

UNIDROIT 2001
Study L – Misc. 23
(English only)

UNIDROIT

International Institute for the Unification of Private Law

WORKING GROUP FOR THE PREPARATION OF
PRINCIPLES OF INTERNATIONAL COMMERCIAL CONTRACTS

SUMMARY RECORDS

of

THE MEETING HELD IN ROME

FROM 4 TO 7 JUNE 2001

(Prepared by the Secretariat of UNIDROIT)

Rome, July 2001

1. The Working Group for the preparation of Part II of the UNIDROIT Principles held its fourth session in Rome (Italy) from 4 to 7 June 2001. The session was attended by M.J. BONELL (UNIDROIT, Chairman), P.-A. CRÉPEAU (Canada), S.K. DATE BAH (Ghana), A. DI MAJO (Italy), E.A. FARNSWORTH (U.S.A.), P. FINN (Australia), M. FONTAINE (Belgium), M. FURMSTON (United Kingdom), HUANG DANHAN (China), C. JAUFFRET-SPINOSI (France), A. KOMAROV (Russian Federation) and P. SCHLECHTRIEM (Germany). F. DESSEMONTET (Swiss Association of Arbitration), H. GRIGERA NAÓN (ICC Court of Arbitration), G. SCHIAVONI (Milan Italian and International Chamber of Arbitration) and J. SEKOLEC (UNCITRAL) attended as observers. The session was also attended by H. KRONKE (Secretary-General of UNIDROIT). The list of participants is attached as APPENDIX I.

2. The session focussed mainly on the revised draft Chapter on Authority of Agents prepared by M.J. Bonell (UNIDROIT 2001 Study L - Doc. 67), the revised draft Chapter on Limitation Periods prepared by P. Schlechtriem (UNIDROIT 2001 Study L - Doc. 68), the revised draft Chapter on Assignment of Rights, Transfer of Obligations and Assignment of Contracts prepared by M. Fontaine (UNIDROIT 2001 Study L - Doc. 69), the revised draft Chapter on Third Party Rights prepared by M. Furmston (UNIDROIT 2001 Study L - Doc. 70) and the draft Chapter on Set-off prepared by C. Jauffret-Spinosi (UNIDROIT 2001 Study L - Doc. 71).

I. AUTHORITY OF AGENTS

3. Crépeau took the Chair.

4. In introducing the draft Chapter on Authority of Agents (UNIDROIT 2001 Study L – Doc. 67) Bonell recalled that the draft Chapter had been the subject of lengthy discussion first in Bozen and then in Cairo. The draft presented in Bozen was modelled on the Geneva Convention on Agency in the International Sale of Goods (hereinafter “Geneva Convention”). Yet on that occasion the had Group decided to introduce some significant changes, above all with respect to the so-called undisclosed principal. In Cairo the revised draft was adopted in substance, subject to one or two changes.

5. The Group proceeded to an article-by-article examination of the draft.

- Article 1: (1) This chapter governs the authority of a person, the agent, to affect the legal relations of another person, the principal, by or with respect to a contract with a third party, whether the agent acts in its own name or in that of the principal.*
- (2) It governs only the relations between the principal or the agent on the one hand, and the third party on the other.*
- (3) It does not govern an agent’s authority conferred by law or the authority of an agent appointed by a public or judicial authority.*

6. Bonell pointed out that there were no changes with respect to the draft agreed in Cairo.

7. The article was adopted.

Article 2: (1) The principal's grant of authority to an agent may be express or implied.

(2) The agent has authority to perform all acts necessary in the circumstances to achieve the purposes for which the authority was granted.

8. Bonell pointed out that there were no changes with respect to the draft agreed in Cairo.

9. The article was adopted.

Article 3: (1) Where an agent acts within the scope of its authority and the third party knew or ought to have known that the agent was acting as an agent, the acts of the agent shall directly affect the legal relations between the principal and the third party and no legal relation is created between the agent and the third party.

(2) However, the acts of the agent shall affect only the relations between the agent and the third party, where the agent with the consent of the principal undertakes to become party to the contract.

10. Bonell stated that a change of substance had been made in paragraph 2 so as to make it clear that the agent could never undertake to become party to the contract without the principal's consent.

11. Finn felt that the third party may not always know with whom it is actually dealing, i.e. the agent as an agent, though party to the contract, or with the agent as a principal. He suggested adding the word "the" before the words "party to the contract" in the last line of paragraph 2 so as to make it clear that it is the agent who is formally the only counter party of the third party.

12. It was so agreed.

Article 4: (1) Where an agent acts within the scope of its authority and the third party neither knew nor ought to have known that the agent was acting as an agent, the acts of the agent shall affect only the relations between the agent and the third party.

(2) However, where an agent acts as the owner of a business, the third party, upon discovery of the real owner of the business, may exercise also against the latter the rights it has against the agent.

13. Bonell recalled the history of this provision which in its original version corresponded in substance to Article 13 of the Geneva Convention and was intended to reconcile the common law doctrine of the so-called undisclosed principal and the civil law concept of commission agent. Indeed paragraph 1 stated the general rule that both the agent acting on behalf of an undisclosed principal and the commission agent, though acting within the scope of their authority, do not directly affect the relations between the principal and the third party, but are themselves parties to the contract, while paragraph 2 provided for an exception to this rule by admitting in case of default by the agent a direct action by the principal against the third party and vice versa. Paragraph 2 had been strongly criticised both in Bozen and in Cairo. Following the instructions received in Cairo he had slightly amended paragraph 1 and added a new paragraph 2. The new provision still provided an exception, though of a much narrower scope, to the general rule laid down in paragraph 2. It was based on *Grinder v. Bryans Road Bldg. and Supply Co.*, 432 A.2d 453 (Md. App. 1981), but also civil law systems admit that in commercial transactions a third party dealing with a person it believes to be the owner of the enterprise but who in fact merely acts as that enterprise's agent may, after discovering the truth, sue both that person and the real owner of the enterprise provided that the former had actual or apparent authority to act on behalf of the latter (see e.g. Article 2208 of the Italian Civil Code; for German law K. SCHMIDT, *Handelsrecht* (1999), p. 123 *et seq.*; BGHZ 62, 216).

14. Di Majo regretted that he had not participated in the Cairo session where he would have spoken in favour of the doctrine of undisclosed principal which he considered very important for the needs of international commercial contracts. He further objected that the new paragraph 2 provided only for a direct action of the third party vis-à-vis the principal and not vice versa.

15. Crépeau also regretted that there was no direct action in favour of the principal. In this respect he referred not only to Article 13 (2) of the Geneva Convention, but also to a similar rule to be found in Article 2165 of the Quebec Civil Code ("A mandator, after disclosing to the third person the mandate he has given, may take action directly against the third person for the performance of the obligations he contracted towards the mandatory who was acting in his own name").

16. Bonell recalled that the Group had decided to provide an exception to the rule in paragraph 1 only in favour of the third party. For him the rationale of such an approach lay in the fact that the third party should not bear the consequences of the agent's non-disclosure of its acting on behalf of an undisclosed principal, while a principal who originally decides that it is more convenient for him to remain behind the scenes and subsequently changes his mind because something goes wrong with the transaction does not deserve the same favourable treatment.

17. Farnsworth had a problem with Illustration 2 which clearly reflected the *Grinder* case. In both there was an implicit restriction which is not in the black letter rule of paragraph 2. So one of the two possibilities: either to introduce also in the black letter rule a similar restriction or to change the illustration to refer to a situation where A contracts in his own name without disclosing to supplier B that he is in fact acting only as the managing director of a company. His preference was for the first alternative, i.e.

to redraft the provision so as to suggest that there had to be some sort of responsibility for non-disclosure on the part of the former owner of the business.

18. Bonell agreed that there was a certain inconsistency between the rule and the illustration. However for him, though this may not be sufficiently clearly expressed, the rule was subject to a further qualification, i.e. that the act carried out by the agent must not be an isolated act with no reference whatsoever to a business but must fall within the activities of that business. Also DeMott to whom he had submitted the draft for further comments had made a comment much along the same lines as Farnsworth's, in the sense that for her too the exception to the rule in paragraph 1 was justified only in certain cases. However while Farnsworth referred to the agent's negligence in failing to disclose the changes which had occurred, DeMott put more emphasis on the fact that it must not be the third party's first contract with the supposed owner of the business but in fact its agent.

19. Finn seconded Farnsworth's remarks. For him what was decisive in paragraph 2 was that the agent held himself out as the owner or the business, i.e. represented to the third party a false situation.

20. Farnsworth suggested that Bonell and Finn prepare a new draft paragraph.

21. It was so agreed.

22. The new paragraph reads as follows:

“(2) However, where such an agent, when contracting with the third party on behalf of a business, represents itself to be the owner of that business, the third party, upon discovery of the real owner of the business, may exercise also against the latter the rights it has against the agent.”

23. Crépeau wondered what was the exact meaning of “business”. He felt that the rule should apply not only to commercial enterprises but to any sort of activity carried out by professional organisations.

24. Schlechtriem suggested that the Comments should make it clear that the term “business” should be understood in a broad sense so as to include professional organisations.

25. The Group agreed on the new wording of paragraph 2.

Article 5: (1) Where an agent acts without authority or exceeds its authority, its acts do not affect the legal relations between the principal and the third party.

(2) However, where the principal causes the third party reasonably and in good faith to believe that the agent has authority to act on behalf of the principal and that the agent is acting within the scope of that authority, the principal may not invoke against the third party the lack of authority of the agent.

26. Bonell pointed out that there were no changes with respect to the draft agreed in Cairo.

27. The article was adopted.

Article 6: (1) An agent that acts without authority or exceeds its authority is, failing ratification by the principal, liable for damages that will put the third party in the same position as if the agent had acted with authority and not exceeded its authority.

(2) However, the agent is not liable if the third party knew or ought to have known that the agent had no authority or was exceeding its authority.

28. Bonell recalled the decision taken in Cairo to hold the false agent liable not only up to the so-called negative or reliance interest, but up to the so-called positive or expectation interest.

29. Di Majo regretted that he had not participated in the Cairo session where he would have spoken in favour of reliance interest.

30. Furmston felt that in Illustration 2 it should be made clearer that the third party was dealing with a false agent. This could be done by replacing the word “senior” with “junior”.

31. The article was adopted.

Article 7: (1) If a contract concluded by an agent involves the agent in a conflict of interests with the principal of which the third party knew or ought to have known, the principal may avoid the contract. The right to avoid is subject to Articles 3.12 and 3.14 to 3.17.

(2) However, the principal may not avoid the contract

[(a)] if the principal had consented to, or knew or ought to have known, the agent’s involvement in the conflict of interests [;or

(b) if the agent had disclosed the conflict of interests to the principal and it had not objected within a reasonable time].^()*

32. Bonell pointed out that there were no changes with respect to the draft agreed in Cairo.

^(*) Since lit. (a) already covers the situation where the principal upon disclosure by the agent consents to the agent’s involvement in the conflict of interest, it might be argued that lit. (b) only makes sense if it deals with a disclosure by the agent after the contract has been made. If this is the case, lit. (b) could be considered superfluous since it goes without saying that the principal loses its right to avoid the contract if it fails to object once it has been informed that the agent had concluded the contract in a situation of conflict of interests.

33. Huang pointed out that Illustration 3 could be understood to mean that bank A sells its own shares to B and not Company X's shares as requested by B.

34. Bonell completely agreed and promised to change the wording so as to avoid such a misunderstanding.

35. The article was adopted.

Article 8: An agent has implied authority to appoint a subagent to perform acts which it is not reasonable to expect the agent to perform itself. The rules of this chapter apply to the subagency.

36. Bonell pointed out that there were no changes with respect to the draft agreed in Cairo.

37. The article was adopted.

*Article 9: (1) An act by an agent that acts without authority or exceeds its authority may be ratified by the principal. On ratification the act produces the same effects as if it had initially been carried out with authority.
(2) The third party may by notice to the principal specify a reasonable period of time for ratification. If the principal does not ratify within that period it can no longer do so.*

38. Bonell pointed out that there were no changes with respect to the draft agreed in Cairo.

39. The article was adopted.

*Article 10: (1) Termination of authority is not effective in relation to the third party unless the third party knew or ought to have known of it.
(2) Notwithstanding the termination of its authority, an agent remains authorized to perform the acts that are necessary to prevent harm to the principal's interests.*

40. Bonell pointed out that there were no changes with respect to the draft agreed in Cairo.

41. The article was adopted.

II. DRAFT CHAPTER ON LIMITATION PERIODS

42. In introducing the draft Chapter on Limitation Periods (UNIDROIT 2001, Study L – Doc. 68) Schlechtriem recalled that previous versions of the draft had been discussed by the Group at its second and third sessions in Bozen and in Cairo.

43. The Group then proceeded to make an article by article examination of the draft

Article 1: (1) Rights governed by these Principles cannot be exercised after expiration of a period of time, referred to as “limitation period”.

(2) This chapter does not govern the time within which one party is required under these Principles, as a condition for the acquisition or exercise of its right, to give notice to the other party or perform any act other than the institution of legal proceedings.

(3) In these rules

(a) [“legal proceedings” includes judicial, arbitral and administrative proceedings]

(b) [“person” includes corporation, company partnership, association or entity, whether private or public, which can sue or can be sued:]

(c) [“year” means a year according to the Gregorian calendar.]

44. With respect to paragraphs 1 and 2, Schlechtriem explained that it was Farnsworth who had suggested using the word “rights” instead of “actions” or “claims” because not only claims could be cut off by limitation periods, but also rights such as the right to terminate a contract. As to the term “limitation period” it was in conformity with the United Nations Convention on the Limitation Period in the International Sale of Goods (hereinafter Limitation Convention) and, unlike the term “prescription” used in the Principles of European Contract Law (hereinafter PECL), implied that the lapse of time does not extinguish rights but only limits their enforcement.

45. Fontaine agreed but pointed out that the French version will have to use the term “prescription”.

46. The Group agreed to Article 1 (1) and (2).

47. With respect to paragraph 3 Schlechtriem recalled that the definitions in square brackets had been taken from the Limitation Convention entirely and that the Group should decide whether to retain them or not.

48. Crépeau wondered whether the definitions could be built into Article 1.10 of the present edition of the Principles in which case they would apply in all instances.

49. Bonell felt that at least with respect to the definition of “legal proceedings” this could prove to be problematic because the inclusion of administrative proceedings made

sense only in the special context of the present Chapter, but not for instance in the Chapter on Hardship.

50. Schlechtriem agreed.

51. Furmston suggested using the wording “proceedings before administrative tribunals” rather than “administrative proceedings”.

52. Dessemontet questioned the definition in *lit.* (a) in view of Article 10 on Alternative Dispute Resolution (ADR). He felt that one might infer from it an exclusion of ADR.

53. Schlechtriem was reluctant to include ADR as a kind of legal proceeding in the definition. ADR covered too great a variety of ways of settling disputes.

54. Fontaine pointed out that the term “legal proceedings” only appeared in Article 12, while Article 8 expressly referred to “judicial proceedings”, Article 9 to “arbitral proceedings” and Article 10 to “ADR”. Perhaps it was not worth the effort to have a definition of legal proceedings if the term was used only once.

55. The Group decided to delete *lit.* (a)

56. With respect to *lit.* (b) Bonell wondered whether there the term “person” was used elsewhere in this Chapter.

57. The Group decided to delete *lit.* (b).

58. With respect to *lit.* (c) Schlechtriem recalled that there had been a lively discussion in Cairo on the term “year” which did not have the same meaning in all languages and all legal systems. He felt that for the sake of clarity reference to the Gregorian calendar might be useful. However if only the definition to be retained was “year” it could be placed in the Comments. He recalled that no such definition appeared in the PECL which however are confined to Europe where there can be no misunderstanding about what “year” means. On the other hand the Limitation Convention had a definition of “year”.

59. Furmston wondered whether there were different cultures in which a year was not composed of 365 days. In his view the most obvious difference between the different calendars was the system for calculating when the year starts. Yet since in the context of a chapter on limitation periods what mattered was the length of the year and not when it starts, he felt that such a difference was irrelevant.

60. Date Bah agreed.

61. Dessemontet wondered whether it might not be advisable to say something in the Comments to the effect that the “year” is something depending on the proper interpretation of the contract.

62. Bonell saw two aspects to the problem: on the one hand, how to interpret the concept of “year” as used in the Principles; on the other hand, how to interpret the term “year” if used by the parties in their contract. The latter question could be settled under Chapter 4, while with respect to the former, he wondered whether the meaning of the term “year” could be addressed in the Comments only.

63. Farnsworth agreed.

64. Bonell saw no further support for keeping the definition in the black letter rules and suggested that the Rapporteur mention in the Comments the problem of differently termed and/or structured years, referring to the way in which it was settled for instance in the Limitation Convention.

65. Schlechtriem agreed and the Group decided to delete *lit. (c)*.

Article 2: The general limitation period is three years beginning on the day after the day the obligee knows or ought to know the facts as a result of which the right has become due.

Article 3: The maximum limitation period is ten years beginning on the day after the day the right became due.

66. Schlechtriem pointed out that in substance the two provisions had already been adopted in Cairo and that he had simply divided them into two separate articles.

67. Di Majo wondered whether only Article 3 dealt with limitation periods while Article 2 addressed what is known in Italian law as “decadenza”.

68. Bonell replied that “decadenza” was addressed in Article 1 (2) while both Article 2 and Article 3 dealt with limitation periods distinguishing between a shorter one commencing on “the day after the day the obligee knows or ought to have known” and a maximum period of time which applies irrespective of any (constructive) knowledge of the creditor.

69. Finn wondered whether this could be clarified by beginning Article 2 with “Subject to Article 3 the general limitation period is ...”.

70. As an alternative Bonell suggested the wording “In no case shall the period be more than 10 years”.

71. Furmston wondered whether in Article 2 “knew” or “ought to have known” would be preferable to “knows” and “ought to know”.

72. Farnsworth liked the present draft.

73. Crépeau had a problem with the term “the right becomes due”. PECL used the formula “when the debtor has to effect performance” and “from the date of the act

which gives rise to the claim” and the Limitation Convention “when the claim accrues”. In French one speaks in this respect of *exigibilité*.

