declared that the general obligation of good faith and fair dealing was not only sheltered by several legal systems, but also recognized as a fundamental principle of international commercial contracts under Article 1.7 of the Principles[65].

On another occasion, the Principles were used by a Dutch court to enlarge the French law's concept of good faith, applicable in the particular case. The dispute involved a contract for delivery of fish signed by a French seller and a Dutch purchaser, subject to the 1980 *UN Convention on Contracts for the International Sale of Goods* (Vienna Convention). Following the first delivery the purchaser

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65 Federal Court of Australia, *Hughes Aircraft Systems International* v. *Airservices Australia*, [1997] 558 FCA (30 June 1997), available online: Federal Court of Australia [http://www.fedcourt.gov.au/judgments/judgmts.html]. 30.06.1997 – Federal Court of Australia, nr. 558, in [www.unilex.info] – UNIDROIT Principles – cases (by date).

refused to receive further consignments, alleging that its customers had complained about the fish quality. According to the seller, the purchaser had lost the right to rely on the product's lack of conformity, since it failed to send proper notice of the fact in a timely manner. The purchaser, however, sustained that the merchandise defects were such that he could not have reasonably discovered them within the short period that preceded the giving of notice provided in the contract[66].

Article 39(1) of the Vienna Convention, applied by the court, stipulates that the purchaser loses the right to rely upon the lack of conformity of the product if he does not give notice to the seller, specifying the nature of the lack of conformity of the goods within a reasonable term after he has discovered it or ought to have discovered it. According to the court, it was necessary to refer to the domestic law applicable under Article 7(2) of the Vienna Convention to interpret the concept of good faith under the light of the expression "or ought to have discovered it", provided in Article 39(1) of the Convention. In French law, according to the court, the concept of good faith is understood in a subjective way.

For such reason, the court decided to adopt the wider concept of good faith, set forth in the Principles, and concluded that the purchaser should have inspected the product more carefully, which would have allowed him to discover the respective defects in time.

D. Use of the Principles as a Means of Interpreting and Supplementing an International Instrument of Uniform Law

The Principles can also be used to interpret and supplement international uniform law instruments, especially the 1980 *UN Convention on Contracts for the International Sale of Goods* (Vienna Convention).

Among the MERCOSUR countries only Argentina and Uruguay are signatories to the Vienna Convention, which essentially establishes substantive provisions on the formation of the international contract of sale of goods as well as on the rights and obligations of

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66 Nederlands Internationaal Privaatrecht, vol. 15 (1997), 282. 05.03.1997 – RB Zwolle, nr. HA ZA 95-640, in [www.unilex.info] – UNIDROIT Principles – cases (by date).

the seller and buyer. For matters not governed by the Convention, the contracting parties, judges and arbitrators must refer to the general principles on which the Vienna Convention is based and, by lack thereof, to the law applicable by virtue of conflicts rules.

In some situations the Vienna Convention can also be applied in Brazil and Paraguay, because of these countries' conflicts rules. Under Article 1 of the Vienna Convention, its uniform law applies where the contracting parties are domiciled on the territory of the Convention's signatory States as well as where the conflict rules applicable to the contract determine the application of the law of one of its signatory States.

This means that the rules of the Vienna Convention can be applied by the Brazilian courts, for instance, when under Article 9 of the LICC this is the current law for international sale contracts in the State in which the contract was executed (*lex celebrationis*). The Vienna Convention can also be applied if the parties to a dispute submitted to arbitration have agreed so, under the provision of Article 2 of the Brazilian *Arbitration Law*.

Similarly in Paraguay, the Vienna Convention can be applicable to the international contract of sale of goods by virtue of the country's rules of conflicts, when it is the current law for international sale contracts in the place where the contract must be performed (*lex executionis*).

Case-law shows a number of examples of the use of the Principles as a supplement to the Vienna Convention provisions. A 1996 ICC arbitration held in Switzerland dealt with a dispute between French (claimant) and Austrian companies (defendant), where the conclusion and performance of a manufacture contract and of related contracts were controverted. According to the parties' choice the tribunal applied both the French law and the Vienna Convention to the case. Considering the silence of the Vienna Convention with respect to the interests claimed, the tribunal, deeming appropriate to apply a "commercially reasonable" interest rate, referred to Article 7.4.9 (2) of the Principles[67].

The Principles are not only helpful to interpret and supplement the 1980 Vienna Convention, but also other uniform law

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67 00.12.1996 – ICC International Court of Arbitration, case 8769, in [www.unilex.info] – UNIDROIT Principles – cases (by date).

instruments. For example, the Supreme Court of Venezuela availed itself of the Principles to justify an enlarged concept of "international contract" for the purposes of application of Article 1 of the 1975 *Inter-American Convention on International Commercial Arbitration* (Panama Convention), which validates arbitration agreements in the context of international contracts.

