

Policy Department C  
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**THE LEGAL BASIS FOR AN OPTIONAL INSTRUMENT  
OF EUROPEAN CONTRACT LAW**

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**Directorate-General Internal Policies**  
**Policy Department C**  
**Citizens Rights and Constitutional Affairs**

## **THE LEGAL BASIS FOR AN OPTIONAL INSTRUMENT OF EUROPEAN CONTRACT LAW**

### **SHORT STUDY**

#### Summary:

In its Action Plan on European contract law of 2003, the European Commission announced that it would examine whether problems in the European contract law area may require non-sector-specific solutions such as an optional instrument. The present study discusses the existence of a legal basis for such an optional instrument. The European Community only has the power to take any measures, including an optional instrument relating to contract law, insofar as a power is attributed to it by the founding Treaties. The EC Treaty does not provide a specific competence to create private law instruments nor does it provide any general competence to harmonize private law. Therefore, recourse is sought to the functional competences laid down in the Treaty. The potentially relevant competences include the ones following from Articles 61-67, 94, 95, and 308 of the EC Treaty.

Considering the relevant EC Treaty provisions and ECJ case law concerning legal bases, the study suggests that Article 308 EC seems to be the most likely provision to provide a legal base for enacting one or more optional instruments concerning European contract law. However, even Article 308 EC cannot serve as a legal basis for enacting the entire CFR; any optional instrument will have to be limited to rules on the subjects that are particularly relevant to the internal market.

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# **The legal basis for an optional instrument on European contract law**

Short study for the European Parliament

on the different options for a future instrument on a Common Frame of  
Reference (CFR) in EU contract law, in particular the legal form and the legal  
basis for any future optional instrument

in accordance with

Addendum to specific contract No IP/C/JURI/FWC-SC/2006-211/LOT3/C1/SC1

implementing Framework Service Contract No IP/C/JURI/FWC/2006-211/LOT3/C1

*Final Report – 8 February 2008*

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## Table of Contents

|  |        |
|--|--------|
| Executive summary .....  | - 4 -  |
| 1. Introduction .....  | - 6 -  |
| 2. The idea of an optional instrument .....                        | - 7 -  |
| 2.1. General .....   | - 7 -  |
| 2.2. Objective .....   | - 8 -  |
| 2.3. Binding nature: opt-in or opt-out.....                        | - 8 -  |
| 2.4. Mandatory and non-mandatory rules .....                       | - 10 - |
| 2.4.1. Freedom of contract.....                                    | - 10 - |
| 2.4.2. The revision of the consumer acquis .....                   | - 10 - |
| 2.4.3. Rome I .....  | - 12 - |
| 2.5. B2B and B2C contract.....                                     | - 14 - |
| 2.6. Cross-border and purely internal contracts .....              | - 15 - |
| 2.7. Content .....   | - 15 - |
| 2.7.1. Relation to the CFR .....                                   | - 15 - |
| 2.7.2. Relation to CISG .....                                      | - 16 - |
| 2.8. One or more optional instruments? .....                       | - 16 - |
| 2.9. Legal form: regulation, directive or recommendation? .....    | - 17 - |
| 2.10. Legal basis .....  | - 18 - |
| 3. The reactions from the other Institutions .....                 | - 18 - |
| 3.1. The Council of the European Union .....                       | - 18 - |
| 3.2. The European Parliament .....                                 | - 19 - |
| 4. Articles 65 EC: the area of freedom, security and justice ..... | - 21 - |
| 4.1. General .....   | - 21 - |
| 4.2. Legislative procedure .....                                   | - 21 - |
| 4.3. Types of measures.....  | - 22 - |
| 4.4. Subject matter .....  | - 22 - |
| 4.5. Conclusion .....  | - 23 - |
| 5. Articles 94 and 95 EC: the approximation of laws .....          | - 23 - |
| 5.1. General .....   | - 23 - |
| 5.2. Legislative procedure .....                                   | - 24 - |
| 5.3. Types of measures.....  | - 24 - |
| 5.3.1. Directives and Regulations .....                            | - 24 - |
| 5.3.2. Approximation measures .....                                | - 25 - |
| 5.4. Subject matter .....  | - 27 - |
| 5.4.1. Improving the conditions for the Internal market .....      | - 27 - |
| 5.4.2. Obstacle to trade.....                                      | - 28 - |
| 5.4.3. Other obstacles.....  | - 29 - |
| 5.5. The CFR as an optional instrument under 95 EC.....            | - 30 - |
| 5.5.1. B2B and B2C contract .....                                  | - 30 - |
| 5.5.2. Cross-border and purely internal contracts .....            | - 30 - |
| 5.5.3. Property law excluded? (Article 295 EC).....                | - 30 - |
| 5.6. Article 94 .....  | - 31 - |
| 5.6.1. Legislative procedure .....                                 | - 31 - |
| 5.6.2. Types of measures .....                                     | - 31 - |
| 5.6.3. Subject matter .....  | - 31 - |
| 5.6.4. Conclusion .....  | - 31 - |
|  | - 2 -  |

|   |        |
|---|--------|
| 5.7. Conclusions.....   | - 31 - |
| 6. Article 308 EC: the catch-all provision.....                     | - 32 - |
| 6.1. General .....  | - 32 - |
| 6.2. Legislative procedure .....                                    | - 33 - |
| 6.3. Types of measures.....   | - 33 - |
| 6.4. Subject matter .....   | - 33 - |
| 6.4.1. General .....  | - 33 - |
| 6.4.2. The CFR as an optional instrument under Article 308 EC ..... | - 34 - |
| 6.5. Conclusions.....   | - 35 - |
| 7. The CFR as an interinstitutional agreement.....                  | - 35 - |
| 7.1. General .....  | - 35 - |
| 7.2. Permissibility .....   | - 36 - |
| 7.3. Legally binding? .....   | - 36 - |
| 7.4. Horizontal effect? .....                                       | - 36 - |
| 8. Conclusions.....   | - 37 - |
| Official documents from the institutions.....                       | - 39 - |
| Cases from the European Court of Justice.....                       | - 41 - |
| Bibliography.....   | - 42 - |

## Executive summary

### *Introduction*

In its Action Plan on European contract law of 2003, the European Commission announced that it would examine whether problems in the European contract law area may require non-sector-specific solutions such as an optional instrument. Private parties would be able to select this instrument to govern their transactions, either in cases when the parties make a choice for its applicability (opt-in) or in all cases except when they exclude its applicability (opt-out). The present report discusses the existence of a legal basis for such an optional instrument.

It follows from the communications from the Commission and from the resolutions from the Council of the European Union and from the European Parliament that the binding nature, scope and content of an optional instrument are still rather unclear. As a consequence, any conclusions with regard to the legal basis of such an instrument can only be tentative.

The European Community only has the power to take any measures, including an optional instrument relating to contract law, insofar as a power is attributed to it by the founding Treaties, in particular the EC Treaty (Article 5 I EC). The EC Treaty does not provide for a specific competence to create private law instruments, as for instance an optional instrument, nor does it provide any general competence to harmonize private law. Therefore, recourse must be sought to the functional competences laid down in the Treaty. The potentially relevant competences include the ones following from Articles 65, 94-95, and 308 EC. These functional competences differ, inter alia, with regard to the legislative procedures that must be followed and the institutions that would be involved, the types of measures that could be adopted, and the subject matters that could be dealt with.

### *Article 65*

It seems implausible that an optional instrument containing (almost) exclusively rules of substantive private law could be regarded as a harmonizing instrument concerning conflict of laws. Consequently, it is very unlikely that Article 65 can provide a proper legal base for enacting an optional instrument.

### *Articles 94 and 95*

It is not clear that an optional instrument, especially a mere opt-in instrument which is limited to cross-border contracts, would amount to a measure for the approximation of the laws of the Member States, as required by Article 94 and 95 EC. Moreover, many of the subjects contained in the forthcoming draft CFR would almost certainly not pass the *Tobacco* test because they are not directly relevant to the internal market. Finally, Article 94 EC is an unattractive legal base for an optional instrument, since only directives can be adopted on the basis of this provision while a directive is not a suitable legal form for an optional instrument. Moreover, Article 94 EC requires unanimity in the Council.



### *Article 308*

It seems likely that Article 308 EC could provide a legal basis for adopting one or more optional instruments on subjects of contract law that are particularly relevant for the operation of the internal market. Several other private law instruments, such as the *Societas Europaea*, the European Cooperative Society, the Community Trade Mark, were adopted on the basis of this Article. The drawbacks of this legal basis are that unanimity in the Council is required and (from a democratic perspective) that the Parliament has no right of co-decision; it only has to be consulted.

### *Interinstitutional agreement*

It is not certain that an interinstitutional agreement on a CFR could be legally binding on the European Institutions. However, the question is largely a theoretical one since the Council has explicitly stated that the CFR will be a non-binding instrument.

### *General conclusion*

Considering the relevant EC Treaty provisions and ECJ case law concerning legal bases, the description of an optional instrument by the European Commission in its Action Plan and its follow-up communications on European contract law, and the private law measures already in place, Article 308 EC seems to be the most likely provision to provide a legal base for enacting one or more optional instruments concerning European contract law. Art 95 EC seems to be excluded since an optional instrument would not be an instrument for the harmonisation of the laws of the Member States. From the perspective of a legal basis it would not make a difference whether the optional instruments would be applicable to B2B or B2C contracts or both, nor whether they would apply only to cross-border contracts or also to purely internal contracts. However, even Article 308 EC cannot serve as a legal basis for enacting the entire CFR; any optional instrument will have to be limited to rules on the subjects that are particularly relevant to the internal market.

## 1. Introduction

In its Action Plan on European contract law of 2003, the European Commission announced that it would examine whether problems in the European contract law area may require non-sector-specific solutions such as an optional instrument. Private parties would be able to select this instrument to govern their transactions, either in cases when the parties make a choice for its applicability (opt-in) or in all cases except when they exclude its applicability (opt-out). Presumably, such an instrument would co-exist with the national legal systems, at least to some extent. Moreover, the presumption is that an optional instrument would not require harmonization of national legal systems or only with respect to minor issues. The present report discusses the existence of a legal basis for such an optional instrument.

The European Community only has the power to take any measures, including an optional instrument relating to contract law, insofar as a power is attributed to it by the founding Treaties, in particular the EC Treaty (Article 5 I EC). The EC Treaty does not provide a specific competence to create private law instruments, as for instance an optional instrument, nor does it provide any general competence to harmonize private law. Therefore, recourse must be sought to the functional competences laid down in the Treaty. The potentially relevant competences include the ones following from Articles 61-67, 94, 95, and 308 EC. These functional competences differ, inter alia, with regard to: (i) the legislative procedures that must be followed and the Institutions that would be involved; (ii) the types of measures that could be adopted; and (iv) the subject matters that could be dealt with.

After a presentation of the idea of an optional instrument, as proposed by the European Commission (Section 2), and of the reactions from the other institutions, in particular the Council of the European Union and the European Parliament (Section 3), this study discusses in detail whether a proper legal basis for the enactment by the European Union of one or more optional instruments on contract law provisions, can be found in Articles 61-67 EC, concerning the area of freedom, security and justice (Section 4), Articles 94-95 EC, concerning the approximation of laws (Section 5), or Article 308 EC, the catch-all provision (Section 6). Subsequently, the question will be discussed whether the Common Frame of Reference can be the object of a valid interinstitutional agreement (Section 7). Finally, this report will draw some conclusions (Section 8).