74. Fontaine had understood “due” in the sense of *exigible*.

75. Schlechtriem recalled that this matter had been discussed in Cairo at length and that the Group had decided to understand the word “due” as “enforceable”. He would mention this in the Comments.

76. Crépeau insisted that the French concept of “exigible” corresponded in English either to “enforceable”, “exigible” or “accrued”, but certainly not to “due”.

77. Schlechtriem recalled that the PECL had a provision stating that the period of limitation does not begin to run before the claim can be enforced as long as the obligor has a defence. He thought it would be possible and a bit more elegant to say “due” and explain in the Comments that “due” means “enforceable”.

78. Furmston pointed out that, although the word “exigible” might be found in the Oxford English Dictionary, no English lawyer would ever use it. On the contrary, the word “enforceable” was often used. He felt that the illustrations in the Comments should clarify this point.

79. Farnsworth thought that Canadian and US English may be different in this respect. He thought that a right that was on a term would be an enforceable right. One would not say it was not enforceable, but just that it was not yet “due”. Therefore he preferred “due” to “enforceable”, but wondered whether the discussion should not be discussed in the context of the chapter on set-off.

80. Schlechtriem referred to his comments where he had stated that “the right has become due” includes the notion of enforceability regardless of the technical dogmatic explanations of the obligor’s defences in domestic legal systems. If the obligor/debtor has a defence which may defeat the obligee’s/creditor’s claim, the claim is not yet due regardless of whether the defence has to be raised in court or takes effect *ipse jure*. For that reason he thought that “due” would cover it. He feared that “enforceable” might be misunderstood as something having to do with the law of procedure and execution.

81. Furmston thought it not just a question of defences and gave the following illustration: I have an account with a bank and I have a contract. Sometimes the account is in credit, sometimes it is in debt. Sometimes the bank owes me money and sometimes I owe the bank money. In English Law limitation period is not running because the money is not due until a demand is made. Limitation period starts to run only when I demand payment or when the bank demands payment. And that is a fundamentally different question from whether there is a debt. Of course there is a debt. But the debt is not immediately payable. It is payable on demand and therefore the limitation period is not running. That is not a question of defences. No English lawyer would explain that on the grounds that the debtor has a defence. The money is not due and that is absolutely clear in English or Australian law.

82. Schlechtriem saw no controversy between Furmston and himself.

83. Jauffret-Spinosi wondered why it was necessary to know the facts as a result of which a right has become due. If you know that the right has become due you normally know why the right has become due and what the facts are which have made that right become due.

84. Schlechtriem recalled that this too had already been discussed. In his first draft he had used the wording “knows his right” but then the question was brought up that the obligee might know the facts but might interpret them wrongly, because he does not have the necessary legal knowledge.

85. Crépeau asked Schlechtriem why Article 2 says “the facts as a result of which the right has become due” and Article 3 “after the day the right becomes due”. He wondered whether there was a difference in substance.

86. Schlechtriem was not sure that he had understood Crépeau. “The right has become due” has been used in both Articles 2 and 3 as a starting point. In addition to becoming due, to apply Article 2 the general period of limitation, the obligee must know the facts which lead to this claim or the right becoming due.

87. Crépeau was perfectly willing to go along, but the present wording seemed to introduce a difference between the two periods of limitation. He thought that the ambiguity arising from the necessity of knowing the facts as a result of which the right becomes due was such that the question was when the right itself becomes exigible.

88. Schlechtriem insisted that the basic idea was that a claim or right becomes due and from that moment on the maximum period begins to run, while the general 3 year period needs an additional element, i.e. the actual or constructive knowledge of the obligee of these facts that made the claim.

89. The Group agreed on Articles 2 and 3 as proposed.

Article 4: [The limitation periods in Articles 2 and 3 also apply to ancillary claims such as claims for interest or costs.]

90. Schlechtriem recalled that so far the Group had taken no decision on the length of limitation periods for ancillary claims. There were two possible solutions and several arguments for or against them. One solution was that ancillary claims are cut off together with the main claim. The other solution (which he proposed though between square brackets) was that every ancillary claim should have its own limitation period. The reason for his favouring the second solution was that it was very difficult to define the very concept of “ancillary claim”. If it was decided to state “Ancillary claims are cut off together with the main claim”, he was sure that in practice this would induce parties to claim that their claims were not cut off because they were not ancillary claims but main claims. Were penalties, for instance, ancillary claims? He suggested mentioning in the Comments that any attempt to distinguish between ancillary and main

claims had been given up and the decision taken that all claims fall under Article 2 and 3 with the consequence that there was no further need to qualify claims for penalties, interest and so on.

91. Dessemontet pointed out that not only Finnish law and Swiss law (Article 133 of the Code of Obligations) but also PECL (Article 17:114) adopted the opposite solution. He had no definite opinion on the matter but wanted the Group to bear in mind that there were not only things that were strictly accessories such as the interest on arrears, but also personal sureties such as pledges where there is a question of the protection of the debtor. If someone is engaged for the debt of someone else, of course he is not protected by the solution proposed in the draft, but would be protected by the Finnish/Swiss/PECL solution.

92. Di Majo thought the concept of “ancillary claim” should be defined and that this was not easy to do.

93. Komarov on the contrary preferred not to have a special provision on ancillary claims in the chapter.

94. Date Bah agreed.

95. Also Fontaine favoured the deletion of Article 4. In order to demonstrate how difficult it might be to decide whether a given claim was ancillary or not he gave the example of a penalty clause. One may argue that it was an ancillary claim but if in case of non-performance by one party the other asks for the payment of the penalty this is clearly a main claim.

96. Bonell wondered whether the Group could agree to delete the article between square brackets and to mention in the Comments that with respect to so-called ancillary claims, no hard and fast rule had been adopted given the extreme difficulties in defining the concept and deciding whether a particular claim was ancillary or not.

97. Schlechtriem thought it a good suggestion. Contrary to consumer transactions, in international trade it should be up to the parties to decide whether a particular claim is to be considered ancillary or not. Thus for instance when drafting a surety document parties may state that all claims should or should not fall under the same limitation period as a claim for repayment of the capital. It would be a matter of calibrating the sureties.

98. It was so agreed.

Article 5: (1) The parties can modify the periods of limitation.

(2) However the parties cannot

(a) shorten the general limitation period to less than one year;

(b) shorten the maximum limitation period to less than 4 years;

(c) extend the maximum limitation period to more than 15 years.

99. It was decided to replace in both the title and in the text the term “periods of limitation” by the term “limitation period” and to replace the words “can” and “cannot” by “may” and “may not”.

100. As to the substance Schlechtriem recalled that there were two reasons for allowing parties to modify the limitation period: first, the Principles were intended to apply to contracts between experienced merchants who can take care of their needs; secondly, commercial practice needed a flexible system.

101. Bonell asked for comments on paragraph 2 *lit.* (a).

102. As there were no comments, the paragraph was adopted.

103. Bonell asked for comments on paragraph 2 *lit.* (b).

104. As there were no comments, the paragraph was adopted.

105. With respect to paragraph 2 *lit.* (c) Di Majo suggested it be deleted so that parties may not extend the maximum limitation period.

106. Bonell recalled that in Cairo the extension to 15 years had been envisaged bearing in mind the important area of construction contracts where it made sense to permit the parties to extend the limitation period beyond ten years.

107. Komarov and Date Bah wondered whether the article was a mandatory provision or not. In view of the fact that Article 1.5 of the Principles states that all provisions are non-mandatory unless otherwise provided in the Principles, if this article was considered to be mandatory, it should be expressly stated so.

108. Bonell felt that the semi-mandatory nature of the provision was already clearly expressed because it stated that parties can only modify the length of the limitation period within certain limits.

109. Schlechtriem added that the point could be dealt with in the Comments to both this article (with a reference to Article 1.5) and to Article 1.5 (with a reference to this article).

110. Huang requested clarification concerning the possibility of an implied modification of the limitation period, i.e. an agreement to this effect being inferred from the parties’ conduct.

111. In Schlechtriem’s opinion the general rules on contract agreement apply, i.e. not only is no writing required, but it can be either expressly or implicitly.

112. Di Majo, referring to a similar provision in Article 2937 of the Italian Civil Code, wondered whether the obligor may after the expiry of the limitation period renounce that exception and if so whether this could also be done implicitly.

113. According to Schlechtriem if the limitation period has expired there were several options. One option was mentioned in his comments (No. 4) to Article 7, i.e. an agreement between the parties to create a new obligation (novation). Another possibility was the unilateral renunciation of the exception of the expiration of the limitation period as envisaged in the provision of the Italian Civil Code cited. In the first case a new limitation period would begin to run with respect to the obligee's new right, while in the second case the obligor would be estopped from raising the defence of the exception. Both possibilities however followed from the general principles on party autonomy laid down elsewhere in the Principles so that it would not be necessary to expressly mention them in the black letter rules; mention could be made of them in the Comments.

114. Dessemontet first of all missed a provision stating explicitly that the expiry of the limitation period cannot be raised *ex officio* by the judge or arbitrator. Secondly he thought it should be made clear in Article 5 that modifications of the length of the limitation period may be agreed upon by the parties only before or after the commencement of the limitation period itself so as to distinguish more clearly the cases envisaged by this article from possible renunciation or waiver of the limitation period after its expiry.

115. Bonell wondered whether the last suggestion by Dessemontet could be taken care of by redrafting Article 5 (1) so as to read "The parties may, either before or after the commencement of the limitation period modify it".

116. Schlechtriem thought that a Comment to that effect would be enough.

117. Fontaine thought that the rule that the parties may not waive limitation periods in advance was already there. Indeed, by saying that parties cannot shorten the limitation period to less than 1 year or to less than 4 years, *a fortiori* it would not be possible to waive limitation periods in advance. This would reduce limitation periods to zero year.

118. The Group agreed to adopt Article 5 with the amendments indicated in paragraph 99 above and to ask the Rapporteur to include in the Comments references to the other issues discussed.

Article 6: [The limitation periods under Articles 2 and 3 can be suspended or interrupted. A "suspension" of the limitation period means that during a suspension the limitation period ceases to run for the time of the existence of the event causing suspension or up to a certain date, while »interruption« causes the limitation period to begin again at the time stated in the special provision on interruption.]

119. Schlechtriem expressed a slight preference for having a provision defining the two concepts of suspension and interruption of the limitation period.

120. While Date Bah and Crépeau thought that these definitions would be well placed in the Comments rather than in the black letter rule, Di Majo and to a certain extent also Farnsworth expressed their preference for a black letter rule.

121. Schlechtriem acknowledged that suspension would also be defined in Article 8. With respect to the notion of interruption, he suggested starting the Comment on Article 7 with a statement that the effects of an acknowledgement are usually called an interruption and to use that notion throughout the Comments wherever needed. In this case Article 6 would become superfluous.

122. The Group decided to delete Article 6 and asked the Rapporteur to incorporate, at least as far as interruption is concerned, its content in Comment No. 1 on Article 7.

Article 7: Where the obligor, before the expiration of the limitation period, acknowledges expressly or impliedly the right of the obligee, a new general limitation period begins on the date of the acknowledgement but the maximum limitation period is not affected.

123. It was agreed to replace the words “on the date of acknowledgement” by “on the day after the day of the acknowledgement” so as to align the provision with the wording used in Articles 2 and 3.

124. Schlechtriem recalled that in the previous version of the draft (UNIDROIT 1999 – Study L Doc. 64) the article contained a second paragraph stating that acknowledgement could be either express or implied, orally or in writing, and providing some examples of implied acknowledgement such as part performance, payment of interest, etc. Following the decision the Group took in Cairo to delete paragraph 2, what was left of this paragraph were the words “expressly or impliedly” which appeared in the present version of Article 7.

125. Farnsworth pointed out that a matter of general drafting policy was involved, i.e. whether to specify that agreements may be not only express but also implied whenever the question arises or to have such a principle stated once and for all in a general provision. He felt that the matter should, in any case, be considered in the context of the general revision of the Principles in view of their new edition.

126. Crépeau wondered whether it was necessary to include the words “expressly or impliedly” since the same already followed from Article 5.1 of the Principles.

127. Schlechtriem thought that it could be questioned whether acknowledgement was in fact a juridical act to which Article 5.1 applied.

128. Bonell agreed with Crépeau in the sense that it would be one of the few, if not the only, instances where such additional language is used and recalled, as an example where this had not been done, ratification in the chapter on agency.

129. Farnsworth suggested adding in the Comment on Article 5.1 that this provision applied also to acts such as acknowledgements and ratifications.

130. The Group decided to delete the words “expressly or impliedly”.

131. Di Majo wondered why after acknowledgement only the general limitation period begins to run without affecting the maximum limitation period.

132. Schlechtriem replied that the Group had so decided on the assumption that interruption should not prolong the maximum period. The parties could only agree on a prolongation of up to 15 years and if this was not enough they could still agree on a novation so that a new limitation period for the newly created claim would run even after the expiration or before the expiration of the old limitation period.

133. Bonell felt that there was yet another justification for the rule. If only the general limitation period can be interrupted by acknowledgement, this was due to the fact that such limitation period starts running after the parties’ actual or constructive knowledge of the right, while the maximum limitation period envisages a situation where the obligee does not know.

134. Schlechtriem agreed. Any acknowledgement means that the other party now knows and there are the three years. But it cannot be another ten years. That is in the last part of the article. If parties wanted to prolong it then other means must be employed such as novation.

135. Finn wondered whether on account of acknowledgement a new right became due.

136. Schlechtriem pointed out that this was not the case and agreed that in the Comments acknowledgement does not create a new right or claim but it is still the old claim with an extended limitation period. A new right could only be created by an agreement between the parties after the expiration of the limitation period.

137. Dessemontet wondered whether Article 7 would lead to the result that an interruption, which normally would lead to an extension of another three years, in the ninth year would cause an extension of only one additional year.

138. Schlechtriem pointed out that the provision merely intended to exclude that an acknowledgement causes an extension of another ten years, while it should not be understood in the sense indicated by Dessemontet. In other words he agreed with Dessemontet that in his case there should still be an extension of a full three years, bringing the total length of the limitation period to twelve years. If the text was ambiguous it should be clarified.

139. Furmston on the contrary thought that the rationale behind the maximum limitation period was that at some point it must be over. If this was the case he would draw the opposite conclusion in the situation mentioned by Dessemontet, i.e. that an acknowledgement in the ninth year would result in an extension of only another year.

140. Farnsworth saw some merits in a solution according to which the maximum limitation period should be extended up to three years.

141. Date Bah agreed.

142. Bonell urged the Group to reach a conclusion on this matter.

143. Crépeau wondered whom the provision intended to protect: the obligee, the obligor or society?

144. According to Grigera, while the general interest of certainty in legal relationships was the prevailing rationale of the rules on limitation periods in domestic laws, in the context of the Principles more consideration should be given to the interests of the parties.

145. Fontaine agreed. In favour of permitting the extension of the maximum limitation period for another three years, he pointed out that the obligor has a maximum of ten years to bear the risk of being sued, but when he acknowledges, he should lose part of his protection.

146. Dessemontet agreed. The maximum period of ten years was in the interest of both the obligor and society as a whole which has no interest in legal proceedings brought to court after more than ten years after the claim became due. Yet if the obligor acknowledges the obligee's right, the situation was substantially different in so far as difficulties as to how to prove the right no longer existed.

147. Huang and Di Majo saw a contradiction between the present article and the previous one permitting a prolongation of the maximum limitation period up to fifteen years by agreement.

148. Schlechtriem argued that it was easier to say to an obligor "the period of limitation is running out, so if you don't do anything or acknowledge, I have to sue in order to suspend under Article 8" than to say to him "let's make an agreement modifying the period of limitation up to fifteen years". The obligor would be much more reluctant to enter into such an agreement. For substantially the same reasons he – Schlechtriem – was in favour of the possible prolongation of the maximum limitation period by the entire three year period. If we say the ten year period runs out regardless of acknowledgement, we are inviting judicial proceedings at this late stage, because this is the only means the obligee has to prevent the period of limitation from running out. He will address the debtor and say "you know the period of limitation is coming to an end. It was clearly in the interests of society if law suits could be avoided as a consequence of the debtor's acknowledgement. In order to avoid any misunderstanding he – Schlechtriem - suggested deleting the last part of the sentence in Article 7 and add in the Comments that only the general limitation period starts anew from the day after the day of acknowledgement and that the extension may well prolong the maximum period for an additional three years.

149. Date Bah was not sure whether in so doing matters would be sufficiently clarified.

150. Finn suggested deleting the words “but” in the second last sentence and “is not affected” in the last sentence and putting in “the maximum limitation period notwithstanding”.

151. Schlechtriem was not so sure whether such wording would avoid the sort of misunderstanding caused by the present text. At any rate he promised to clarify matters in the Comments. The Comments would also make it clear that if parties have shortened the general limitation period, in case of acknowledgement that period would be extended only up to such shortened period.

152. It was so agreed.

Article 8: (1) A limitation period ceases to run when the obligee performs any act that is recognized under the law of the court where the proceedings are instituted, as commencing judicial proceedings against the obligor or as asserting the obligee’s right in such proceedings already instituted against the obligor, for the purpose of obtaining satisfaction or recognition of the obligee’s right. Suspension lasts until a final decision has been issued or until the case has been otherwise disposed off.
(2) In case of the obligor’s insolvency or dissolution, the running of the limitation period shall be suspended when the obligee has asserted the right in the insolvency or dissolution proceedings for the purpose of obtaining satisfaction or recognition. Para. (1) s. 2 applies in regard to the end of the suspension respectively.

153. Schlechtriem pointed out that the article, with the exception of paragraph 2 which he had been asked to add, had already been discussed and agreed on in Cairo. Paragraph 2 corresponded in substance to Article 6 (4) of the previous draft.