The court dealt with a dispute between two Venezuelian companies (*Bottling Companies* v. *Pepsi Cola Panamericana, S.A.*), parties to a contract that provided, in the event of a dispute, the submission of the matter to arbitration in New York, under the ICC Rules of Arbitration. When one of the parties invoked the arbitration clause, the other refused to comply with its provisions, alleging its unenforceability and filed an action asking the Venezuelian courts to confirm jurisdiction over the dispute[68].

By confirming a lower instance judgement, the Supreme Court of Venezuela rejected the request and declared the validity of the arbitration agreement executed by the parties. It based its decision on the 1958 New York Convention and the 1975 Panama Convention, both ratified by Venezuela, whose provisions validate the arbitration agreement by means of which the parties to an international contract agree to submit their future disputes to arbitration. Though both parties had their main offices in Venezuela, the Supreme Court decided in favor of the application of the New York and Panama Conventions on the basis that one of the companies was in fact a branch of a U.S.-based company. In order to support the wider definition of international contract, such as provided in the 1975 Panama Convention, the Supreme Court referred to the official comments in the preamble of the Principles, which recommends to consider the concept of "international" contracts in the widest possible manner, so as to exclude from its scope only those situations where no international element is actually involved.

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68 (1998) 1 *Unif. L. Rev.* 176 and 177. 09.10.1997 – Supreme Court of Venezuela, in [www.unilex.info] – UNIDROIT Principles – cases (by date).

III. Conclusions: Possibilities and Paradoxes

This brief analysis of the Principles' effectiveness in the MERCOSUR countries reveals not only the different levels of acceptance of party autonomy in the region but also a face of the possibilities and paradoxes of the MERCOSUR as an integration process.

As to the **possibilities** of integration, they are several. The MERCOSUR is best defined as a process, a *work in progress* based on pragmatism and not necessarily on a pre-conceived and idealized integration model, as was the case at the origin of the European Union. It constitutes a potential market of 215-million population, endowed with a US$ 1 trillion GDP, which places it among the four largest world economies, after the NAFTA, the European Union and Japan.

On the 10th anniversary of the 1991 Asuncion Treaty, the MERCOSUR can celebrate the removal of 95% of its tariff barriers to intra-regional trade and, despite the recent Argentine crisis, MERCOSUR still experiences increasing trade exchange between its members and partners, and increasing integration initiatives in cultural, political, educational and social sectors.

The underlying interest of studying the application of the Principles in the South Cone region relates to the actual needs that arise in the world of international trade, where this non-legislative means of unification or harmonization of law reveals undeniable usefulness.

Despite the fact that a high level of legislative harmonization in some MERCOSUR areas already exists, notably in the fields of inter-jurisdictional cooperation (letters rogatory, contractual jurisdiction, provisional measures, foreign judgements and arbitral awards), consumers' rights and civil liability, it could not be exaggerated to expect from the MERCOSUR authorities greater efforts to harmonizing conflict rules in contractual matters.

Assuming the importance and effectiveness of the Principles to harmonizing the law of international commercial contracts, it becomes necessary for the MERCOSUR countries to establish legal provisions allowing the parties to an international contract to make wide use of their autonomy to choose the law applicable to the

contract, including non-national rules, which are part of the *lex mercatoria.*

An example of such movement towards evolution is the 1998 Argentine Draft Civil Code which incorporates the general theory of sale contracts underlying in the 1980 Vienna Convention. In drafting the new *Civil Code*, the Argentine jurists took into account the Principles, specially with respect to the interpretation criteria applicable to international commercial contracts and other substantive rules. Unfortunately, the Draft Code still lacks express acceptance of the party autonomy principle in the choice of the law applicable to international contracts[69].

In Brazil, on the eve of the entry into force of a new *Civil Code*, the anachronism of our private international law system regarding contracts, which binds judges to rigid territorialist rules and takes no account of the party autonomy principle, is unhappily obvious. Modernization arrives in small steps through arbitration, where the domestic regulation allows for wide exercise of party autonomy, including the *lex mercatoria.*

However, the main problems resulting from anachronistic conflict rules still remain, since not all international disputes are brought before arbitral tribunals, and national judges are bound to such rigid conflicts provisions.

In Paraguay, the enactment of a modern arbitration law, based on the 1985 UNCITRAL Model Law on International Commercial Arbitration, will hopefully entail the acceptance of the Principles in that country, as now occurs in Brazil.

In Uruguay, according to the leading doctrine and case-law, the Principles can be applied through the indirect acceptation of the party autonomy principle, as we could verify it in a recent decision pronounced by a local court. The Principles can also be incorporated in the country's legal practice by means of the 1980 Vienna Convention, also ratified by Argentina, which, as we have seen, is a powerful instrument of uniform law.

