The Limits of Harmonising Contract Law in the European Union

§ 1. On the Method and Aims of the Study
1. The Role of Comparative Private Law

When attempting to assess the plans the European Union has worked out for the harmonisation of private law, and in particular contract law several methods may be applied. A traditional analysis would approach the issue in terms of the discipline of private law, and examine: first, the legal institutions of the national legal systems that afford such an opportunity; second, the possible comparative legal bases of adopting common rules; third, the methods of assessing this possibility; and, fourth, the ways and means of resolving the problems arising from varying legal cultures and traditions with divergent terminologies and languages. It will necessarily be scholars of comparative private law who will come to take a stand on the possibilities of legal harmonisation. Such an assessment is a fundamental and indispensable condition of elaborating any justifiable programme on legal harmonisation. This was essentially the approach taken by both the Lando Commission when preparing Principles of European Contract Law, the Trento Project and the Study Group on the European Civil Code when analysing the possible solutions to concrete cases according to the various rules of the national legal systems.

2. The EU law Approach

It would not be irrelevant – and would indeed aptly supplement the method of examination mentioned above – to approach the harmonisation of contract laws from the point of view of the institutional and legal system of the European Union. In so doing, we would face such questions: How far does the functioning of European integration require the common adoption of rules for certain types of transaction? What legal bases does the Treaty on the Functioning of the European Union provide for putting into practice the said harmonisation? And how can the actual application and unified interpretation of acts of the European Union be ensured? Referring to former studies of mine, I will apply this latter, integration-oriented approach, and, on this basis, we will arrive at a position on the possibilities and limits of the approximation of contract laws in the European Union. This was the attitude which the European Commission itself followed in three recently issued communications which sought to explore the possibilities of harmonising European contract laws.

§ 2. The Need for Legal Harmonisation – the Pros and Cons

1. The Needs of the Internal Market

In arguing for the harmonisation of contract laws, the requirements of the internal market are the most frequently cited. These imply the establishment of an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured. The desire for a level-playing-field in a unified regulatory area ties in well with this concept in respect of private law too. The preambles of directives regulating consumer contracts repeatedly use this reasoning. But the literature on law also has a predilection to claim the necessity of approximation of laws on the grounds of the needs of a single economic area. Ole Lando, for instance, refers to the requirements of the free movement of goods, persons, services and capital when regarding the diversity of contract laws as a non-tariff type of restriction of trade. Peter-Christian Müller-Graff and Konstantinos D. Kerameus also hold a similar view, stating that the varieties and parallelisms of national regulations, which sometimes even

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7 Article 14 (7/A) of the Treaty establishing the European Community (EC Treaty), Art 26(2) TFEU.


10 Kerameus, op. cit., p. 480.
overlap, are a source of confusion and uncertainty. Carla Joustra and Filip De Ly invoke the same “internal-market argument” in their studies of consumer law\textsuperscript{11} and \textit{Lex Mercatoria}\textsuperscript{12} respectively.

Oddly enough, the actors of commercial life themselves have noticed the trade-restricting effects of the divergence of contract laws while perceiving the possible related legal uncertainties much less. According to a survey by the European Commission the legal insecurities connected to cross-border contracts and transactions was only the ninth on the list of factors obstructing establishment of the single market, and only 17\% of those asked regarded this as a problem. (In contrast, the first four in the list were as follows: (i) divergent national technical provisions; (ii) unusual procedures of testing and authorisation; (iii) discriminating state subsidies; (iv) different systems of value-added tax.)\textsuperscript{13} The regular participants of international commerce seem to be quite satisfied with the opportunities of choosing governing law and a reliable mechanism of international arbitration.\textsuperscript{14} Nor does Hugh Collins regard the reference to the requirements of the single market as sufficient. In his opinion, the different private-law rules of the various countries can increase competition, as they add the competition of rules to those of goods and prices.\textsuperscript{15} Jules Stuyck is similarly unconvinced about the argument that the single market undoubtedly calls for legal approximation, and he even demonstrates, on the basis of examining the substantive regulation of consumer transactions, that excessive interference jeopardises the single market and the economic freedom and competition it epitomises.\textsuperscript{16}

The European Commission has repeatedly discussed the effects the various contract laws have on the internal market in its communications, particularly in its action programme entitled: “A more coherent contract law. An action plan.”\textsuperscript{17} In this study, it calls attention to the conflict of mandatory rules under the laws of the Member States, which is little redressed by the possibility of choosing law. There are significant differences between the contract laws of the Member States, and the communication cites several examples. There are major divergences in the formal requirements for concluding contracts, the use of notaries public, writing and prescribed language in particular. There are differing ways of

\textsuperscript{17} See points 5, 14, 25-54 of COM(2003) 68 final.
inserting general conditions and standard terms of contract into contracts and of implementing them, with the laws of some countries regarding simple references as sufficient, while Italian law requires that the be annexed to the contract and signed. There are substantial differences in respect of restricting and excluding liabilities resulting from contracts, as well as with regards to the transmission of property and movable collateral. Moreover, European private laws interpret the concepts of damage and compensation differently.\textsuperscript{18} There are special difficulties in respect of cross-border financial services, and insurance contracts in particular. The difficulties arising from the differences in contract laws are therefore not insignificant.