## 2. The idea of an optional instrument

### 2.1. General

The European Commission introduced the idea of an optional instrument in its first communication on *European contract law* in 2001.<sup>1</sup> Thereafter, in its *Action Plan* of 2003 the Commission announced that it would produce a Common Frame of Reference (CFR), one of the objectives of which would be to form the basis for further reflection on an optional instrument in the area of European contract law. It further announced that a reflection on an optional instrument would be carried out in parallel to the CFR process and that the results of the Commission's examination could only be expected some time after the finalisation of the CFR.<sup>2</sup> In its following Communication *The Way Forward* in 2004, the Commission announced that it would continue its consultation as to the opportuneness of an optional instrument.<sup>3</sup> It underlined that it is not the Commission's intention 'to propose a "European civil code"'.<sup>4</sup> In that communication the Commission also presented a number of parameters for the reflections on the need for an optional instrument. These include:<sup>5</sup> the need to take into account differences between business to business (B2B) and business to consumer (B2C) contracts; the degree to which other solutions (e.g. EU wide standard terms) already offer satisfactory solutions; and the need to respect different legal cultures in the Member States. These parameters were further explained in an Annex to the Communication.<sup>6</sup> In its First Annual Progress Report on European Contract Law and the Acquis Review (2005) the Commission mentioned that it has introduced the idea of an optional instrument in European contract law ('26<sup>th</sup> regime') in the discussion concerning financial services and those on mortgage contracts. The Second Progress Report on the Common Frame of Reference (2007) does not mention an optional instrument.<sup>7</sup>

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<sup>1</sup> Communication from the Commission, European Contract Law, Brussels, 11.07.2001, COM(2001) 398 (hereafter: *Communication* 2001).

<sup>2</sup> Communication from the Commission, A more Coherent European Contract Law, an *Action Plan*, Brussels, 12.2.2003, COM(2003) 68 (hereafter: *Action Plan*), 54.

<sup>3</sup> Communication from the Commission, European Contract Law and the revision of the *acquis*: the way forward, Brussels, 11.10.2003, COM(2004) 651 (hereafter: *The Way Forward*), 4.

<sup>4</sup> *The Way Forward*, n 3 above, 8.

<sup>5</sup> *Ibid.*

<sup>6</sup> *Ibid.*, Annex II.

<sup>7</sup> Report from the Commission, Second Progress Report on the Common Frame of Reference, Brussels 25.7.2007, COM (2007) 447.

## 2.2. *Objective*

In the Action Plan, the Commission seems to regard the facilitation of cross-border contracting in the internal market as the main objective of an optional instrument. The Commission says in this regard:<sup>8</sup>

'Some arguments have been made in favour of an optional instrument, which would provide parties to a contract with a modern body of rules particularly adapted to cross-border contracts in the internal market. Consequently, parties would not need to cover every detail in contracts specifically drafted or negotiated for this purpose, but could simply refer to this instrument as the applicable law. It would provide both parties, the economically stronger and weaker, with an acceptable and adequate solution without insisting on the necessity to apply one party's national law, thereby also facilitating negotiations. Over time economic operators would become familiar with these rules in the same way they may be familiar with their national contract laws existing at this moment. This would be important for all parties to a contract, including in particular SMEs and consumers, and in facilitating their active participation in the internal market. Thus such an instrument would facilitate considerably the cross-border exchange of goods and services.'

Thus, in the Commission's view, two features of an optional instrument stand out as factors that might make it capable of contributing to a smoother functioning internal market. Such an instrument would provide: (i) a non-national legal regime specifically adapted to cross-border transactions and (ii) an acceptable and adequate solution for economically stronger and weaker parties. This double neutrality would render the instrument attractive for all parties to cross-border contracts, especially SMEs and consumers. It would facilitate their participation in the internal market.

## 2.3. *Binding nature: opt-in or opt-out*

In its Communication of 2001, when discussing the binding nature of any measures of comprehensive legislation at EC level (option IV) to be proposed, the Commission mentioned as possible alternatives:<sup>9</sup>

'a) A purely optional model which has to be chosen by the parties. An example would be a Recommendation or a Regulation which applied when the parties agree that their contract was to be governed by it.

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<sup>8</sup> *Action Plan*, n 2 above, 90-91. See also *The Way Forward*, n 3 above, Annex II: 'it is important to remember the main goal of the optional instrument, namely the smoother functioning of the internal market.'

<sup>9</sup> As a third model the Commission mentioned '(c) A set of rules whose application cannot be excluded by the contract.' However, this third model is not optional and therefore is not relevant in the present context.

b) A set of rules which would apply unless their application were excluded within the contract. This kind of legislation already exists in the context of the late payments directive or in the CISG. '

The first model (a) is usually referred to as the *opt-in* model, the second model is usually called an *opt-out* regime.

It is sometimes suggested that the opt-in model is more respectful of the freedom of contract. See for example the Commission, in the Action Plan:<sup>10</sup>

'It [i.e. the optional instrument] could either apply to all contracts, which concern cross-border transactions or only to those which parties decide to subject to it through a choice of law clause. *The latter would give parties the greatest degree of contractual freedom.* They would only choose the new instrument if it suited their economic or legal needs better than the national law which would have been determined by private international law rules as the law applicable to the contract.'

However, this reasoning is questionable. Given that a legal system, national or European is always applicable, it cannot be said that the default applicability of an optional instrument will be more respectful of the parties' freedom.

It is likely, however, that an opt-out regime would lead to a much more frequent applicability of an optional instrument than the opt-in regime. The reason being that most contracting parties - especially consumers and small and medium enterprises (SME) - do not make a conscious choice for the applicable law, because they cannot rely on sophisticated legal advisors who inform them concerning the advantages and disadvantages of the different options. Therefore, it can be said that an opt-out regimes interferes more with the legislative autonomy of the Member States than an opt-in regime.

For the autonomy of the parties, whether the default regime is national or European, is in itself neutral. The case might be different, of course, if the content of a national legal system were to be more respectful of freedom of contract than the optional instrument. However, that would not be an intrinsic characteristic of an optional instrument. The case would also be different if the vast majority of parties to cross-border contracts today have a preference for a national legal system to be applicable to their contract rather than a European instrument. In that case their substantive freedom of contract would be reduced because, as said, an opt-out regime is likely to lead in many cases to a passive choice for the optional instrument (*de-facto* binding character).<sup>11</sup> However, if indeed there proves to be a pervasive preference by economic operators for

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<sup>10</sup> *Action Plan*, n 2 above, 92 (emphasis added); see also *The Way Forward*, n 3 above, Annex II.

<sup>11</sup> See M.W. Hesselink, Non Mandatory Rules in European Contract Law, *ERCL* 1(2005), 43-83.

national law rather than a European instrument for cross-border contracts,<sup>12</sup> there would be a much more fundamental problem: this would significantly weaken the Commission's case for the need of an optional instrument for the internal market.

#### 2.4. *Mandatory and non-mandatory rules*

##### 2.4.1. Freedom of contract

An optional instrument could include both mandatory rules and non-mandatory rules. Mandatory rules are rules that apply whatever the parties agree to in their contract, whereas non-mandatory rules can be waived by the parties in their contract.

According to the Commission, only a limited number of rules within an optional instrument (for example: rules aimed at the protection of the consumer) should be mandatory.<sup>13</sup> This strong emphasis by the Commission on the freedom of contract, has received criticism from legal scholars.<sup>14</sup>

In the section dealing with an optional instrument the question whether a choice by the parties for such an optional instrument could exclude the application of conflicting mandatory national provisions for areas which are covered thereby, will be addressed. This question is closely linked to two other current legislative projects of the European Union, i.e. the revision of the consumer contract acquis<sup>15</sup> and the conversion of the 1980 Rome Convention on the law applicable to contractual obligations into a regulation (Rome I).<sup>16</sup>

##### 2.4.2. The revision of the consumer acquis

In the current revision of the consumer contract law acquis one of the possibilities seriously considered is a horizontal approach combined with full or

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<sup>12</sup> Whether this is the case is an empirical question on which today hardly any reliable statistical data exist. Both the Commission's consultation and the Clifford Chance report (see S. Vogenauer, S. Weatherill, 'The European Community's competence to Pursue the Harmonisation of Contract Law – an Empirical Contribution to the Debate', in: *The Harmonisation of European Contract Law, Implications for European Private Laws, Business and Legal Practice*, S. Vogenauer, S. Weatherill (eds.) Oxford: Hart Publishing, 2006, 105 – 147) only give some very rough indications; they do not claim to be representative.

<sup>13</sup> *Action Plan*, n 2 above, 94.

<sup>14</sup> See e.g. Study Group on Social Justice in European Private Law, 'Social Justice in European Contract Law: a Manifesto', *ELJ* 10(2004) 653 – 674; M.W. Hesselink, 'The Politics of a European Civil Code', *ELJ* 10(2004) 675-697; B. Lurger, 'The Common Frame of Reference/Optional Code and the Various Understandings of Social Justice in Europe', in: *The Common Frame of Reference/ Optional Code and the Various Understandings of Social Justice in Europe, Private Law and the Many Cultures of Europe*, T. Wilhelmsson, E. Paunio, A. Pohjolainen (eds.), Kluwer Law International, 2007, 177-199; J.W. Rutgers, 'An Optional Instrument and Social Dumping', *ERCL* 2006, 199 – 212.

<sup>15</sup> See Green Paper on the Review of the Consumer Acquis, Brussels, 08.02.2007, COM(2007) 744 (hereafter: Green Paper).

<sup>16</sup> Proposal for a Regulation of the European Parliament and the Council on the law applicable to contractual obligations (Rome I), Brussels 15.12.2005, COM (2005) 650 final.

maximum harmonisation.<sup>17</sup> Unlike in a vertical approach where directives are revised one by one, in a more horizontal approach certain issues which are common to several or all directives, are dealt with by general rules (e.g. general rules on cooling off periods). In other words, in a horizontal approach the revision would lead to a set of general rules of consumer contract law.

Until fairly recently, most directives in the area of consumer contract law allowed the Member States to provide consumers with a higher level of protection than the one provided for in the directive (minimum harmonisation). However, the Commission has announced that it intends to move to a policy of full harmonisation where the Member States have no freedom to extend consumer protection beyond the level required by the directive.<sup>18</sup> This new policy has already been implemented in the unfair commercial practices directive.<sup>19</sup>

Obviously, the more the revision of the consumer contract acquis moves in these two directions - as it seems to be envisaged by the Commission<sup>20</sup> - the more an optional instrument on B2C contracts becomes obsolete. In a recent 'Report on the outcome of the public consultation on the green paper on the review of the consumer acquis' the Commission states:<sup>21</sup>

'A majority of respondents call for the adoption of a horizontal legislative instrument applicable to domestic and cross-border transactions, based on full targeted harmonisation; i.e. targeted to the issues raising substantial barriers to trade for business and/or deterring consumers from buying cross-border. The horizontal legislative instrument should in the view of most respondents be combined with vertical revisions of the existing sectoral directives (for example revision of the Timeshare and Package Travel Directives).'