154. Crépeau suggested that it should be made clear in the text that dissolution referred only to an entity.

155. Finn proposed inserting after the word “insolvency” the words “or, if an entity, its dissolution”.

156. Di Majo questioned the very substance of the provision. He thought that the commencement of a legal proceeding should be considered, as was the case of a number of domestic laws, a cause of interruption and not of a mere suspension of the limitation period.

157. Schlechtriem agreed that this was the position of a number of domestic laws but both the Limitation Convention (Article 13) and the PECL (Article 17:106) adopt a different solution, i.e. suspension.

158. Finn brought up the matter of discontinuance and urged the Rapporteur to refer to it in the Comments as an example of what is referred to in the provision by the words “the case has otherwise been disposed of”.

159. Furmston pointed out that paragraph 1 and paragraph 2, though addressing basically the same issues, used different language which made the whole article not very elegant. He produced the following amended draft in which nothing of substance had been changed.

“(1) The running of the limitation period shall be suspended

- (1.1) when the obligee performs any act that is recognised under the law of the court where the proceedings are instituted, as commencing judicial proceeding against the obligor; or
- (1.2) when the obligee performs any act that is recognised by the law of the court as asserting the obligee’s right in proceedings already instituted against the obligor;
- (1.3) in the case of the obligor’s insolvency when the obligee has asserted his rights in the insolvency proceedings; or
- (1.4) in the case of proceedings for dissolution of the entity which is the obligor when the obligee has asserted his rights in the dissolution proceedings.

(2) Suspension lasts until a final decision has been issued or until the case has been otherwise disposed of.”

160. Farnsworth had a problem with 1.1 because it did not refer to the right in question. In practice it may well happen that one commences proceedings which do not refer to the right in question but may only have some relationship to it and then later there may be an amendment, in which case 1.2 would apply. He suggested deleting 1.1 and broadening 1.2 by inserting the words “by commencing proceedings or otherwise”. The new sub-paragraph (1.1) would read as follows:

“(1) The running of the limitation period shall be suspended

- (1.1) when the obligee performs any act, by commencement of judicial proceedings or otherwise, that is recognised by the law of the court as asserting the obligee’s right against the obligor;”

161. Furmston pointed out that in his legal system there were endless cases where the claimant – the obligee – starts an action and then after a time it becomes clear that it had not formulated the claim in the right way and wants to amend. But in between the starting and the amending the limitation period has run out. This was a central problem and he wondered whether this was covered by the suggested wording.

162. Schlechtriem liked the draft amendment proposed by Farnsworth. As to Furmston’s last intervention he thought that the problems clearly related to procedural law and the answer to questions such as what exactly makes a claim or a right “pending” in a litigation differs considerably from country to country.

163. Finn raised a question about paragraph 2 referring to the final decision. Speaking from his own legal system there may be multi-party litigations with a final decision that may take years. But a decision may be rendered which is final in respect of

a particular right at a very early date. He wondered whether also such a final (partial) decision was covered by paragraph 2.

164. Schlechtriem wondered whether Finn's concerns could be met if the words "suspension lasts until a final decision has been issued or until the case has otherwise been disposed of under the law of the court" were added in paragraph 2. This would make it clear that the answer to his question depends on the of the court that decides.

164. Grigera Naón pointed out that the same problem very often arose with respect to arbitration and in his view paragraph 2 should definitely cover also partial awards that in a binding way put an end to specific claims.

166. Furmston felt that paragraph 2 was only important in cases where for some reason or other it is arguable that time has started to run again. If the judicial proceedings actually disposed of the claim, the limitation is no longer of any interest. Limitation would only be of interest in the very unusual cases where for some reason or another it is arguable that the limitation period has started to run again. But that after all is what suspension is. Suspension is to do with stopping the period running until it starts again. And that is all it is to do and therefore there is no need for an elaborate provision to deal with that.

167. With respect to the wording proposed by Farnsworth, Fontaine felt that the formula "by commencing judicial proceedings or otherwise" was too broad. There were other ways of asserting one's right such as "mise en demeure" which however would not be a cause of suspension. "Otherwise" should be linked to "judicial" and not to "judicial proceedings".

168. Farnsworth agreed and suggested changing the formula so as to read, "by commencing judicial proceedings or in judicial proceedings already instituted".

169. The Group tentatively agreed on the following text of Article 8:

"(1) The running of the limitation period shall be suspended

(1.1) when the obligee performs any act, by commencing judicial proceedings or in judicial proceedings already instituted, that is recognised by the law of the court as asserting the obligee's right against the obligor;"

(1.2) in the case of the obligor's insolvency when the obligee has asserted its rights in the insolvency proceedings; or

(1.3) in the case of proceedings for dissolution of the entity which is the obligor when the obligee has asserted its rights in the dissolution proceedings.

(2) Suspension lasts until a final decision has been issued or until the case has been otherwise disposed of."

Article 9: Where the parties have agreed to submit to arbitration, Art. 8 applies with appropriate adaptations. In the absence of regulations for an arbitral proceeding or provisions determining the exact date of the commencement

of an arbitral proceeding, proceeding shall be deemed to commence on the date on which a request that the right in dispute should be adjudicated reaches the obligor. Suspension lasts until a final award has been issued by the arbitration tribunal or until the case has been otherwise disposed of.

170. Schlechtriem pointed out that in substance this provision had already been agreed on in Cairo. Changes were merely of a drafting nature.

171. With respect to the last sentence Komarov suggested replacing the word “final” by “binding”.

172. Schlechtriem agreed.

173. Grigera Naón apologised for raising a point of substance. In his opinion Article 9 seemed to be oriented towards a suspension of the limitation period by the fact that arbitration proceedings have been initiated. But the problem was that in arbitration there may be not only claims against the respondent but also cross-claims against other parties, and/or claims based on different contracts. Suppose that there is a multi-party arbitration clause or an arbitration clause which may affect several contracts at the same time and that claims against the respondent are claims in contract or in tort. He wondered whether the provision should be more elaborate and address the situation where the suspension of limitation periods does not commence when arbitration proceedings are begun but at a later stage during that proceeding. He submitted the following alternative drafts:

Alternative I:

“If the parties submit to arbitration, a limitation period is suspended in respect of a claim against a party, when such claim shall have been served upon such party as provided in the applicable arbitration rules, or if silent, in the applicable law. Unless the claim subject to the limitation period shall not have been otherwise disposed of before, the suspension shall end upon such claim being settled through a binding award.”

Alternative II:

“If the parties submit to arbitration, a limitation period is suspended as of the date arbitral proceedings introduced against the obligor as respondent are deemed as commenced. In any other case, or absent a provision in such rules to that effect, a limitation period regarding a claim subject to arbitration shall be suspended when such claim shall have been served upon the relevant obligor as provided under the applicable arbitration rules or, if silent, according to the applicable law., Unless the claim subject to the limitation period shall not have been otherwise disposed of before, the suspension shall end upon such claim being settled through a binding award.”

174. Bonell expressed to Grigera Naón the Group’s appreciation for his efforts and asked for comments.

175. Farnsworth felt that Grigera Naón’s concerns with respect to arbitration were perfectly symmetric to the problems just discussed in the context of judicial proceedings and which had been taken care of in the new version of Article 8. He therefore wondered whether Article 9 could follow the basic formula used in Article 8 and simply read as follows:

“ (1) The running of the limitation period shall be suspended when the obligee performs any act, by commencing arbitral proceedings or in arbitral proceedings already instituted, that is recognised by the law of the arbitral tribunal as asserting the obligee’s right against the obligor;”

(2) Suspension lasts until a binding decision has been issued or until the case has been otherwise disposed of.”

176. Both Grigera Naón and Schlechtriem agreed with Farnsworth and the Group agreed in substance with the proposed new wording of Article 9.

Article 10: The provisions of Articles 8 and 9 apply with appropriate modifications to other proceedings to which the parties have agreed with the aim of resolving their dispute.

177. Schlechtriem recalled the origin of this provision. The question of alternative dispute resolution (hereinafter ADR) had been brought up in Cairo by Herrmann. The Group at that time agreed to have such a provision but in view of the great variety of types and procedures of ADR it was decided to use a very broad formula such as “other proceedings to which the parties have agreed with the aim of resolving their dispute”. The use of the word “proceedings” should make it clear that mere negotiations between the parties would not suspend the limitation period. On the other hand what was important was that the corresponding proceedings must be based on an agreement between the parties. And since it is not known when and how the different ADR proceedings have commenced, the reference to Articles 8 and 9 have been made with the reservation “with appropriate modification”.

178. Bonell recalled the work presently underway within UNCITRAL and asked Komarov, who had attended the Working Group’s last meeting, whether ADRs have been further defined.

179. Komarov stated that the Group was dealing in particular with conciliation procedures but no final definition has been worked out. He also recalled the recently adopted ICC ADR rules. All these developments showed the usefulness of a provision on this matter in the present draft.

180. Bonell agreed and asked the Rapporteur to make a reference to the preparation of these and other international instruments in the field of ADR in the Comments.

181. The Group adopted the article.

Article 11: (1) Where the obligee has been prevented by an impediment that is beyond its control and that it could not reasonably be expected to have avoided or overcome, from causing a limitation period to cease to run under the preceding articles, the limitation period is suspended so as not to expire before one year after the relevant impediment has ceased to exist.

(2) Where the impediment consists of the incapacity or death of the obligee or obligor, suspension ceases when a representative for the incapacitated or deceased party or its estate has been appointed or a successor inherited the respective party's position; the additional one-year period under para 1 applies respectively.

182. Schlechtriem pointed out that the article had already been adopted by the Group in Cairo.

183. No further remarks were made.

Article 12: Expiration of the limitation period entitles the obligor to invoke this expiration in any legal proceeding as a defence.

184. Schlechtriem recalled the discussion which had taken place in Cairo and the conclusions reached on that occasion by the Group, i.e. that the expiration of the limitation period should only be a defence to be raised by the obligor and not lead to the extinction of the right.

185. While agreeing on the substance of the provision, Crépeau wondered whether it would not be preferable to use the formula of Article 24 of the Limitation Convention which reads "Expiration of the limitation period shall be taken into consideration in any legal proceedings only if invoked by a party to such proceedings."

186. Schlechtriem recalled that such wording was already discussed in Cairo but the Group felt that it could be further simplified.

187. Bonell suggested that the more elaborate wording of Article 24 could be used in the Comments.

188. Schlechtriem drew attention to the fact that there was no longer a definition of "legal proceedings" in Article 1. Since he felt that the defence of limitation periods could be raised also in administrative proceedings he thought this should at least be clarified in the Comments.

189. Farnsworth suggested going even further and insert in the black letter rule the words "any judicial, arbitral or administrative proceeding".

190. Bonell questioned what about ADRs referred to in Article 10. He felt that the Comments were a more appropriate place to clarify matters.

191. Schlechtriem agreed.

Article 13: [Notwithstanding the expiration of the limitation period for a right, a party may rely on this right as a defence or for the purpose of set off against a claim asserted by the other party.]

192. The Group decided to take a final decision on this article after the discussion on the chapter on set-off.

Article 14: Where a right is performed after the expiration of the limitation period for the right, the obligor or another performing party shall not on that ground alone be entitled to claim restitution even if the performing party did not know at the time of performance that the limitation period had expired.

193. Schlechtriem recalled that this provision had been agreed in Cairo. The only addition was the reference to “another performing party” which he found useful in order to cover cases where the performance was rendered by a third party.

194. Furmston wondered whether it was appropriate to speak of rights being performed. It was usual to speak of duties being performed.

195. Crépeau suggested the following formula: “the obligor, or any other party performing after the expiration of the limitation period shall not on that ground alone be entitled ...”.

196. Bonell drew attention to Article 17:113 (2) of PECL which used an even shorter phrase and asked the Rapporteur to redraft the provision in the light of the suggestions made.

197. It was so agreed.

III. ASSIGNMENT OF RIGHTS, TRANSFER OF OBLIGATIONS AND ASSIGNMENT OF CONTRACTS

198. In introducing the draft Chapter on Assignment of Rights, Transfer of Obligations and Assignment of Contracts (UNIDROIT 2001 Study L - Doc. 69) Fontaine recalled that while Section I dealing with Assignment of Rights had already been discussed at the sessions in Bozen and Cairo, Section 2 on the Transfer of Obligations and Section 3 on the Assignment of Contracts were still in a preliminary stage.

SECTION 1: ASSIGNMENT OF RIGHTS

Article 1: In these Principles, « assignment » of a right means the transfer [, including one as security,] by agreement from one person (the "assignor") to another person (the "assignee") of the assignor's right to payment of a monetary sum or other performance from a third person ("the obligor").

199. Fontaine indicated that in accordance with the decision take by the Group in Cairo the words “or other performance from a third person” had been added.

200. Bonell wondered why only the word “assignment” had been put in inverted commas and suggested that the three words “assignment of a right” be put in inverted commas. It was so agreed.

201. Fontaine solicited comments as to the reference to security in square brackets.

202. According to Finn the reference to security should remain since in legal systems based on the English Judicature Act transfer by way of security is expressly excluded. It only deals with absolute assignments. He suggested that the language be changed to “an assignment by way of security”. It was so agreed.

203. Di Majo found the whole article a little scholastic, while Komarov was entirely satisfied with the definitions.

Article 2: This Section does not apply to assignments :

(a) made by transfer of a negotiable instrument governed by special rules;

(b) made as a part of the transfer of the assets or of a substantial part of the assets of a business.

204. Fontaine explained that *lit.* (a) was intended to make sure that the Section did not apply to transfers of negotiable instruments governed by special rules while it could still apply where such instruments were transferred by way of a normal assignment.

205. Furmston recalled that in English law most bills of exchange are not negotiable because of their form. He therefore suggested using the more general term “instruments”.

206. Farnsworth agreed with Furmston and recalled that in the United States bills of lading are governed by Statute whether negotiable or not. Also Finn agreed and mentioned insurance policies and shares as yet another example of documents which, though not being negotiable, are governed by special rules.

207. Grigera Naón wondered about the case where the drawer of an order bill of exchange expressly excludes the possibility of it being transferred by endorsement.

208. Schlechtriem was in favour of the present text. A possible change could be as follows “(a) made by transfer of an instrument, the transfer of which is governed by special rules”, so as to make it even clearer that what matters is that the transfer is governed by special rules.

209. Bonell drew the Group’s attention to Art. 12:101 paragraph 3 of the Principles of European Contract Law (hereinafter PECL) (“This chapter does not apply to the transfer by delivery of a bill of exchange or other negotiable instrument or of a

negotiable security or a document of title to goods”). The language was more analytical but the substance was the same.

210. Farnsworth stated that he could live with the present text but would prefer to have the word “negotiable” eliminated. He suggested including the term “document” in addition to “instrument” so as to broaden the scope of the provision and explaining in the Comments the kinds of documents contemplated.

211. Turning to *lit. (b)* Fontaine recalled that in many jurisdictions special rules govern global transfers of businesses. The Comments could make it clear that the Section would nevertheless apply where certain rights pertaining to the business are assigned individually. Also the mere transfer of shares in a company would be governed by the Section.

212. Komarov suggested deleting the paragraph and dealing with this matter in the Comments where more definite criteria for determining a “substantial part of the assets” should be provided such as, e.g. “part giving an active control of the business” or the like.

213. According to Grigera Naón one should not speak of “substantial part of the assets” which is an unclear notion. What matters is whether the transfer concerns a business as a going concern. These are the cases which do not fall under the normal assignment rules.

214. Furmston wondered which rules would apply in the case where an author has made a contract with a publisher to write a book on the law of contract, and the publisher sells all his law publishing business, but without any transfer of shares, to a different company.

215. According to Fontaine it is likely to fall under *lit. (b)*, provided that the law part is a substantial part of the assets of the publishing company and the applicable law provided that in such a case there would be a global transfer governed by special rules.

216. Furmston pointed out that in English law there are no such special rules and the case would definitely fall under the ordinary rules on assignment. Quite different of course was the case of mergers and acquisitions, and the transfer of shares in general.

217. According to Date Bah Furmston’s difficulties could be overcome by also including in *lit. (b)* a reference to special rules governing such transfers

218. Fontaine suggested a new version of the article which read as follows:

“This Section does not apply to transfers

(a) of instruments or

(b) of rights in the course of transferring a business

made under the special rules governing such transfers”.

219. The Group agreed on this text.

*Article 3: (1) A right to payment of a monetary sum may be assigned partially.
 (2) A right to other performance may be assigned partially only [if it is divisible]/[if it does not render the obligation significantly more burdensome].
 (3) The assignor must compensate the obligor for any increase in the expenses incidental to performing in several parts.*

220. In introducing the article Fontaine recalled the lengthy discussion on this point in Cairo. As to the two alternative versions of paragraph 2, he pointed out that one might even think of a third solution whereby the two conditions might be combined and operate cumulatively.

221. Date Bah wondered whether the “more burdensome” proviso in paragraph 2 was not neutralised by paragraph 3. In other words, if performance was significantly more burdensome and yet there was an obligation to compensate for the extra burden, might there not be a problem?

222. Fontaine thought not: if the second alternative in paragraph 2 was chosen, partial assignment was excluded whenever it would render the obligation *significantly* more burdensome, while it would be possible even in cases where the obligation would become more burdensome with the only consequence that in such a case paragraph 3 would come into play.

223. According to Di Majo, the second alternative envisaged in paragraph 2 should apply also to partial assignment of monetary obligations. Indeed even in such cases the obligation may become significantly more burdensome, for instance where the debtor has to pay a new creditor who is in a distant country.

224. Bonell recalled that at the last session of the Commission on European Contract Law the issue of the legitimate interests of the debtor in case of a change of the place of performance due to assignment had been discussed extensively not only in the context of partial assignment but also in general terms. As a result a special provision (Article 12:306) according to which “(1) Where the assigned claim relates to an obligation to pay money at a particular place, the assignee may require payment at any place within the same country or, if that country is a Member State of the European Union, at any place within the European Union, but the assignor is liable to the debtor for any increased costs which the debtor incurs by reason of any change in the place of performance. (2) Where the assigned claim relates to a non-monetary obligation to be performed at a particular place, the assignee may not require performance at any other place.”

225. Fontaine, acknowledging the importance of the issue, remarked however that it had never so far been discussed by the Group.