2. Consumer Protection

As far as consumer contracts are concerned, reference to the fundamental economic freedoms also fares well in arguments. Union-level legislation on consumer protection admittedly \textit{aims at integration}: it must contribute to the free movement of goods and services.\textsuperscript{19} The free movement of the factors of production is established not only through the export-import transactions of traders, but also through the deals made between private persons (consumers) and traders coming from other Member States. Consumer transactions thus play an emphatic role in creating the internal market – which is purportedly jeopardised by the differences between the legal systems of the Member States, which make consumers feel uncertain about their rights in cases of cross-border transactions. This is the reason why the Community seeks to establish a common hard core of regulations, “a uniform set of fair rules.”\textsuperscript{20} Finally, this intention has been boosted further by “developments in electronic trade, which make it even easier to access the sale networks of traders established in other Member States.”\textsuperscript{21}

It has however been pointed out by several observers that, in relation to consumer transactions concluded in traditional ways, language barriers and the difficulties of maintaining contacts after concluding contracts deter consumers from cross-border shopping more than the differences in national contract laws that laymen perhaps do not sense as much as.\textsuperscript{22} In addition, the directives in effect on

\textsuperscript{18} Point 36 and note of the Communication from the Commission to the Council and the European Parliament on European Contract Law.


consumer transactions provide for so-called minimum harmonisation, allowing for significant differences between the laws of the Member States.23

3. Decreasing Transaction Costs

Related to the single-market argument, the so-called transaction costs explanation is also often brought up. The essence of this is the following: the differences in national contract laws entail further costs in cross-border transactions – primarily those incurred through seeking appropriate information on unknown legal systems. Even so, it is quite difficult, as a result of the different, sometimes even conflicting regulations, to anticipate the various difficulties arising in the different stages of the existence of a contract, the legal means and costs of their solution. All these are further magnified when a cross-border transaction ends up in the courts. In such cases, employing top, exorbitantly costly lawyers specialising in international legal dispute is inevitable. Medium and small scale enterprises can hardly afford this; the diversity of national regulations therefore actually favours large firms.24

The argument of decreasing transaction costs can also be deployed against the principle of subsidiarity. In accordance with the principle of subsidiarity, the Union can interfere in areas not within its exclusive competence only if and in so far as the objectives of the proposed action cannot be sufficiently achieved by the Member States, and can therefore be better achieved at Union level by reason of the scale or effects of the proposed action.25 Could private law and contract law not, then, remain within the competence of the Member States? In contrast, the reasons outlined above justify the existence of European regulation, in so far as European rules are capable of decreasing transaction costs to a greater extent than national ones can.26

However convincing this contention might seem to be, it is not immune to challenge: there is little chance of establishing a fully unified system of rules through, for example, juridical acts of the Union, and, notwithstanding the adoption of such uniform legislation, its unified interpretation would also run into difficulties.27 Certain issues resulting from the legal harmonisation realised in directives are settled by either EU law or the laws of the Member States; therefore, a significant part of thorny legal questions – and their embarrassing

23 The European Commission itself admits this, see point 50 of its communication “A more coherent European Contract Law” (COM(2003) 68 final).
24 Mattei, Ugo, “A transaction cost approach to the European Code.” In: European Review of Private Law, vol. 5, no. 4, 1997, p. 538. o. [Mattei, 1997.]. Points 5 and 29-30 in particular of the Commission communication “A more coherent contract law” argues so: “It has also been pointed out that taking advice on the unknown applicable law will involve considerable legal cost and commercial risks for this party to the contract, without necessarily giving the most economically favourable situation. This is particularly important for SMEs since the legal assistance cost are proportionately higher for them. As a result, SMEs will either be dissuaded from cross-border activities altogether or will be put at a clear competitive disadvantage compared to domestic operators.”
25 Article 5 (3/B) of the EC , now Article 5 paragraphe 3. TEU.
26 3 Mattei, Ugo, 1997. 537.
27 The procedure of preliminary ruling in front of the European Court provides only a limited facility for this, see Article 234 (177) of the EC Treaty, now Article 267 TFEU.
cost implications – remain, and may even become more complicated and burdensome. To top it all, the costs of legal harmonisation need to be borne: specially trained civil servants need to be employed at both Union and national levels; not to mention the financial corollaries of several years of drafting co-ordination, Union-level legislation, then translations, and the transposition into the laws of the Member States. The transaction costs that were meant to be evaded seem, in this fashion, to be transformed into the social costs of legal harmonisation.

4. The Approximation of Legal Systems

In many people’s view, contract law seems to be apt to legal harmonisation because it is assumed that the conclusion and implementation of contracts is similar everywhere in the circumstances of a market economy: its regulation is based on the same inherent logic. Moreover, a sort of spontaneous approximation has also taken place; continental Europe has taken over Anglo-American legal institutions, such as leasing and franchising, while English law has come round to protecting consumers, lessees and employees.28

Nevertheless, the differences between legal systems and the divergent outlooks behind them cannot be brushed aside. As Hein Kötz has written, there is a good deal of truth in that British contract law was devised for tradesmen, while its French counterpart was made for farmers, or, in terms of the turn of the millennium, for managers and consumers. It is no wonder, then, that the protection of consumers has a more prominent place in French law than in English law.29 There is also a visible difference in how common law and continental law acknowledge the principle of good faith, with English law providing it very limited application.30

5. Historical Arguments

Based on the study, the teaching and a general application of Roman law, a nostalgic evocation of a once-upon-a-time European legal unity – or, at least, an added emphasis on the common roots embodied in Roman law—31 has been used to provide theoretical ground for the unification, or at least approximation, of private law and contract law within it. Therefore, as Reinhard Zimmerman says, the task of scholars of legal history is to raise the awareness of our

29 See Kötz, op. cit., p. 552.
31 “Up until the time of the of the so-called usus modernus pandectarum in the 17th and 18th centuries, the whole of educated Europe formed a single and undifferentiated unit, not only in general cultural terms but also legally.” Reinhard Zimmermann, “Roman Law and European Legal Unity.” In: Arthur S. Hartkamp et al., op. cit., 1998, p. 27. Zimmermann, in an expression of agreement, refers to Helmut Coing’s 1985 work Europäisches Privatrecht Band 1: Alterses Gemeines Recht (1500-1800) (Munich: Beck Juristiche Verlag), and calls it his opus magnum. For a critical assessment of the law-history justification of legal harmonisation, see Daniela Caruso, op. cit., p. 18.
common legal tradition, which continues to influence the development of modern national legal systems, defining as it does their taxonomical, theoretical and ideological basis, and which is only covered up by the debris of two centuries of legal particularism.  