Of course, the Commission only summarizes the opinions of the respondents to the consultation and the Commission takes care to underline that '[t]his Report does not draw political conclusions from the consultation process'. Nevertheless, the wording of both this document and the Green paper seem to suggest that the Commission aims at full harmonisation of some important general issues of consumer law. Once such harmonisation has taken place,

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<sup>17</sup> See *Green Paper*, n 15 above, questions A1 and A3.

<sup>18</sup> See the Commission's 'Consumer Policy Strategy 2002-2006' (COM(2002) 208 final) 12 ('There is a need to review and reform existing EU consumer protection directives, to bring them up to date and progressively adapt them from minimum harmonisation to "full harmonisation" measures.') and its recent *EU Consumer Policy Strategy 2007-2013: Empowering consumers, enhancing their welfare, effectively protecting them*, Brussels, 13.3.2007 COM(2007) 99 final, 7.

<sup>19</sup> Directive 2005/29 concerning unfair commercial practices, OJ 2005 L 149/22.

<sup>20</sup> This seems to follow from the phrasing of the Green Paper, n 15 above, and the Commission staff working paper: Report on the outcome of the public consultation on the Green paper on the review of the consumer acquis analyse. However, the latter says explicitly: '[t]his Report does not draw political conclusions from the consultation process'.

<sup>21</sup> [http://ec.europa.eu/consumers/rights/cons\\_acquis\\_en.htm](http://ec.europa.eu/consumers/rights/cons_acquis_en.htm).

consumer law in the Member States on these subjects will be fairly identical. Hence, there is little reason to opt for an optional instrument concerning B2C contracts.

### 2.4.3. Rome I

A very controversial question currently under debate in the Council is whether in Rome I the country of origin principle should apply to consumer protection.<sup>22</sup> Should a choice of law be capable of depriving a consumer from the consumer protection that he would enjoy if the law of his own place of residence would be applicable? Today, under the 1980 Rome Convention the answer is negative for so-called passive consumers, i.e. consumers that did not actively engage in cross-border contracting; the foreign seller came to them (see Article 5).

If the answer remains negative under the Rome I Regulation,<sup>23</sup> the question arises whether this should be any different in the case where a choice of law is included in a B2C contract for an optional instrument and where the level of consumer protection in the optional instrument is lower than in the law of the place of residence of the consumer. This, in turn, depends on how the choice for an optional instrument will be regulated. One possibility would be that Article 3 of Rome I would explicitly make a choice for an optional instrument possible. Although this was proposed by the European Commission, it would appear that this will not be accepted by the Council and the Parliament.<sup>24</sup> Another possibility would be that the choice of law is regulated in the optional instrument itself.<sup>25</sup> In the latter case Rome I, including the rule in Article 5 Rome I, would not be applicable (Article 21 1980 Rome Convention).<sup>26</sup>

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<sup>22</sup> See *European Voice*, 29 March - 3 April 2007; 16 – 23 May 2007.

<sup>23</sup> See *Position of the European Parliament adopted at first reading on 29 November 2007 (EP-PE\_TC1-COD(2005)0261)*. If we are informed correctly, a political compromise has been reached between the Council and the Parliament with regard to this text. Article 6 (Consumer contracts) Rome I, the successor of Article 5 Rome Convention will read as follows. '1. Without prejudice to Articles 5 and 7, a contract concluded by a natural person for a purpose which can be regarded as being outside his trade or profession ("the consumer") with another person acting in the exercise of his trade or profession ("the professional") shall be governed by the law of the country where the consumer has his habitual residence, provided that the professional: (a) pursues his commercial or professional activities in the country where the consumer has his habitual residence, or (b) by any means, directs such activities to that country or to several countries including that country, and the contract falls within the scope of such activities. 2. Notwithstanding paragraph 1, the parties may choose the law applicable to a contract which fulfils the requirements of paragraph 1, in accordance with Article 3. Such a choice may not, however, have the result of depriving the consumer of the protection afforded to him by such provisions that cannot be derogated from by contract by virtue of the law which, in the absence of choice, would have been applicable on the basis of paragraph 1. ...'

<sup>24</sup> Indeed, in the text on which Parliament and Council seem to have reached a political agreement (see previous footnote), the rule to this effect in the Commission's proposal (Article 3, Section 2) has been dropped.

<sup>25</sup> The new text (see footnote 24) still seems to allow this. See, in particular, recital 14: 'Should the Community adopt in an appropriate legal instrument rules of substantive contract law, including standard terms and conditions, such instrument may provide that the parties may choose to apply those rules.'

<sup>26</sup> See 23 of the new text (see footnote 24).



A similar question is what should happen in cases of a conflict between an optional instrument and so-called internationally mandatory rules (*lois de police*) (Article 7, 1980 Rome Convention) or with the national *ordre public* (Article 16, 1980 Rome Convention). Can a European optional instrument ever be against national *ordre public* of a Member State?<sup>27</sup>

The Commission seems to favour a situation where after a choice for the optional instrument, no other rules such as overriding mandatory rules (Article 7, 1980 Rome Convention) or mandatory rules concerning consumers will apply.<sup>28</sup>

'the introduction in the optional instrument of mandatory provisions in the meaning of in Articles 5 and 7 of the Rome Convention could represent a great advantage: the parties, by choosing the optional instrument as applicable law to their contract, would know from the moment of the conclusion of the contract which mandatory rules are applicable to their contractual relationship. That would provide legal certainty in cross border transactions and the relevant providers of services and goods could market their services or products throughout the whole European Union using one single contract. The optional instrument would then become a very useful tool for the parties. However, in such a situation, it would need to be certain that, where the parties have chosen the optional instrument as applicable law, other national mandatory rules would no longer be applicable. That would depend on the solution chosen for the articulation of the optional instrument with Rome I.'

In other words, the Commission emphasizes that the means by which an optional instrument is made applicable, for instance by a choice of law on the basis of Article 3 Rome I Regulation or by the optional instrument itself, is decisive with respect to the issue whether other national mandatory rules still play a role. When an optional instrument is rendered applicable by a choice of law on the basis of Article 3 of the Rome Regulation, the other rules included in the Rome Regulation, for instance those with respect to consumer protection or the *lois de police* still apply.<sup>29</sup> If on the other hand, an optional instrument includes a provision according to which it can be made applicable and if the new Rome I Regulation does not preclude an optional instrument,<sup>30</sup> the rules laid down in the Rome Regulation do not play a role anymore.

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<sup>27</sup> Compare Article 9 and 21 respectively in the new text for Rome I (see above, footnote 24).

<sup>28</sup> *The Way Forward*, n 3 above, 21-22. See further: Lurger, n 14 above, 177 – 199; Rutgers, n 14 above, 199 – 212.

<sup>29</sup> H. Heiss, N. Downes, 'Non-Optional Elements in an Optional European Contract Law. Reflections from a Private International Law Perspective', *ERPL* 2005, 693-712, at 702.

<sup>30</sup> Article 23 of the new text (see footnote 24) does not seem to preclude the adoption by the European Union of an optional instrument. See also recital 14 of the new text, quoted above, in footnote 26.

More generally, in *The Way Forward* the Commission underlines the importance of co-ordinating the action plan process with the Rome I process.<sup>31</sup>

## 2.5. B2B and B2C contract

With regard to the personal scope of the instrument, three alternatives are conceivable: a) an optional instrument only for business to business contracts; b) an optional instrument only for business to consumer contracts; or c) an optional instrument for both business and consumer contracts. In the alternative (c), the optional instrument could contain either different sets of rules for B2B and B2C contracts or (also/only) general rules for both types of contractual relationships.

It is sometimes suggested that in terms of the internal market, an optional instrument is only required in B2B contracts. However, it should be kept in mind that it may be quite cumbersome for a business that wishes to sell its products in all Member States (eg an internet shop) to make standard terms that are compatible with the consumer protection rules of all Member States. The possibility to give the consumers the choice to contract with him under European contract law (eg by clicking on a blue button),<sup>32</sup> may be decisive in a business's decision (especially in the case of an SME) whether or not to offer its products across the internal market.

Therefore, it is not surprising that the Commission underlines the importance of B2C contracts for the internal market. In particular it emphasises the potential gain for businesses if they can market their product across the internal market with one single contract, especially if a choice for an optional instrument would imply that national rules in protection of consumers would no longer be applicable. However, the Commission acknowledges that whether this would be the case will depend on the outcome of Rome I Regulation.<sup>33</sup> In addition, it also depends on the optional instrument itself, whether it renders itself applicable or whether its applicability is established through a choice of law as laid down in the 1980 Rome Convention.<sup>34</sup>

It should also be remembered that the question whether a choice of law for an optional instrument must imply the waiver of further-reaching consumer protection under national law is a very controversial question; much will depend on the level of consumer protection in the optional instrument and on the outcome of the revision of the acquis.<sup>35</sup>

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<sup>31</sup> *The Way Forward*, n 3 above, Annex II.

<sup>32</sup> See H. Schulte-Nölke, 'Europäisches Vertragsrecht als blauer Button im Internet-Shop', ZGS 2007, 81.

<sup>33</sup> *The Way Forward*, n 3 above, 18-19 and 21.

<sup>34</sup> As said above (see footnote 24), since the political compromise between Council and Parliament this possibility now seems unlikely.

<sup>35</sup> See above, Section 2.4.2.

## 2.6. Cross-border and purely internal contracts

It is not inherent in the concept of an optional instrument to be only applicable in cross-border cases. However, the Commission seems to assume that any optional instrument that might be adopted could only be chosen in cross-border cases.

This means that a business that wants to market its products across the internal market, including its own country, will still have to operate under two legal regimes, the optional instrument and its own national law, and will have to adapt its standard contract terms accordingly. It would undermine, in part, the success of the blue button idea,<sup>36</sup> and more generally the underlying policy of the optional instrument idea.<sup>37</sup>

## 2.7. Content

### 2.7.1. Relation to the CFR

The substantive scope of the draft Common Frame of Reference that is currently prepared by academics (sometimes called the 'academic CFR') is quite broad. It includes not only rules concerning a vast array of specific contracts but also rules concerning contracts in general, obligations in general, tort law, unjustified enrichment, property law and trust law. It is not certain whether the Commission will include all these subjects in the final CFR (sometimes referred to as the 'political CFR'). However, this may very well be the case since the Commission has indicated that for its purpose as a 'tool box' a CFR with a very wide scope can be useful.<sup>38</sup> Nevertheless, so far the Commission has been rather cautious. In the *Action Plan* it states:<sup>39</sup>

'It is clear that in reflecting on a non-sector-specific instrument, the Commission will take into account the common frame of reference. The content of the common frame of reference should then normally serve as a basis for the development of the new optional instrument. Whether the new instrument would cover the whole scope of the common frame of reference or only parts thereof, or whether it would cover only general contract law rules or also specific contracts, is at present left open.'

In *The Way Forward* the Commission reports that many stakeholders agreed on the fact that an optional instrument should contain some provisions of general contract law as well as provisions relating to specific contracts which have significant importance for cross-border transactions.<sup>40</sup> However, the

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<sup>36</sup> See above, Section 2.5.

<sup>37</sup> See above, Section 2.1.

<sup>38</sup> *The Way Forward*, n 3 above, 14-15.

<sup>39</sup> *Action Plan*, n 2 above, 95.