226. Grigera Naón wondered whether the Group really intended to permit a change of the place of performance by means of an agreement between the assignor and the

assignee without the consent of the obligor. Such a rule would be contrary to the law of many countries.

227. Bonell asked the Rapporteur whether he could give further consideration to the issue.

228. Turning to the two alternatives set forth in paragraph 2, Bonell asked for comments.

229. Date Bah expressed his preference for the first (“if it is divisible”).

230. Finn on the contrary expressed his preference for the second alternative (“if it does not render the obligation significantly more burdensome”) which would provide adequate protection for the obligor.

231. Crépeau agreed with Finn but would have kept both alternatives.

232. Di Majo agreed.

233. The Group agreed on the following text of paragraph 2:

“A right to other performance may be assigned partially only if it is divisible and it does not render the obligation significantly more burdensome”.

Article 4: Variant 1

A future right is deemed to be transferred at the time of the agreement, provided the right, when it comes into existence, can be identified as the right to which the assignment relates.

[Variant 2

A future right is deemed to be transferred when the right comes into existence, provided it can then be identified as the right to which the assignment relates.]

234. In introducing the two Variants Fontaine pointed out that the difference between the two centered on the issue of whether the assignment of a future right has retroactive effect or not, i.e. whether once the right comes into existence the transfer is considered to have taken place at the time of the assignment agreement or when the right comes into existence. He expressed his preference for the retroactive effect as stated in Variant 1: such a provision would increase the value of future rights and so promote their financing.

235. Grigera Naón strongly agreed.

236. Crépeau recalled that when this question had been discussed at the earlier session it was proposed to deal with both future rights and conditional rights. He was impressed by Article 12:202 paragraph 2 PECL stating “an assignment of a future claim

is dependent on the assigned claim coming into existence”. This provision takes into consideration the fact that there can be a present claim with a term, a conditional claim which may come into existence later on, or a purely future claim. He wondered whether any of the proposed provisions did the same.

237. Fontaine was of the opinion that Variant 1 was in substance the same as Article 12:202 (2) PECL.

238. Variant 1 was adopted.

Article 5: A number of rights may be assigned without individual specification provided such rights can be identified as rights to which the assignment relates at the time of the assignment or when they come into existence.

239. Fontaine recalled that the title of the provision had been changed from “transfer of bulk of rights” to the less colloquial expression “Rights assigned without individual specification”. The Comments would make it clear that the subject remains the same. Moreover by stating that a number of rights may be assigned without individual specification, provided that such rights can be identified as rights to which the assignment relates at the time of the assignment or when they come into existence, it is made clear that the provision may apply also to future rights.

240. The Group agreed on Article 5 as proposed.

*Article 6: (1) The right is assigned by mere agreement between assignor and assignee, without notice to the obligor.
(2) The consent of the obligor is not required, unless the right is of an essentially personal character.*

241. In introducing this article Fontaine pointed out that nothing had been changed in substance.

242. Komarov drew the Group’s attention to a misprint in Comment 2. The last word should read “obligor” instead of “obligee”.

243. Di Majo wondered whether there was a contradiction between Article 6 and Article 8 and proposed redrafting Article 6 so as to state that the right is assigned by mere agreement but assignment becomes effective with a notice to the obligor.

244. According to Fontaine there was no contradiction as between the assignor and the assignee the assignment was effective by the mere agreement.

245. The Group agreed.

Article 7: (1) Assignment of a right to payment of a monetary sum is effective notwithstanding an agreement between the assignor and the obligor limiting or prohibiting such assignment. However, the assignor may be liable to the obligor for breach of contract.

(2) Assignment of a right to other performance is ineffective, if it is contrary to an agreement between the assignor and the obligor limiting or prohibiting the assignment. [Nevertheless, the assignment is effective if the assignee, at the time of assignment, neither knew nor ought to have known of the agreement ; the assignor may then be liable to the obligor for breach of contract.]

246. In introducing this article Fontaine recalled that the solution proposed was in line with Article 11 of the UNCITRAL draft Convention on Assignment in Receivables Financing. Its purpose was to promote financing through assignment of monetary obligations. This also explains why non-assignment clauses relating to non-monetary obligations have been treated differently.

247. Kronke thought that the UNCITRAL text had been changed on the insistence of the UK and others invoking requirements of their defence departments.

248. Fontaine denied.

249. Kronke too was in favour of the present text which after all reflected current developments in both case law and legislation throughout Europe.

250. Bonell wondered why Article 12:301 PECL restricted ineffectiveness of a non-assignment clause to future claims of money and asked for comments.

251. Dessemontet referred to the comments to a previous draft of the article where it is stated that it was above all with respect to a stream of claims expected in the future that the need for the exception was particularly felt.

252. Di Majo pointed out that different policies underlay the two approaches, i.e. the protection of the obligor vs the protection of the assignee.

253. Grigera Naón was in favour of the approach proposed by the Rapporteur which in his view was already a compromise in view of the fact that the exception was limited to monetary claims.

254. Farnsworth agreed and paragraph 1 was adopted.

255. With respect to paragraph 2 Grigera Naón expressed his support for the inclusion of the text in square brackets.

256. Huang was prepared to accept the text but suggested that the exception provided therein should be limited by a reference to good faith.

257. Kronke replied that in his view such a limitation was already inherent in the wording “ought to have known”.

258. Finn wanted to know the exact role of the assignee’s knowledge of the non-assignment clause in this context. In other words why did it matter with respect to non-monetary claims, but was irrelevant with respect to monetary claims.

259. Fontaine stressed that with respect to the latter the promotion of financing was essential while there was no such need with respect to the former so that a fair balance between the conflicting interests of the three parties concerned could be achieved.

260. With respect to the Illustration in Comment 3, Furmston argued that even in the absence of a non-assignment clause the right to get X’s legal advice might not be assignable because of its personal nature. Fontaine agreed to think of an illustration where this aspect did not come into play.

261. The Group agreed on the provision including the text in square brackets.

*Article 8: (1) Until receiving a notice of the assignment, from either the assignor or the assignee, the obligor is discharged by paying the assignor.
(2) After receiving such a notice, the obligor is discharged only by paying the assignee.*

262. Fontaine explained the changes of presentation introduced in the new text. He also recalled that in Cairo it had been decided not to assimilate the debtor’s knowledge of the assignment to receiving notice. For this reason the provision now contains only the notice requirement. The Comments contain explanations of the form of notice, its minimum content, silent assignments, anticipatory notice, revocation of notice, etc.

263. With respect to Illustration 1, Furmston pointed out that in the third line X (and not B) is discharged.

264. Date Bah wondered whether the obligor was discharged by paying the obligee where it learns of the assignment without notice from the assignee or assignor.

265. Fontaine insisted that in the light of what had been decided in Cairo the obligor’s awareness alone of the assignment was not sufficient to discharge it by paying the assignee.

266. Finn suggested to replace in Comment 5 “can” by “may be able to be” so as to read “Notice given to the obligor may be able to be revoked”. If “can” were to be kept he suggested adding “in certain circumstances, for example, ...”.

Article 9: If the same right has been assigned by the same assignor to two or more successive assignees, the obligor is discharged by paying according to the order in which the notices were received.

267. The Group adopted the provision with no further comment.

Article 10: If notice of the assignment is given by the assignee, the obligor may request the assignee to provide within a reasonable period of time adequate proof that the assignment has been made, and, unless the assignee does so, the notice is not effective. Adequate proof includes, but is not limited to, any writing emanating from the assignor and indicating that the assignment has taken place.

268. Farnsworth wondered whether the time of the notice would be the time of the notice without adequate proof even if the proof arrived later. If, as he felt, this was the case it would be useful to address that issue in the Comments.

269. Bonell suggested that in Comment 3 to Article 8 a cross reference be made to Article 10.

270. Crépeau wondered about the mechanics of the provision. Was it correct to assume that when the notice is duly made, payment has to be made to the assignee, while whenever a request for adequate proof is made, until such proof is given payment could be made to the assignor.

271. Fontaine thought that, although the question had not been expressly addressed in the black letter rule, he would conclude that during the reasonable time granted to the assignee to gather adequate proof, everything is suspended so that the obligor would not be discharged by paying the assignor. Only if adequate proof is not given after the reasonable time, notice becomes ineffective and the obligor can validly make payment to the assignor.

272. Bonell drew attention to Article 12:303 paragraph 3 PECL stating “pending which the debtor may withhold performance”. He wondered whether according to this provision the obligor has an option either to pay or not to pay.

273. Dessemontet wondered whether a reference could be made in the Comments to the device envisage in Article 12:305 PECL. There the money is put in an escrow account or deposited according to other procedures.

274. Schlechtriem wondered whether it was really a wise decision to attribute retroactive effect to the providing of adequate proof of the notice. He made the case of a creditor/assignor who assigns its right first to Bank A and then to Bank B. Bank A gives notice to the obligor who asks for adequate proof of the assignment. While waiting for that proof, the obligor receives notice from the assignor of the assignment to Bank B. Assuming that Article 10 applies only to notice given by the assignee, the notice of the assignment to Bank B given by the assignor should be considered as having arrived first with the consequence that according to Article 9 the second assignment should prevail over the first. Was there not a conflict between Article 9 and Article 10. He concluded

in the sense that the providing of adequate proof of the notice should no longer be given retroactive effect.

275. Both Fontaine and Farnsworth wondered whether it would not be unfair to protect in the case given by Schlechtriem the assignor who after all is responsible for having made successive assignments of one and the same rights, and therefore favoured the present solution.

276. In view of the fact that Article 10 is relevant not only in the case of successive assignments, but also in the case of a single assignment notified to the obligor by the assignee, Furmston wondered whether it would not be preferable to place the article immediately after Article 8.

277. Furmston also questioned who would decide whether the proof of the assignment given by the assignee in its notice was adequate or not. If it was ultimately up to a court to decide the matter, then he foresaw difficulties and delaying techniques in practice.

278. Grigera Naón wondered whether it was not advisable to stick to domestic laws and require, as for instance was the case in Argentina, that notice be given by public notary.

279. Bonell reminded that the absence of any formal notice requirement was deliberate in view of the fact that for instance notice by public notary proved to be too expensive and burdensome, at least in case of bulk assignments.

280. While Grigera Naón objected that at least in Argentina this was not the case, Schlechtriem wondered whether the best solution would not be not to permit at all a notice by the assignee.

281. Bonell recalled that the whole discussion started with the question of what should (or may) the obligor do pending the reasonable time within which the assignee is requested to provide further evidence of the assignment. He wondered whether the Group was in a position to express a clear recommendation to this effect either in the sense of withholding payment or of conforming to special procedures provided for by the applicable law or both.

282. Date Bah pointed out that strictly speaking Article 10 did not provide a retroactive effect: the assignment becomes effective upon notice and if the evidence was insufficient the assignee was invited to produce additional evidence. In his view between these two moments the obligor could not but withhold payment.

283. Finn agreed and pointed out that there were basically two options. Either to follow the example of the PECL and insert in the black letter rule a provision granting the obligor the right to withhold payment or simply to express a recommendation to this effect in the Comments. The advantage of the first option would be that during the time period concerned the obligor would not incur any additional liability, for instance, for a payment of interest if the payment became due before getting the additional evidence.

284. The Group agreed and asked the Rapporteur to include appropriate language to this effect in Article 10.

Article 11: (1) The obligor may assert against the assignee all [substantive and procedural] defences of which the obligor could assert if the claim was made by the assignor.

[(2) The obligor may assert against the assignee any right of set-off in respect of claims existing against the assignor available at the time notice of assignment was received.]

285. In introducing the article, Fontaine recalled that the language of paragraph 1 had been in substance taken from Article 9 (1) of the UNIDROIT Factoring Convention (the word “of” in the second line was a misprint). As to the words in square brackets they appear in Article 12:307 (1) PECL.

286. While Dessemontet was in favour of keeping these words, if only in the interests of conformity with the PECL, Schlechtriem favoured deleting them because of the risk that in practice doubts may arise as to whether there were further defences not falling either under the concept of “substantive” or of “procedural” defences.

287. The Group decided to delete the words in square brackets.

288. With respect to paragraph 2 it was decided to postpone any decision until the draft Chapter on Set-off had been discussed.

Article 12: Accessory rights, including securities and the right to interest, are transferred to the assignee.

289. Fontaine pointed out that the notion of accessory rights had proven to be rather controversial. He personally would prefer a rewording of the provision so as to read “Securities and accessory rights, including the right to interest, are transferred to the assignee”. This would avoid unnecessary problems with similar provisions to be found both in Section 2 and 3 of this Chapter.

290. Schlechtriem asked whether the right to terminate the contract was to be considered an accessory right and would therefore be transferred to the assignee together with the right to a certain performance in kind. The issue was very much debated under German law.

291. Fontaine was inclined to give a negative answer: he would consider an example of a possible accessory right of a right to payment of a sum of money or to another performance the right to payment of a penalty, but not the right to terminate the contract as a whole.

292. Schlechtriem admitted that it was an open question which should not be dealt with in the black letter rule. A reference to accessory rights which must be transferred together with the assignment of the main right should be kept but the identification of the exact borderline between such accessory rights and non-accessory rights should be left to scholarly writings and the courts.

293. Komarov and Crépeau went even further and suggested simply to state that “accessory rights are transferred to the assignee” and leave it to provide some examples in the Comments. The definition of accessory rights already proved extremely difficult in the context of the Chapter on limitation periods.

294. Schiavoni expressed his uneasiness about the proposed text and drew attention to the difficulty of distinguishing between such a rule and the case of assignment of contract.

295. Farnsworth and Furmston stressed that the very notion of “accessory rights” was completely unknown and mysterious in their countries and therefore were unable to follow Komarov’s and Crépeau’s proposal.

296. Bonell wondered whether the formula used in Article 12.201 (1) (b) PECL “all accessory rights securing such performance” was clearer.

297. Schlechtriem felt that the new version suggested by Fontaine (“securities and accessory rights, including rights to interest ...”) was clearer and should be preferred.

298. Jauffret-Spinosi expressed her preference for retaining the text as it stands.

299. Furmston, on the contrary, still felt uncomfortable with the use of the concept of accessory rights. He suggested getting rid of it and expressly indicating in the provision one by one the so-called accessory rights which are automatically transferred. And since so far at least the Group was able to agree only on securities and the right to interest, he would be perfectly happy with a provision listing only those two.

300. Date Bah agreed.

301. Also Finn agreed but suggested building such a provision into Article 1.

302. Dessemontet and Schlechtriem on the contrary insisted on the necessity of having a catch all concept in the black letter rule. They referred to the long lists of accessory rights usually found in commentaries on paragraphs 398 and 401 of the German Civil Code and wondered whether the Group could agree on at least some of the rights listed, e.g. the right to submit any dispute arising from the assigned right to arbitration which in commercial practice was obviously of utmost importance.

303. Farnsworth reiterated his scepticism as to the use of the concept “accessory right”, all the more so since not even its supporters seemed to be able to give a sufficiently definition thereof.

304. Furmston strongly supported Farnsworth's view. He was decidedly against the use of a concept which, at least to all common lawyers in the Group, was totally obscure. As an example of the apparent confusion he mentioned arbitration clauses which at least in his country would never be considered as accessory to the main claim.

305. Huang wondered whether the term "collateral rights" used in the English version of the Chinese Contract Law was clear.

306. Schlechtriem recalled that the corresponding term used in the German Civil Code was "auxiliary rights".

307. Finn wondered whether the real issue was one of construction of the assignment agreement, i.e. what rights the parties intended to transfer together with the assignment. If so, the use of a catch all concept was of little use, if at all.

308. Date Bah agreed.

309. Furmston went back to the corresponding provision in the PECL which in essence expressed what he had proposed from the outset, i.e. to specify the rights which are automatically transferred and avoid any catch all provision.

310. Fontaine too felt increasingly attracted by the language of Article 12:201 (1): the only change he proposed was the deletion in *lit.* (b) of the word "accessory" before "rights". He formally proposed amending his draft to read "An assignment of rights transfers to the assignee: (a) all the assignor's rights to payment or other performance under the contract in respect of the rights assigned; and (b) all accessory rights securing such performance."

311. The Group agreed by overwhelming majority.

Article 13: The assignor undertakes towards the assignee that :

- (a) the assigned right exists at the time of the assignment, unless the right is a future right;*
- (b) the assignor is entitled to assign the right;*
- (c) the right has not been previously assigned to another assignee, and it is free from any right or claim from a third party ;*
- (d) the obligor does not have any defences [or rights of set-off];*
- (e) the assignor will reimburse the assignee for any payment received from the obligor before notice of the assignment was given.*

312. Fontaine pointed out that no substantial changes had been made and that the provision reflected the decision already taken by the Group in Cairo.

313. The Group agreed on the provision and decided to postpone any decision as to the words in square brackets until the Chapter on Set-off had been discussed.

SECTION 2: TRANSFER OF OBLIGATIONS

Article 1: In these Principles, « transfer of an obligation » means the transfer by agreement from one person (the « transferor ») to another person (the « transferee ») of the transferor's obligation to payment of a monetary sum or other performance to its obligee.

314. In introducing this Section Fontaine pointed out that this was a particularly difficult section to draft as, apart from PECL, there were no other international models to take inspiration from. He recalled the preliminary discussions in Bozen and Cairo and mentioned that Articles 2 and 8 would obviously be redrafted in the light of the Group's recent deliberations relating to Section I.

315. With respect to Article 1 the only change was the replacement of the term "duty" by "obligation" so as to align the language with that used in other parts of the Principles.

316. The Group agreed on the provision as proposed with the only change being the new language "obligation to pay or render other performance" at the end of the provision.

Article 2: This Section does not apply to transfers of obligations made as part of the transfer of the assets or of a substantial part of a business.

317. The Group decided to align the language of this provision along that of Article 2 lit. (b) of Section I so as to read:

"This Section does not apply to transfers of obligations made under the special rules governing such transfers."