The assessment of the past is not equivocal, however, because the European legal tradition itself has many strands. As opposed to Zimmermann and Coing, the legal culture of the mediaeval Europe, as Wilhelm Brauneder has pointed out, was very much multi-faceted. Naturally, Roman law had a definitive role in education and in its interpretative, gap-filling function. Nevertheless, local common-law traditions had an important function; moreover, Roman law was far from a self-enclosed unity lacking all contradiction. In assuming a European legal unity, these scholars neglected to take local and regional sources into consideration, and forewent the study of trade law, and thus the picture they draw and historical reality seem to be at odds with one another.

The debate is far from being closed however. There are some who go so far as to state, referring to the way Roman law has exerted its influence on the various legal systems through the centuries – beginning with the Corpus Iuris through German Pandectist law and the Bürgerliches Gesetzbuch (BGB, civil code of Germany) to the Japanese civil code, which is based on it – that foreign codes and legal systems can indeed be taken over, legal “transplantation” causing no particular confusion. However convincing this elegantly drawn legal historical lineage might seem, it should not be forgotten that, although the influence of Roman law cannot be called into doubt, it was not a matter of simply taking it over but an organic adaptation in all the cases mentioned, where Roman law was cleansed of its elements which recalled a pre-industrial society, and where home traditions were taken into consideration too.

§ 3. The Basis of Legal Harmonisation
1. Limited Powers

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37 This was an explicit aim at the time of drafting the Japanese Civil Code, after its first version based on the French Code Civil had not been put into force. As Gábor Hamza put it, “the legal institutions regulated in the general, the substantive-law and the contract-law parts of the Code are primarily based on Roman law and German Pandectistics.” Az európai magánjog fejlődése [The Development of European Private Law]. Budapest: Nemzeti Tankönyvkiadó, 2002, p. 301.
When assessing the feasibility of legal approximation, it must always be born in mind that the European Union has no general power to legislate: it is obliged to find a particular provision in the Treaty on the Functioning of the European Union that affords legal ground for adopting any act. With regard to contract law, Articles 26, 114, 115, 169 and 352 can serve as the basis of legislation.

Article 115 authorises the Council, acting unanimously, to issue directives for the approximation of such laws, regulations or administrative provisions of the Member States as directly affect the establishment or functioning of the internal market. A related provision laid down by Article 114 lends scope for adopting measures to establish and ensure the functioning the internal market. Taking Union action is easier in this case in so far as the Council may make its decisions according to ordinary legislative procedure by qualified majority voting. Referring to Article 114 TFEU, i.e. the appropriate functioning of the internal market and the elimination obstacles to trade between the Member States – in the same vein as the argumentation outlined above – became a recurrent theme of the directives aiming at the approximation of contract laws. This established practice, however, was limited by the decision the European Court made on the Federal Republic of Germany v. European Parliament and Council of the European Union case in October 2000. In this case, it had to decide whether or not the directive prohibiting virtually all advertisement of tobacco products had sufficient legal ground in Article 95 (100/A) of the EC Treaty. Bringing a crucial judgment, it declared that the reference to the establishment and appropriate functioning of the internal market does not vest Community institutions with a general power to legislate. This would be a breach of the express wording of the regulations on internal market and the principle of subsidiarity enshrined in Article 5 (3/B) of the EC Treaty. Moreover, the Community measure must genuinely have as its object the improvement of the conditions for the establishment and functioning of the

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39 Former Articles 94 (100), 95 (100/A), 153 (129/A), 308 (235) of the EC Treaty. For an analysis of the issue in respect of the harmonisation of private law as a whole, see Walter van Gerven, “Coherence of Community and national laws. Is there a legal basis for a European Civil Code?” In: European Review of Private Law, vol. 5, no. 4, 1997, pp. 465-470 [van Gerven, 1997.]
40 I decline from defining the competing concepts of the common market and the single market, formerly included in the EC Treaty, as this would lead beyond the actual scope of this study. For a discussion of the question, see Anthony Arnall, Alan Dashwood, Malcolm Ross, and Derrick Wyatt, European Union Law. London: Sweet & Maxwell, 2000, pp. 502-503.
41 As the decision-making procedure in this respect is defined by Article 294 TFEU. earlier Article 251 (189/B) of the EC Treaty.
internal market. In justifying its adoption, it is not sufficient to refer to the disparities between national rules and to the abstract risk of obstacles to the exercise of fundamental freedoms or of distortions of competition liable to result therefrom. Such risks would have to be verified on the basis of or at least reasonably inferred from actual market conditions, and Community action should be appropriate to eliminating them.\(^44\)

Though the ruling was not passed on a directive that is aimed at the approximation of contract law, it has far-reaching consequences in that respect, as well. The European Court provided an authentic piece of legal interpretation of Article 95 of the EC Treaty that will have to be taken into consideration by the Community, now Union legislature if it intends to regulate the internal market with recourse to it as a legal basis. The requirement of verifying the concrete trade-restricting effects resulting from the disparities of national laws will presumably stand in the way of the lofty notions of codification that wish to regulate - in obligatory legal sources - the whole field of contract law and civil law at Union level.\(^45\)

2. Consumer Contracts

By virtue of Article 153 (129/A) of the EC Treaty, now Article 169 TFEU legislation on the harmonisation of laws governing consumer contracts has been granted specific power. Accordingly, the Community contributes to the high level of consumer protection by of measures (laws) adopted pursuant to Article 95 (100/A) of the EC Treaty, now Article 114 TFEU in the context of the completion of the internal market.\(^46\) The Treaty of Amsterdam extended the article, as it were, affirming the competences of the Community.\(^47\)

3. Residual Power

Article 352 TFEU, formerly Article 308 (235) of the EC Treaty might again seem to confer a general legislative power, in so far as it lays down that if action by the Union should prove necessary within the framework of the policies defined in the Treaties, to attain one of the objectives set out in the Treaties, and the Treaties have not provided the necessary powers, the Council, acting unanimously on a proposal from the Commission and after obtaining the consent of the European Parliament, shall adopt the appropriate measures.