<sup>40</sup> *The Way Forward*, n 3 above, Annex II.

Commission does not make any choices yet in this regard. It limits itself to emphasising the necessary link between the optional instrument and the internal market. It states:<sup>41</sup>

'An optional instrument should only contain those areas of contract law, whether general or specific to certain contracts, which clearly contribute to addressing identified problems, such as barriers to the smooth functioning of the internal market.'

#### 2.7.2. Relation to CISG

A specific and rather complex question is how the optional instrument should relate to the UN Convention on the International Sale of Goods (Vienna, 1980) (CISG). Most, but not all, EU Member States are parties to this convention. Especially difficult questions would arise if the optional instrument were to be an opt-out instrument since the CISG is also based on an opt-out mechanism. In cases where parties to an international sales contract have made no provision on the applicable law in their contract, the question would arise which instrument would apply: the CISG, the European optional instrument or both (and if so, to which extent)?

In this regard, the Commission stated in the *Action Plan* that it would welcome comments on the scope of an optional instrument in relation to the CISG. It suggested:<sup>42</sup>

'The optional instrument could be comprehensive, i.e. covering also cross-border contracts of sale between businesses, and thereby include the area covered by the CISG. It could also exclude this area and leave it to the application of the CISG.'

#### 2.8. One or more optional instruments?

The next question is whether the whole CFR (or the relevant part of it; see *supra* Section 2.7) should be converted into *one* optional instrument or whether it should be divided into a number of optional instruments relating to different specific subjects, eg an optional instrument on sales contracts, one on insurance contracts et cetera.

The latter approach would have the advantage that the optional instrument(s) would be limited to the rules most relevant to the internal market which might be relevant with a view to a legal basis.<sup>43</sup>

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<sup>41</sup> Ibid.

<sup>42</sup> *Action Plan*, n 2 above, 96.

<sup>43</sup> See below, Sections 5 and 6.

However, this approach also has its drawbacks. For example, in an opt-in regime (not in the opt-out model) the parties may make a choice for the wrong instrument. For example, the parties consider their contract a sales contract but according to the definition in the optional instrument it is not. What should happen then? Would the national law which is indicated by private international law (1980 Rome Convention or the future Rome I Regulation) apply? This would seem odd in the light of the parties' explicit choice for a non-national legal regime. Alternatively, depending on the division of the CFR into several codes, two optional instruments could be applicable at the same time (eg the instrument on sales contracts and the one on distribution contracts (in the case of a 'mixed' contract), or e.g. the instrument on sales contracts and the instrument on unjustified enrichment). Furthermore, what if the parties are not aware of the applicability of more than one instrument and they opt only for one? Will their contract then be governed partly by national law and partly by the optional instrument?

There are several different ways in which the CFR could be divided. One possibility would be a horizontal division, according to the (conceptual) distinctions of the CFR: an instrument on general contract law, one on sales contracts, one on property et cetera. Another would be to provide legal regimes for an entire legal relationship. E.g. the optional instrument on sales contracts would not only include sales law but also general contract law and maybe also some property law (transfer of property). This more vertical approach would follow the example of CISG. However, just like in CISG, the question would arise how comprehensive such a set of rules should be. Should it only contain the rules that are relevant in typical sales contracts or all the rules that might be of relevance in such a contract. In an extreme version of the latter approach there would not be much difference with turning the whole CFR into an optional instrument.

## 2.9. *Legal form: regulation, directive or recommendation?*

In its Communication of 2001, the Commission explicitly addressed the issue of which legal instrument should be chosen:<sup>44</sup>

'The choice of instrument depends on a number of factors, including the degree of harmonisation envisaged. A Directive would, on one hand, give Member States a certain degree of flexibility to adapt the respective provisions of the implementation law to their specific national economic and legal situation. On the other hand, it may allow differences in implementation which could constitute obstacles to the functioning of the internal market. A Regulation would give the Member States less flexibility for its integration into the national legal systems, but on the other hand it would ensure more transparent and uniform conditions for economic operators in the internal market. A Recommendation could only be envisaged if a purely optional model is chosen.'

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<sup>44</sup> *Communication 2001*, n 1 above, 62-65.

Subsequently, in the Action Plan, the Commission expresses a preference for a regulation or a recommendation.<sup>45</sup>

'As to its form one could think of EU wide contract law rules in the form of a regulation or a recommendation, which would exist in parallel with, rather than instead of national contract laws.'

Finally, in *The Way Forward* the Commission links the issue up to the binding nature of the instrument: a recommendation, which lacks direct applicability, seems inappropriate for an opt-out system.<sup>46</sup>

### 2.10. *Legal basis*

Only on one occasion has the Commission explicitly and directly addressed the issue of a legal basis for an optional instrument in the field of contract law. In *The Way Forward* it says:<sup>47</sup>

'The question of the legal base is closely linked with the questions of the legal form of the optional instrument, of its content and its scope. More reflections on the important issue of the legal base will be necessary within a larger debate on the parameters of an optional instrument.'

The remainder of the present report aims to contribute to that debate by taking into account different possible choices in relation to these parameters.

## 3. The reactions from the other Institutions

The other institutions of the European Union have responded to the Commission's proposals. This section discusses the opinions of the Council of the European Union and the European Parliament.<sup>48</sup>

### 3.1. *The Council of the European Union*

The Council responded to the European Commission's Action Plan in a resolution<sup>49</sup> and to the Commission's First Annual Progress Report on

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<sup>45</sup> *Action Plan*, n 2 above, 92.

<sup>46</sup> *The Way Forward*, n 3 above, Annex II.

<sup>47</sup> *Ibid.*

<sup>48</sup> The European Economic and Social Council also gave its opinion, on several occasions: *Thoughts on the legal framework for consumer policy*, 20.04.2006, INT/263; *Opinion on the Protection of Consumers in respect of Distance Contracts*, 30.05.2007, INT/334; *Opinion on the Green Paper on the review of the Consumer Acquis*, 12.07.2007, INT/336.

<sup>49</sup> Council Resolution On "A More Coherent European Contract Law", 14.10.2003, OJ C 246/1-

European Contract Law and the Acquis Review in the conclusions of the Competitiveness Council of 28-29 November 2005.<sup>50</sup>

On the idea of an optional instrument, the Council said, in its reaction to the Action Plan, that further reflection was needed:<sup>51</sup>

'Further reflection is necessary on the need for non-sector specific measures, for example an optional instrument in the area of European contract law: the Commission should pursue this reflection, in close collaboration with Member States and taking due account of the principle of contractual freedom.'

With regard to the Common Frame of Reference, as suggested by the Commission, the Council said that it would not be a binding instrument:<sup>52</sup>

'Community law rules, in particular in the area of contract law, should be consistent and ensure proper transposition into national law. In this context, the Common Frame of Reference suggested by the Commission could contribute to improving the quality and consistency of both existing and future Community legislation in this area. This Common Frame of Reference would not be a legally binding instrument.'

In its reaction to the Commission's First Annual Report the Council did not say anything specific concerning the characteristics of a Common Frame of Reference or an optional instrument.

### 3.2. *The European Parliament*

The European Parliament responded, in resolutions, to the Commission's first Communication,<sup>53</sup> its Action Plan,<sup>54</sup> its Communication 'European contract law and the revision of the acquis; the way forward',<sup>55</sup> and its First Annual Report.<sup>56</sup>

The European Parliament is in favour of adopting one or more optional instruments. Indeed, in its resolution on the Commission's Action Plan the European Parliament calls on the Commission, as a matter of priority, to

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<sup>50</sup> *European Contract Law, Council conclusions*, (Competitiveness Council) 28-29.11.2005, 14155/05 (Presse 287), 27-30.

<sup>51</sup> Council resolution on Action Plan, no. 3. See also: Council of the European Union, Press Release 2794<sup>th</sup> Council Meeting Justice and Home Affairs, Luxembourg, 19 – 20 April 2007, 21 – 22, 8364/07 (Presse 77).

<sup>52</sup> Council Resolution On "A More Coherent European Contract Law", 14.10.2003, OJ C 246/1.

<sup>53</sup> European Parliament resolution on the approximation of the civil and commercial law of the Member States, 15.11.2001, OJ C140E, 538-542.

<sup>54</sup> European Parliament resolution on the Communication from the Commission to the European Parliament and the Council – A more coherent European contract law – An action plan, 02.09.2003, P5\_TA(2003)0355.

<sup>55</sup> European contract law and the revision of the acquis; the way forward (2005/2022(INI)), 23.03.2006, P6\_TA(2006)0109, OJ C 292E, 109-111.

<sup>56</sup> See *Parliament Resolution on The Way Forward*, note 50 above.

produce an opt-in instrument in the areas of consumer contracts and contracts of insurance. The European Parliament:<sup>57</sup>

'Considers that, in order to facilitate cross-border trade within the internal market, it should be an early priority to proceed with the establishment of an optional instrument in certain sectors, particularly those of consumer contracts and insurance contracts, and therefore calls on the Commission as a matter of priority, whilst having regard to a high level of consumer protection and the integration of the appropriate mandatory provisions, to produce an opt-in instrument in the areas of consumer contracts and contracts of insurance'

In its reaction to the Commission's communication *The Way Forward* the European Parliament points out that the legal basis for any binding instrument as a result of the *Action Plan* process is unclear.<sup>58</sup>

'whilst it seems that the European contract law initiative ... should be seen primarily as an exercise in better law-making at EU level, it is by no means clear what it will lead to in terms of practical outcomes or on what legal basis any binding instrument or instruments will be adopted'

The European Parliament also makes clear that, in its view, such an instrument should be based on the CFR.<sup>59</sup>

'Calls, therefore, for the elaboration of a body of rules based on the 'common frame of reference', to be offered to the contracting parties as an 'opt-in /opt-out' solution; considers, in other words, that the parties should initially have the option of using it voluntarily, and that it could later become binding.'

Finally, the European Parliament leaves no doubt that, in its view, not mere consultation but codecision is required when it comes to the participation of the European Parliament in adopting any legislation as a result in the area of civil law:<sup>60</sup>

'Insists that the codecision procedure involving the full participation of the European Parliament must in principle be used when adopting legislation in the field of civil law'

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<sup>57</sup> *Parliament Resolution on Action Plan*, n 55 above, 14. In its resolution on the Commission's 2001 Communication, the Parliament Called on the Commission 'to have recourse to the legal basis provided by Article 95 of the EC Treaty (internal market) for the further consolidation and development of the harmonisation of civil law'.

<sup>58</sup> *Parliament Resolution on The Way Forward*, n 56 above, A.

<sup>59</sup> *Parliament Resolution on The Way Forward*, n 56 above, 15.

<sup>60</sup> European Parliament resolution on the approximation of the civil and commercial law of the Member States, 15.11.2001, OJ C140E, 538-542, 21.



#### 4. Articles 65 EC: the area of freedom, security and justice

##### 4.1. *General*

Title IV of the EC Treaty, on 'Visas, Asylum, immigration and other policies related to free movement of persons', includes rules with respect to the harmonisation of conflict of law rules. Article 65, paragraph b, EC provides:

'Measures in the field of judicial cooperation in civil matters having cross-border implications, to be taken in accordance with Article 67 and insofar as necessary for the proper functioning of the internal market, shall include ...

(b) promoting the compatibility of the rules applicable in the Member States concerning the conflict of laws and jurisdiction.'