In the **regional context,** there may be no need to go as far as the European Union, whose 1997 *Amsterdam Treaty* gave the

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69 Julio Cesar RIVERA, "Droit comparé et droit uniforme dans le projet de *Code civil* argentin", (1998) 3 *Unif. L. Rev.* 869.

community bodies the task of harmonizing conflict rules at regional level, *supra-nationalizing* a mission previously under its member-States jurisdiction[70]. In the MERCOSUR context suffice is that its countries ratify the 1994 *Inter-American Convention on the Law Applicable to International Contracts* (Mexico Convention), and the region will benefit from a modern system of conflict rules regarding international contracts, including express acceptance of the party autonomy principle in contractual matters and the possibility of referring to general principles of international trade.

Practical experience reveals that the Principles are more efficiently and easily used in international arbitration. Though the MERCOSUR countries' legislations are generally favorable to arbitration, the ratification and entry into force of the 1998 MERCOSUR *Agreements on International Commercial Arbitration* would be very helpful to consolidate arbitration as an alternative means to resolve international trade disputes. These Agreements, signed between the MERCOSUR countries and between the MERCOSUR and its associated countries (Bolivia and Chile) provide in Article 10 that the contracting parties can choose the law applicable to the arbitration, including international trade law.

Along with the 1998 MERCOSUR Agreements, the 1975 *Inter-American Convention on International Commercial Arbitration* (Panama Convention), the 1958 *UN Convention on the Recognition and Enforcement of Foreign Arbitral Awards* (New York Convention) and the 1979 *Inter-American Convention on the Extraterritorial Efficacy of Foreign Arbitral Sentences and Awards* (Montevideo Convention) form a group of modern international instruments that deliver high effectiveness not only to the party autonomy principle, but also to the international circulation of arbitral awards and judicial decisions.

There remain, however, some **paradoxes** in the MERCOSUR integration process, which hamper, also at legal level, the goals of uniformisation and harmonization of law.

The existence of obsolete conflicts rules on international contracts in the region represents a high "cost" for the block's

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70 Article 65(b) of the Rome Treaty, modified by the *Amsterdam Treaty* (1997), includes among the missions of the European Community the "promotion of the compatibility of the rules applicable in the member-States concerning conflicts of laws".

international transactions, since it delivers insufficient legal certainty and stability to foreign trade partners, particularly in a region meant to be an exports platform of primary and manufactured products. Moreover, the goals of regional integration can go no further without the harmonization of the national legal systems, especially in the areas essential to international trade such as contract law.

Brazil, as the MERCOSUR's largest and most important member should lead the process of modernization and harmonization of conflict rules in the region. Unfortunately, while the Brazilian attitude in favor of regional integration is firm at political level, it doesn't correspond from a legal perspective to the pressing needs for change at the level of international commercial contracts.

As recently stated by João Grandino Rodas, with civic indignation, on the absence of new conflicts rules in the new Brazilian *Civil Code*:

> *The primitivism and inadequateness of our private international law rules are not compatible with the fact that Brazil is the "condottiere" in the regional integration process and seeks an outstanding role in the hemispheric integration process. That undesirable paradox reappears when we consider that the world's ninth biggest economy has been, for a long time, seeking to increase its exports, their indispensability having been recently proclaimed: "exports or death" or "exports to live".*
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> [...]
>
> *Brazil, whose juridical respectability is uncontested, even at international level, does not deserve that terrible omission.*[71]

The economic policy of free flows of goods, services, capitals and individuals relates not only to the MERCOSUR's regional integration goals, but also has to do with the individual countries' goals of international reinsertion in the context of the late XXth century economic globalization.

Legal instruments that stimulate, both at hemispheric and global levels, the exchange of goods and services indicate an evolution in respect to the treatment of foreign partners and investments because they can deliver the needed certainty and

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71 Article published in the Brazilian Newspaper *Gazeta Mercantil* on September 9, 2001.

stability to international transactions increasingly deterritorialized and unconnected with a single national legal system.

To this end the public sector must join the private sector's efforts in promoting the diffusion, acceptation and application of the Principles.

As guise of conclusion, we show below some of the 1999 UNIDROIT model clauses indicating the Principles as the applicable law. Contracts should also contain an arbitration agreement so as to ensure effectiveness to the choice of the Principles as the applicable law.

The first suggested formula indicates the parties' intention to submit their contract to the Principles, which can be expressed by the use of the following expressions, with the exceptions or modifications the parties should find convenient to their interests:

> *This contract shall be ruled by the Principles of the UNIDROIT (1994)* [under the exception of articles ...]

The second suggested formula indicates the parties' intention to supplement the adoption of the Principles with the norms of a national legal system:

> *This contract shall be ruled by the Principles of the UNIDROIT (1994)* [under the exception of articles ...], *completed, when necessary, by the laws of* [country X].

Considering the several alternatives for the choice of the Principles as the law applicable, partially or totally, to the contract, we can also conceive a number of variations around the model clauses above, which indicate the Principles along with the choice of a national law or international convention of uniform law (such as that of Vienna on International Purchase and Sale of Goods – 1980), for the purpose of completing them or construing them.

What now needs to be done is get to work and incite, among businessmen and legal practitioners, the utilization of the *UNIDROIT Principles of International Commercial Contracts.*