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\(^{44}\) See points 83-90 of the judgment.

\(^{45}\) But a few years earlier, Winfried Tilmann had conceived the possibility creating a European Civil Code on the basis of Article 95 of the EC Treaty. See his “The Legal Basis for a European Civil Code.” In: *European Review of Private Law*, vol. 5, no. 4, 1997, pp. 471-472.

\(^{46}\) Article 169 paragraph 1. TFEU, formerly Article 153 paragraph 3. (a) of EC Treaty.

\(^{47}\) For a detailed analysis of the amendments of the EC Treaty, see Jules Stuyck, op. cit., p. 380. In view of the conferrals of specific powers to legislate, Article 65 of the EC Treaty, now Article 81 TFEU could also be mentioned – but it has import in respect of the approximation of the civil proceedings, family law with cross-border implications and the private international law of the Member States, as well as the promotion of the cooperation between national courts. Though it might contribute to the regulation of certain areas of private law, it has little bearing on contract law.
Nevertheless, the Union legislature has to be aware of two serious limitations before adopting any act by recourse to Article 352 TFEU as its legal basis. One of them is the requirement of unanimity clearly stated in the text, which was quite difficult to achieve even between the fifteen Member States at the time. The other one is actually a substantive limitation imposed by Opinion 2/94 of the European Court. According to this, the former Article 308 (235) of the EC Treaty, predecessor of Article 352 TFEU could not be used as a basis for the adoption of a provision which would widen the scope of Community powers beyond the general framework created by the provisions of the Treaty as a whole and, in particular, by those that define the tasks and the activities of the Community. No measure of constitutional importance, i.e. one that would mean a significant widening of the scope of action of the Union, could therefore be adopted on the basis of a conferral of power under Article 352 TFEU; in other words, the powers conferred on integration cannot be increased in this way. Though the invocation of Article 352 TFEU is not without precedent in legislation touching on private law, in view of the above, it could hardly be relied on as a basis of, say, a comprehensive, obligatory regulation of contract law at Union level.

§ 4. The Means of Legal Harmonisation
1. International Treaties or Private Codification?

Like clarifying the competence to legislate, choosing the means of approximation of laws (or even legal unification) is equally important. Before discussing the possible legal sources of such an endeavour, it is worth noting that, irrespective of the EU legal system, the advantages and disadvantages of the compulsory and non-compulsory instruments of legal harmonisation have been disputed for centuries. The doubts of English scholars of law concerning international treaties are well known, some deeming these documents as unfortunate “multicultural compromises” which may even jeopardise legal security. Equally distrustful of the international codification of contract law as embodied in compulsory sources of law is Michael Joachim Bonell, who

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49 See especially point 30 of the Court opinion.
51 See van Gerven, 1997, p. 408. In October, 1999, the Tampere European Summit Conclusions urged legal approximation, “greater convergence in civil law”, and stated: “As regards substantive law, an overall study is requested on the need to approximate Member States’ legislation in civil matters in order to eliminate obstacles to the good functioning of civil proceedings. The Council should report back by 2001.” Point VII/39, Presidency Conclusions, Tampere European Council, 15-16 October.
52 See Ole Lando, op. cit., discussing the famous debate between Anton Friedrich Justus Thibaut and Friedrich Carl von Savigny.
53 Nicholas Barry, op. cit., who, by the bye, has some critical points to make on traditional English scepticism.
corroborates his stance also by criticising the Vienna Convention,\textsuperscript{54} bringing up the compromises, the provisions of vague content, legal loopholes that found their way into it, as well as the areas it left unjustifiably unregulated.\textsuperscript{55} Simultaneously, many emphasise the advantages of the non-compulsory instruments of legal approximation, pointing out that these, rather than finding the least common denominator, seek to create the best possible rules, and that they are capable of a more comprehensive regulation of an area, and are framed by experts not diplomats bound by their negotiation mandates.\textsuperscript{56} These advantages are manifest in such private codifications as the Principles of European Contract Law\textsuperscript{57} or the Principles of International Commercial Contracts prepared under the tutelage of UNIDROIT.\textsuperscript{58} Basil S Markensinis\textsuperscript{59} and Thijmen Koopmans\textsuperscript{60} have a similar opinion on the issue, and so does Hein Kötz\textsuperscript{61} to some extent.

However, other authors have called attention to the limited efficacy, especially in the systems of law of the European continent, of non-compulsory codifications drawing on the \textit{Restatements of the Law}, which summaries and rules of jurisprudence were developed on the law of the Unites States of America.\textsuperscript{62} As both Lando and Müller-Graff have argued, European national courts have to apply private-law codes and laws, and cannot deviate from them even for the sake of a private collection of rules elaborating the fundamental principles of contract law, however good it might be. The convincing power of such works is thus limited to a rather small area. Nevertheless, this non-compulsory effect should not be underrated. First, private codifications may find their way into arbitration procedures on international commercial transactions;\textsuperscript{63} second, they can – \textit{de lege ferenda} – exert significant influence on national legislation.

2. Regulations

\textsuperscript{56} Ibid, p. 516-517.
\textsuperscript{57} Ole Lando and Hugh Beale, op. cit.
\textsuperscript{60} Thijmen Koopmans, op. cit., pp. 541-547; he, however, mentions the disadvantages of non-compulsory sources of law, as well.
\textsuperscript{61} Hein Kötz, op. cit., p. 550, has doubts concerning the framing of a European Civil Code.
\textsuperscript{62} Ole Lando, op. cit., p. 534.
\textsuperscript{63} Müller-Graff, op. cit., p. 80.
In theory, as far as the compulsory sources of the EU law are concerned, both regulations and directives could be used for regulating certain areas of private law at European level. However, these two types of legal source are fundamentally different: a regulation is to be applied directly in all Member States; while a directive compels, as to the results to be achieved, the Member States it addresses to adopt national acts in accordance with its content. Thus, in order to implement the substance of a directive, a special piece of national legislation, transposing or adapting it, has to be adopted in individual Member States. The Member States also have the opportunity to enter into international conventions between one another. In recent decades, all these types of legal source have been applied. For instance, a regulation was adopted on the European Economic Interest Grouping (EEIG), and a convention was concluded on the law applicable to contractual obligations. In respect of substantive-law issues of contracts, directives are the dominant form of Community legislation.