Since the article deals with 'civil matters having cross-border implications' it has prima facie relevance for an optional instrument on European contract law.

##### 4.2. *Legislative procedure*

At present, measures pursuant to Article 65 EC can be adopted by qualified majority voting in the Council, after the co-decision procedure of Article 251 EC (Article 67, paragraph 5 EC). This means that the European Commission, the European Parliament and the Council of the European Union would be involved in adopting any legislative (or other) measure.

Not all Member States are automatically bound by the measures adopted under Article 61-67 EC. The United Kingdom, Ireland and Denmark have a special position (Article 69 EC).<sup>61</sup> The positions of the United Kingdom and Ireland differ from that of Denmark. The United Kingdom and Ireland have the possibility to decide with respect to each particular measure whether they will participate or not.<sup>62</sup> In contrast, Denmark does not have the possibility of opting in with respect to any individual instrument.<sup>63</sup> However, it can declare that it will participate, totally or partly, with respect to Title IV of the Treaty.<sup>64</sup>

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<sup>61</sup> Cf J. Basedow, 'The Communitarization of the Conflicts of Laws under the Treaty of Amsterdam' *CLMRev* 37 (2000) 687-708, at 695 ff; O. Remien, 'European Private International Law, the European Community and its Emerging Area of Freedom, Security and Justice' *CMLRev* 38 (2001) 53-86, at 61.

<sup>62</sup> Article 3 of Protocol (No 4) on the position of the United Kingdom and Ireland (1997) *OJ* 2006, C 321/198. M. Bogdan, *Concise Introduction to EU Private International Law*, Groningen, Europa Law Publishing, 2006, 13.

<sup>63</sup> Article 7 of Protocol (No 5) on the position of Denmark (1997), *OJ* 2006, C 321/201-202. M. Bogdan, n 62 above, 13; Basedow, n 61 above, 696.

<sup>64</sup> Article 7 of Protocol (No 5) on the position of Denmark (1997), *OJ* 2006, C 321/201-202.

#### 4.3. *Types of measures*

According to Article 65 EC 'measures' can be adopted. The provision itself does not specify what type of measures it concerns. However, pursuant to Article 249 EC the European Parliament acting jointly with the Council, the Council and the Commission can make regulations, issue directives, take decisions, make recommendations or deliver opinions.<sup>65</sup>

#### 4.4. *Subject matter*

Any measure adopted on the basis of Article 65, paragraph b, EC must be 'promoting the compatibility of the rules applicable in the Member States concerning the conflict of laws and of jurisdiction'.<sup>66</sup>

Typical measures based on this Article include the Regulation concerning jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (Brussels I)<sup>67</sup>, the new Regulation concerning jurisdiction and the recognition and enforcement of judgments in matrimonial matters, and parental responsibility (new Brussels II)<sup>68</sup> and the draft regulations on the law applicable to contractual and non contractual obligations (Rome I and Rome II)<sup>69</sup>.

The wording of Article 65, paragraph b, EC seems to refer quite clearly to traditional private international law measures, i.e. choice of law and jurisdictional matters, not substantive private law. In any case, that is the way in which it has been understood by the Commission thus far. Moreover, there seems to be no reason, neither in the wording of the Article (neither in the English nor the other language versions) nor in its broader context ('judicial cooperation'), that suggests that measures concerning substantive private law (e.g. contract law) could be based on this Article as well.

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<sup>65</sup> Basedow, n 61 above, 706 ff.

<sup>66</sup> See also the French ('favoriser la compatibilité des règles applicables dans les États membres en matière de conflits de lois et de compétence') and the German language version ('Förderung der Vereinbarkeit der in den Mitgliedstaaten geltenden Kollisionsnormen und Vorschriften zur Vermeidung von Kompetenzkonflikten')

<sup>67</sup> Council Regulation (EC) No 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters *OJ* 2001, L 12/1-23.

<sup>68</sup> Council Regulation (EC) No 2201/2003 of 27 November 2003 concerning jurisdiction and the recognition and enforcement of judgments in matrimonial matters and the matters of parental responsibility.

<sup>69</sup> Proposal for a Regulation of the European Parliament and the Council on the law applicable to contractual obligations (Rome I) Brussels, 15.12.2005, COM (2005) 650 final; see also Green Paper on the conversion of the Rome Convention of 1980 on the law applicable to contractual obligations into a Community instrument and its modernisation, Brussels, 14.1.2003, COM(2002) 654 final.

Nevertheless, in the Presidency Conclusions of the Tampere European Council of 15<sup>th</sup> and 16<sup>th</sup> October 1999, whilst discussing the European area of justice, under the heading 'Greater convergence in civil law' the Council said:<sup>70</sup>

'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.'

This Council conclusion was the starting point for the Action Plan process.<sup>71</sup> However, it seems somewhat far-fetched to conclude from this passage that the Council considers Article 65 EC to be the proper legal basis for enacting an optional instrument on contract law.

Finally, Article 65 EC requires that the measures be taken 'insofar as necessary for the proper functioning of the internal market'. It has been suggested in the literature that also with respect to measures adopted on the basis of Article 65 must meet 'the Tobacco-requirement'<sup>72</sup> which will be discussed below.<sup>73</sup> However, there is no case law of the European Court of Justice to confirm this suggestion.

#### 4.5. Conclusion

It seems implausible that an optional instrument containing exclusively or almost exclusively rules of substantive private law could be regarded as a harmonizing instrument concerning conflicts of laws. Consequently, it is very unlikely that Article 65 EC can provide a proper legal base for enacting an optional instrument.

### 5. Articles 94 and 95 EC: the approximation of laws

#### 5.1. General

Article 95 EC (former 100A EEC) was inserted into the Treaty as a result of the Single European Act in 1987 with a view to enhancing the construction of the common market and has since then rapidly superseded Article 94 EC.<sup>74</sup> Therefore, the main focus will be on Article 95 EC. For the same reason they will be discussed in reverse order, which incidentally will also be the new order

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<sup>70</sup> Tampere European Council. Presidency conclusions, 15-16.10.1999, 38.

<sup>71</sup> Cf. D. Staudenmayer, 'The Commission Action Plan on European Contract Law', *ERPL* 2003, 113 – 127; *Parliament resolution on Communication 2001*, 10.

<sup>72</sup> S. Weatherill, 'European Private Law and the Constitutional Dimension', in: *The Institutional Framework of European Private Law*, F. Cafaggi (ed.) Oxford: OUP, 2006, 79 – 106, at 93. Contra Bogdan, n 62 above, 10.

<sup>73</sup> In Section 5.

<sup>74</sup> Kapteyn VerLoren van Themaat, *Het recht van de Europese Unie en van de Europese Gemeenschappen*, Deventer: Kluwer, 2003, 260; Weatherill, n 72 above, 84.

of the Articles under the Reform Treaty.<sup>75</sup> It should be noted that Article 95 EC is a residual competence. Article 95 EC comes into play insofar as there are no other competences included in the Treaty.<sup>76</sup>

## 5.2. *Legislative procedure*

On the basis of Article 95 EC, the Council can adopt measures by qualified majority voting after having followed the co-decision procedure of Article 251 EC and after having consulted of the European Economic and Social Committee.<sup>77</sup>

## 5.3. *Types of measures*

### 5.3.1. Directives and Regulations

Article 95 EC provides for the adoption of 'measures for the approximation'. The provision does not itself further specify the type of measures that can be adopted. However, it is generally assumed that directives and regulation can be adopted on the basis of Article 95 EC.<sup>78</sup>

Nevertheless, in the area of European contract law the European Community has thus far consistently opted for directives rather than for regulations. Moreover, with regard to the current revision of the *acquis communautaire* in the area of consumer contract law the Commission is also considering a framework directive rather than a regulation as the appropriate measure.<sup>79</sup> This may be explained by the fact that directives, as the less intrusive legislative device, are considered to be more in accordance with the principle of subsidiarity (Article 5 EC) than regulations which leave the Member States with no freedom to adapt the measure to the national context.<sup>80</sup> Indeed, the Protocol on the application of the principles of subsidiarity and proportionality to the Treaty of Amsterdam, (OJ C 340 of 10 November 1997) says (under 6):

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<sup>75</sup> See Draft Treaty amending the Treaty on European Union and the Treaty establishing the European Community, approved at the Intergovernmental Conference of 18 October 2007 in Lisbon ('Reform Treaty'), art 2, section 80.

<sup>76</sup> Case C-533/03 *Commission v. Council* [2006] ECR I-1025 para 44; C. Barnard, *The Substantive Law of the EU, the Four Freedoms*, Oxford: OUP, 2007, 568, 581; P. Craig, G. de Búrca, *EU Law, Text, Cases, and Materials*, Oxford: OUP, 2003, 1184; Kapteyn VerLoren van Themaat, n 74 above, 263; see also Advocate General Leger in his opinion to Case C-233/94 *Germany v. European Parliament and Council* [1997] ECR I-2405, at 2421.

<sup>77</sup> See in this respect: Weatherill, n 72 above, 84 ff; S. Weatherill, 'Constitutional Issues – How Much is Best Left Unsaid?', in: *The Harmonisation of European Contract Law*, S. Vogenauer, S. Weatherill (eds.), Oxford: Hart Publishing, 2006, 89 – 103, at 93.

<sup>78</sup> Craig & de Búrca, n 76 above, 1184; W. van Gerven, 'Bringing (Private Laws) Closer at the European level', in: *The Institutional Framework of European Private Law*, F. Cafaggi (ed.), Oxford: OUP, 2006, 37 – 77, at 46; Kapteyn VerLoren van Themaat, n 74 above, 260.

<sup>79</sup> Commission staff working paper: Report on the outcome of the public consultation on the Green paper on the review of the consumer *acquis* analyse, 3.

<sup>80</sup> See also the proportionality principle (Article 5 EC).

'Other things being equal, directives should be preferred to regulations and framework directives to detailed measures.'

However, in its 2005 Communication 'Implementing the Community Lisbon programme: A strategy for the simplification of the regulatory environment',<sup>81</sup> under the heading 'From Directives to Regulations', the Commission announced its intention to move, where possible, from directives to regulations:

'As the Commission made clear in its Communication on Better Regulation for Growth and Jobs, the choice of the appropriate legal approach must be based on a careful analysis. Replacing directives with regulations can under certain circumstances be conducive to simplification as regulations enable immediate application, guarantee that all actors are subject to the same rules at the same time, and focus attention on the concrete enforcement of EU rules. This contribution to simplification was widely recognised in the consultations underlining the view that it would prevent divergent national implementation. In conformity with Treaty provisions and taking into account the Protocol to the Treaty on subsidiarity and proportionality, the Commission intends to further exploit, on a case by case basis, the potential for simplification through substituting directives with regulations.'

In any case, with regard to an optional instrument it can hardly be maintained that 'other things [are] equal' in the sense of the Amsterdam Protocol: as said, it is difficult to see how a an optional code could be introduced through a directive.