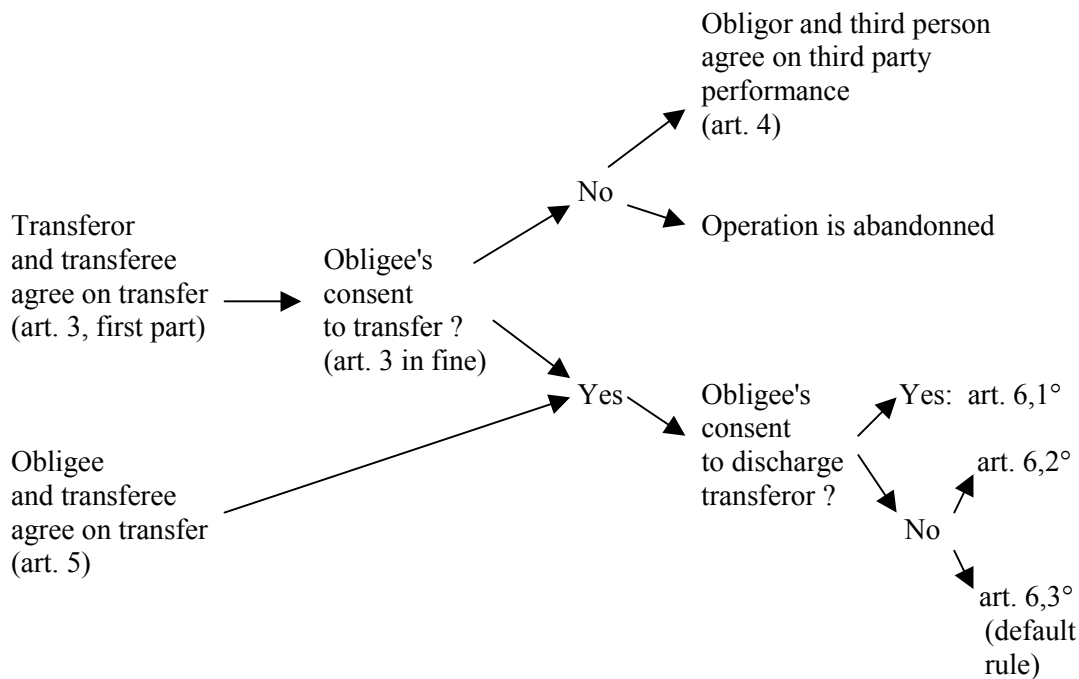
Article 3: An obligation can be transferred by an agreement between a transferor and a transferee, with the consent of the obligee.

*Article 4: (1) Without the obligee's consent, a person may undertake to the obligor that it will perform the obligation in place of the latter, unless the obligation has an essentially personal character.
(2) In such a case, the obligee retains its claim against the obligor.*

Article 5: An obligation can also be transferred by an agreement between the obligee and a new obligor.

*Article 6: (1) When giving its consent, the obligee may discharge the transferor.
(2) The obligee may also retain the transferor as an obligor in case the transferee does not perform properly.
(3) Otherwise the transferor remains as an obligor, jointly and severally with the transferee.*

318. For a better understanding of the whole system underlying Articles 3 to 6 Fontaine produced the following scheme.



319. Dessemontet asked whether according to Fontaine's scheme there could be transfer of obligations without preliminary contract between the former obligor and the obligee.

320. Fontaine confirmed and referred to a similar solution accepted in German law (paragraph 414 BGB) and perhaps in other systems. In the case at hand the obligee would take the initiative to have an agreement with the transferee that the transferee would take up the obligations without the intervention of the obligor.

321. Dessemontet wanted to know whether it would be possible to have a transfer of obligation without the first debtor agreeing to it. Such a possibility was provided for with respect to bills of exchange in the Geneva Uniform Law, but there the so-called intervention by a third party was subject to special conditions.

322. Finn wanted to know whether he was right in assuming that the combined effect of Article 5 and Article 6 was that an obligee and a new obligor could enter into an agreement to transfer the obligation to the latter with the obligee having the power unilaterally to dismiss the original obligor from the performance of that obligation.

323. Fontaine confirmed.

324. Finn wondered what was the rationale of such a rule which allowed in effect unilateral variation of the contract, i.e. substitution for the purpose of performance of one part of a contract of party, without the consent of the party that is being removed.

325. Fontaine admitted that Article 5 did not require any intervention of the original obligor. There was an agreement between the obligee and the new obligor and nothing was said about giving notice to the former obligor. In such a case Article 6 would apply and the obligee could then totally discharge the original obligor. As an example he cited again paragraph 414 of the German Civil Code (“An obligation can be transferred by a contract between the third party and the obligee to the effect that the third party takes the place of the former obligor”).

326. According to Dessemontet in German law the original obligor could always reject the transaction. This followed from paragraph 333 of the German Civil Code dealing with the third party’s right to reject in the context of contracts for the benefit of third parties.

327. Schlechtriem confirmed and pointed out that a similar possibility was missing in Fontaine’s draft. He thought of two possible solutions: either to include the original obligor’s right of rejection expressly in the provision or to refer to the corresponding provision in the Chapter on third party rights in the Comments.

328. Farnsworth too had difficulties with Article 5 since it envisaged a transfer of an obligation without a transferor. Indeed neither the obligee nor the new obligor owed the obligation and were therefore in a position to transfer it.

329. Furmston agreed and put the following question: suppose there was a contract in which A had agreed to do building work for B for a certain price and B announced to A that B was going to get somebody else to do the building work and that A was discharged. Was A still entitled to be paid for the building work, even if it had not done that work?

330. Schlechtriem felt that this was a case of transfer of the whole contract, and should therefore be dealt with in Section 3. With respect to Farnsworth’s concern, he agreed that it was inappropriate to speak also in such a case of a transfer of obligations. As a matter of fact the German Civil Code used a different concept (“Schuldübernahme”). Yet terminology apart, what still remained to be seen was whether the original obligor should be entitled to reject the benefit.

331. Bonell wondered whether the hypothesis addressed in Article 5 was all that important in practice so as to justify the provision.

332. According to Schlechtriem the provision could well be deleted provided that there was agreement that under the rules of third party beneficiary contracts such a release of the old obligor was possible and the old obligor could reject it.

333. Fontaine expressed his preference for having a special provision in this Section.

334. Bonell recalled that also the Italian Civil Code expressly dealt with this situation (Article 1272 on “Espromissione”).

335. Finn too preferred a provision in the present Section but suggested to insert in Article 5 the words “with the consent of the obligor”.

336. According to Dessemontet the main difference between the German system and other systems of law which do not know this possibility is the time element. In fact, what Article 3 foresees and what Article 5 foresees is just inverse in time. Under Article 3 there is first the agreement between the original obligor and the new obligor, while under Article 5 there is first the agreement between the obligee and the new obligor. It follows that if the words “with the consent of the original obligor” were to be inserted in Article 5, the Comments could explain that consent can be either before or after operation.

337. Schlechtriem thought it would be an elegant solution just to make it a matter of time of consent before or afterwards. Yet there was a difference between Finn’s solution and the one that had been discussed so far, namely that the old obligor should be entitled to a rejection. In the former someone relying on that agreement has to prove that there was a consent, while in the second the consent was presumed unless a rejection is proved.

338. Farnsworth on the contrary favoured the deletion of the provision and a reference to the rules on third party beneficiaries in the Comments.

339. Bonell wondered whether also in Article 3 it would not be preferable to speak instead of transferor and transferee of old obligor and new obligor and to reframe Articles 3, 4 and 5 on the basis of who in each respective case takes the initiative, i.e. the old obligor in Article 3, the old or the new obligor in Article 4 and the new obligor in Article 5.

340. Schlechtriem expressed his preference for having a provision of the kind of Article 5 in the present Section, but suggested no longer speaking of “transferring an obligation”, but of “assumption of an obligation by a third party”.

341. Huang on the contrary would have preferred to delete the provision and to deal in the present Section only with veritable transfers of obligations, specularly to Section I dealing with assignment of rights.

342. While still preferring not to have the provision in the present Section, Farnsworth expressed sympathy for Schlechtriem’s suggestion and proposed changing the title of the Section to “Transfer and assumption of obligations”.

343. Fontaine hesitated to agree to the proposal since if the title were to be changed it should fit in with all three different situations dealt with, i.e. transfer of obligations in

Article 3, third party performance in Article 4 and assumption of obligations in Article 5. He wondered whether Article 3 could be redrafted so as to read “An obligation can be transferred (a) by an agreement between a transferor and a transferee with the consent of the obligee or (b) by an agreement between the obligee and a new obligor with the consent of the original obligor”.

344. Schlechtriem on the contrary insisted on changing the title to read “Transfer and assumption of obligations” and to redraft Article 5 to read “An obligation can be assumed by an agreement between the obligee and the new obligor. The old obligor can reject its release.”

345. Farnsworth reiterated his sympathy for a such a solution, but wondered whether it would not be even better to change the title to “Transfer and undertaking of obligations”. “Undertaking” had already been used in Article 4 and also Article 5 could be recast so as to use the word “undertake”.

346. In the light of Farnsworth’s remarks Schlechtriem reformulated his proposal for a new version of Article 5 so as to read “An obligation can also be undertaken by an agreement between the obligee and a new obligor. Unless rejected the consent of the old obligor is presumed.”

347. Jauffret-Spinosi drew attention to the fact that the PECL used the term “substitution of debtor”. She wondered whether Article 5 could be amended so as to read “substitution of debtor can be realised by an agreement between the obligee and the new obligor”.

348. Fontaine objected that such a formula would cover the situation contemplated in Article 6 (1) but certainly not those contemplated in Article 6 (2) and 6(3).

349. Bonell agreed and pointed out that Article 13:101 (1) PECL dealt only with the case where a third person undertook with the agreement of the debtor and the creditor to be substituted as debtor with the effect that the original debtor was discharged.

350. Farnsworth, looking at the title of the whole Chapter, wondered why the Rapporteur, instead of speaking of “Assignment of rights, obligations and contract”, had chosen to speak of “assignment of rights” and “transfer of obligations”.

351. Fontaine reminded Farnsworth that it had not been his choice but that of one of the common lawyer members of the Group.

352. With respect to Article 6 Fontaine explained that in the case dealt with by Article 5 there were three possibilities: the obligee may discharge the transferor, he may retain the transferor as an obligor in case the transferee does not perform properly or - and this is a default rule – the transferor remains as an obligor jointly and severally with the transferee.

353. Schlechtriem and Farnsworth wondered what the difference was between the situation in paragraph 2 and paragraph 3.

354. Fontaine once again pointed out that the difference between paragraphs 2 and 3 was that in 3 the original obligor and the new obligor are on the same level and the obligee can ask performance from either, while in 2 the original obligor is a sort of security in case the new obligor fails to perform.

355. According to Farnsworth Article 6 obscured the fact that there were really two default rules involved. The first came up if the obligee says “I consent”. Period. Did that mean “I consent and the old obligor is discharged” or did it mean “I consent and the old obligor is not discharged”? This was the first question of a default rule. Then the second default rule was - in the case of the answer “no, I do not mean to discharge the old obligor” - what the relative liability of the old obligor and the new obligor was if the old obligor was not discharged. He felt that the Rapporteur had understood “jointly and severally” in a different way than was used in his country: indeed in the United States one would say that the new obligor who has taken an obligation must ultimately bear the cost of the performance and that would give the old obligor a right to recover 100% of what he had performed. He urged the Rapporteur to explain better how he understood “jointly and severally”.

356. Fontaine replied that “joint and several” was the civil concept of solidarity. The obligee would have the choice: when performance was due he could require performance from either the new or the old obligor. Then of course there would be arrangements between the new and the old obligor. He promised to provide an explanation in the Comments.

Article 7: The transferee may assert against the obligee all [substantive and procedural defences] of which the transferor could assert against the obligee if the claim was made against it.

357. Fontaine stated that in the light of what had been decided with respect to the corresponding provision in Section I, the words in square brackets should be deleted.

358. Jauffret-Spinosi wondered whether it was necessary to include the words “if the claim was made against it”.

359. Fontaine agreed on their deletion.

Article 8: The obligee may avail itself against the transferee of all accessory rights, including the right to interest, it could avail itself against the transferor.

360. Fontaine pointed out that this provision has to be redrafted in the light of the decisions taken by the Group with respect to the corresponding provision in Section I.

361. Schlechtriem wondered whether the rule expressed in Article 8 was suitable also in the case of Article 6(3) where the new and old obligor are joint debtors.

362. Fontaine agreed that the issue was worth being discussed and that at least the Comments should mention the special case of the new and old obligor being joint debtors.

363. Farnsworth suggested as a drafting point that also in Article 8 the word “assert” be used instead of “avail itself”.

364. Fontaine reminded the Group that the Article was still incomplete because it did not address the issue of securities. He referred to Article 13:101 PECL (paragraph (4): “The discharge of the original debtor also extends to any security of the original debtor given to the creditor for the performance of the obligation, unless the security is over an asset which is transferred as part of a transaction between the original and the new debtor”; paragraph (5): “Upon discharge of the original debtor, a security granted by any person other than the new debtor for the performance of the obligation is released, unless that other person agrees that it should continue to be available to the creditor”). The two paragraphs distinguish between securities over assets and securities granted by persons. In the first case the discharge of the original debtor also discharges such securities over assets, unless it is over an asset which is transferred as part of a transaction between the original and new debtor. In the second case the discharge of the original debtor also discharges the person giving the security, unless that person consents to continue to be available to the creditor.

365. According to Finn a question of securities should not be expressly addressed. It was up to the obligee to decide whether it wants to keep securities alive, in which case it will not discharge the old obligor; or whether it does not want to keep them alive, in which case it will discharge the old obligor.

366. Schlechtriem on the contrary saw the merits of paragraph 5 to envisage an intermediate solution, i.e. the obligee discharges the original debtor but gets the guarantor’s agreement to continue to guarantee the debt.

367. Fontaine too was in favour of having a rule along the lines of Article 13:101 (4) and (5) PECL.

368. A small Drafting Group was charged with the task of preparing a new consolidated version of Section 2:

SECTION 2: TRANSFER AND ASSUMPTION OF OBLIGATIONS

Article 1 (Definitions)

In these Principles “transfer of an obligation” means the transfer by agreement from one person (the “old obligor”) to another person (the “new obligor”) of an obligation to pay a monetary sum or render other performance.

Article 2
(Exclusion)

This Section does not apply to transfers of obligations in the course of transferring a business made under the special rules governing such transfers.

Article 3
(Agreement between old and new obligors with obligee's consent)

An obligation may be transferred by an agreement between an old and a new obligors with the consent of the obligee.

Article 4 (ex – 6)
(Discharge of the old obligor)

- (1) When giving its consent, the obligee may discharge the old obligor.*
- (2) The obligee may also retain the old obligor as an obligor in case the new obligor does not perform properly.*
- (3) Otherwise the old obligor remains as an obligor, jointly and severally with the new obligor.*

Article 5
(Agreement between obligee and new obligor)

An obligation may be assumed by agreement between the obligee and a new obligor. [The old obligor may refuse to be discharged by this agreement].

Article 6 (ex – 4)
(Third party performance)

- (1) Without the obligee's consent, the obligor may contract with another person that this person will perform the obligation in place of the obligor, unless the obligation has an essentially personal character.*
- (2) In such a case, the obligee retains its claim against the obligor.*

Article 7
(Defences)

The new obligor may assert against the obligee all defences which the old obligor could assert against the obligee.

Article 8
(Accessory rights)

The obligee may avail itself against the new obligor of all rights to payment or other performance under the contract in respect to the obligation transferred and of all rights securing such performance.

SECTION 3 – ASSIGNMENT OF CONTRACTS

369. In introducing this Section Fontaine pointed out that there were very few but good models on assignment of contracts, i.e. the Italian, Portuguese and Dutch Civil Codes, from which he had tried to take inspiration.

Article 1: In these Principles, “assignment of a contract” means the transfer by agreement from one person (the “assignor”) to another person (the “assignee”) of the assignor’s rights and obligations arising out a contract with another person (the “other party”).

370. The Group accepted.

Article 2: This Section does not apply to assignment of contracts made as part of the transfer of the assets or of a substantial part of a business.

371. Fontaine proposed to rewrite Article 2 so as to put it in line with what had been decided with respect to the corresponding provisions in Sections 1 and 2. The new text would read as follows:

“This Section does not apply to assignment of contracts in the course of transferring a business made under the special rules governing such transfers”.

372. The Group agreed.

Article 3: A contract can be assigned by an agreement between an assignor and an assignee, with the consent of the other party.

373. Schiavoni welcomed the fact that the draft did not follow the rule of the Italian Civil Code – heavily criticised by legal writings and case law – according to which the assignment of contracts can only take place as long as the contract has not been performed. In international practice – e.g. in construction contracts – it is frequent to transfer the bulk of rights and obligations arising out of a certain contract even when the contract has already partially been performed.

374. No further objections having been made, the Group agreed on the provision as proposed.

*Article 4: (1) The other party can give its consent in advance.
(2) In such a case, the assignment of the contract becomes effective when it is notified to the other party or when the other party accepts it.*

375. Fontaine stressed the practical importance of the provision which however had a counterpart only in the Italian and Portuguese Civil Codes.

376. Schlechtriem found it very interesting and wondered about the situations envisaged in Italy by the corresponding provision (Article 1407 Civil Code).

377. Schiavoni explained that the provision envisaged two different forms of giving consent in advance. One is an ordinary clause in the contract between the original parties. The other is the so-called “clausola all’ordine”, i.e. a statement in the document containing all the elements of the contract whereby one of the parties may, by mere endorsement of the document, assign its contractual rights and duties to somebody else.

378. Fontaine recalled that the Dutch Civil Code dealt with advance consent in connection with the assignment of debts and extended this solution to the assignment of contracts. If the Group so wished he could do likewise, i.e. include in Section 2 a provision to this effect and have a mere reference to it in the present Section.