3. Directives

Member States are bound by a directive addressing them; but they themselves determine the type of act with which they intend to achieve its objectives in their national legal systems. This is therefore a flexible means of legal harmonisation that can, in felicitous circumstances, ensure both the desirable level of approximation and the consideration of national characteristics. The delicate balance between legal approximation and the appreciation of national features, however, is particularly difficult to find in the area of private law based as it is on very precise, closely intertwined rules. A directive might easily be either exceedingly detailed not leaving any leeway for the legislators of the Member States or too loosely formulated allowing differences that might actually imperil the approximation objective itself.

The difficulties involved in legal approximation through directives are clearly demonstrated by the directives on consumer transactions. Numerous directives issued over several decades have resulted in piecemeal regulation. Whether in respect of the terminology they employ or the legal consequences they lay down, there are significant differences between them. This unending stream of piecemeal legislation may have grave consequences in the long run,

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64 Article 249 (189) of the EC Treaty. Now Article 288 TFEU.
65 Regulation 2137/85/EEC.
67 For an account of the most important directives on contract law, see Hans Schulte-Nölke, Christian Twigg-Flesner, Martin Ebers (eds.) op.cit and Király, 2000.
69 Lajos Vékás has called this called this a “pointilist” method, see Vékás, 2000.
70 Carla Joustra, op. cit., 139-142.
demolishing the delicately balanced structure of national contract laws. Not that a directive or two may not have a beneficial effect on legal development; the point is that the lack of systematisation in a given area of supranational regulation is bound to lead to contradictions in the laws of the Member States. Any such occurrence would be adverse particularly in private law, where the claim to consistency goes back to as far as the glossators. Hungarian commentators on law have also called attention to the dangers of system disruption, pointing out that un-co-ordinated European legislation can jeopardise the unity of civil law.

The efficiency of approximation is also impaired by the fact that directives sometimes do not regulate essential matters, but refer to the laws of the Member States, and that the minimal harmonisation provided by all directives on consumer protection encourages diversity in national legislation. Naturally, just like international treaties, directives attempt to find a balance between the different legal traditions and arrangements of the Member States, and this compromise-seeking attitude might explain the loopholes in the legislation that have no professional justification.

§ 5. The Transposition of Directives into National Laws

1. Characteristic Difficulties

In order to achieve the aims formulated in a directive, it must be appropriately transposed, i.e. enacted in national legislation. In this respect, belated transposition or implementation, partial or inappropriate adaptation may lead to problems. The difficulties are clearly demonstrated by the example of Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts. Five Member States: Denmark, the United Kingdom, Luxembourg, Portugal, and Spain, adapted it only after several years’ delay. What is more, the directive was implemented only partially by several Member States. The laws of several Member States, notably France, Greece, the Netherlands, and

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72 Daniela Caruso, op. cit., p. 45.
76 It took four years for Spain to legislate. Such a delay is not at all exceptional. To bring up an example from another area of contract law: for over a decade, France failed to pass the required legislation on Directive 85/374/EEC on product liability. See Daniela Caruso, op. cit., pp. 22-23. True, it finally solved the problem at very high standard according the literature. See also Lajos Vékás, “Az új Polgári Törvénykönyv néhány elméleti és rendszertani előkéréséről” [On some of the Preliminary Theoretical and Taxonomical Questions of the New Civil Code]. In: Magyar Jog, 2006, no. 7, p. 390, where he refers to the French law in question: Loi no. 98-389 of 19 May, 1998.
Germany, diverged from the requirements of the directive even in the spring of 2000, i.e. five years after the deadline for transposition had expired.\(^{77}\) This was but little mitigated by the promise the European Commission drew from the countries concerned that they would redress their shortcomings in implementation.\(^{78}\) The ability to wrest this pledge from them was presumably linked with a possible action the Commission might bring against Member States for breaching Community law under Article 226 (169) of the EC Treaty.\(^{79}\)

Making use of the liberty directives provide, the Member States follow different models of transposition. Some adopt a special act on each directive touching on contract law, while others revise existing laws, and finally some go as far as to amend their civil codes, which is, of course, the most exacting and laborious course to take.\(^{80}\) It is a quite challenging task for the European Commission to assess the appropriate quality of the implementation of a directive when the great national codes in particular need amendment, as it is the result of scores of provisions in such codes that have to be found and reconsidered, and even the relevant jurisprudence of the national courts have to be taken into account.

2. Requests for Preliminary Rulings

In view of a unified interpretation of directives and, indirectly, the national laws implementing them, the national courts faced with problems of Community law may have recourse to seek a preliminary ruling by the European Court of Justice under Article 234 (177) of the EC Treaty.\(^{81}\) The most important pre-condition of the efficiency of this means of interpretation is that the courts of the Member States do make use of it, entering into dialogue, so to speak, with the European Court. However, the closer we reach to the hard core of contract law, the less national courts seem to be inclined to request the judgment of the European Court, not deeming the settlement of a given private-law issue to be part of Union law. This was obviously the case with regard to Directive 93/13/EEC on unfair terms in consumer contracts, when the Commission report on its implementation stated: “Indeed the doctrine reveals the reluctance of national courts to refer cases to the Court of Justice in this legal field,”\(^{82}\) which was a fair assessment as the Court had made a preliminary ruling on one case only until the year 2000.\(^{83}\)