### 5.3.2. Approximation measures

It is not entirely clear from the ECJ's case law how the words 'measures for the approximation' in Article 95 EC should be understood.<sup>82</sup> However, in a number of cases the Court sheds some light on some aspects of this concept's interpretation.<sup>83</sup> First, the ECJ has held that the European legislature has a discretion with respect to the measures to be adopted. There are at least two cases, where the ECJ ruled in this sense. In both cases, the UK challenged

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<sup>81</sup> COM(2005) 535. Already in 2002, in its reaction the Commission's 2001 Communication, the European Parliament had called on the Commission 'to examine whether it might not be more effective and reasonable to use the instrument of the regulation for future single market legislation'.

<sup>82</sup> Cf. V. Randazzo, note to Case C-217/04, *United Kingdom v. European Parliament and Council* of the European Union, judgment of the Grand Chamber of 2 May 2006, nyr, *CMLRev* 44(2007) 155 –169.

<sup>83</sup> Case C-359/92 *Germany v. Council* [1994] ECR I-3681; Opinion 2/94, Opinion pursuant to Article 228 (6) of the EC Treaty, [1996] ECR I-1759; Case C-377/98 *Kingdom of the Netherlands v. European Parliament and Council* [2001] ECR I-7079; Case C-66/04 *UK v. European Parliament and Council* [2005] ECR I-10553; Case C-217/04 *UK v. European Parliament and the Council*, ECJ [2006] ECR I-3771. See V. Randazzo, note to Case C-217/04, *United Kingdom v. European Parliament and Council of the European Union*, judgment of the Grand Chamber of 2 May 2006, nyr, *CMLRev*. 44(2007) 155 –169.

measures adopted on the basis of Article 95 EC. In the first decision it concerned the setting up of a centralised procedure at European level for the authorisation of smoke flavourings for food<sup>84</sup>, whereas in the second decision it concerned the establishment of a European Network and Information Security Agency on the basis of Article 95 EC.<sup>85</sup> In both instances the UK lost. The ECJ reasoned as follows:<sup>86</sup>

‘that by the expression “measures for the approximation” in Article 95 EC the authors of the Treaty intended to confer on the Community legislature a discretion, depending on the general context and the specific circumstances of the matter to be harmonised, as regards the method of approximation most appropriate for achieving the desired result’

However, there are restrictions to the European legislator’s discretion. In a case concerning the legal basis of Regulation (EC) No. 1435/2003 European Cooperative Society, which was adopted on the basis of Article 308 EC, the ECJ has held explicitly that ‘measures for approximation’ within the meaning of Article 95 EC do not include new Community instruments that co-exist with national rules:<sup>87</sup>

‘Finally, .. it is apparent ... that the European Cooperative Society is a form which coexists with cooperative societies under national law. In those circumstances, the contested regulation, which leaves unchanged the different national laws already in existence, cannot be regarded as aiming to approximate the laws of the Member States applicable to cooperative societies, but has as its purpose the creation of a new form of cooperative society in addition to the national forms. That finding is not affected by the fact that the contested regulation does not lay down exhaustively all of the rules applicable to European cooperative societies and that, for certain matters, it refers to the law of the Member State in the territory of which the European cooperative society has its registered office, since, as pointed out above, that referral is of a subsidiary nature.’

This is highly relevant since the introduction of an optional instrument will not, as such, affect the national legal systems, but will rather co-exist with it. Therefore, the conclusion seems to be that an optional instrument is not a measure of approximation within the meaning of Article 95 EC.

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<sup>84</sup> Case C-66/04 *UK v. European Parliament and Council* [2005] ECR I-10553.

<sup>85</sup> Case C-217/04 *UK v. European Parliament and the Council*, ECJ [2006] ECR I-3771.

<sup>86</sup> Case C-66/04 *UK v. European Parliament and Council* [2005] ECR I-10553 para 45; Case C-217/04 *UK v. European Parliament and Council* [2006] ECR I-3771 para 43.

<sup>87</sup> Case C-436/03 *European Parliament v. Council* [2006] 3733 para 43 ff. See also: Case 45/86 *Commission v. Council* [1987] ECR 1493, para 13; Case C-350/92 *Spain v. Council* [1995] ECR I-1985, para 26 ff; Case C-377/98 *The Netherlands v. European Parliament and Council* [2001] ECR I-7079, para 24.

#### 5.4. Subject matter

##### 5.4.1. Improving the conditions for the Internal market

Provided that an optional instrument can be regarded as a measure for approximation within the context of Article 95 EC, which, as said, seems unlikely, there are additional requirements to be met.

First, and most importantly, any approximation measures pursuant to Article 95 EC must 'have as their object the establishment and the functioning of the internal market'. It follows from the ECJ case law that to have as its object the establishment and the functioning of the internal market, a measure must

'genuinely have as its object the improvement of the conditions for the establishment and functioning of the internal market.'<sup>88</sup>

The Court subsequently links these words to 'obstacles to the exercise of fundamental freedoms or of distortions of competitions'<sup>89</sup>. The conclusion which can be drawn is that when either an obstacle to trade or an appreciable distortion of competition occurs or is likely to occur, there is a competence to harmonize.<sup>90</sup> In addition, the ECJ has held that the mere diversity of national legal systems with respect to a certain subject matter does not suffice to establish competence under Article 95 EC.<sup>91</sup>

'If a mere finding of disparities between national rules and of the abstract risk of obstacles to the exercise of fundamental freedoms or of distortions of competition liable to result there from were sufficient to justify the choice of Article 100A [now Article 95 EC], judicial review of compliance with the proper legal basis might be rendered nugatory.'

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<sup>88</sup> Case C-376-98 *Germany v. European Parliament* [2000] ECR I-8419 para 83 ff; Case C-377/98 *The Netherlands v. European Parliament and the Council* [2001] ECR I-7079, para 15; C-66/04 *UK v. European Parliament and the Council* [2005] ECR I-10553 para 41; Case C-217/04 *UK v. European Parliament and the Council* [2006] ECR I-3771, para 42; Case C-380/03 *Germany v. European Parliament and Council* [2006] ECR I-11573. See also Craig & de Búrca, n 76 above, 1185.

<sup>89</sup> Case C-376-98 *Germany v. European Parliament* [2000] ECR I-8419 para 84. See also Kapteyn VerLoren van Themaat, n 74 above, 266.

<sup>90</sup> Case C-376/98 *Germany v. European Parliament and Council* [2000] ECR I-8419; see further inter alia: Case C-380/03 *Germany v. European Parliament and Council* [2006] ECR I-11573 para 67 with note by M. Ludwigs, *CMLRev.* 44(2007) 1159 - 1176. Cf Craig & de Búrca, n 76 above, 1185.

<sup>91</sup> Case C-376-98 *Germany v. European Parliament* [2000] ECR I-8419 para 84. See also inter alia: Case C-434/02 *Arnold André GmbH & Co KG v. Landrat des Kreises Herford* [2004] ECR I-11825 para 30; Case C-210/03 *Swedish Match AB, Swedish Match UK Ltd v. Secretary of State for Health* [2004] ECR I-11893, para 29; Case C-380/03 *Germany v. European Parliament and Council* [2006] ECR I-11573. Craig & de Búrca, n 76 above, 1185; Van Gerven, n 78 above, 39; Weatherill, n 72 above, 92.

#### 5.4.2. Obstacle to trade

An obstacle to trade occurs, *inter alia*, when an infringement of the free movement of goods (Article 28 EC) or services (Article 49 EC) is established or when it is likely to occur.<sup>92</sup> Thus, with respect to private law rules it has to be ascertained to what extent these may result in an infringement of one of the free movements. Different views have been expressed in the literature with regard to the question if and when national rules of private law and private international law rules result in an infringement of one of the free movements.<sup>93</sup>

In this respect the *Alsthom Atlantique* decision of the ECJ is relevant. In that case, in 1989, the ECJ said the following<sup>94</sup>:

‘Furthermore, the parties to an international contract of sale are generally free to determine the law applicable to their contractual relations and can thus avoid being subject to French law.’<sup>95</sup>

From this *obiter dictum* it seems to follow that only internationally mandatory rules can constitute a violation of the free movement of goods, as they are the only ones that the parties cannot deviate from, neither by substantive clauses nor by a choice of the applicable law.<sup>96</sup> As a result, non-mandatory rules of substantive law as a category could never be the object of harmonisation measures under Article 95 EC. Indeed, this has been the conclusion of several observers.<sup>97</sup>

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<sup>92</sup> Case C-210/03 *Swedish Match AB, Swedish Match UK Ltd v. Secretary of State for Health* [2004] ECR I-11893, nr. 30. See also: Case C-491/01 *British American Tobacco* [2002] ECR I-11453, nr. 60 ff; Case C-66/04 *UK v. European Parliament and Council* [2005] ECR I-10553; Barnard, n 76 above, 574.

<sup>93</sup> See for an overview of the different opinions: H. Muir Watt, ‘Integration and Diversity: The Conflict of Laws as a Regulatory Tool’, in: *The Institutional Framework of European Private Law*, F. Cafaggi (ed.) Oxford: OUP, 2006, 107 - 148; W.-H. Roth, ‘Secured Credit and the Internal Market: The Fundamental Freedoms and the EU’s Mandate for Legislation’, para III, *European Company and Financial Law Review*, forthcoming; J. W. Rutgers, *International Reservation of Title Clauses*, The Hague: T.M.C. Asser Press, 1999, 169 ff.

<sup>94</sup> The case was about a rule of national contract law, but one which was mandatory: the French rule of product liability which places an un rebuttable presumption on producers (towards anybody else than producers in the same sector) to have known of any hidden defect in their products. Therefore, in this case the only way for the producer to avoid liability would have been to make a choice for the law of the buyer’s place of residence. However, the scope of the *obiter dictum* is broader, it obviously also concerns non-mandatory rules.

<sup>95</sup> Case C-339/89, *Alsthom Atlantique SA v Compagnie de construction mécanique Sulzer SA*, [1991] ECR I-107, para 14.

<sup>96</sup> See e.g. Article 7 1980, Rome Convention. See about this and literature references: J.W. Rutgers, ‘The rule of reason and private law or the limits to harmonization’, in: *The Rule of Reason*, A. Schrauwen (ed.), Europa Law Publishing, Groningen, 2005, 145 – 159.

<sup>97</sup> See eg S. Grundmann, *Europäisches Schuldvertragsrecht* (Berlin: de Gruyter, 1999) 68; H. Muir Watt, ‘Choice of Law in Integrated and Interconnected Markets: a Matter of Political Economy’, *Ius Commune Lectures on European Private Law*, 7, (Maastricht: METRO, 2003).



An obvious further conclusion - most relevant here - is that Article 95 EC would not provide a legal basis either for an optional instrument because, even if the optional instrument is an opt-out code.<sup>98</sup>

However, it has been pointed out that *de facto* the freedom to deviate from non-mandatory rules often does not exist.<sup>99</sup> Therefore, it has been argued that non-mandatory rules should also be the object of scrutiny by the courts - ultimately by the ECJ -,<sup>100</sup> as they can equally harm the EU citizens' free enjoyment of their fundamental freedoms.<sup>101</sup> On the same grounds an optional code, especially an opt-out code, could also be *de facto* mandatory, especially when the parties lack the resources to obtain sophisticated legal advice needed for making a rational choice of law (see the example of CISG).<sup>102</sup>

Finally, there is the general question whether an obiter dictum in a twenty year old case (still) represents the Courts view today. Nevertheless, more recent decisions such as *Überseering* and *Inspire Art*, neither do reject nor contradict the obiter dictum in *Alsthom Atlantique*.<sup>103</sup>

#### 5.4.3. Other obstacles

In the literature it has also been argued, on the basis of empirical research that the diversity of national systems of private law is a major cause for obstacles to trade with respect to B2B contracts.<sup>104</sup> The empirical research consisted of a survey that was conducted in 2005 amongst 175 firms in 8 countries by an independent firm.<sup>105</sup> Nearly two third of the respondents had experienced obstacles to trade whilst doing business in Europe; an important reason for those obstacles to trade are the different legal systems in the Member States.<sup>106</sup> 25 % of the firms interviewed was refrained from undertaking cross-border business as a consequence of the legal differences. On the basis of, inter alia, these facts, the commentators draw the conclusion that '... a case can be made for further Community action in the field of European contract law on the basis of Article 95 EC.'<sup>107</sup>

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<sup>98</sup> See above, Section 2.3.