379. Schlechtriem supported this proposal.

380. It was so decided.

*Article 5: (1) When giving its consent, the other party may discharge the assignor ;
 (2) The other party may also retain the assignor as an obligor in case the assignee does not perform properly ;
 (3) Otherwise the assignor remains as the other party’s obligor, jointly and severally with the assignee.*

381. No objections.

*Article 6: (1) The assignee may assert against the other party all [substantive and procedural] defences arising out of the assigned contract which the assignor could assert against the same party.
 (2) The other party may assert against the assignee all [substantive and procedural] defences arising out of the assigned contract which it could assert against the assignor.*

382. Schlechtreim wondered whether this provision, which had been taken from the Italian, Portuguese and Netherlands law, was really necessary. Transfer of contract means a transfer of rights and obligations and, since Section 1 and 2 already contain provisions on defences in case of assignment of rights and transfer of obligations, they could be sufficient.

383. Fontaine agreed.

384. The Group decided to delete the Article.

Article 7

385. Fontaine announced that a draft provision dealing with accessory rights, securities and interest would be prepared.

386. A small Drafting Group prepared a new version of Articles 2 and 7:

Article 2
(Exclusion)

This Section does not apply to assignment of contracts in the course of transferring a business made under the special rules governing such transfers.

Article 7
(Accessory rights)

(1) The assignee may avail itself against the other party of all rights to payment or other performance under the contract assigned in respect to the rights transferred and of all rights securing such performance.

(2) The other party may avail itself against the assignee of all rights to payment or other performance under the contract assigned in respect to the obligations transferred and of all rights securing such performance.

IV. THIRD PARTY RIGHTS

Article 1: If the parties to a contract expressly or impliedly agree that the contract, or some obligation under it, is intended to benefit a third party that third party shall acquire rights in relation to the contract or obligation.

387. In introducing Article 1 Furmston recalled that this article was preceded in his previous draft by an article stating that generally a contract creates rights and duties only between the parties to the contract. This provision was considered to be too dogmatic and was deleted by a slight majority in Cairo. The present Article 1 was a combination of the former Articles 2 and 3 which dealt with the case of an express statement in the contract that it is intended to benefit a third party and with the case where one of the commercial purposes of the contract was to benefit a third party, respectively. A last change concerned the use of the formula “shall acquire rights in relation to the contract or obligation” in lieu of “shall be entitled to enforce the contract or obligation”: the expression “enforce” might be understood, at least by civil lawyers, as meaning that the third party beneficiary was always entitled to performance *in natura*, while sometimes the third party was entitled only to damages.

388. Schlechtriem argued that it was not always a “right” that was acquired by the third party. It could also be a mere expectation or a release from a previous obligation. He therefore suggested that the article should be rephrased to read: “The parties to a contract made expressly or impliedly agree that the contract or some obligation under it is intended to benefit a third party”. What exactly the benefit to the third party was depended on the contract between the contracting parties.

389. Furmston replied that some of the situations mentioned by Schlechtriem would be covered by Article 3 dealing with defences which would cover releases. As to expectations, he thought that in international commercial practice it was rather rare for parties to agree to put money in banks for the benefit of unborn grandchildren.

390. Farnsworth felt that Schlechtriem's concerns could be dealt with, at least in part, if Article 1 and Article 3 were merged so as to read "the contract or some provisions under it" which would mean that if there was for instance an exculpatory clause in the contract that was intended to benefit a third party it could be enforced by the third party.

391. Fontaine agreed with Schlechtriem that there might be a case where a new obligor agrees with the obligee to be bound and the two release the old obligor without the latter's consent. When discussing such a possibility in the context of the section on transfer of obligations, the Group thought that this could be a case of a contract to the benefit of a third party and should therefore be at least mentioned in the Comments to the present article.

392. Furmston had understood the previous discussion that if A and B make a contract which confers rights on X, it should be open to X to renounce those rights. He had no objection to saying that either in a black letter rule or in the Comments though he thought it was self-evident. As to the suggestion to merge Articles 1 and 3 he felt that Article 3 dealt with a problem that was of enormous significance in international commercial contracts (Himalaya clauses) and should therefore stand on its own.

393. Schlechtriem suggested adding a second sentence to Article 1 to read "The third party can reject that benefit or that right".

394. Bonell asked whether there was further support for this proposal.

395. Furmston proposed to add a new Article 6 to this effect.

396. Crépeau questioned the use of the words "expressly or impliedly" which are self-evident since it always depended on the intention of the parties to the contract. Sometimes it was by express agreement in words or could also be given by way of conduct expressed in the course of negotiation.

397. Bonell recalled the reason for including this formula to which also the Rapporteur had referred in his opening remarks.

398. Furmston insisted on the necessity of stating expressly that a contract may confer rights on a third party even if there is no express contractual term to this effect.

399. Fontaine agreed, all the more so since Article 5.1 of the Principles did not apply in this case.

400. Farnsworth understood Article 5.1 differently, i.e. so as to cover also contractual obligations of a party to someone not originally a party to the contract. Yet if there were doubts about such an interpretation he was prepared to keep the word “expressly or impliedly” in the present article provided that the issue will be reconsidered at a later stage in the context of the revision of the text of the Principles as a whole.

401. Crépeau suggested rephrasing Article 1 so as to read “Parties may by express or implied agreement confer a right in favour of a third party.”

402. Jauffret-Spinosi expressed her support for this wording which after all had the merit of being more concise.

403. Crépeau stated it was not because it is civilian, but because we rise above both systems and say in an explicit way, henceforth parties may confer benefits, rights, in favour of third parties.

404. Finn disagreed and stressed that at least for common law countries which are not too familiar with the third party beneficiary doctrine it was necessary to specify that a third party acquires rights under a contract between two other parties only if there is a statement of intention to that effect between these parties.

405. Farnsworth agreed with Finn on the importance of the concept of “intention” which was essential also in order to distinguish between the case where the contract merely benefits somebody else and the case where it confers a right on that third person. In this respect he referred to the Comments which also highlight the difference between the two cases making the intention of the parties the decisive factor.

406. Crépeau pointed out that obviously also his suggested formula attached utmost importance to the intention of the parties. The very essence of an agreement between the parties is their common intention to do something.

407. Fontaine agreed with Crépeau. He too felt it necessary to distinguish between cases where an agreement creates benefits for third parties and cases where the parties intended to create that benefit. He thought that the formula proposed by Crépeau, even though it did not use the word intention, was very clear. If by agreement you confer a right, of course you have the intention to create a right. The Comments could make this clear.

408. Komarov also supported Crépeau’s formula.

409. Schlechtriem stated that there were two problems involved. First whether the third party beneficiary can enforce its right: the black letter rule rightly does not give a clear answer since this will depend on the terms of the contract. The second question was whether the promisee can sue the promisor to perform to the third party: in general the answer is yes but again party autonomy may allow another solution. He suggested mentioning this in the Comments and in this respect quoted paragraph 335 of the German Civil Code “Right to claim of promisee. The promisee may, unless a contrary

intention of the contracting parties is to be presumed, demand performance in favour of the third party, even if it is the latter who has the right to the performance.”

410. Furmston thought that would be very helpful.

411. Bonell asked for an indicative vote and Crépeau’s formula was adopted by 6 to 3. It was agreed that Article 1 would read as follows:
“Parties may by express or implied agreement confer a right in favour of a third party.”

412. Bonell invited Furmston to introduce his illustrations.

413. Furmston explained that he had prepared two sets of examples, one where there was an implicit intention to benefit the third party, the other where there was no such implicit intention. As to the first set this was absolutely clear in illustrations 1 and 2, less so in 3 and 4.

414. With respect to Illustration 3, Finn said that he had no fixed view but warned that it might have significant implications for group companies.

415. Also Bonell felt that the illustration risked raising issues of corporate law that were better not addressed. He asked the Rapporteur whether by giving such an illustration he wanted to suggest that in any contract entered into by a subsidiary the holding company has a right to sue the contractor?

416. Dessemontet agreed. He wondered whether it was wise to give arguments in favour of the group of companies doctrine by providing an example of third party rights.

417. Date Bah felt that the trap was not the corporate structure. The whole purpose of the operation was to benefit the beneficiary for tax reasons and this was worth illustrating.

418. According to Schlechtriem the illustration confirmed his personal view that everything has to be determined according to the terms of the contract and the circumstances of the case. In the case at hand, if it was known to the contractor that the building was for the University, the University clearly has a right to sue if there was defective performance.

419. Furmston thought that this was self-evident.

420. Farnsworth suggested that the point could be made more clearly by saying, for instance, “T wishes to build a new library on land owned by the University”.

421. In view of the fact that different opinions have been expressed with respect to Illustration 3, Bonell suggested deleting it.

422. Furmston acknowledged that it would be better to have examples where all members of the Group would give the same answer. On the other hand he was not so

sure about that because if only absolutely clear examples were given, they would not actually help people in applying the Principles.

423. Bonell asked for comments on illustration 4.

424. Furmston explained that in English law there was clearly a tort action on these facts, while in the United States similar cases have often been treated as third party beneficiary cases.

425. Farnsworth agreed. Courts did not hesitate to consider the prospective heirs' right enforceable in view of the fact the testator knows he will be dead by the time the dispute arises so that only the beneficiary could enforce his agreement with the lawyer.

426. Schlechtriem asked Furmston whether after the new English legislation the House of Lords would now decide the case otherwise.

427. Furmston was not so sure but he would not mind if under English law and the UNIDROIT Principles different approaches were taken.

428. Bonell concluded that the illustration would be kept and called for comments on the second set of examples.

429. Farnsworth felt that Illustrations 1 and 3 were consumer cases and product liability cases which, at least in his country, would be dealt with by somewhat different rules.

430. Crépeau expressed doubts with respect to Illustration 1. He would have thought that a hospital buying blood surely did so not for its own benefit but for that of its patients. For this reason he thought there was an implied intention to benefit the latter. He mentioned the similar but simpler illustration with respect to the Canadian national health schemes. The Government pays hospitals to provide services for the population. If something goes wrong and the patients sue the hospital as third party beneficiaries.

431. Bonell wondered whether in view of the scope of the Principles it was not advisable to stick to commercial cases and in this respect he referred in particular to cases involving carriage of goods.

432. It was agreed to delete Illustration 1.

433. With respect to Illustration 2 Date Bah expressed doubts that it was outside implied intention.

434. Also Crépeau felt that if the husband buys a fur coat it is certainly not for himself but for someone else, so that it seemed clearly to be a case of an implied stipulation for the benefit of the wife.

435. Fontaine's interpretation was different. Referring to the distinction that was made previously between simply contracting for the benefit of a third party and contracting with the intention of creating a right for a third party, he wondered whether the husband, by buying the mink coat, really intended to allow his wife, if a problem arose, to sue the store herself. He doubted it.

436. Schlechtriem felt that the difficulties the Group had in discussing the examples were due to the fact that they did not deal with commercial situations and all related to situations where everything depended on the terms of the single contract. Perhaps the Group should try to discuss examples in a commercial setting. He referred to a case which was litigated in a Tokyo court between a German and a Japanese firm. The Japanese firm had delivered some raw materials to a Swiss dealer, who had in turn delivered the raw material to a German firm. The Swiss firm and the Japanese firm knew that the raw material was intended to be used by the German firm to produce certain drugs. It later turned out that the Japanese manufacturer's raw material had some impurities. The German firm had to take all the drugs off the market to the tune of 160 million DM. The question arose whether the contract between the Japanese manufacturer and the Swiss firm was a third party beneficiary contract protecting the German manufacturer of drugs.

437. Asked by Bonell whether he thought this was an example of the second set, Schlechtriem confirmed

438. Crépeau on the contrary felt that for instance in a case where a manufacturer of computers sells a computer to a dealer and the dealer sells it to a company and something goes wrong with the computer, one could argue that there was a stipulation for the benefit of a third party because the warranty in relation to the defects as it were runs with the computer and therefore the ultimate company buyer would have a contractual right against the producer.

439. Dessemontet wondered whether it was good methodology to say in the illustrations what the concrete solution to such a problem is. It all depended on the facts of the given case and it was not possible to give a firm answer without seeing the contract. Maybe there should be a list of situations such as the Rapporteur's first set of illustrations in which the answer was clear enough followed by a second series of illustrations where the conclusion was that it all depended on the terms of the contract. Take for instance the case where somebody asks his bank to transfer funds to the bank of a beneficiary. Was this a case of a contract to the benefit of a third party? Most probably not, but there might be cases where the contrary could be argued. At any rate for the users of the Principles it would be preferable to have cases related to everyday international commercial practice rather than to family law or other examples of professional malpractice.

440. Bonell reminded that not all illustrations which appear in the present text are clear cut. In a number of cases they end with "unless circumstances clearly indicate otherwise" or "unless different language appears in the contract" just to show that the solution might well be different from what appears at first sight.

441. It was agreed that this should be done also in this context.

Article 2: The third party must be identifiable with adequate certainty by the contract but need not be in existence at the time the contract is made.

442. Furmston recalled that the article had already been discussed and agreed in Cairo.

443. Schlechtriem had no problems with the black letter rules but wanted to know at what time the third party must be identifiable. He made the example of the purchase at the stock exchange of shares to be delivered in three months with the contract stating that the shares should be delivered to a person to be named later. Such person would not be identifiable at the moment when the cover contract is concluded. Another example concerned mail order houses which very often find their customers after they have contracted with the manufacturer to produce and deliver 50,000 ice boxes to customers to be named later. It should be made clear in the Comments that it is not necessary that the identification of the third party beneficiary be possible at the time of the conclusion of the cover transaction. The German Civil Code (paragraph 332) and the Italian Civil Code (Article 1401) both contain provisions allowing the third party beneficiary to be named later by the promisee.

444. Fontaine agreed and referred to the sector of transport insurance where it was extremely common for somebody to make the contract and the indemnity be paid to the person who will have an interest in the goods at the time of the loss.

445. In the light of Schlechtriem's and Fontaine's remarks, Dessemontet wondered whether it was correct to say that the third party must be identifiable with adequate certainty by the contract. He preferred the wording "under the contract" so as to make it clear that the third party must not be identifiable right from the moment the contract is made.

446. Furmston observed that "identifiable" and "certain" may mean different things in different countries. He regarded the test as being satisfied if the contract provided a mechanism for identifying the beneficiary.

447. Crépeau wondered whether the article should contain a further phrase saying that the third party must be in existence at the time when the right accrues in its favour.

448. Furmston accepted to put something to that effect in the Comments.

449. Furmston wondered whether the Group agreed with the solution of example 2.

450. According to Fontaine this case raised different problems, i.e. the identification of the third party and what is meant by shareholders. Accountants have been asked to prepare a report for distribution to shareholders. If shareholders are third party beneficiaries, are they sufficiently identifiable? As long as the present

shareholders are concerned, yes. But what about those people who buy shares and become shareholders later because they were going to make a good deal?

451. Farnston replied that T1 are the shareholders to whom the report is distributed and they have a much stronger claim than those who later buy shares simply having seen the report but not having been shareholders at the time the report was published. He conceived however that there might be between these two groups, yet another group who buy shares while the report was being produced.

452. In Farnsworth's opinion the reason T2 does not prevail is not because T2 is not identified or identifiable but because of Article 1.

Article 3: For the purposes of this chapter, the creation of rights in the third party shall be treated as including reliance by way of defence on a clause in the contract which excludes or limits the liability of the third party.

453. Farnston recalled that the black letter rule had already been agreed.

454. Date Bah wondered whether since the new Article 1 speaks of conferment instead of creation drafting changes were necessary also in the present Article.

455. Farnsworth felt that the words "The creation of rights ... shall be treated as including reliance by way of defence ..." seemed a somewhat awkward way of addressing the problem. Reliance often suggested something else in the contracts context.

456. Bonell wondered whether the words "the right to rely on an exemption clause" would be preferable.

457. Farnsworth suggested the following formula: "For the purposes of this Chapter the creation of rights in the third party includes the right to rely on a clause in the contract which excludes or limits the liability of a third party".

458. Dessemontet recalled Date Bah's point and suggested using the words "the conferment of rights" instead of "the creation of rights".

459. Farnsworth agreed.

460. Crépeau questioned the reasons for the opening words "for the purposes of this Chapter". He would have thought that this went without saying.

461. Schlechtriem suggested leaving it to the Rapporteur whether or not to leave those words or delete them.

462. The Group agreed on the following new wording of Article 3:

“For the purposes of this chapter the conferment of rights in the third party includes the right to rely on a clause in the contract which excludes or limits the liability of the third party”.

Article 4: The promisor may rely against the third party on any defence that could have been validly raised against the promisee

463. Fontaine felt that the language of the provision should be aligned along the language used in connection with assignment, so as to read “The promisor may assert against the third party all defences which the promisor could assert if the claim was made by the promisee”.

464. Bonell asked Furmston to be a bit more elaborate in the Comments.

465. Schlechtriem suggested adding an even more striking example in the context of insurance third party beneficiary contract. If the insurance contract was void, the insurer can use that as a defence against any claims.

466. The Group agreed on the following new wording of Article 4:
“The promisor may assert against the third party all defences which the promisor could assert if the claim was made by the promisee”.

Article 5: The contracting parties (or one of them if the contract so provides) may revoke the rights granted by the contract to the third party until the third party has accepted them or relied on them.

467. Schlechtriem reiterated his conviction that it is always up to the parties to the cover contract to shape the right of the third party beneficiary. He proposed to amend the article as follows “Unless otherwise provided, the right of the third party is irrevocable as soon as he has accepted or relied on it”.

468. Bonell recalled a similar provision in Italian Civil Code (Article 1411). He wondered, however, whether it was really necessary to expressly state “unless otherwise agreed” as all the rules laid down in the Principles are considered non-mandatory unless otherwise stated.

469. Crépeau wondered how the third party right could be revoked after the third party has accepted it.

470. Schlechtriem gave the example of a life insurance policy in favour of his wife which she declares to the insurance company that she accepts, but which nevertheless, in case of divorce, he can revoke unless otherwise provided in the policy.

471. For Crépeau this followed from a statutory provision.

472. Fontaine thought there were two different sets of causes of revocation. A stipulation in favour of a third party is irrevocable after acceptance. However if it is a gratuitous contract it can be revoked even if it has been accepted.