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\(^{77}\) 31 December, 1994.
\(^{78}\) The Commission Report, p. 5-8.
\(^{79}\) Now Article 259 TFEU. See e.g. the ruling condemning Spain failing to transpose fully Directive 93/13/EEC: Case C-70/03, Commission of the European Communities v. Kingdom of Spain, *ECR* (2004), I-7999.
\(^{80}\) See Lajos Vékás, 2000, p. 646.
\(^{81}\) Essentially the same procedure is guaranteed by Article 267 TFEU: The Court of Justice may give preliminary rulings concerning: (a) the interpretation of the Treaties; (b) the validity and interpretation of acts of the institutions, bodies, offices or agencies of the Union.
\(^{82}\) The Commission Report, p. 35.
\(^{83}\) Joined cases C-240/98 and 244/98, Océano Grupo Editorial SA and Salvat Editores SA v. Rocío Murciano Quintero and Others, *ECR* (2000), p.1-4941. Since then, further judgments have been made, see e.g.: case C-237/02, Freiburger Kommunalbauten GmbH Baugesellschaft & Co. KG v. Ludger Hofstetter et Ulrike
For a while, the rejecting mindset was rather terse in the jurisprudence of German courts, which have otherwise seldom hesitated in requesting a decision by the European Court. The Bundesgerichtshof categorically denied taking into account the provisions of the Directive when applying the AGB-Gesetz,\(^4\) i.e., to be more precise, to invoke the Community act for the interpretation of the German law implementing it.\(^5\)

It does indeed make a difference how long the European Court takes to make its ruling establishing a uniform interpretation, in so far as national courts request such guidance. Experience shows that the “three-year rule” applies in this field: a minimum of three years is needed for a case to go through the proceedings of a national court or courts to that of European Court from the time of the adoption of a piece of Union legislation.\(^6\)

3. Direct Effect

To a certain extent, the failure to implement directives for approximating contract laws or their delay can be counterbalanced by the legal principles elaborated in the jurisprudence of the European Court. In theory, three such doctrines apply in this respect, namely: direct effect, directive-conform interpretation or indirect effect and the liability for damages of Member States.

If the European Court of Justice establishes the direct effect of a Community rule, private persons may invoke it before the courts of the Member States. If it has vertical direct effect, it can be invoked against the Member State concerned; if it has horizontal direct effect it can be referred to in an action against a private person. Direct effect applies to a directive if it was not implemented or not implemented appropriately within the given deadline, and if it includes provisions precise and clear enough, not conditional on other factors, for courts to base their judgments on. This is what the English language literature on law calls justiciability.

Several advocates-general assisting the European Court of Justice argued for horizontal direct effect of directives between private persons, referring to the protection of the legitimate expectations of citizens and their equality before the law, which cannot be dependent on whether a Member State transposes the directive concerned in time. The Court, however, has to date, upheld its traditional position, stating that the requirement of legal security does not permit

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\(^4\) Gesetz zur Regelung des Rechts der Allgemeinen Geschäftsbedingungen, the German Standard Terms and Conditions Act.


\(^6\) Irene Klauer, op. cit., p. 37.
this. In other words, consistently with its jurisprudence, it has refused to give horizontal direct effect to any directive. In all probability, it was motivated not only by the argument of legal certainty in these rulings; it had reason to fear that some of the courts of the Member States, such as the German constitutional court, would not allow the extension of the principle of direct effect. This is exactly why some commentators have suggested that the rejection of horizontal direct effect can be interpreted as a cautious attempt by the European Court of Justice to protect the relative autonomy of private-law legislators, preventing the direct intervention of Union law in this area. It is thus a rather peculiar development that the Supreme Court of Spain, in spite of the rejection by the European Court of Justice, endorsed the horizontal direct effect of a directive – the one on unfair terms in consumer contracts –, and based its judgment on it. Earlier on, Italian tribunals had attempted to recognise the horizontal direct effect of the Directive, but the Supreme Court of Cassation declared their rulings void.

4. Indirect Effect

The rejection of the direct horizontal direct effect of the directives regulating private-law matters seems to be a particularly austere decision because, due to the very structure of civil law, these directives are unlikely to be invoked, i.e. their horizontal direct effect will hardly be asserted, against Member States in litigation. As a result, there is a danger that if the directives mentioned are not implemented in the Member State, their provisions will not be applied in proceedings before the courts of the Member States, and so they will become, so to speak, “second-class” directives.

To mitigate the austerity of its decision to reject the principle, the European Court of Justice, in several rulings, affirmed the so-called directive-conform interpretation and the liability for damages of Member States. Directive-conform interpretation or indirect effect means that a national court, when applying national law, must interpret that law, “as far as possible, in the light of the wording and the purpose of the directive so as to achieve the result it
has in view.94 The limited efficiency of the principle of directive-conform interpretation is evidenced by the phrase “as far as possible”, which discharges the courts from having to rule contra legem, i.e. to ensure the enforcement of Union rules through interpretations obviously contrary to national law.95 The principle, as a “clever judicial strategy”,96 is not particularly popular. On the one hand, it can lead to uncertainty, because, after all, it is an un-implemented directive that results in success or failure in a lawsuit: an attempt is made to interpret national law in accordance with the directive. It therefore runs similar risks to direct horizontal effect, only softened by the exclusion of contra legem interpretation. In turn, however, this limitation has its own side effects: the enforcement of the directive depends on the condition of national law; in other words, on the extent to which laws and private-law codes can be distorted or expanded according to the provisions of the directive concerned. As concrete cases have demonstrated, there are Member States where, lacking a formal transposition of a directive, national law cannot be interpreted in the light of its provisions, though others have no such problems. Nevertheless, we have come back to square one: the harmonisation objective of a directive stumbling on the diversity of the laws of the Member States.97