<sup>99</sup> See *Action Plan*, n 2 above, 32; Hesselink, n 11 above.

<sup>100</sup> In principle, the same problem can occur in the case of a conflict between a non-mandatory rule and any other rule from a 'higher level of governance', eg a national constitution. Similar questions will arise: can a non-mandatory rule ever violate the Constitution?

<sup>101</sup> Tassikas, n 101 above. W. van Gerven, the Advocate General in this case, had already indicated in his opinion (in footnote 15) that for the applicability of (now) art 29 it makes no differences whether a rule is mandatory or not.

<sup>102</sup> See above, Section 2.3.

<sup>103</sup> Case C- 212/97 *Centros* [1999] ECR I-1459; Case C-208/00 *Überseering* [2002] ECR I-9919; Case C-167/01 *Kamer van Koophandel en Fabrieken voor Amsterdam v. Inspire Art Ltd.* [2003] ECR I-10155.

<sup>104</sup> S. Vogenauer, S. Weatherill, n 12 above, 136.

<sup>105</sup> *Ibid.*, 117 ff.

<sup>106</sup> *Ibid.*, 125 ff, 136.

<sup>107</sup> *Ibid.* 117 ff, 125 ff, 136.

### 5.5. The CFR as an optional instrument under 95 EC

The forthcoming academic CFR contains many rules which cannot be said to be directly relevant to the Internal Market. Therefore, following the *Tobacco* judgement of the ECJ it seems unlikely that the entire Common Frame of Reference (CFR), or even large parts of it, could ever be enacted as an optional instrument under Article 95 EC.

At most, certain parts especially relevant to the Internal Market, e.g. all the rules relating to certain specific contracts (for example sales or franchising) and the relevant general contract law but not for instance benevolent intervention in another's affairs or tort law.

In this respect it does not seem to make a difference whether the part of the CFR that is most relevant to the internal market were to be adopted as one single instrument or whether it be split up into specific (vertical) optional on specific subjects.<sup>108</sup>

#### 5.5.1. B2B and B2C contract

It has not yet been made clear whether there will be separate optional instruments for commercial contracts and consumer contracts or one instrument that would apply to both. However, from the perspective of a legal basis this does not seem to make a difference.

#### 5.5.2. Cross-border and purely internal contracts

It is conceivable that the option to declare the instrument applicable would be given, not only to the parties to cross-border contracts, but also in the case where both parties have their residence or place of business in the same Member-State (opt-in; opt-out would practically amount to near harmonization). From the perspective of a legal basis this does not seem to make a difference.<sup>109</sup>

#### 5.5.3. Property law excluded? (Article 295 EC)

Article 295 EC provides: 'This treaty shall in no way prejudice the rules in Member States governing the system of property ownership'. This provision may suggest that it precludes the harmonization of property law on a European level. This would imply that Article 295 EC precludes an optional instrument that concerns (issues of) property law.

However, it follows from the ECJ case law that Article 295 EC does not exclude harmonization in the area of property law nor an optional instrument.<sup>110</sup> It is

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<sup>108</sup> See above, Section 2.8.

<sup>109</sup> Cf P. Oliver, W.-H. Roth, 'The Internal Market and the Four Freedoms', *CMLRev.* 41(2004) 407 – 441, at 434.

<sup>110</sup> Case C- 182/83 *Fearon v. Irish Land Commission* [1991] ECR I-1603; C-350/92 *Spain v. Council* [1995] ECR I-1985; Case C-423/98 Proceedings brought by A. Albore [2000] ECR I-5965. With respect to industrial and commercial property: Case C- 30/90 *Commission v. United*

submitted that the large majority of the decisions deal with the issue whether national rules of property law are contrary to the free movements. In answering this question, the ECJ has held that property law is a matter for the Member States, but that does not prevent the Court from assessing whether those national rules constitute an infringement of the free movements.<sup>111</sup> The result is that national property law also comes within the sphere of European community law, which renders it apt for harmonization or for inclusion in an optional instrument.

## 5.6. Article 94

### 5.6.1. Legislative procedure

Measures adopted on the basis of Article 94 EC require unanimity in the Council after consultation of the European Parliament and the European Economic and Social Committee.

### 5.6.2. Types of measures

Only directives can be adopted pursuant to Article 94 EC. Since directives must be transposed into national legal systems, this does not seem to be suitable measure for adopting an optional instrument.<sup>112</sup> This makes Article 94 EC unattractive as a legal basis.

### 5.6.3. Subject matter

With regard to the subject matter the same considerations apply as for Article 95 EC.

### 5.6.4. Conclusion

Article 94 EC is an unattractive legal base for an optional instrument, since on the basis of this Article only directives can be adopted and a directive is not a suitable legal form for an optional instrument. Moreover, measures adopted on the basis of Article 94 EC require unanimity within the Council.

## 5.7. Conclusions

It is not clear that an optional instrument, especially a mere opt-in instrument which is limited to cross-border contracts, would amount to a measure for the approximation of the laws of the Member States, as required by Articles 94 and 95 EC. Moreover, many of the subjects contained in the forthcoming draft CFR would almost certainly not pass the *Tobacco* test, as they are not directly relevant to the Internal Market. Finally, Article 94 EC is an unattractive legal

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*Kingdom* [1992] ECR I-829. See also Rutgers, n 93 above, 175 ff.; S. Weatherill, Diversity between National Laws in the Internal Market, in: *Divergences of Property Law, an Obstacle to the Internal Market?*, U. Drobnič, H.J. Snijders, E.-J. Zipporé (eds.), Sellier. European Law Publishers, 2006, 131 – 150, at 145 ff.

<sup>111</sup> Cf Kapteyn, VerLoren van Themaat, n 74 above, 554.

<sup>112</sup> See above, Section 2.9.

base for an optional instrument because on the basis this Article only directives can be adopted while a directive is not a suitable legal form for an optional instrument. Moreover, Article 94 EC require unanimity in the Council.

## 6. Article 308 EC: the catch-all provision

### 6.1. General

Article 308 provides:

‘If action by the Community should prove necessary to attain, in the course of the operation of the common market, one of the objectives of the Community and this Treaty has not provided the necessary powers, the Council shall, acting unanimously on a proposal from the Commission and after consulting the European Parliament, take the appropriate measures.’

Thus, in order to have a competence to adopt an optional instrument or optional instruments pursuant to Article 308 EC, it is necessary that the Treaty does not include any other powers according to which an optional instrument can be established.<sup>113</sup> In this respect it should be noted that the ECJ has ruled that the competences of Article 95 and Article 308 EC are mutually exclusive. In the decision in which the legal basis of Regulation (EC) No 1435/2003 on the Statute for a European Cooperative Society was challenged while referring to prior decisions the ECJ held that<sup>114</sup>:

‘In that regard, Article 308 EC may be used as the legal basis for a measure only where no other provision of the Treaty gives the Community institutions the necessary power to adopt it’

As to the boundaries of the competence included in Article 308 EC, the ECJ case law is scarce.<sup>115</sup>

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<sup>113</sup> Craig & de Búrca, n 76 above, 125; Kapteyn VerLoren van Themaat, n 74 above, 185. Cf Opinion 2/94, Opinion pursuant to Article 228 (6) of the EC Treaty, [1996] ECR I-1759, at 1788; Case C-377/98 *Kingdom of the Netherlands v. European Parliament and Council* [2001] ECR I-7079, 7157; Case C-436/03 *European Parliament v. Council* ECJ 2 May 2006, [2006] ECR I-3733.

<sup>114</sup> Case C-436/03 *European Parliament v. Council* [2006] ECR I-3733 para 36. See also Case 45/86 *Commission v. Council* [1987] ECR 1493 para 13; Case C-350/92 *Spain v. Council* [1995] ECR I-1985, at 2012. Cf J. Basedow, ‘Codification of Private Law in the European Union: the Making of a Hybrid’, *ERPL* 2001, 35 – 49, at 44.

<sup>115</sup> Opinion 2/94 pursuant to Article 228 (6) of the EC Treaty [1996] ECR I-1759; Case T-315/01 *Yassin Abdullah Kadi v. Council and Commission*, [2005] ECR II-3649; Craig & de Búrca, n 76 above, 126 ff.

## 6.2. *Legislative procedure*

For adopting a measure under Article 308 EC unanimity within the Council and consultation of the European Parliament are required.<sup>116</sup>

## 6.3. *Types of measures*

Article 308 EC speaks of 'appropriate measures' without specifying any further what kind of measures these might be. It is generally accepted that the wording of the Article does not per se exclude any type of legislative measure as they are included in Article 249 EC.<sup>117</sup> In particular, depending on the circumstances, a regulation and a recommendation may be appropriate measures.

On the basis of Article 308 EC several regulations have been adopted which introduced private law instruments, such as the *Societas Europea*,<sup>118</sup> the *European Cooperative Society*<sup>119</sup>, the *Community Trade Mark*.<sup>120,121</sup> The features of these instruments are similar to the likely features of the optional instrument under consideration here. First, they all concern private law institutions on a European community level. Secondly, they exist in addition to the various national types. Thirdly, the parties have a choice between the national instrument and the European one. Finally, they were all introduced on the basis of regulations.

## 6.4. *Subject matter*

### 6.4.1. *General*

Article 308 EC provides that measures adopted pursuant to Article 308 EC must pursue one of the objectives of the internal market.<sup>122</sup> When the ECJ was asked whether the European Community could accede to the European Convention on Human Rights by means of an international agreement, the ECJ expressed itself as to the boundaries of Article 308 EC. It stated:<sup>123</sup>

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<sup>116</sup> In the Lisbon Treaty the wording is different. Once this Treaty is ratified the Council will need to obtain the consent of the European Parliament.

<sup>117</sup> Kapteyn VerLoren van Themaat, n 74 above, 185.

<sup>118</sup> Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European Company (SE) *OJ* 2001, L 294/1.

<sup>119</sup> Council Regulation EC No 1435/2003 of 22 July 2003 on the Statute for a European Cooperative Society (SCE) *OJ* 2003 L 207/1-24.

<sup>120</sup> Council Regulation EC No 40/94 of 20 December 1993 on the Community trade mark, *OJ* 1994 L 11/1-36.

<sup>121</sup> Cf J. Basedow, Ein optionales Europäisches Vertragsgesetz – opt-in, opt-out, wozu überhaupt ?, *ZEuP* 12(2004) 1- 4, at 1 ff.

