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INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW

PROGRESSIVE CODIFICATION OF INTERNATIONAL TRADE LAW

UNIFORM RULES ON INTERNATIONAL CONTRACTS IN GENERAL

Chapter 3 : THE SUBSTANTIVE VALIDITY OF INTERNATIONAL CONTRACTS

(Section 2 : Public Prohibitions and Permission Requirements)

(Text prepared by Professor Maskow of the Institut für ausländisches Recht und Rechtsvergleichung, Potsdam-Babelsberg, for consideration by the Informal Working Group on the Progressive Codification of International Trade Law)

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## CHAPTER 3

### THE SUBSTANTIVE VALIDITY OF INTERNATIONAL CONTRACTS

#### Section 2: PUBLIC PROHIBITIONS AND PERMISSION REQUIREMENTS

##### Introduction

1. The new version of Chapter 3, sect. 2 considers the decisions and discussions during the third meeting of the Informal Working Group on the progressive codification of international trade law (from 11. to 13. april 1983 as contained in the report UNIDROIT 1983, P.C. - Misc. 4). Some further amendments proved to be necessary, to maintain a consistent text mainly relating to drafting.
2. The main idea of the proposal as amended remained the combination of conflicts of law and direct rules. For the time being this approach is inevitable since it turns out to be impossible to unify all the relevant national regulations on prohibitions and permission requirements. Furthermore this would go far beyond the terms of reference of UNIDROIT. On the other hand it would be a serious gap in the rules of the progressive codification if they would not deal with this problem at all, being of extreme importance for the international trade.

In solving the conflicts of law problems the principle of a cumulative application of different national prohibitions and permission requirements has been used. This relates to the conditions, procedures and legal consequences. The prohibitions and permission requirements relevant in the sense of the rules are determined in Art. 1 and in Art. 2 together with certain further limitations (Article 2, sect. 2) or with extensions

(Article 2, sect. 3). These provisions correspond to the international practice, though they are up to now not yet clearly and in a general manner reflected in legal rules.

3. The proposed rules unify certain consequences for the contract resulting out of the existence of national regulations of different countries as far as it is possible at this stage. They distribute the obligation to obtain permissions and determine the consequences in case of breach (Art. 3), fix the date of full effectiveness of a contract subject to permission requirements (Art. 4), are directed against certain forms of abuse (Art. 5), and deal with the fate of the contract where only individual terms are prohibited or not permitted (Art. 6).
4. The point of gravity of the proposed rules are the unified rules, but they presuppose that their scope is described and this can only be done by reference to national regulations, which include regulations based on international agreements.
5. The former Art. 7 (mandatory character) has been left out, since this problem shall be clarified in a more general framework. Furthermore especially this provision caused objections at the 62nd session of the Governing Council (UNIDROIT 1983, C.D. 62nd session, p.8). Indeed it is difficult to prescribe a mandatory character of the one or the other provision, since it is in most cases possible to make amendments in the one or the other direction. Lastly, the proposed rules are a mixture of conflicts of law rules and direct regulations, therefore the mandatory character does not only depend on the rules

themselves, but also on the prescriptions to which they relate. Therefore it seems advisable to postpone the decision up to the clarification of the character of the whole undertaking.

#### Article 1: Definitions

1.A "public prohibition" means a prohibition mainly directed at the implementation of a general policy of the State, and not mainly aimed at justice between the parties, which results from general accessible rules of law and the non-observance of which according to the law of the State establishing such public prohibition makes the contract or individual terms of the contract null and void.

2.A "public permission requirement" means a permission requirement mainly directed at the implementation of a general policy of the State, and not mainly aimed at justice between the parties, which results from general accessible rules of law, whereby the right to permit is exercised by an institution exercising public authority, and the absence of which according to the law of the State establishing such public permission requirement prevents the contract or individual terms of the contract from taking full effect.

#### Comment

Art. 1 defines the national public prohibitions and permission requirements falling within the scope of the rules by three main features: aim, accessibility, and legal consequences of non-observance. The aim is described in a positive and in a negative way, which shall explain each other. This was in particular advisable,

since it may be looked at also as the general policy of the State to achieve justice between the parties, though this special aim should not be taken into consideration by the rules. The condition of accessibility was necessary, since the existence of prohibitions and permission requirements has farreaching effect according to the rules, so that either party must know the respective prescriptions or must at least have the possibility to make himself known of them (ought to have known them). Where the parties inform each other about further permission requirements they can be made subject to the proposed rules by contractual stipulations. The legal consequences are the criterion for the distinction between prohibitions and permission requirements. They may be laid down in the same prescriptions as the prohibitions and permission requirements or may be derived from general rules of law related thereto. Though the legal consequences of the instruments used to ensure the general policy of the State in matters of external economy are much more differentiated than reflected here, the most important forms can be subsumed under the definitions in an abstract manner.

Since a public permission is an individual act it is granted by specified organs which may be organs of the State, but also other bodies to which this function is endorsed, but in any case these are "institutions exercising public authority".

A contract is null and void, if it is invalid ab initio and cannot become valid later on. A contract does not take full effect, where it does not take effect in respect of the most important obligations of the parties relating to the performances to be rendered by them, but takes effect insofar as it imposes

certain obligations on the parties to ensure the contract taking full effect, as described especially in Art. 3.

Article 2: Public prohibitions and permission requirements to be considered

1. The provisions of this section apply to public prohibitions and permission requirements provided in legal rules which claim application to the contract whatever be the law governing the contract and have a close and significant connection with the contract.