5. The Liability for Damages of the Member States

Should the purpose of a directive not be attainable through the mode of interpretation outlined above, the liability for damages of a Member State may arise.98 The Treaty on the Functioning of the European Union can of course be the basis of judging the Member States for breaching EU law on the initiative of the Commission or another Member State, and today even a penalty payment may be imposed on them.99 According to the recent jurisprudence of the European Court, however, the Member States are obliged to make good the damage caused to individuals by their failure to transpose a directive, provided that three conditions are met, namely: (i) the result prescribed by the directive must entail the grant of rights to individuals; (ii) the content of those rights must be identifiable on the basis of the provisions of the directive; and (iii) there must be a causal link between the breach of the State’s obligation and the damage suffered. However, determining the actual damage the consumer suffered due to

95 Irene Klauer, op. cit., 51-52.
97 See case C-91/92
98 See Articles 226-228 of the EC Treaty, now Articles 258-260 TFEU . However, due to conflict with EU private law, such a procedure can seldom occur, as it would imply that the European Commission has a full knowledge of the very details of the private law of the Member States. Moreover, it is often impossible to establish that a directive has not been appropriately transposed from the mere comparison of its original and transposed text; their divergences often become apparent only before the courts. See Irene Klauer, op. cit., p. 73.
99 See for this the joined cases C-6/90 and C-9/90, Frankovich and Others v. Italy, ECR (1991), p. I -5357; according to certain observers, this was “the ruling of the century”, in which the Court first adumbrated its famous thesis.
the failure to transpose a directive remains a separate and sometimes difficult issue.100

On the topic of ascertaining the underlying liability of the Member States, a critical remark seems justified. The liability for damages of the states is no more than a supplementary means, a sort of “Notbehelf.”101 Recourse to it is conditional on having instituted a civil proceeding beforehand. In so far as a citizen of the Union is unsuccessful in invoking the protection of a directive – because, for instance, the directive relevant to the dispute has no direct horizontal effect, or the acknowledgment of its direct effect does not redress the damage the private person suffered, or again the interpretative principle of indirect effect does not contribute to a Union-conform interpretation of national law – he may seek compensation from the Member State for his rights that have become latent due to its failure. This is an extraordinarily long and expensive mode of making claims good, all the more so because a second procedure might give reason to seek a preliminary ruling by the European Court. There are therefore a number of ways of substituting the regular transposition of directives and mitigating damages suffered as a result of delayed implementation; however, their applicability is limited, and has its side effects.

§ 6. The Limits of Legal Harmonisation
1. From Legal Bases to Preliminary Ruling

Union legislature may have to face difficulties which have accumulated in the course of harmonising contract laws. Any effort at legal harmonisation has to grapple with such complications; but some of these issues stem from EU law particularly. It is perhaps opportune to mention some of them again, illustrating the obstacles to harmonisation which arise at various stages of its implementation by means of a fictitious example.

The European Commission drafts a proposal for a directive on the harmonisation of certain area of contract law. The initiative sparks heated debate with the Member States, members of the European Parliament, stakeholders and scholars of law divided over the need for this harmonisation.

(i) The proposal due to the limited scope of provisions (legal grounds) granted for Community legislation covers a smaller area than the context of the private-law matters at hand would otherwise require.

(ii) In order to strike a deal between the Member States, the directive stipulates alternative rules, and refers back to the laws of the Member States, thereby accomplishing only a relative degree of harmonisation.

(iii) After several years of drafting, the directive is transposed by a number of Member States with considerable delay, while others pass faulty legislation implementing it. Further, the European Court refuses to acknowledge its direct horizontal effect, i.e. its applicability between private persons before

100 Irene Klauer, op. cit., p. 57.
101 Ibid., p. 56.
national courts. On top of this, the laws of Member States allow different
degrees of room for manoeuvre for the directive-conform interpretation, or the
courts take different positions on the issue.

(iv) The transposition of the directive varies, too: some legislatures pass a
special act while others amend their existing codes at the price of significant
differences and contradictions.

(v) As a result of such factors as the differences between court rules and
civil procedure, and the assertion of rights under the directive before the courts
of the Member States, the duration and costs of lawsuits are quite different
between the Member States.

(vi) Finally, the courts of some of Member States are reluctant to request
preliminary rulings from the European Court, and thus it has little chance of
shaping a single interpretation of the directive.

In its communications, the European Commission has often taken into
account the difficulties of harmonisation, especially the consequences of
piecemeal and transaction-specific regulation. It has observed that there are
unjustified divergences between current European directives on contract law,
which may treat similar life situations differently, and stipulate varying
requirements. For instance, in the case of consumer transactions they prescribe
divergent durations and methods of calculation of withdrawal – withdrawal
which is characteristically provided for consumers. As an unwanted side effect,
several EU acts may be applicable to the same situation, or their national
transpositions may have diverge in their content. Two different legislative
approaches may feature in a single directive. Directives often use abstract legal
terms, but they might not define them, or give them an overly broad definition.
Certain terms are defined in some directives, while they are not defined in
others, raising the interpretation issue of whether a definition in one directive
can be exported to another. Apart from this, a situation might easily occur when
the terms used by EU acts are simply alien to one legal system or another.102

2. Seeking Proportion and Restraint

At this point, questions inevitably arise: Has the harmonisation of a given
area of contract law actually been attained? Does the result justify the vast
amount of money and time expended on it? Naturally, not all attempts at
harmonisation lead to such a magnitude and accumulation of problems.
Nevertheless, the difficulties outlined are genuine and typical, so much so that
they render the establishment of a comprehensive, monolithic European regime
of contract law unreal and unreasonable. It would therefore be only justified for
the European Union to seek proportion and exercise restraint, in other words, to
take full account of the principle of subsidiarity, in any future harmonisation
touching on contract law. Such a realistic approach has been given increasing

emphasis in the legal literature. Thus, the third edition of the collection of now classic studies on private-law harmonisation, *Towards a European Civil Code*,\(^{103}\) has afforded much more attention than it had done to the cultural differences that limit the possibilities of legal harmonisation. One eminent contributor to the volume, Brigitta Lurger, pointed out the lack of mapping of the social background of contract law,\(^{104}\) while Vincenzo Zeno-Zencovich and Noah Vardi foresee immense difficulties in any future adoption of a European contract-law codex.\(^{105}\) Not to mention the long-time critic of private-law unification, Pierre Legrand, who point-blank calls the proposal for a European Civil Code “a diabolical idea,” a boorish assault on the diversity of the laws of the Member States.\(^{106}\)