<sup>122</sup> Cf Opinion 2/94, Opinion pursuant to Article 228 (6) of the EC Treaty, [1996] ECR I-1759; Case T-315/01 *Yassin Abdullah Kadi v. Council and Commission*, Court of First Instance, 21 September 2005, [2005] ECR II-3649 with note by C. Tomuschat, *CMLRev.* 43(2006) 537 - 551.

<sup>123</sup> Opinion 2/94, Opinion pursuant to Article 228 (6) of the EC Treaty, [1996] ECR I-1759 para 23, 24, 29. Cf Kapteyn VerLoren van Themaat, n 74 above, 185.

'It follows from Article 3b [now Article 5 EC] of the Treaty, which states that the Community is to act within the limits of the powers conferred upon it by the Treaty and of the objectives assigned to it therein, that it has only those powers which have been conferred upon it.

That principle of conferred powers must be respected in both the internal action and the international action of the Community. ...

Article 235 [now Article 308] is designed to fill the gap where no specific provisions of the Treaty confer on the Community institutions express or implied powers to act, if such powers appear none the less to be necessary to enable the Community to carry out its functions with a view to attaining one of the objectives laid down by the Treaty.

That provision, ... cannot serve as a basis for widening the scope of the 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.'

In a rather atypical case, many years later, the ECJ elaborates what is meant by the words 'Community objectives':<sup>124</sup>

'the objectives of the Treaty, as expressly set out in the Articles 2 EC and 3 EC'

Thus, Article 308 EC may provide a legal basis for an optional instrument or optional instruments insofar as such an optional instrument aims at achieving one of the objectives as laid down in Articles 2 and 3 EC. Amongst those objects are an internal market without any obstacles to the free movement of goods, services, persons and capital (Article 3 (c) EC) and a system in which the competition is undistorted (Article 3 (g) EC).<sup>125</sup>

#### 6.4.2. The CFR as an optional instrument under Article 308 EC

As stated above, some realistic link with the operation of the common market seems to be required.<sup>126</sup> Therefore, it seems that Article 308 EC cannot serve as a legal basis for enacting the entire CFR as an optional instrument. More specific sets of rules, eg sets containing all the relevant rules relating to a certain type of contract, will have to be enacted as one or more optional instruments.

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<sup>124</sup> Case T-315/01 *Yassin Abdullah Kadi v. Council and Commission*, Court of First Instance, 21 September 2005, [2005] ECR II-3649 para 103. Cf *Kapteyn VerLoren van Themaat*, n 74 above, 185.

<sup>125</sup> See above, section 5.4.1.

<sup>126</sup> Opinion 2/94, Opinion pursuant to Article 228 (6) of the EC Treaty, [1996] ECR I-1759; Case T-315/01 *Yassin Abdullah Kadi v. Council and Commission*, Court of First Instance, 21 September 2005, [2005] ECR II-3649; *Craig & de Búrca*, n 76 above, 126 ff.

## 6.5. Conclusions

In all likelihood Article 308 EC cannot serve as the legal basis of an optional instrument that includes the entire CFR. However, it is probable that Article 308 EC provides the legal basis for one or more optional instruments insofar as they contribute to attaining one of the objectives of the Community as specified in the Articles 2 and 3 EC.

## 7. The CFR as an interinstitutional agreement

### 7.1. General

The European Commission has suggested that the Common Frame of Reference might become the object of an interinstitutional agreement (IIA).<sup>127</sup> The idea of an interinstitutional agreement on a common frame of reference (CFR-IIA) raises several questions as to the legal status of such an IIA, in particular whether it would be valid and whether it would be binding.

IAs have existed almost as long as the European Communities. They come in a great variety as far as the number of parties involved, the subject matter and their binding nature are concerned.<sup>128</sup> In practice, it is often suggested, the main aim of IAs is to enhance the influence of the European Parliament. However, this suggestion has been challenged in the literature.<sup>129</sup>

Most IAs are instrumental in implementing policies and competences determined in primary or secondary Community law. In this respect a CFR-IIA would be an atypical IIA. True, one could argue that a CFR-IIA would pertain to the organisation of the legislative process with a view to the coherence of the existing and future community *acquis* in the area of contract law. However, the

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<sup>127</sup> See eg Commissioner Kyrianiou's opening address at the conference on 'European contract law: better lawmaking to the common frame of reference' (first European Discussion Forum), London, 26 September 2005: 'To achieve this, it is not enough for only the Commission to use the CFR for drawing up coherent legislative proposals. If we want the final product to offer coherence and quality, we will also need a clear agreement from all institutions to use this tool.' In the *Action Plan*, 80, the Commission had said that 'for the area of European contract law, the common frame of reference as a guideline should not only be used by the Commission in the preparation of its proposals, but should also prove useful to the Council and the European Parliament in case they propose amendments', and in *The Way Forward*, it pointed out that '[i]t would also be desirable that the Council and the EP could use the CFR when tabling amendments to Commission proposals'.

<sup>128</sup> Cf W. Hummer, 'From "Interinstitutional agreements" to "Interinstitutional Agencies/Offices"?', *European Law Journal* 13 (2007) 47-74; I. Eiselt, P. Slominski, 'Sub-Constitutional Engineering: Negotiation, Content, and Legal Value of Interinstitutional Agreements in the EU', *European Law Journal* 12 (2006) 209-225; C. Bobbert, *Interinstitutionelle Vereinbarungen im Europäischen Gemeinschaftsrecht*, European University Studies, Frankfurt etc: Peter Lang 2001. M. Gauweiler, *Die rechtliche Qualifikation interorganschaftlicher Absprachen im Europarecht*, Dissertation, University Mainz 1988.

<sup>129</sup> See eg Eiselt and Slominski, *op cit*.

anomaly seems to be that the scope of the CFR is much broader than that of the community acquis and than that of the Community legislative competences.

### 7.2. *Permissibility*

The ECJ has never addressed the issue whether IIAs are permitted in general terms, but only on a case by case bases. This approach seems to imply that the ECJ does not regard IIAs invalid as such.<sup>130</sup> In particular, it cannot be said that all IIAs are always contrary to the principle of attributed competence (Article 5 EC).

Nevertheless, IIAs may potentially raise issues of competence creep, also in the case of an interinstitutional agreement on a Common Frame of Reference. This may be the case, in particular, with regard to the subjects and in the cases where there would be no legal basis for enacting a legally binding (optional) instrument (see above).

### 7.3. *Legally binding?*

The next question is what happens if one of the Institutions fails to respect the CFR-IIA. Much will depend on the formulation of the IIA.

If the IIA were to compel the Commission, Parliament and Council always to make sure that the revised *acquis communautaire* and any new legislative measures in the area covered by the CFR ('new *acquis*') be in conformity with the CFR and never to deviate from it, the issue might arise whether such an agreement should not be regarded as binding.

However, it seems unlikely that an IIA on the CFR will ever be phrased in such terms. Rather, it will probably state that the Institutions will have to take the CFR into account when enacting rules relating contract law (and other subjects dealt with in the CFR).

Indeed, the Council has already stated explicitly that the CFR will not be a legally binding instrument.<sup>131</sup>

### 7.4. *Horizontal effect?*

If the IIA is not going to be a legally binding agreement between the Institutions to legislate in conformity with the CFR the question does not occur whether the Court of Justice or the legislatures and courts in the Member States (or even the parties to contract) might be under an obligation to interpret relevant community legislation in conformity with the CFR.

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<sup>130</sup> See Hummert, *loc. cit.*

<sup>131</sup> See above, Section 3.1.



Such questions would only arise, however, if the IIA would somehow have the effect, and would be capable of doing so under Article 5 EC, that the Institutions were somehow bound to the CFR.

## 8. Conclusions

In its Action Plan on European contract law of 2003, the European Commission announced that it would examine whether problems in the European contract law area may require non-sector-specific solutions such as an optional instrument. Private parties would be able to select this instrument to govern their transactions, either in cases when the parties make a choice for its applicability (opt-in) or in all cases except when they exclude its applicability (opt-out). The present report discusses the existence of a legal basis for such an optional instrument.

It follows from the Communications from the Commission and from the Resolutions from the Council of the European Union and from the European Parliament that the binding nature, scope and content of an optional instrument are still rather uncertain. Consequently, any conclusions with regard to the legal basis of such an instrument can only be tentative.

The European Community only has the power to take any measures, including an optional instrument relating to contract law, insofar as a power is attributed to it by the founding Treaties, in particular the EC Treaty (Article 5 I EC). The EC Treaty does not provide for a specific competence to create private law instruments, e.g. an optional instrument, nor does it provide for any general competence to harmonize private law. Therefore, recourse must be sought to the functional competences laid down in the Treaty. The potentially relevant competences include the ones following from the Articles 65, 94, 95, and 308 EC. These functional competences differ, *inter alia*, with regard to the legislative procedures that must be followed and the institutions that would be involved, the types of measures that could be adopted, and the subject matters that could be dealt with.

It seems implausible that an optional instrument containing (almost) exclusively rules of substantive private law could be regarded as a harmonizing instrument concerning conflict of laws. Consequently, it is very unlikely that the Article 65 EC can provide a proper legal base for enacting an optional instrument.

It is not clear that an optional instrument, especially a mere opt-in instrument which is limited to cross-border contracts, would amount to a measure for the approximation of the laws of the Member States, as required by Articles 94 and 95 EC. Moreover, many of the subjects contained in the forthcoming draft CFR would almost certainly not pass the *Tobacco* test because they are not directly relevant to the Internal Market. Finally, Article 94 EC is an unattractive legal base for an optional instrument, since only directives can be adopted on the basis this Article while a directive is not a suitable legal form for an optional instrument. Moreover, Article 94 EC requires unanimity in the Council.

It seems likely that Article 308 EC could provide a legal basis for adopting one or more optional instruments on subjects of contract law that are particularly relevant for the operation of the Internal Market. Several other private law instruments, such as the *Societas Europea*, the European Cooperative Society, the Community Trade Mark, were adopted on the basis of this Article. The drawbacks of this legal basis are that unanimity in the Council is required and (from a democratic perspective) that the Parliament has no right of co-decision; it only has to be consulted.<sup>132</sup>

It is not certain that an interinstitutional agreement on a CFR could be legally binding on the European Institutions. However, the question is largely a theoretical one, since the Council has explicitly said that the CFR will be a non-binding instrument.

In conclusion, considering the relevant EC Treaty provisions and ECJ case law concerning legal bases, the description of an optional instrument by the European Commission in its Action Plan and its follow-up Communications on European contract law, and the private law measures already in place, Article 308 EC seems to be the most likely article to provide a legal base for enacting one or more optional instruments concerning European contract law. Article 95 EC seems to be excluded since an optional instrument would not be an instrument for the harmonization of the laws of the Member States. From the perspective of a legal basis it would not make a difference whether the optional instruments would be applicable to B2B, B2C or to both, nor whether they would apply only to cross-border contracts or also to purely internal contracts. However, even Article 308 EC cannot serve as a legal basis for enacting the entire CFR; any optional instrument will have to be limited to rules on the subjects that are particularly relevant to the Internal Market.

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<sup>132</sup> As said, the situation will be better after ratification of the Lisbon Treaty: then, pursuant to art 308 (new) the Commission needs to obtain the consent of the European Parliament before it can make a proposal for adopting any measures under art 308.

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