473. Bonell asked whether Fontaine therefore disagreed with the provision proposed.

474. Fontaine stated that the provision was acceptable provided that it was made clear that revocation could take place only with the agreement of the third party.

475. According to Finn at least in common law systems there is nothing wrong with the revocation of the right even after acceptance by the third party provided that the contract conferring that right so provides.

476. Date Bah agreed.

477. Also Fontaine agreed that if the possibility of revocation is provided in the contract the third party must accept revocation even after having accepted the right. Yet he had referred so far to situations where nothing is said in the cover contract.

478. Furmston wanted confirmation that the Group agreed that it will be open to the parties to provide for a different regime in the contract but if there is no such contract term the black letter rule as proposed would operate. He wondered whether he should include the words “unless otherwise provided in the contract” before the words “the contracting parties”.

479. Date Bah wondered whether in doing so usages to the same effect e.g. in a particular industry might be excluded.

480. Fontaine felt that reference to usages was very important and should be in the Comments. Earlier one had the example of marine insurance where somebody contracts a policy covering the goods to the benefit of the person who will have interest in the goods. This is stipulation for the benefit of a third party which cannot be accepted by the eventual beneficiary until much later. In the meantime it would be revocable according to the general rules of the Belgian Civil Code but many think that there is a usage against revocation.

481. Schlechtriem quoted paragraph 328(2) of the German Civil Code: “In the absence of express stipulation it is to be deduced from the circumstances, especially from the object of the contract, whether the third party shall acquire the right, whether the right of the third party shall derive forthwith or only under certain conditions, whether any right shall be reserved to the contracting parties to take away or modify the right of the third party without his consent”.

482. Farnsworth, though not disagreeing in substance, recalled that also in the past on a number of occasions the Group had discussed whether or not to insert such language in the black letter rules but as always decided not to do so on the understanding that they were all default rules.

483. A small drafting Group was charged with the task of either revising the text of Article 5 or drafting a new provision of a more general character. The Group suggested a new Article 1bis which reads as follows:

“Article 1 bis

The existence and content of a beneficiary’s right is determined by the contract of the parties and is subject to any conditions or other limitations under the contract”.

484. The Group decided to adopt this article.

V. SET-OFF

485. In introducing her paper (UNIDROIT 2001 Study L – Doc. 71) Jauffret-Spinosi pointed out that she saw at least four main problem areas: the different conceptions of set-off; whether set-off operates *ipso jure* or by declaration of the parties; whether or not set-off has retroactive effect; the conditions for set-off. In addition, and more in general, the Group had to decide whether it favoured a broad or a narrow scope of set-off. She recalled that business lawyers sometimes avoid choosing Swiss law as the applicable law simply because Swiss law has a too wide conception of set-off allowing too great powers to the judge. Of course these problems were all interlinked but she suggested addressing them in the order indicated.

486. Furmston had no strong views on the order of discussion provided that somebody would explain to him what set-off means in the present context.

487. Farnsworth too confessed that he had difficulty in understanding what the subject of the discussion precisely was. One possibility was to deal with the case where set-off is raised before a court, yet such cases would be of no particular interest in his country. The other possibility was the situation envisaged in paragraph 2-717 of the Uniform Commercial Code where parties are not before a judge and which could be considered a sort of self-help (“The buyer on notifying the seller of his intention to do so may deduct all or any part of the damages resulting from any breach of the contract from any part of the price still due under the same contract”).

488. Crépeau, quoting Article 1672 of the Quebec Civil Code which reads “Where two persons are reciprocally debtor and creditor of each other, the debts for which they are liable are extinguished by compensation up to the amount of the lesser debt”, wondered whether this could not be taken as a starting point of the discussion.

489. Furmston expressed considerable doubts in this respect. If set-off was limited to debts in the technical sense, i.e. money payments in each direction, the discussion could be wound up very soon since at least in common law countries in 95% of disputed cases of set-off involved a claim for money payment and a claim for damages for defective performance of a non-monetary obligation.

490. Di Majo pointed out that set-off involved a limitation of the freedom of one party. There is a creditor who can extinguish its duty not by performance but by another right. This is a limitation of the freedom of the other party. The conditions for these mechanisms has still to be defined.

491. Finn had understood that the premise of the present discussion was to create a regime where the parties do not have to go to court, but a workable regime of private ordering. If this was so a first concern must be that the system is not prejudicial to third parties. A second concern was that it is not oppressive of either party.

492. Bonell suggested taking the draft Chapter on Set-off of the PECL (Articles 15:101 – 15:107) as a starting point for a more concrete discussion on the subject.

493. It was so agreed and Bonell asked the Rapporteur to express her views on Article 15:101 (*“Conditions of Set-Off. - If two parties owe each other obligations of the same kind, either of them may set off his claim against the other party's claim, if and to the extent that, at the time of set-off, (a) he is entitled to effect his own performance and (b) he may demand the other party's performance”*) and on Article 15.102 (*“Unascertained Claims. - A debtor may not set off a claim which is unascertained as to its existence or to its amount unless the set-off will not prejudice the interests of the other party. Where the claims of both parties arise from the same legal relationship it is presumed that the other party's interests will not be prejudiced”*.)

494. With respect to Article 15:101 Jauffret-Spinosi agreed with the first condition, i.e. reciprocity.

495. Schlechtriem saw a hidden problem in the very short formula “if two parties owe each other obligations of the same kind”, i.e. that one party might have acquired its claim against the other party later. That is possible and has tremendous consequences in bankruptcy situations. Very often one tries to acquire a claim to set off because the other party is bankrupt and one cannot get any money from it.

496. Crépeau felt that the article did not set forth all the conditions for set-off. He quoted Article 1673 of the Quebec Civil Code which states in a more coherent and complete manner that “Compensation is effected by operation of law upon the co-existence of debts that are certain, liquid and exigible and the object of both of which is a sum of money or a certain quantity of fungible property identical in kind”. He found particularly important the reference to “a sum of money or a certain quantity of fungible property identical in kind”.

497. Bonell asked whether “obligations of the same kind” in PECL did not amount to the same thing.

498. Schiavoni expressed some difficulties with such a formula and proposed to speak of “obligations of the same object”.

499. Furmston asked whether he was right in assuming that under such a formula if in a contract one obligation was to pay money and the other obligation was to deliver goods or render services these were not obligations of the same kind.

500. Bonell confirmed they were not.

501. Furmston then sought confirmation that Article 15:101 only dealt with contracts in which one party's obligation is to pay money to the other and the other party's obligation is to pay money to the former, or two obligation to deliver oranges etc.

502. Bonell confirmed but pointed out that in his view Article 15:102 PECL provided a considerable enlargement because it envisaged the case where a claim for the payment of the price could be set off against a claim for damages for defective performance.

503. Finn insisted in asking whether an obligation to pay a debt was for these purposes an obligation of the same kind as an obligation to pay damages, say, for defective performance.

504. Jauffret-Spinosi confirmed provided that damages are liquidated and known as to their amount.

505. Bonell felt that if this was the case it was a situation covered by Article 15:101 while 15:102 went further referring to a case where the claim for damages was not yet ascertained as to its existence or to its amount.

506. Farnsworth objected that Article 15:102 did not give a right to set-off in such a case but excluded it.

507. Bonell drew attention to the phrase "unless ..." in the second line.

508. Farnsworth conceded that it was a matter of drafting then. The article should be rephrased so as to begin "A party may set-off a claim ...".

509. Schlechtriem was not sure whether everybody understood Article 15:102 in the same way. In his view it had nothing to do with a difference in kind. It had to do with a restriction on the right to set off if one of the obligations is not ascertained. The object of the obligation still had to be of "the same kind" in accordance with Article 15:101.

510. Bonell felt that the discussion touched upon a crucial issue, i.e. the possibility to set off the debt in money against a claim for damages. Such a possibility was excluded in for instance the Italian system or, more precisely, the set-off did not operate automatically but could only be declared by a court (Article 1243 (2) of the Italian Civil Code). He understood Article 15:102 as broadening the scope of set-off without the intervention of the courts.

511. Fontaine felt that what was presently expressed in a negative way as a condition of set-off should be stated in a positive way: “The claim must be ascertained”.

512. Farnsworth was still uncertain as to the meaning of “object of the obligation”. If under a contract for the sale of oranges there was a breach by the seller and the buyer had a claim for monetary damages, but the seller had a claim for the price in money, were those obligations of the same kind because they were both money or were they not of the same kind because one was a contractual right and one a remedial right?

513. In response to Farnsworth’s concern Crépeau stated that the answer was no until such time a claim for damages has been settled, i.e. the court has decided the amount of money owed.

514. Bonell agreed that this was the correct answer under Article 15:101. However in his understanding under Article 15:102 the answer would be yes, i.e. the debtor may set off a claim even if it is not yet ascertained either as to its existence or to its amount, provided that “the set-off will not prejudice the interests of the other party”.

515. Dessemontet felt that the difficulties encountered in the discussion derived from the wording “If two parties owe each other obligations of the same kind”. In an attempt to combine the definitions of the German Civil Code (paragraph 387: “Schulden zwei Personen einander Leistungen, die ihrem Gegenstand nach gleichartig sind...”; English translation: If two persons mutually owe acts of performance which are of the same kind ...) and of the Swiss Code of Obligations (Article 120 “Geldsummen oder andere Leistungen, die ihrem Gegenstande nach gleichartig sind ...”) he suggested the following wording “If two persons owe each other money or other acts of performance which are of the same kind ...”.

516. Jauffret-Spinosi quoted Article 1291 of the French Civil Code: “La compensation n’a lieu qu’entre deux dettes qui ont également pour objet une somme d’argent ou une certaine quantité de choses fongibles de la même espèce qui sont également liquides et exigibles”.

517. Also Farnsworth felt that the language used in PECL was not appropriate since its precise meaning was disputed even among the civil lawyers in the Group. As to Farnsworth’s example it was actually not regarded as a case of set-off in English law but was what is called abatement and what in civil law may be called *actio minoris*. He gave the following example: if a client comes to me and says “I made a contract to buy 100,000 pounds worth of oranges and they are not very good and I don’t want to reject them, like most English lawyers I would say “send them a cheque for 75,000 pounds”. One would not plan to pay the 100,000 pounds and then start an action for damages. One would pay less than the full amount.

518. Fontaine denied that there was a disagreement among the civil lawyers. They only were referring to different fact situations. In Farnsworth’s case if for claim for damages one intended “claim for damages that is not ascertained” then the answer is no. If on the contrary the claim was for damages which had been ascertained, then the answer was yes.

519. With respect to the example given by Furmston Bonell felt that the same solution could be justified also under 15:102.

520. Date Bah had difficulties in accepting this since the claim for damages is still disputed.

521. Bonell replied that this was possible because under 15:102 set-off was exceptionally admitted also if one of the claims was not yet ascertained as to its existence or to its amount.

522. Schlechtriem stated that under German law Article 15:102 would not have been necessary. He thought that it was intended as a compromise with the Romanic system.

523. Bonell felt that the discussion clearly showed that the language in 15:101 needed further improvement. First, “obligations of the same kind” was considered ambiguous and could be replaced by “performance of the same kind”. Secondly, the other condition for set-off, i.e. that the claim must be ascertained should be stated. This would make it possible to begin 15:102 with a statement that “Even if a claim is unascertained either as to its existence or its amount, it may still also be set off provided it does not prejudice ... and such a prejudice is presumed not to exist if the two claims come from the same relationship”.

524. Fontaine agreed and gave yet another example of two obligations which are at the outset of the same kind but one of which is uncertain so that set-off cannot take place: suppose two parties claim from each other sums of money (obligations of the same kind) and while one claim is not challenged at all, the other claim is challenged on the ground that the contract is void.

525. According to Bonell another example of obligations not having the same object was given in Article 15:103, i.e. monetary obligations expressed in different currencies.

526. Schlechtriem favoured the replacement of the wording “If two parties owe each other obligations of the same kind” by “if two parties owe each other performances of the same kind”.

527. Dessemontet and Jauffret-Spinosi suggested expressly mentioning monetary obligations: “If two parties owe each other money or other performances of the same kind”.

528. As to the condition of the claim being ascertained, Dessemontet suggested redrafting Art. 15.101 *lit.* (b) so as to read: “it is ascertained that he may demand the other party’s performance”.

529. Schlechtriem was not sure whether the additional requirement of ascertainability was really necessary and whether a clear majority was in favour of it. The German and Swiss laws did not have it.

530. Dessemontet admitted that in this regard he had been enlightened during the coffee break by Date Bah who questioned the use of having set-off if in any event one has to go to court. Indeed, if ascertainment, i.e. a sort of settlement by court order or some other official way, is required, this is mainly due to the Romanic systems where there was an automatic set-off. The relevant chapter in PECL is based on a different system, i.e. on declaration. He wondered whether certainty was still required once the system was no longer one of automatic legal compensation but one based on the will of the person to whom money is owed.

531. Schlechtriem agreed. If the ascertainability requirement is kept, you have to have two litigations: one to ascertain and then one to set off and that might be disputed. In the German system for instance the question whether and to what extent there is a counterclaim will be litigated in one and the same litigation, namely when it comes to the point where someone sues the other party, saying “I have set off” and then the other party replies “no, you couldn’t set off”. Just to make the German system even clearer: if in Farnsworth’s example you as the buyer and obligor to pay the purchase price kicked Farnsworth so that he has a tort claim – still uncertain as to what amount – he could set off that claim too, outside the court.

532. Crépeau urged to forget the domestic systems and think of the system which is proposed here. One may not like it but as far as he understood the system in PECL Article 15:102 is an exception to 15:101, and if 15:102 talks about the possibility of set-off of unascertained claims, 15:101 must implicitly provide for such a condition.

533. Jauffret-Spinosi wondered whether if the requirement of certainty of the claim was abandoned there was not a risk that a debtor asked by the creditor to pay, will say “yes, but I can set off” even though he knows that the debt is disputed. Was there no possibility of postponing the payment?

534. Dessemontet denied. There would be sanctions against such a postponement in the sense that in Jauffret-Spinosi’s example, the debtor would have to pay arrears, judicial costs, etc.

535. Finn questioned the meaning of *lit. (b)*.

536. According to Dessemontet *lit. (b)* was intended to make it clear that the other party’s performance is due. He said he would prefer to amend his previous proposal so as to read: “it is ascertained that the other party’s performance is due”.

537. Bonell wondered how one could be in a position to demand performance because performance is due if the obligation is not yet ascertained.

538. According to Schlechtriem this happens all the time: one claims punitive damages for 100,000 marks expecting 50,000 marks. The amount one will get is not yet ascertained but one can still go to court.

539. Bonell reminded that the Group's assumption was that set-off should be kept out of court.

540. Crépeau suggested further amending Dessemontet's proposal for *lit.* (b) so as to read: "the other party's performance is due and ascertained" because these were the two conditions for set-off under 15:101 for which 15:102 then provided an exception thereby coming closer to the German system as he understood it.

541. Jauffret-Spinosi and Fontaine agreed with Crépeau.

542. Schlechtriem wanted it reflected in the records that he thought that the requirement of the claim being ascertained was not necessary.

543. Crépeau failed to understand Schlechtriem's objection since he felt that Schlechtriem's position was taken care of by Article 15:102.

544. Furmston had difficulties in following the discussion. In his view it was obvious that there would be a large number of cases where the dispute does not go to court because in one way or another it will be resolved either by the parties agreeing or by one of the parties deciding it is not sensible in practical terms to go to court. To come back to the oranges case, if the price is 100,000 pounds and the buyer pays 80,000, the seller will often decide that in fact the sensible way forward is to take the 80,000 and get on with life although he may think that he should have got 85,000 but it is not worth it to sue him. In the English system that is actually what set-off is all about. In many cases it is a question of forcing the other party to decide whether he wants to go to court. You don't want to go to court and litigate the question of the defects of the oranges, you want to force the seller to go to court and sue for the balance. In many cases the seller will give up at this point. It is a question of judgment and how much you take off. Only sometimes will there have to be a resolution by the court.

545. Turning to Crépeau, Schlechtriem wanted to know whether in the following situation a counterclaim would in his view be certain or not: I have bought oranges from Bonell, I owe him the price but I don't have the money. Farnsworth says he has a tort claim against Bonell for about the same amount. So he assigns his tort claim to me. Now I go to Bonell, I bring along Farnsworth as my witness and say, well he has a \$100,000 tort claim and I set it off. Is that certain enough?

546. Crépeau wondered whether a distinction has to be made between "certain" and "ascertained". When you say "I have a tort claim for \$100,000" this is your opinion about the value of your claim and if it is disputed by me I think there cannot be any set-off unless the court comes down with a judgment saying "you are right" or "you are not right, it is only for \$75,000" and then the set-off is made for \$75,000.

547. Schlechtriem said that that was exactly what would happen in his system: if one sets off a sum in excess there is always a risk that in the end there will be litigation and that party will have to bear the costs.

548. Asked by Bonell whether the same could said of common law systems, Furmston denied, not because it was a question of certainty or uncertainty but because the two claims did not arise out of the same transaction.

549. Bonell asked whether therefore the further qualification in Article 2 was important.

550. Furmston confirmed.

551. Farnsworth agreed.

552. Crépeau felt that the Group was getting close to a consensus. He referred again to his example: there was a claim for \$100,000 and there was objection as to the liquidity or the ascertainability of that claim. He wanted to know from Schlechtriem when in his system set-off becomes effective. Was it when the party sets off its claim for \$100,000 or when the judge decides that it is \$75,000 or \$ 50,000?

553. Schlechtriem stated that set-off became effective retroactively but the condition was that the set-off claim had to be ascertained by a court. He still wanted to know whether “ascertainment” or “certainty” meant something different in those systems which expressly required it.

554. Dessemontet wondered whether the difficulty with “ascertained” was that it is a passive form of the verb and it was not clear who has to “ascertain”. He further questioned what was the relationship between a system where you have to declare set-off and a system where ascertainment is required.

555. Crépeau recalled that in his system the terms “certain” and “liquid” were used.

556. Fontaine objected that these were two different concepts. Liquid meant that the amount was fixed, while ascertained meant that it was not disputed. A debt could be liquid but not certain/ascertained because it is disputed; on the other hand a debt could be certain but its amount still to be fixed.