§ 7. The Proposals of the European Commission

1. The First Communication

In its 2001 communication, the European Commission outlined four possible scenarios on the role of the Community.\(^{107}\) (i) The Community does not take any action in this field, trusting that the entwining markets, the initiatives of the commercial organisations and the Member States will establish the required harmony between European contract laws. (ii) The second possibility is that the Commission—in conjunction with scholars of comparative law, legal theorists and practitioners—promotes the development of non-binding common principles of contract laws, which could lead to the eventual approximation of the contract laws of the Member States in so far as these principles are accepted in commercial practice and their voluntary application becomes wide-spread. In line with this kind of development, standard contracts modelled for cross-border transactions would be compiled. (iii) The review and improvement of existing legislation in view of its revealed shortcomings. (iv) Finally, it is conceivable that the Community would undertake to regulate contract law comprehensively through regulations, directives or recommendations. The aim of the communication was primarily to foster widespread discussion of the issues surrounding the future of European contract law for stakeholders, academic workshops, legal practitioners, governments and the Commission itself.

2. Common Frame of Reference

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The results of the ensuing debates were first published in 2003, and were summed up, in a largely congenial way, by the Commission in 2004. According to the 2003 summary, only a fragment of the opinions delivered to the Commission believed that reliance on the market was enough. Significantly more respondents supported the elaboration of the common principles of contract law, but the greatest majority deemed that the way forward was the review and improvement of existing acts. This also meant that the majority rejected the idea of Community legislation on the harmonisation of European contract laws, at least in the situation prevailing at the time. In the light of this, the Commission declared in its 2004 communication that it is not “the Commission’s intention to propose a ‘European civil code’ which would harmonise contract laws of Member States.” Instead, it would support, in order to improve the coherence of existing and future acquis, the development of a Common Frame of Reference (CFR), and foresaw its adoption in 2009, following thorough preparatory work. The CFR would set out common fundamental principles of contract law, including guidance on exceptions, such as contractual freedom and the application of mandatory rules. The fundamental principles would be followed by the definition of terms ranging from contract to damages. Chapter three of the CFR would include model rules for the various contractual periods, from conclusion to performance and non-performance, and it would have specific rules for both contracts of sales and insurance. This part would treat the issues of concessions and forfeiture.

According to the Commission, the CFR could fulfil a number of different roles. First and foremost, by laying down the fundamental principles of contract law, clarifying legal terms and even providing model rules, it could provide guidance on the review of EU rules, for instance, the directives on consumer transactions. It could also afford a clear theoretical basis for the future adoption of EU acts. Further, the CFR could be used by the legislators of the Member States and courts of arbitration. Though emphatically a non-binding instrument, the CFR would bear some features of codification. In so doing, as

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Martijn W. Hesselink has pointed out, it could establish a comprehensive, systematic, long-term – as yet soft-law – order of rules, which could generate tensions between the levels of legislation of the Member State and the Union. Such new strains could occur not between the various elements of piecemeal regulation in the directives concerned, but between the comprehensive European “codex” and the traditional codes of the Member States.\textsuperscript{111}

Beyond the above, the European Commission deems the development of Standard Terms and Conditions (STC) desirable,\textsuperscript{112} the content of which is for market participants to determine while the decision whether to use it is also one for economic operators. The Commission only intends to act as a facilitator and an “honest broker”, i.e. bringing interested parties together without interfering with the substance. Furthermore, it did not exclude the possibility of contributing in the long run to the adoption of an optional instrument in European contract law\textsuperscript{113} and the development of its fundamental principles, if there is demand for it beyond sector-specific Community directives, the Common Frame of Reference and the Standard Terms and Conditions. At the current stage of thinking on the issue, it seems obvious that this would be no more than a collection of opt-in rules, i.e. these rules would only be applicable if the parties opted for them to govern their contractual relationship.\textsuperscript{114} As yet, it is still an open question which articles of the funding Treaties would provide legal grounds for adopting such a document, and what the relationship would be between the fundamental principles of European contract law and the planned Common Frame of Reference.

In conclusion, the Commission exercised considerable self-restraint in drafting its proposals and setting its time schedule for the tasks involved. As attested to by the 2004 communication, this cautiousness can perhaps be attributed to its recognition of “the need to respect different legal and administrative cultures in the Member States” and “the range of different legal traditions in the European Union.”\textsuperscript{115} This cautious approach to the harmonisation of contract law was confirmed by the Stockholm Programme\textsuperscript{116} of the European Union for 2010-2014 which invited the Commission to submit a proposal on the CFR. According to this programme the CFR should be a non-binding set of fundamental principles, definitions and model rules to be used by


\textsuperscript{112} Points 2.2 of Communication 2004/0651.

\textsuperscript{113} Points 2.3 ibid.

\textsuperscript{114} Annex II ibid.

\textsuperscript{115} Points 2.3 and 3.1.2 ibid. We therefore fully agree with the conclusion that the new Member States of European Union “must carry out the comprehensive reform and codification of their private laws within the framework of their national legal systems.” See Vékás, 2006, p. 386.

lawmakers at Union level to ensure greater coherence and quality in the lawmaking process.\textsuperscript{117}

\textsuperscript{117} The European Commission set up the Expert Group on Common Frame of Reference in the area of European contract law by its decision of 26 April 2010. \textit{OJ L 105}, 27.4.2010, pp. 109–111. This expert group has the mandate to assist the Commission in preparing a proposal for a Common Frame of Reference in the area of European contract law, using the Draft Common Frame of reference as a starting point.