2. Foreign public prohibitions and permission requirements may be refused application if they do not satisfy the essential requirements of international trade or the legitimate interests of other States having a close and significant connection with the contract.

3. Nothing in these rules shall limit the application of legal rules of the forum which claim application to the contract.

Comment

While Art. 1 defines prohibitions and permission requirements in general, Art. 2 further limits the application of the respective rules by general criteria referring to the intention of the State establishing the prohibitions or permission requirements and to the individual circumstances of the case (para 1). But even if this criteria are met, the application of foreign rules on prohibitions and permission requirements may be refused under certain circumstances (para 2), while on the other hand

the legal rules of the forum may be applied, even if they do not correspond to the definitions of the rules or the criteria for applicability laid down therein, e.g. have no close and significant connection with the contract (para 3). The last half sentence of para 3 shall make clear that in particular an arbitration acting in a third State which has nothing to do with the contract at all is not bound to apply the corresponding legal rules of that State.

The public order requirements of the State of the forum may be covered either by para 2, since also the legitimate interests of the State of the forum have to be taken into account, or by para 3, since they might be looked at as legal rules of the forum, with the peculiarity that they are directed at the nonapplication of certain foreign rules.

The basic principle according to which the conflicts of law problems in this special field are solved by Art. 2 is the cumulative application of relevant regulations. The problem of conflicting national prohibitions and permission requirements is not expressly dealt with, though it may be partly solved by paras 2 and 3.

Article 3: Obligation to obtain public permission

1. The party whose place of business is situated in the State that requires the public permission shall take such measures as are necessary to obtain such permission. If public permission is required by the law of a State in which none of the parties has his place of business that party shall take such measures as

are necessary to obtain permission who has to perform the act subject to permission or, where the contract as a whole is subject to permission, who is in a better position to do so.

2. The party required to take such measures as are necessary to obtain public permission (the applicant party) shall do so without undue delay and with the due diligence. The applicant party shall bear any expenses entailed and inform the other party of receipt or final refusal of such permission without undue delay.

3. If the applicant party does not take the measures required within an agreed period or within a reasonably extended period fixed by the other party or where no period has been determined in this manner within /6/ months from the formation of the contract, the other party is entitled to terminate the contract. The same applies, if the applicant party has not informed the other party of the receipt of the public permission within such period.

4. Both parties are entitled to terminate the contract, if notwithstanding the fact that the applicant party took all measures required, he failed to obtain the public permission within the period indicated in paragraph 3 or if the public permission was finally refused.

5. Where a party fails to fulfil his obligations according to paragraphs 1 and 2, the other party may claim damages, without prejudice to any other rights he may have.

#### Comment

This Art. creates and distributes the obligation to apply for permissions (para 1). Since it might be difficult to determine



the party who is in a better position to get the permission (para 1, second sentence second case) the parties should reach a contractual arrangement.

Para 2 precises the details of the obligation to obtain permission. Para 3 gives a right to the innocent party to terminate the contract, if the obligation to obtain permission has not been fulfilled within certain time limits. In this case termination means that the partial effect which was attributed to the contract (comment to Art. 1) ceases to exist. As long as the innocent party does not terminate the contract it may claim performance, that means that the other party undertakes the measures required. The other party is not responsible for the success of his efforts, but only for doing the acts necessary for that aim.

According to para 4 both parties are entitled to termination, where the nonobtainment of the permission does not depend on either of them.

The amount of the damages the innocent party is entitled to according to para 5 is to be determined by later chapters of the rules. The other rights mentioned in the last part of para 5 are especially the right to terminate the contract.

#### Article 4: Granting of public permissions

1. A contract which is subject to public permission requirements becomes fully effective upon the granting of the last permission required, unless a later date is indicated in one of the permissions.

2. If the applicant party does not inform the other party of the receipt of the public permission, the applicant party cannot

rely on the full effectiveness of the contract in relation to the other party.

#### Comment

The full effectiveness is made dependant on the last permission or the latest date indicated in the permissions. The effect of the granting of permission is regulated directly and not by reference to national law/since, as the case may be, several permissions have to be taken into consideration. Here as well the cumulative application becomes apparent (para 1).

Para 2 shall inter alia cover the case, where the dates for performance are made dependant on the contract taking full effect. A party does not commit a breach of contract if his acts or omissions are caused by his lack of information about ~~the~~ of the contract taking full effect.

#### Article 5: Party with more than one place of business

A party may not rely on any public prohibition or permission requirement applicable according to these rules, where he can reasonably be expected to perform the contract by a branch operating in a State where, no such prohibition or permission requirement exists.

#### Comment

This provision shall prevent that a party may abuse these rules by claiming nullity or the contract not taking full effect, where he is in a position to perform the contract via a branch

not subject to the prohibitions or permission requirements in question, provided this does not amount to an evasion of the law valid at the originally relevant place of business, since in that case performance via a different branch cannot reasonably be expected.

Article 6: Public prohibitions and public permission requirements concerning individual terms of contract

Where public prohibitions or permission requirements refer only to individual terms of the contract, then in cases of such prohibition or of failure to obtain such permission within the period fixed in Article 3 paragraph 3 or of refusal of permission, the contract shall be considered to be concluded, if giving due consideration to all circumstances of the case, it is reasonable to uphold the remaining contract.

Comment

The principle used for upholding the contract is the same as used in Art. 15 of Chapter 3, section 1.