557. Schlechtriem found Crépeau’s intervention very interesting. If a claim has to be ascertained by the court, then the defence of set-off must be admitted despite the fact that at that moment the claim is not yet ascertained. This would mean that they were very near the German system.

558. Bonell thought that this was what in his system was called “judicial set-off”, while he understood the German system as well as Article 15:102 admitted also set-off of unascertained claims by mere declaration of the parties.

559. Jauffret-Spinosi drew attention to her draft at page 15 where she had proposed as one possible approach to require that the two obligations to be set-off must be “liquid” and that when such requirement is not fulfilled the parties may agree on a judicial set-off.

560. Bonell asked whether the English speaking members would prefer the term “liquid”.

561. Furmston definitely preferred the term “ascertained”.

562. Asked by Bonell whether for her the two terms were equivalent, Jauffret-Spinosi confirmed.

563. It was decided to use the wording “ascertained as to its existence or to its amount”.

564. Bonell asked for comments on Article 15:102.

565. Schlechtriem objected that Jauffret-Spinosi and Crépeau had made a different proposal, i.e. that if a claim was not ascertained the parties could have the matter decided in court. For him it was then a matter of the quality of the judgment. Maybe Crépeau had thought of a system where the judgment had constitutive effect, while he was thinking of a system where the judgment was merely declaratory.

566. Bonell felt that that the Group had agreed to set up a system of set-off which could work outside court intervention. In the case of disputes there was of course always the possibility of court intervention, just as in the case where a party avoids or terminates by declaration the contract and the other party challenges its right to do so.

567. Schlechtriem saw the difference in the following terms: if ascertainment was a requirement for set-off, the court might throw off the defence from the very beginning, while if it was not, the court has to go into the merits of the claim raised as a defence in set-off.

568. Furmston stated that in his system there was a fundamental difference between the defects in the oranges and the kick on the shins. If the seller of the oranges sues for the price, the buyer cannot set up a defence that the seller of the oranges kicked him in the shins. So he has to pay the price and sue for the injury. But he can set up a defence that the oranges are defective.

569. According to Bonell this was precisely why Article 15:102, while requiring in general for the set-off of an unascertained claim that it will not prejudice the interests of the other party, presumes that the other party’s interests are not prejudiced if the claims of both parties arise from the same legal relationship.

570. Date Bah wondered what was meant by “will not prejudice the interests of the other party”.

571. Farnsworth too had difficulties with the article. Was it not true that set-off was, by its very nature, an encroachment on the liberty of the other party and will therefore prejudice the interests of the other party? Moreover as to the condition that the claims arise from the same legal relationship, he recalled that international contracts very often were extremely complex so that it was very difficult to establish whether or not given claims related to one and the same relationship. Lastly and above all if it was only presumed that in such a case there was no prejudice to the other party, in practice this will always be disputed so that recourse to set-off would in practice be seriously limited.

572. Bonell asked whether Farnsworth would therefore prefer a provision stating that unascertained claims may always be set off provided that they arise from the same legal relationship.

573. Farnsworth confirmed.

574. Schlechtriem found the proposal very interesting given the scope of the Principles which deal with international commercial contracts and could therefore well adopt a solution different from the ones provided at domestic level including the German system.

575. Komarov agreed.

576. Bonell asked whether there was general agreement on a provision stating that a debtor may set off a claim which is unascertained where the claims arise from the same legal relationship.

577. It was so agreed. The Group also agreed to adopt an article along the lines of Article 15:101 PECL stating that the conditions for set-off were that (a) the party declaring set-off was entitled to effect its own performance; and (b) the other party's performance is due and ascertained".

578. Jauffret-Spinosi presented two draft articles she had prepared together with Crépeau which read as follows: "Article 1 (Conditions of Set-off). If two parties owe each other obligations, the object of which is a sum of money or performance of an obligation of the same kind, either of them may set off his obligation against the other party's obligation if, at the time of set off (a) he is entitled to effect his own performance and (b) the other party's performance is due and ascertained. – Article 2 (Unascertained Claims). A debtor may however set off an obligation which is not ascertained as to its existence or to its amount provided the obligations of both parties arise from the same legal relationship".

579. After discussing several proposed amendments the Group agreed on the following text of the two articles:

"Article 1 (Conditions of Set-off). Where two parties owe each other obligations to pay money or to render performances of the same kind, either of them may set off its obligation against the other party's obligation if, at the time of set off (a) it is entitled to perform its obligation and (b) the other party's obligation is due and ascertained.

Article 2 (Unascertained Claims). However, an obligor may set off an obligation which is not ascertained as to its existence or to its amount provided the obligations of both parties arise from the same legal relationship”.

580. Moving on to Article 15:103 (*“Foreign Currency Set-Off. - Where parties owe each other money in different currencies, each of them may set off his claim against the other party's claim, unless the parties have agreed that the party declaring set-off shall pay exclusively in a specified currency”*), Bonell recalled that with respect to currency of payment the Principles, given their universal scope of application, adopt a different approach than PECL. Indeed according to Article 6.1.9 if a monetary obligation is expressed in a currency other than that of the place for payment it may be paid by the obligor in the currency of the place for payment, unless the parties have agreed that payment should be made only in the currency in which the monetary obligation is expressed or that currency is not freely convertible. Since the PECL do not provide for the second exception, he wondered whether also the present provision, if included in the Principles, needed to be adapted accordingly.

581. Dessemontet agreed but wondered whether it was not enough to require that the currency of the party against whom set-off is declared is freely convertible: indeed it is only that party against whom something is imposed. He suggested the following wording “Where the parties owe each other a sum of money in different currencies, each of them may set off his claim against the other party’s claim unless the currency of the other party’s obligation is not freely convertible or the parties have agreed that the party declaring set-off shall pay exclusively in a specified currency”.

582. Bonell wondered what “the other party’s currency” would mean. Was it the currency in which that party was going to pay?

583. Fontaine pointed out that while Article 6.1.9 referred to the currency of payment, in the present context the currency of account was relevant: indeed the party which is setting off does not yet know what currency the obligor will choose as currency of payment.

584. Di Majo raised the issue of the rate of exchange.

585. Farnsworth pointed out that a provision of the kind contained in 15:103 or just proposed by Dessemontet appeared to be inconsistent with the opening article of this chapter stating “Where two parties owe each other obligations to pay money ...” followed by the restrictions to the possibility of set-off which had been discussed at length. How could the present article state “Where parties owe each other money in different currencies ... ” without referring to those restrictions? At least one should change the wording so as to read “Where the obligations are to pay money in different currencies, a right of set-off may be exercised if...”: this would make the provision more consistent with Article 1.

586. Schlechtriem wondered whether Article 3 should become a second paragraph in Article 1 and thereby clarify the notion of “obligations of the same kind” if different currencies are involved.

587. Farnsworth felt that Schlechtriem’s proposal could lead one to believe that such a foreign currency rule had nothing to do with Article 2 while in his view one could imagine an Article 2 case with foreign currencies.

588. Bonell agreed and asked Farnsworth to read out his proposal again.

589. Farnsworth proposed that the opening wording of Article 3 should be “Where the obligations are to pay money in different currencies, a right of set-off may be exercised ...”

590. Crépeau supported the proposal.

591. It was agreed.

592. Crépeau raised another issue. If the parties are in different countries and there is set-off between two debts where the place of payment is different, then the set-off involves not only a question of how payment is to be made but also a question of the expenses for performing from one country to another. He quoted a provision in the Quebec Civil Code (Article 1674) “Compensation is effected even though the debts are not payable in the same place provided allowance is made for the expenses of delivery if any”.

593. Schlechtriem agreed on the importance of the issue and quoted a similar provision in the German Civil Code (Article 391) “Set-off is not excluded by the fact that different places for performance or delivery exist for the claims. The party making the set-off shall however compensate for any damage which the other party suffers by reason of the fact that in consequence of the set-off he does not receive or cannot effect the performance in the fixed place”.

594. Di Majo read the corresponding provision in the Italian Civil Code (Article 1245) stating that when the two debts are not payable at the same place, the cost of the transport to the place of payment has to be taken into account.

595. Fontaine wondered what was the fact situation envisaged by such rules. Was it the case where because of set-off one party would not receive a certain amount of money it was expecting to receive?

596. Schlechtriem confirmed and read out paragraph 2 of Article 391 of the German Civil Code stating that if it is agreed that payment should be made only at a certain place, it is presumed that set-off is excluded. The reason for such rules was that if a party wanted to have the money paid for instance in New York, because it needed the money there, there was a set-off; this meant that that party had to transfer money from its own account to New York which may cause expenses.

597. Dessemontet questioned the rationale of such a rule. If set-off is a right, why should the party exercising it become liable for possible losses the other party may suffer as a consequence thereof?

598. Schlechtriem disagreed: the right to set-off was a kind of favour given to the debtor.

599. In view of the fact that different views had been expressed with respect to a special rule dealing with compensation for costs caused by the set-off, Bonell asked the Rapporteur to prepare a draft provision but to place it in square brackets.

600. Bonell asked for comments on Article 15:104 (*Set-Off by Notice. - The right of set-off is exercised by notice to the other party*”).

601. Schlechtriem expressed his support for a provision of this kind.

602. Jauffret-Spinosi, while agreeing in substance, felt it necessary to state expressly that set-off must be declared and that the declaration must be exercised by notice to the other party.

603. Bonell drew attention to similar provisions already contained in the Principles, namely Articles 3.14 and 7.3.2 (1). He also referred to Article 1.9.

604. Finn too thought that the notice requirement necessarily involved a declaration.

605. It was agreed to have a provision along the lines of Article 15:104 PECL.

606. Bonell asked for comments on Article 15:105 (*“Plurality of Claims and Obligations. - (1) Where a party giving notice of set-off has two or more claims against the other party, the notice is effective only if it identifies to which of that party's claims it relates.*

(2) Where the party giving notice of set-off has to perform two or more obligations towards the other party, the rules in Article 7:109 apply with appropriate modifications”).

607. Crépeau wondered about the relationship between such a provision and Article 6.1.12 relating to imputation of payment.

608. Bonell drew attention to paragraph 2 where there was an express reference to the corresponding provision of PECL.

609. Farnsworth proposed a stylistic change in the wording of both Articles 5 and 6. Instead of speaking of “effective only if it identifies to which of that party’s claim it relates” he proposed “only if it identifies the claims to which it relates”.

610. Dessemontet wondered whether it was appropriate in the context of paragraph 1 to require the identification of the claim, i.e. to consider the notice of set-off ineffective if the claim is not identified. He referred in particular to the case where a

customer has several different accounts with the same bank and where it was quite frequent that the customer declared to set off “any claim you (i.e. the bank) could have against me”. He suggested that if the debtor does not identify the claims a default rule along the lines of Article 6.1.12 (2) should apply.

611. Jauffret-Spinosi and Schlechtriem agreed.

612. Finn and Fontaine were, on the contrary, in favour of the solution adopted in PECL.

613. The Group agreed on a provision along the lines of Article 15:105 PECL.

614. Bonell asked for comments on Article 15:106 (“*Effect of Set-off. – Set-off discharges the obligations, as far as they are coextensive, as from the time of notice*”).

615. Jauffret-Spinosi had some difficulties with the rule stating the *ex nunc* effects of the declaration of set-off. She conceded that in a system in which set-off operates by declaration it makes sense to state that set-off takes effect only from that moment. However she still preferred retroactivity.

616. Dessemontet pointed out that if the Group was going to adopt the rather unusual rule contained in this article, this should at least be made subject to trade usages to the contrary.

617. Bonell recalled the general rule on usages contained in Article 1.8 of the Principles.

618. Schlechtriem expressed his preference for retroactivity which after all was the absolutely predominating solution at domestic level.

619. Finn wondered what the practical implications of the two solutions were.

620. Jauffret-Spinosi mentioned interest.

621. Schlechtriem pointed out that if set-off discharges the debtor retroactively, then there would be no breach of contract, whereas if it discharges the debtor only *ex nunc* there might in the meantime be a request for termination of the contract. Yet there were also practical reasons in favour of the retroactive effect. For instance, A has a claim against B and B has a claim against A. B is a bit shakier and might go bankrupt. If the effect of set-off is *ex nunc*, A must give notice of it as soon as possible. If on the contrary A knows it has retroactive effects, it can wait and see. Perhaps B will pay. And since the declaration – the notice – of set-off is always regarded as some sign of distrust, he thought merchants tended to wait until the situation becomes difficult. If provision was made for the *ex nunc* effect this would induce merchants to give notice of set-off as soon as possible. Finally if set-off has no retroactive effect, a party must sue the other party before the limitation period expires in order to suspend the running of the limitation period. If a party can set off with this retroactive effect then it must not sue. So the retroactive effect solution would avoid litigation.

622. Furmston wondered why the drafters of PECL had chosen the *ex nunc* effect solution.

623. Schlechtriem indicated certainty as one possible reason. Indeed, while the moment when notice can easily be established, it was harder to establish the exact moment when for the first time the two obligations matched each other.

624. Finn and Komarov expressed support for the rule adopted in PECL.

625. Farnsworth had difficulty with the notion “co-extensive”, the meaning of which was to him entirely obscure.

626. Dessemontet stated that some codifications used the formula “retroactive to the time where for the first time setting off could be opposed”.

627. Crépeau understood “co-extensive” to mean that set-off will operate “up to the amount of the lesser debt” to use the formula of Article 1672 of the Quebec Civil Code.

628. Fontaine expressed his preference for the latter wording.

629. Schlechtriem quoted Article 389 of the German Civil Code “The set-off has the effect that the claims insofar as they cover each other are deemed to have expired at the moment at which being suitable for set-off they are balanced against each other”.

630. Farnsworth did not like “balanced” and suggested the following wording “Discharge by set-off is effective from the time that the right of set-off could be exercised”.

631. The Group agreed on this wording.

632. Bonell asked for comments on Article 15:107 (“*Exclusion of Right of Set-Off. - Set-off cannot be effected (a) where it is excluded by agreement, (b) against a claim to the extent that that claim is not capable of attachment, and (c) against a claim arising from a wilful delict*”).

633. Jauffret-Spinosi stated that she had no objections as to the substance of the provision.

634. According to Schlechtriem the exception of claims arising from wilful delict went without saying.

635. Fontaine recalled that apart from alimony which in the context of international commercial contracts obviously is irrelevant, there were other claims which could not be attached and are relevant such as salaries.

636. Crépeau wondered whether instead of wilful delict one should not speak of wilful conduct.

637. Dessemontet found *lit. (b)* of no interest in the context of international business relationships. As to *lit. (c)* he was afraid it could open a Pandora's box. In practice it quite frequently happened that somebody has entered into a contract and later on would like to get out of it, claiming that it had been induced to conclude the contract by fraud or by wilful deceit of the other party. This would make set-off impossible.

638. Schlechtriem saw some merits in *lit. (c)*. He made the following example: in the context of a sales arrangement, the seller has granted access to the buyer to its trademarks or business secrets. If the buyer/debtor violates the trademark or the business secret, it will be liable in damages on account of some wilful misconduct. If *lit. (c)* was deleted one could be induced to such misconduct in order to open up a chance of set-off.

639. Bonell wondered whether there was a risk that *lit. (c)* could be understood in the sense of covering also cases of intentional breach of contract. If so, this would be yet another argument in favour of deleting *lit. (c)*.

640. Farnsworth agreed with Bonell.

641. Summing up the discussion Bonell saw little support for *lit. (b)* because of its irrelevance in the context of international commercial contracts. There were likewise rather strong objections to *lit. (c)* and since *lit. (a)* expressed a general principle, he wondered whether the Group could agree on the deletion of the entire article.

642. The Group agreed.

643. Furmston drew attention to the fact that the parties may by agreement change the rules of set-off in either direction, i.e. not only exclude set-off but ease the conditions for set-off. True, this too followed from the general principle of party autonomy but perhaps it would be advisable to mention it in the Comments.

644. It was so agreed.

645. Dessemontet raised the issue of waiver of the right to set off.

646. Bonell recalled other contexts in which the possibility of a waiver had been discussed such as the defence of limitation period and asked Finn whether he was prepared to give further thought to whether waiver should be addressed in general terms in a separate section and, if so, to prepare a preliminary draft for the next session of the Working Group.

647. Finn agreed.

VI. AGENDA FOR THE NEXT SESSION AND OTHER BUSINESS

648. Bonell announced that the next session of the Working Group would be held in Rome from 3 to 7 June 2002. On that occasion the Group would be in a position to

have a final reading of the draft Chapters on Limitation Periods, on Assignment of Rights, Transfer and Assumption of Obligations and Transfer of Contracts, on Third Party Rights and on Set-off. There should also be the position paper on waiver.

649. The Summary Records of the current session would be sent out as soon as possible so as to permit the Rapporteurs to prepare their revised drafts. He reminded the Rapporteurs that they should also revise, wherever necessary, the Comments so as to align them as to their format and structure with the Comments in the existing version of the Principles. In particular he recalled that the Comments should not be too lengthy nor too succinct; each main question addressed in the Comments should be dealt with in a separate paragraph, preceded by a short title and whenever appropriate including one or more illustrations; the Comments should not contain any reference to domestic law or to PECL (the reciprocally beneficial influence of the UNIDROIT Principles and PECL will be acknowledged in the Foreword in general terms).

650. Bonell recalled that the Group had decided at its first session to determine whether the present edition of the Principles needed to be amended and if so in what way in order to take into consideration the peculiarities of e-commerce. Uchida had been entrusted with the task of preparing a paper on this matter. Yet in order to collect as much information and/or comments as possible on e-commerce and the UNIDROIT Principles, it was agreed that Farnsworth would identify also a person in his country for this purpose. The other members of the Group were invited to do likewise.

APPENDIX I

WORKING GROUP FOR THE PREPARATION OF PRINCIPLES OF INTERNATIONAL COMMERCIAL CONTRACTS

Fourth session

Rome, 4-7 June 2001

LIST OF PARTICIPANTS

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